

Research Paper Provides Real Story Behind AT&T/T-Mobile Merger

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T-Mobile Was Stuck in Neutral, AT&T Is Best For Workers and Consumers

The Communications Workers of America today released a [research paper](#) documenting in detail how a merger between AT&T and T-Mobile will better serve consumers, workers and communities than the only other alternative: A Sprint/T-Mobile merger.

“Sprint or AT&T, The Real Story Behind the Proposed AT&T/T-Mobile Merger” reveals how T-Mobile’s owner, Deutsche Telekom (DT), had determined to stop investing in T-Mobile and the only two serious contenders for merger were AT&T and Sprint. AT&T is by far the best match according the detailed analysis.

“There are four facts that are brought to light here,” said CWA Senior Director George Kohl. “First, DT was seeking a buyer. Second, AT&T or Sprint were the two leading suitors. Third, merging with Sprint would be technologically and financially burdensome and finally, AT&T is the best option for consumers and workers.”

The fact that Sprint carries a BB - or “junk” credit rating and a merger would have added billions in debt to the highly leveraged company are discussed, as well as the fact that a merger would have brought major operational and technological problems. Further, a Sprint/T-Mobile merger would only exacerbate Sprint’s long history of outsourcing work outside the U.S. and trampling labor rights here in America.

“AT&T is financially strong and has the resources to build out broadband to 97 percent of American homes and businesses, a key to our national competitiveness in the years to come,” Kohl said. “Finally, AT&T allows its workers to make their own decision about whether or not they wish to join a union – the way every company should.”

NOTE: The full research paper follows:

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SPRINT OR AT&T?

THE REAL STORY BEHIND THE PROPOSED AT&T/T-MOBILE MERGER

T-Mobile Was Going to Be Sold; AT&T Acquisition, Not the Sprint Alternative, Is Best Option for Consumers and Workers

On March 20, 2011, AT&T announced an agreement to purchase T-Mobile USA. This development did not come out of the blue: **Deutsche Telekom (DT) was actively considering a sale to either Sprint or AT&T.** The alternative to the AT&T merger was not a standalone T-Mobile but a merger with Sprint. Thus, a comprehensive assessment of the impact of the AT&T/T-Mobile merger should include a comparison with the only real alternative that was being considered seriously: a Sprint/T-Mobile merger. As shown below, **consumers, workers, and communities will be better served by a T-Mobile merger with AT&T than one with Sprint.**

We will show:

- T-Mobile was in trouble;
- Deutsche Telekom had decided to sell T-Mobile to either AT&T or Sprint;
- A merger with Sprint would have been harmful to consumers, workers, and communities;
- AT&T is the better option.

T-MOBILE WAS IN TROUBLE

T-Mobile USA has been struggling to remain a strong competitor in the wireless marketplace. Despite marketing efforts to improve its standing, T-Mobile USA has steadily lost market share—both nationally and across major markets—over the past two years.¹

—Thorsten Langheim, Senior Vice President of
Mergers and Acquisitions, Deutsche Telekom

In 2001, Deutsche Telekom (the largest telecommunications company in Germany) paid \$35 billion for VoiceStream Wireless in order to gain a foothold in the fast growing U.S. wireless market. In 2002, the company was renamed T-Mobile USA. In 2008, DT expanded its U.S. investment when it purchased SunCom Wireless with 1.1 million customers. In 2010, T-Mobile was the fourth-largest wireless carrier in the U.S. with 34 million customers and 2010 revenue of \$21.35 billion.

However, Deutsche Telekom was not pleased with T-Mobile's performance: it was losing customers even after offering relatively cheap rate plans and smartphone promotions; had poor revenue growth, high rates of customer defections, and low margins; and was poorly positioned in the race to create the next generation high-speed wireless network (called 4G). Furthermore, DT was not willing to commit additional capital resources to fund the buildout of a fast 4G network.

- **Deutsche Telekom Was Not Willing to Commit Resources to T-Mobile.** Deutsche Telekom's CEO, René Obermann, stated publicly that T-Mobile USA "has to develop into a self-funding platform that is able to fund its future itself."² However, it was clear that T-Mobile was not in a position to be "self-funding."
- **T-Mobile Had No Clear Path to Develop Next Generation Wireless (4G LTE) to Remain Competitive.** All of T-Mobile's top competitors have plans to roll out 4G networks. For example, Verizon states that its 4G LTE network will reach two-thirds of Americans by mid-2012.³ AT&T's pre-merger plan was to reach 80% of Americans in 2013. Thorsten Langheim, Deutsche Telekom's Senior Vice President of Mergers and Acquisitions stated the problem: "T-Mobile USA lacks a clear path to deployment of LTE that is necessary for it to compete robustly in the U.S. longer term. . . . Unlike its competitors . . . T-Mobile USA does not have access to the spectrum needed to deploy LTE in an economically and technically sustainable fashion."⁴
- **Loss of Customers and Market Share.** T-Mobile was the only one of the top four wireless carriers to lose customers. From the first quarter of 2010 to the first quarter of 2011, T-Mobile actually lost 0.3% of its retail subscribers while AT&T gained 6.2%, Verizon Wireless gained 3% and Sprint gained 2%.⁵
- **Higher Rate of Churn.** The "churn" rate refers to the percentage of customers who leave their provider during a given time period. It is an indicator of possible customer dissatisfaction and/or better offers from competitors. T-Mobile consistently has the highest churn rate among the top four wireless carriers. For example, in the last quarter

of 2010, T-Mobile had a churn rate of 3.6% compared to 1.3% for AT&T, 1.3% for Verizon Wireless and 2.7% for Sprint.

- **Lagging Average Revenue per User (ARPU).** One important statistic used by analysts and investors is the average revenue generated per customer. T-Mobile, once again, has the worst performance in terms of ARPU than the other four largest operators. For example, in the last quarter of 2010, the ARPU for T-Mobile was \$46 compared to \$48.98 for AT&T, \$50.61 for Verizon and \$47.87 for Sprint.⁶
- **Lagging Average Revenue per User from Data.** Data is one of the largest growing components for wireless carriers. However, T-Mobile was 2 years late in launching its 3G network. As a result, data ARPU for T-Mobile is significantly lower than its top competitors. For example, in the last quarter of 2010, T-Mobile's data ARPU was \$12.80 compared to \$17.50 for AT&T, \$18.79 for Verizon and \$20.73 for Sprint.⁷

One research firm neatly summed up Deutsche Telekom's challenge with its T-Mobile subsidiary when stating "We do not see clear value enhancing strategies for T-Mobile US, with unsolved churn, market share and margin issues. In addition, Verizon could have access to the iPhone in early 2011, a clear negative for T-Mobile US."⁸

DEUTSCHE TELEKOM WAS GOING TO SELL T-MOBILE TO EITHER SPRINT OR AT&T

In general, all options are open in the U.S. —the sale of the whole business or of parts.⁹

—*Timotheus Hoettges, Chief Finance Officer, Deutsche Telekom*

The objective for us is to find a future proof solution for our U.S. business which generates value for our Deutsche Telekom shareholders as well as improves our path forward regarding cost of capital. This again has utmost priority for the entire Deutsche Telekom management board.¹⁰

—*René Obermann, CEO, Deutsche Telekom*

In 2010, there were media reports that DT was exploring a sale, spin-off, or an initial public offering of its T-Mobile subsidiary.¹¹ There were also even reports that DT would expand its investment in the U.S. by purchasing an equity stake in Clearwire with a deal to lease additional spectrum at a discount.

However, it is clear now that DT had eliminated all other options and decided to sell T-Mobile. Up to mid-March 2011, there were media reports about serious merger discussions between Sprint and Deutsche Telekom.¹² Deutsche Telekom CFO Timotheus Hoettges stated that DT was open to "all options."¹³ Obviously, DT was having other discussions with AT&T at the same time.¹⁴ On March 20, 2011, the AT&T/T-Mobile deal was announced.

A SPRINT/T-MOBILE MERGER WOULD HAVE BEEN HARMFUL TO CONSUMERS, WORKERS, AND BROADBAND BUILDOUT

What you never want to do is take one company that is going through challenges and take another company going through challenges.¹⁵

—Robert Dotson, former CEO, T-Mobile USA

A Sprint/T-Mobile merger would have faced major financial and technological obstacles, creating significant risks for consumers, workers and communities.

- **Major Financial Problems.** A merger would have placed incredible financial strains on an already weak Sprint. It is certain that Sprint's key financial metrics would have worsened significantly if it had been able to acquire T-Mobile.
 - **Sprint has a poor credit rating.** Even before the AT&T/T-Mobile deal was announced, all three credit rating agencies listed Sprint-Nextel's debt as speculative, non-investment grade (aka "junk") with a "negative" outlook and just one notch above a "highly speculative" rating. For example, on March 9, 2011, Standard & Poor's reiterated its "BB-" rating (with a negative outlook)—three notches below investment grade, citing "weak business profile because of its elevated churn relative to its peers; declining post-paid subscribers; significant competition from other wireless carriers, which is particularly important as the industry continues to show signs of maturation; and elevated leverage." A low credit rating raises the costs of borrowing and puts the company at a competitive disadvantage to those companies that have higher credit rankings and lower borrowing costs.
 - **A merger would have added billions more debt to an already highly leveraged Sprint.** T-Mobile's \$39 billion sales price is fully three times Sprint's total market value of \$13.8 billion. In fact, just the \$14 billion in AT&T equity that is part of T-Mobile's purchase price is roughly equal to Sprint's total market capitalization (Sprint's market cap has ranged from \$13.7 to \$15.5 billion since the transaction was announced). Even assuming that Sprint would have been able to negotiate the same \$39 billion price AT&T did to acquire T-Mobile (which seems highly unlikely), Sprint would clearly have been required to borrow tens of billions of dollars to fund the transaction, at least doubling its current \$20 billion in long term debt. In addition, Sprint has some \$5 billion in debt coming due over the next three years. Sprint had a debt-to-equity ratio of 138% in 2010. Any purchase of T-Mobile would add billions more debt to an already highly leveraged firm.
 - **Sprint's cashflow and capital expenditures couldn't support the merger.** While it has logged positive cashflows in 2010, Sprint's capital expenditures (capex) were very low compared to other telecoms. For 2010, Sprint's capital expenditures represented only 5.9% of revenues. This compares very poorly with typical telecom capital expenditures of 10% to 15% of revenues.

T-Mobile's capex was 12.8% of revenues, and clearly well below what was required to compete effectively with Verizon and AT&T. Just the additional \$8 billion in capital expenditures that AT&T committed to bring wireless broadband coverage to 97% of the U.S. population represents four full years of Sprint's total 2010 capital spending, and AT&T's capex starts from a much higher base of 16.3% of total revenues in 2010 (\$20.3 billion).

▪ **Major Operational and Technological Problems**

- **Sprint/T-Mobile would have had major interoperability problems.** A Sprint/T-Mobile merger would have required the combination of four different wireless operating systems—with significant interoperability problems. For example, T-Mobile uses GSM for its basic network which has significant interoperability problems with Sprint's CDMA-based system. In terms of the 4G network, Sprint chose WiMAX, which also has interoperability problems with LTE (the technology that is most compatible with T-Mobile's GSM platform and has been chosen by AT&T).

As MobileBeat wrote on March 8, 2011, "in practice a union between the companies would likely result in disaster. Sprint and T-Mobile's 3G networks are completely incompatible, and at the moment the companies are also pursuing completely different 4G strategies. T-Mobile is focusing on expanding its 3G network with HSPA+ technology, while Sprint is counting on its majority stake in Clearwire to deliver WiMAX 4G. Having the separate networks coexist under a single company sounds like a major headache, and it would be years before Sprint and T-Mobile subscribers could coexist on the same network."¹⁶

▪ **Inability to Adequately Develop and Integrate T-Mobile's Assets**

- **Financial weakness and technological problems.** A financially weak Sprint would not only have had to take on billions of additional debt just to finance a purchase of T-Mobile; it would also have had to raise additional billions of dollars to invest in developing and integrating T-Mobile's assets and moving it to a 4G network. This challenge would have been made even more difficult due to the incompatibility of Sprint's and T-Mobile's networks.

▪ **A failed attempt to integrate T-Mobile assets could have fatally weakened the number three competitor in the U.S. wireless market.**

- **Sprint is making incremental progress in digging itself out of the hole it created with the Nextel merger.**¹⁷ By the first quarter of 2011, it had reduced losses per share while it had lowered customer churn. It was even able to raise average revenue per customer in the face of Verizon Wireless' introduction of the iPhone and AT&T's aggressive pricing on iPhones in response. Sprint has more spectrum than any competitor, and is pursuing a viable 4G strategy.
- **The last thing Sprint needed was to expose itself to another potentially disastrous Nextel-like distraction.** Wall Street agrees: the average analyst rating for Sprint, according to Capital IQ, in April 2011, is "outperform."¹⁸ In other words, the opinion on the Street is that Sprint is currently an attractive stock for investors.

- **Sprint has long outsourced significant parts of its work, thereby lowering incomes and diminishing accountability.**
 - **Sprint outsources network management.** Sprint admitted that the transfer of 6,000 employees (10% of the workforce) in July 2009 to Ericsson to manage Sprint's network was done at least partially for costs.¹⁹ At the 2010 annual meeting of shareholders, Sprint CEO Dan Hesse admitted that the outsourcing deal, combined with significant layoffs, reduced costs by a third.²⁰ Sprint is the only U.S. wireless company that outsources network management.²¹
 - **Sprint network management has gone abroad.** According to one source, a "great part" of the Ericsson work had been sent abroad by November 2010.²²
 - **Sprint outsources a significant chunk of customer contact work.** The company stated that it had outsourced up to 70% of its customer contact workforce to places like the Philippines, India, and Mexico.²³ It is currently trying to reduce that percentage because it recognizes that first call resolution, difficult to achieve in foreign settings, is critical to consumer satisfaction.
 - **Outsourcing puts downward pressure on employment and incomes.** For workers that means lower compensation and for communities diminished purchasing power.
 - **Outsourcing in general reduces transparency for the customers and blurs accountability for the company.**

- **Sprint has history of trampling labor rights. A Sprint/T-Mobile merger would have been bad for American workers.**
 - **Sprint has a history of interfering in workers' decisions about whether or not to join a union.** The organizing drive at La Conexion Familiar, a Sprint long distance service marketed to Latinos, has become legendary. In a show of courage and solidarity, 70 percent of the workers at a San Francisco call center joined a petition to the NLRB to hold an election.²⁴ It was scheduled for July 22, 1994. There was no question the workers were going to win a union. Then on July 14, all 235 workers, most of them female, immigrants, and Latinas, were met at the door by guards, handed cardboard boxes, told to collect their belongings, searched, and fired en masse.²⁵ The office was permanently closed. In subsequent proceedings, an NLRB Administrative Law Judge found Sprint guilty of more than 50 violations of the law. The ALJ said he had never seen so many labor violations.²⁶ In an unanticipated consequence of the North American Free Trade Agreement, the first challenge under its labor complaint provisions was brought by the Mexican telecommunications workers union against Sprint in protest of the treatment of the La Conexion workers.²⁷
 - During the La Conexion experience and others, it came to light that Sprint had a management handbook on a union-free workplace that it issued to managers across the country. Managers were trained in union avoidance tactics.²⁸
 - At one time, there were organized units at Sprint, but most of those were organized under previous owners, local telephone carriers such as United Telephone, that Sprint acquired in a string of mergers. Sprint's strategy for dealing with those units was to isolate them, wall them off from the long distance

and wireless elements of the company so that those divisions would remain union free. Indeed, when Sprint changed its business plan once again in 2005, it spun off those properties which are today known as Embarq.

- There was a successful effort to organize three call centers in North Carolina. The workers persevered in the face of Sprint's relentless anti-union attacks over an eight year period (1986-1994). Once the unit was organized, Sprint dragged out contract negotiations for another year and a half, using a variety of delaying tactics while trying to decertify the unit even before the contract was signed.
- Together, these experiences had the effect of freezing workers' interests in forming a union. CWA members who were involved in those efforts have said that throughout the company there was a climate of fear. The workers knew they were likely to lose their jobs if anyone tried to organize.

AT&T IS THE BETTER OPTION FOR CONSUMERS, WORKERS, AND COMMUNITIES

AT&T is financially strong, has a good track record with past mergers, uses the same technologies as T-Mobile, has worked with its union to bring back 3,000 outsourced jobs, and allows its workers to make their own decisions about whether or not to join a union. Sprint has a poor merger track record, uses different technologies than T-Mobile, and actively interferes in workers' decisions about whether or not to join a union.²⁹ Given its highly leveraged position, Sprint is far less able to absorb a company its own size.

The chart on the following page summarizes the reasons why American consumers, workers, and communities are better off with a T-Mobile merger with AT&T than one with Sprint.

AT&T IS A BETTER MERGER PARTNER THAN SPRINT

ISSUE	SPRINT	AT&T
TECHNOLOGY	Different Network Technologies. The T-Mobile-Sprint merger would require the combination of four different wireless operating systems—with significant interoperability problems.	Common Network Technology. AT&T and T-Mobile utilize similar and compatible technologies for their basic networks and the 4G expansion. AT&T and T-Mobile use GSM and HSPA+ technologies for their basic network; both are compatible with AT&T's LTE 4G expansion.
PAST MERGERS	Poor Merger Track Record. The Sprint-Nextel merger was a disaster. Sprint has had trouble merging dissimilar networks. Sprint was not able to integrate its iDen and CDMA networks and has announced plans to phase out the iDen network beginning in 2013.	Good Merger Track Record. AT&T mergers all went smoothly: Bell South Wireless and SBC Wireless to form Cingular in 2001; Cingular and AT&T Wireless in 2004 to form AT&T Mobility; AT&T and Centennial in 2009.
FINANCIAL HEALTH	Financially Weaker: Less Able to Absorb T-Mobile <ul style="list-style-type: none"> ▪ “Junk” credit rating ▪ Debt-to-equity ratio of 138% in 2010; any purchase of T-Mobile would add billions more debt to an already highly leveraged firm. ▪ Net losses of \$8.6 billion from 2008-10. ▪ Bottom line: Sprint is financially weak and would have problems developing T-Mobile's assets. 	Financially Stronger: Better Able to Absorb T-Mobile <ul style="list-style-type: none"> ▪ Investment grade credit rating ▪ Much healthier debt-to-equity ratio of 59.1% in 2010. ▪ Net profits of \$30.3 billion from 2008-10. ▪ Bottom line: AT&T has the financial resources needed to develop T-Mobile's assets.
OUTSOURCING	More Outsourced Tech and Customer Contact Work. Network management has been outsourced while up to 70% of customer contact work is being performed by third parties.	Less Outsourced Customer Contact Work. Outsourced jobs continue to be a subject of negotiations with unions. AT&T and its unions negotiated the return of 3,000 DSL-related customer service jobs.
WORKERS RIGHTS	Anti-Union Policy. Strongly anti-union and takes a very active role in opposing efforts by workers to unionize. When bilingual call center workers sought to join CWA, Sprint closed the center and moved the work to Mexico.	Neutral Union Policy. Remains neutral and allows workers to make their own decisions about whether or not to be represented by unions.

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- ¹Federal Communications Commission, WT Docket No. 11-65, Application of AT&T and T-Mobile, Declaration of Thorsten Langheim, Senior Vice President of Mergers and Acquisitions, Deutsche Telekom, April 2011, p. 5.
- ²Briefing by Deutsche Telekom and T-Mobile to Analysts, January 20, 2011, http://www.telekom.com/dtag/cms/contentblob/dt/en/979218/blobBinary/transcript_20012011.pdf
- ³"Verizon Wireless Unveils Suite of 4G LTE Smartphones, Tablets, a Mi-Fi Hotspot and Notebooks," Verizon Wireless press release, January 6, 2011.
- ⁴Federal Communications Commission, WT Docket No. 11-65, "Description of Transaction, Public Interest Showing, and Related Demonstrations," Application of AT&T and T-Mobile, Declaration of Thorsten Langheim, Senior Vice President of Mergers and Acquisitions, Deutsche Telekom, April 2011, p. 5.
- ⁵Morgan Stanley, "Deutsche Telekom: U.S. Options – No Easy Way Out," January 10, 2011, p. 17.
- ⁶*Ibid.*
- ⁷*Ibid.*
- ⁸*Ibid.*, p. 2.
- ⁹"Sprint, Deutsche Telekom Said to Discuss T-Mobile USA Deal," *Bloomberg Businessweek*, March 8, 2011
- ¹⁰Briefing by Deutsche Telekom and T-Mobile to Analysts, January 20, 2011.
- ¹¹"Analysis: T-Mobile USA has done right but may be sold by parent wanting more," *Computerworld*, February 5, 2010; "T-Mobile's USA owner weighs IPO," *Wall Street Journal*, February 4, 2010.
- ¹²"Deutsche Telekom and Sprint hold U.S. mobile talks," *Financial Times*, March 8, 2011.
- ¹³Pamela Weaver, "Deutsche Telekom keeps it US Options Open," *telecoms.com*, March 9, 2011. <http://www.telecoms.com/25215/deutsche-telekom-keeps-its-us-options-open/>
- ¹⁴Sprint never seemed to be DT's first option. For example, when asked whether T-Mobile would consider a merger with Sprint, the former CEO of T-Mobile USA stated in 2010, "What you never want to do is take one company that is going through challenges and take another company going through challenges," quoted in Morgan Stanley, "Deutsche Telekom: U.S. Options—No Easy Way Out."
- ¹⁵Morgan Stanley, Jan. 10, 2011, p.4.
- ¹⁶Devindra Hardawar, "Worst Idea Ever: Sprint in Talks to Buy T-Mobile," *MobileBeat*, March 8, 2011 <http://venturebeat.com/2011/03/08/worst-idea-ever-sprint-in-talks-to-buy-t-mobile-report>
- ¹⁷Analysts were not excited by the prospect of a Sprint/T-Mobile merger. See Chris Nolter, "Talk of T-Mobile deal brings Sprint integration anxieties," *Daily Deal/The Deal*, March 11, 2011. Bloomberg ranked the Sprint-Nextel merger as among the worst in corporate history for shareholder value. Zachary R. Mider, "M&A Losers in \$10 Trillion Deal Binge Led by McClatchy, Sprint," Bloomberg, August 13, 2010. <http://www.bloomberg.com/news/2010-08-13/m-a-losers-in-10-trillion-takeover-binge-led-by-mcclatchy-sprint-nextel.html>
- ¹⁸This is based on a mix of analyst recommendations ranging from "buy" to "sell."
- ¹⁹<http://gigaom.com/2009/07/09/sprint-will-pay-ericsson-5b-to-run-its-network>
- ²⁰Mark Davis, "At shareholders meeting, Hesse paints a brighter picture of Sprint's outlook," *The Kansas City Star*, May 12, 2010.
- ²¹Phil Goldstein, "Networking outsourcing: Why the U.S. is an exception," *FierceWireless*, Sept. 7, 2010, <http://www.fiercewireless.com/special-reports/networking-outsourcing-why-u-s-exception>
- ²²Gulveen Aulakh, "Ericsson to serve US clients using 'competent' workforce in India," *The Economic Times*, Nov. 26, 2010.
- ²³Alena Semuels, "Sprint focused on keeping customers happy so they don't leave," *Los Angeles Times*, March 5, 2009, <http://latimesblogs.latimes.com/technology/2009/03/sprint-and-cust.html>
- ²⁴Jon Pattee, "Sprint and the Shutdown of La Conexion Familiar: A Union-Hating Multinational Finds Nowhere to Run," *Labor Research Review*, Vol. 1: No. 23, Article 8, p. 15, <http://digitalcommons.ilr.conrell.edu/lrr/iss23/8>
- ²⁵*Ibid.*, page 13.
- ²⁶Lysa M. Saltzman and Antonio Salazar-Hobson. "The Ultimate Hangup on the NLRA: Denial of Section 10(J) Injunctive Relief for La Conexion Familiar," *California Western Law Review*, 1996.
- ²⁷Pattee, pp. 18-21; Richard Ivey School of Business, University of Western Ontario, "Sprint – La Conexion Familiar (B)," 1997.
- ²⁸Ivey School of Business. "Sprint – La Conexion Familiar (A)," pp. 5-6.
- ²⁹For a more detailed examination of the benefits of the AT&T/T-Mobile merger see, Communications Workers of America, "The AT&T/T-Mobile Merger: Benefits for Consumers and Workers," April 2011,