

Why Your Cell Phone Stinks



The carriers should get out of the business of subsidizing devices, and focus on service

Of all the technical marvels the networking industry has delivered, the cell phone has had the greatest impact on the greatest number of people's lives. However, like the introduction of wired telephone service 100 years earlier, its acceptance was not entirely a process of a competitive market. As wireless technologies progress, the business model that launched the industry may not be the best model to sustain it.

Like the wired telephone business, the shaping of the cellular business in the early 1980s was a product of regulatory intervention. The original analog cellular licenses were divided between "A" or non-wireline and "B" or wireline (read telephone company) carriers. The result was that roaming was expensive and inefficient, and it took a decade for nationwide services to emerge. The PCS spectrum auctions and the introduction of digital cellular in the early 1990s provided the industry with enough capacity to finally meet consumer demand, but by then, the basic business plans were already well-entrenched.

The phenomenal growth of cellular has been spawned in large part by a Faustian bargain the carriers have struck with their customers: the carriers underwrite the cost of your handset to hook you in for a long-term contract. Some carriers are now questioning the wisdom of that plan. Sprint's Gary Forsee has indicated that the business model for their new WiMAX service will not be built on subsidized devices, so possibly this idea will disappear from the wireless market.

The Deal

I call the fundamental business plan for the cellular industry The Deal, the basic tenet of which is "give 'em the razor, then sell 'em the blades." Cell phones are expensive (lose one and you'll find out just how expensive), so the cellular carriers subsidize the equipment to lessen the upfront pain of subscribing. The carriers protect their investment by locking the phone (i.e., setting it so it will only operate on their network) and charging significant termination penalties. Locking the cell phone is the equivalent of locking the cell door, so while you may possess the cell phone, there's no doubt who "owns" it. Only the technically adventurous will want to go through the process of getting their cell phone unlocked.

Of course they'll give you one razor (or "Razr"), and when you lose it, it's time to make you pay. In buying a replacement you find the real price. I've always wondered if the cell phone manufacturers charge the consumer the same price for that phone that they charge the cellular carriers? Forget that, I think we all know the answer.

When it comes to replacement phones, you can be quite sure someone is keeping statistics on the relative percentage of subsidized versus replacement phones that are sold; given that many people will want the same phone they're used to, the manufacturers can count on selling a predictable percentage of full-price phones relative to all the "discounted" ones they distribute through the cellular carriers. And there's always that lucrative add-on business of replacement batteries, car chargers, holsters and all of that other stuff.

This is clearly an environment where one hand washes the other. The phone comes loaded with do-dads like cameras and browsers that generate network revenues. Did you ever notice that all the soft keys on your new phone are programmed to point you to those revenue-producing services?

The great thing about this arrangement is that the consumer thinks they're getting a deal on their phone, when in reality, they're buying into The Deal. The problem with The Deal is the consumer is the guy least likely to come out ahead!

So What's Wrong With That?

The fundamental problem with subsidized phones is that you're letting someone else choose your phone, and that party is smart enough to make choices that are in their best interest; their best interest does not necessarily coincide with yours. All too often the cell phone companies' choices have ranged from just plain bad to anti-consumer.

I just got a new Samsung A707 when I re-upped with AT&T. It's got a camera (that I never use), Web access (that I've only turned on by mistake), an address book, a calendar, and an integrated MP3 player. Those latter three, particularly the MP3 player, I might actually use.

Of course then I found out that it could only download songs from PCs, not Macs—Huh? With all the resources that Samsung has at their disposal, they couldn't get someone to write an interface for Macs? Checking around I found that there's a

company called Datapilot that makes software that transfers not only MP3s from Macs but address book and calendar entries, even image files. Unfortunately the A707 is not supported. In the end, it's a good phone, which could be great with a little work. But if I were buying a consumer electronic device, I wouldn't be buying something as dysfunctional as this in a hundred years.

While my experience was simply annoying, other tactics have been just short of a stick in the eye. In 2005, Verizon introduced the Motorola V710, one of the first handsets with a Bluetooth interface and integrated MP3 player. Once consumers got it home, they found the file transfer capability had been disabled so the only way to get files into the phone was over Verizon's wireless data service. Consumers returned the phones in droves and a group filed a class action suit, so carriers aren't likely to be that heavy-handed again.

With the development of multifunction devices, this issue is getting more contentious. A case in point is dual-mode Wi-Fi/cellular handsets. Those phones are used in fixed-mobile convergence (FMC) services where a call can be handed off from the cellular network to the customer's wireless LAN. Are the cell phone companies going to subsidize a handset that makes calls on a network from which they receive no revenue?

T-Mobile is subsidizing the dual-mode Samsung and Nokia handsets marketed with their consumer-oriented HotSpot@Home FMC service. In an interesting twist, they have also introduced a Cisco/Linksys Wi-Fi router that supports two SIM cards, so you can have up to two wired phones along with your Wi-Fi/cellular handsets. So along with the Wi-Fi/cellular service, you can replace your existing wired phone line with one that can make calls over the VOIP service that is part of HotSpot@Home.

The iPhone Impact

No device has brought this whole matter into a clearer focus than Apple's iPhone. I have been an Apple fan and Mac user since 1984, and Apple did hit a solid double with the iPhone (not a home run). The major development was that Apple convinced the customer they should spend their own money (\$500 or \$600 of it) to get a phone that's really worth having.

I've tried it out and was decently impressed. However, even though I am an AT&T cellular customer, I was informed that the iPhone isn't supported by my particular plan. So being a member of the non-preferred class (an existing customer), if I want an iPhone I'll wind up paying about 30 percent more for my service.

It looks like there are two winners and one loser in this deal. Apple sells an iPhone, and AT&T can jack up the rate while avoiding the cost of a subsidized handset. Guess who the loser is? Maybe when the initial sales slow down they'll get desperate, start bottom feeding, and find me!

Apple seems to have played their end of the game better than AT&T. Apple gave AT&T an exclusive, but then equipped it for a wireless data service that was out of date two years before the lines started forming outside the Apple stores. The initial iPhones will only support the 2.5G EDGE service, not the higher speed 3G UMTS or HSDPA. Apple's treating AT&T like an add-on to their phone, and AT&T is sucking up like a whipped puppy. I love Apple's TV ads where they describe the iPhone as the gadget of your dreams that stores pictures, songs and movies, and at the end, point out that it makes phone calls, too!

Conclusion—The New Game Is A Better Game

The cellular market has always been crazy because the carriers are selling two different things: a practical mobile network service and a cool consumer appliance. Getting the carriers out of the appliance business will force them to focus their efforts on providing better service—and they certainly have a lot to work on in that regard.

The operative phrase in cellular seems to be: "We strive for mediocrity." Sound quality is poor, network-busy conditions are more frequent than they should be, and unless someone is springing for an indoor antenna system, you still might have to go outside to make a call. In the Northeast we're still smarting from the August 2003 blackout when we found the carriers didn't have back-up power for all their base station sites. So the one day when people really needed reliable communications, we had stranded commuters lining up to use the few available payphones.

Taking The Deal out of the cell phone business would force the carriers to compete on service, and leave the equipment decision where it belongs, with the consumer.

Your equipment options are being curtailed by the carriers' business plans, which were created in a time when a cell phone was just a cell phone. As devices have become more complex, the carriers have not proved to be adept at judging requirements in consumer electronics; certainly not as good as folks like Apple. A cell phone isn't that tricky to build anymore, so we should be able to get that capability in any number of devices.

As the carriers have bred customers on subsidized handsets, they may still have to offer those deals, but they should price the service and the phone deal separately. They might also consider limiting those offers to low-end voice-only handsets. Wouldn't it be nice to be able to buy a cell phone that didn't have a camera in it?□

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The iPhone may point the way to a new business model