

Amid shake-up, US cell carriers look to new models

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(AP)—How's this for gall? Take away hundreds of dollars in subsidies that cellphone customers have enjoyed for years. Then pass it off as an improvement.

The major U.S. wireless companies are doing just that. And many of their customers seem to like it.

The U.S. wireless industry is in the midst of a shake-up, sparked by T-Mobile's decision in March to stop subsidizing phones bought by its customers. National rivals followed with similar plans. Since then, U.S. carriers have been announcing new prices and plans every few weeks.

The move is essentially giving the customer more flexibility—at a price.

With subsidies, consumers typically pay \$200 up front for a phone that costs \$600 or more. Wireless companies make up the difference by padding the monthly service charges over the life of the two-year contract. Under that approach, customers save some money but are stuck with a phone for two years, which can be frustrating when a new model comes out just months or weeks later.

By forgoing subsidies, customers aren't locked into contracts and can upgrade more frequently.

Driving this trend is the rapid pace with which new phones are released from Apple Inc., Samsung Electronics Co., Sony Corp., LG Electronics

Inc., HTC Corp., Nokia Corp. and others.

"It's happening at least every 12 months, if not even faster," said David Christopher, chief marketing officer for AT&T Inc.'s wireless business. "The tech cycles are speeding up."

Many models will be unveiled this week at the Mobile World Congress wireless show, which begins Monday in Barcelona, Spain. Among the most keenly awaited will be Samsung's successor to its flagship Galaxy S4.

The bevy of new phones could push even more U.S. customers into subsidy-free installment plans such as AT&T's Next, Verizon's Edge or Sprint's Easy Pay. These all let people trade in phones before the two years are up. T-Mobile US Inc., which now sells all phones without subsidies, also lets people trade in phones early if they join a \$10-a-month Jump program.

The carriers are beneficiaries from these programs because they no longer have to pay for the subsidies. Instead, they get their customers to pay the entire cost of the phones, all at once or in installments.

In a sense, the shift away from subsidies is inevitable. Subsidies helped attract customers as the wireless industry grew. But most Americans now have cellphones.

Even if T-Mobile hadn't made the move to end subsidies as part of an effort to lift itself from fourth place in the market, competition likely would have forced carriers in the U.S. to do so, just as they already had in parts of Europe.

There, low-cost carriers were poaching customers from the big companies just as they were breaking even on the subsidies, said John

Strand, CEO of the telecom research firm Strand Consult in Copenhagen, Denmark. Instead of enjoying profits on that customer, the big carrier had to spend money to acquire a new one. Ultimately, many carriers decided to end subsidies and charge for phones separately.

Mike Katz, vice president of marketing at T-Mobile, said phone bills had gotten confusing with the true costs of phones hidden in monthly service fees. He said many customers mistakenly thought that phones cost just \$200, without realizing they were really paying back the carriers for the subsidies over time.

He described subsidies as a drug for carriers. It was an easy way of retaining customers, he said, as subsidies "put handcuffs on and forced people to stay" until their contracts expired. Without subsidies, he said, carriers can try to lure customers with good service and prices instead.

Of course, subsidies haven't gone away entirely in the U.S. and might never do so. T-Mobile is the only national carrier to have dropped subsidies completely. There's no exact number on how many subscribers are opting for subsidy-free plans. AT&T Inc. said 15 percent of new smartphones and upgrades in the last three months of 2013 were through Next. That's significant, but hardly a majority.

So far, these plans appeal to those who absolutely must have the latest device and the newest features. But there are spillover benefits for remaining customers, too.

Customers benefit most from subsidies when they upgrade phones right at the two-year mark. If they hold on to phones longer, they still have to pay for the cost of subsidies through what's baked into the monthly phone bills.

Now, those people will benefit from the same service discounts enjoyed

by frequent upgraders.

"A lower-priced service plan coupled with a financed handset may not be much cheaper than a subsidized plan initially, but if you're going to keep your handset for a while it can be a big savings," said Craig Moffett, a telecom analyst with MoffettNathanson.

In addition, subsidies encourage people to buy expensive devices because the overall cost is spread out, so getting rid of them could make cheaper phones more appealing.

Dan Hays, U.S. wireless advisory leader at the consulting firm PwC, said buying phones will ultimately be like buying a car: You can buy one outright or in installments. You can lease and upgrade to new models. You can buy a used model or trade in an old one.

It may seem unfair to consumers that phone companies are backing away from subsidies.

But consumers may indeed be the big winners in getting choice and freedom instead.

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