Telefonica's O2 buyout buoys outlook

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Business hopes are high at Telefonica in acquiring O2, a deal that was officially announced Monday after weeks of speculation.
The Spanish company, which is the world's fifth-largest telecommunications group in terms of market value, said it will pay $31.5 billion for the British mobile provider by paying $3.55 per O2 share, which is about 22 percent more of the company's closing price last Friday.

The former state-owned enterprise dominates the telecommunications markets in Spain and Latin America with about 145 million subscribers worldwide. It has not, however, been as successful in expanding across the European continent, and the buyout of the British mobile group is expected to bolster Telefonica's presence in Britain and Germany in particular.

In a news release, Telefonica stated that "the combination with O2 is a logical step for Telefonica in pursuing its strategic goal of providing its shareholders with both growth and cash returns," adding that the buyout will "provide enhanced scale by entering two of Europe's largest markets, Germany and (Britain), with critical mass."

Certainly, the corporate climate that prevails in the two companies is not dissimilar, as O2 itself was part of British telecommunications giant British Telecom until November 2001, when it became an independent carrier. It currently has about 25 million subscribers in Britain, Ireland and Germany.

Telefonica Chairman Cesar Alierta stated, "O2 is an excellent company that, driven by a top class management team, has been able to become one of the highest growth mobile operators in Europe. Its integration in the Telefonica group will enhance our growth profile, it will allow us to gain economies of scale, it will open the group to the two largest European markets with sizeable critical mass and it will balance our exposure across business and regions."

Meanwhile, O2 Chairman David Arculus welcomed the buyout, stating that the deal is "an excellent opportunity for O2 shareholders to realize significant value in cash now. ... Our successful brand will be retained and extended bringing benefits to both customers and employees as part of an enlarged, strengthened group."

In a phone conference with reporters shortly after the announcement, O2 Chief Executive Peter Erskine said that the company was "very excited" about the company's prospects going forward, adding that the Spanish phone group will "have no overlapping territory, so they will be able to offer our customers better roaming and better services around the world." Both Arculus and Erskine will have seats on Telefonica's board if the deal goes through. The companies expect the move to be completed by February 2006, pending shareholders' approval.

Investors have warmly welcomed the news, or at least those with shares in the British mobile company have, as O2's stock price soared 25.42 percent to 206. Telefonica, meanwhile, saw its share price tumble 2.94 percent to 13.22.

Still, analysts largely agree that the deal is good for both companies, and not just O2.

"This is, potentially, good news for both operators. For Telefonica, it allows it to enter two of the largest European markets in terms of

subscribers and revenues, as well as two of the most advanced and highly competitive markets: U.K. and Germany," said Marta Munoz Mendez-Villamil, senior analyst at Ovum, a private London-based telecommunications research group.

"For O2, it was something bound to happen. They were operating in a market with large players like Vodafone, France Telecom and Deutsche Telekom. They had become too small a fish, and sooner or later were to be eaten," she added.

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