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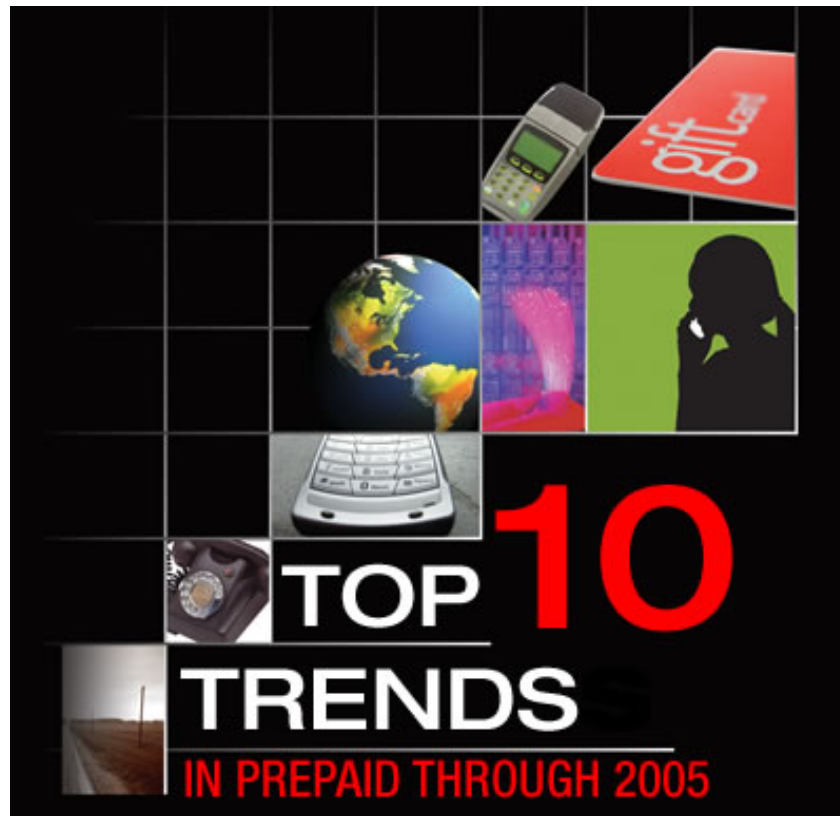
### Top 10 Trends in prepaid through 2009

*Sizing up opportunities, markets and technologies affecting the industry*

**by: Dr. Judy Reed Smith and Fedor Smith**

Prepaid is hot. To say it isn't your father's prepaid industry, however, would be an understatement; it's not even the industry we knew a few short years ago. Likewise, today's prepaid world does not represent the one we will know a few years hence.

In considering the many ways the industry will change, we offer our top 10 influences of change, stealing the data from our newest report, "Prepaid Insights 2005-2009: Sizing Up Opportunities, Markets and Players," and the most recent update of our prepaid wireless study. Here are our picks for the top influences of change.



#### 1. VoIP evolution

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VoIP has, and will continue to have, a great impact on the cost of telephony, with an especially important impact on international service. As VoIP quality improves, people talk longer and drive more minutes. In addition to the decline of transmission costs and the increasing time on calls, this digital technology enables new features and functions such as those mentioned above.

## **2. New products and revenue streams**

Revenue opportunities will continue to evolve. Who would have guessed that ring tones would pull in \$375 million a year? And with segments of customers wanting to further differentiate themselves and their services, there are ring back tones, which sound different to the caller when dialing inward; short video segments for mobile phones; phone-based payment systems for fast food or vending machines; and other money-making ideas not yet created.

ESPN, owned by Disney, plans a service with sports content access that we expect will find a very healthy market. With the technology-readiness of the population increasing year by year, more interesting handsets and increased broadband availability will offer opportunities for creative companies.

## **3. Point-of-sale activation**

Point-of-sale activation (POSA) will continue to bring significant changes to the industry. The savings in theft and fraud alone are significant to providers and retail outlets distributing prepaid products, and the ability to reduce inventory offers additional savings.

Currently, POSA terminals represent investments of capital, training time and requirements for more capable staff than former prepaid products, but simpler, more efficient and cost-effective versions of POSA services are being developed. These newer versions will filter through to smaller shops and offer the benefits of POSA to a broader population of outlets providing prepaid services to the public.

## **4. Stored value offers the largest new prepaid opportunity**

Stored value cards, working with magnetic stripes or chips that cardholders use to store money for future payments, provide a new form of currency for their customers. Clever, flexible and easy to use, stored value cards are employed in many different applications markets and excel in each of them.

Christmas gift cards showed up in the 2004 season with more sales than ever, solving every problem of size, color and taste. Health care flexible spending accounts and the replacement of payroll checks for unbanked populations offer large dollar opportunities for providers and have lured major credit card providers into prepaid opportunities.

Atlantic-ACM expects stored value card fees and residuals to go up from \$800 million in 2003 to more than \$5.7 billion by 2009. These fees and residual payments include a range of fees charged by service providers or card issuers in relation to their card offerings. The fees may be charged to the customer and/or to the retailer, including charges on residual money remaining on the card over time. Some of these fees are in the spotlight of regulators and consumer advocates and are likely to disappear.

Stored value cards allow a wonderful loyalty effect for retailers, gaining new customers (through gift cards), retaining existing customers (through loyalty cards) but also boosting their sales – more than half the time, customers spend more money in the store than the actual value of the card.



## **5. Evolving demographics will favor prepaid and wireless services**

As we head through the second half of this decade and into the teens of the century, the U.S. population will be growing up. The teen-agers of today will be likely to continue using some of the brands they adopted in their youth and some of the product patterns they have come to enjoy.

Currently, the bulk of customers who use only cellular services rather than wired phones are in their youth. They think of a phone number connected to an individual rather than connected to a building. Each decade, more customers will make this mental leap, with wired services shrinking in importance and revenue. In addition, the youth, as well as new immigrants in this country, are the most likely users of prepaid services. If prepaid providers can continue to evolve their pricing and product features to hold their customers, they can build margin-supporting loyalty.

In the past years, however, prepaid providers knew very little about their customers. They accomplished little research because it was much more challenging to perform on people whose name and/or address they do not necessarily know. This will need to change if the providers hope to shift to loyal customers.

## **6. Increased youth population buying power while younger users come online**

Growth of the youth segment of the population continues to outpace that of the general population and will continue to do so until almost 2010. Young Americans, on average, spend about \$100 of disposable income per week, and cell phones are on par with clothes and shoes in their shopping priorities. Young consumers grow more financially independent every year but without the credit histories necessary for cellular calling plans and, therefore, depend heavily on prepaid services.

Cellular users will become increasingly younger as the cost of handsets continues to decline. Second graders don't need \$50, 1,200-minute-per-month calling plans; they just need access to call mom after piano practice or when they become scared at sleepovers. Prepaid packages are ideally suited for these needs.

## **7. MVNO power increase with prepaid wireless an increasingly interesting product**

Sprint has committed to the support of mobile virtual network operators (MVNOs), demonstrating the company can build a strong business with a wholesale offering, using resellers in much the way the large companies used them in long distance during the 1990s.

In that model, a network owner looks strategically at the markets it cannot profitably serve, and reaches those customers through entrepreneurial niche marketers who can resell their products to those markets. Many of these clever companies have used the prepaid model. Virgin Wireless, which has been coming on strong in the youth market, is now discussing an offering of public shares in conjunction with Sprint.

Again, improved trust in the telecom markets as investments can bring more of these models forward in the prepaid wireless world, growing the number and economic strength of the players.

## **8. Industry consolidation shapes a new landscape**

Consolidation and an evolving marketplace will occur within large multiproduct providers, wireless players and companies that focus on

prepaid. Many major 2005 mergers have been announced. Financial services players tend to gain confidence from seeing one action in play, which tends to rapidly impact the momentum (for or against) additional mergers.

At this point, it appears that 2005 is the beginning of an increase in confidence, and therefore activity, in telco mega-mergers. This overall trend toward returning confidence in telco investments will bring new financial services players to the prepaid world as well, with MVNO roll-ups being a potential opportunity.

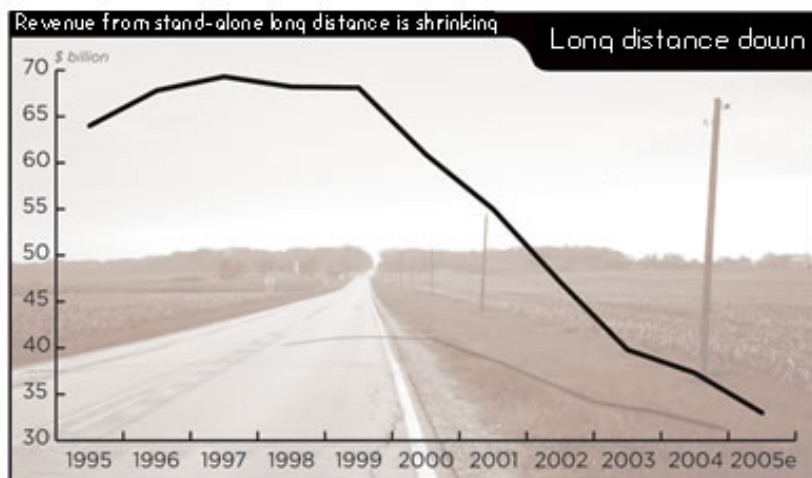
**9. Growing international prepaid long distance**

International long distance in the prepaid sector is a somewhat different story. Although the cost of a call has dropped dramatically, the number of first-generation immigrants has risen. It is this segment that tends to boost international calling due to family or business connections in the native countries. So not only has the number of buyers increased, but also lower costs have created an elastic effect on the volume – both in call numbers and lengths.

This trend toward increased usage will continue regardless of whether the connection technology is circuit- or packet-switched. However, circuit-switched services will disappear as companies experience equipment maintenance costs greater than their thin margins can support and as VoIP quality continues to improve.

**10. Time and distance are dead for U.S. calling**

In 1997, the economist Frances Cairncross wrote a book called "The Death of Distance." In it, she predicted what has happened to date and will continue to happen to the long distance sector over the coming decade; namely, its revenue decline. According to our "2004-2009 U.S. Long Distance Sizing and Share" report, interexchange voice revenues in the United States were forecasted to be \$33 billion in 2005, down from almost \$70 billion less than a decade ago, and they will continue to shrink at a significant rate – to less than \$15 billion – by 2015. As the distance of a U.S. call no longer matters, time spent speaking domestically is also a concept of the past. With the buckets, bundles and unlimited calling packages, time and distance are both dead for U.S. calling.



Source: Atlantic-ACM report, "2004-2009 U.S. Long Distance Sizing & Share"

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ACM's newest report, "Prepaid Insights 2005-2009: Sizing Up Opportunities, Markets and Players." For information on this report, visit <http://www.atlantic-acm.com/>.

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