Syniverse Holdings, Inc. (NYSE:SVR)

McIntire Investment Institute
Long Fund Memo

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Date: November 30, 2009 **Price:** 15.86 **Analyst:** Hideyuki Liu

52-Week Range	Market Cap	Cash	Total Debt	P/E	Gross Margin	EPS
7.51 - 19.56	1.10B	216.2M	515.6M	16.11	64.57	0.98

Business Overview

Syniverse Holdings, Inc. ("Syniverse") serves as one of the wireless industry's only operator-neutral intermediaries and is an enabler of wireless voice and data services for telecommunications companies worldwide. Syniverse's data clearinghouse, network and technology services solve technical and operational challenges for the industry by translating incompatible communication standards and protocols and simplifying operator interconnectivity. Syniverse's services allow operators to deliver seamless voice, data, and next generation services to wireless subscribers including wireless voice, data roaming, short message service (SMS), multimedia messaging services (MMS), mobile instant messaging (MIM), number portability and wireless value-added services.

Syniverse's main services are as follows:

- Technology Interoperability Services
- Network Services
- Number Portability Services
- Call Processing Services
- Enterprise Solutions
- Off-network Database Queries

The company provides its services to more than 650 operators in over 140 countries. Clients include most of the largest global wireless operators including AT&T, Sprint Nextel, Verizon Wireless, AmericaMoviles, China Telecom, KDDI, TeliaSonera, Vodafone, VimpelCom, and SK Telecom.

The majority of revenue is generated on a per-transaction basis and Syniverse often receives revenue from multiple transactions during a single call or data session. Additionally, these charges are determined by long-term contracts, typically averaging three years in duration. The remainder of revenue is generated from custom software development fees, hardware sales, professional services, and recurring non-transaction fees for network connections and software maintenance.

Market misperception

The market constantly questions the current environment for Syniverse. Both the general belief that the recessionary environment will hamper consumer usage of value-added services like text messaging and the macroeconomic movement of telecommunication companies to consolidate themselves have pushed down Syniverse's prices. Recent developments like the Verizon-Alltel **merger, which have cut into Syniverse's revenues**, drive this perception home very strongly. Fears that wireless standardizations like 3G will make intermediaries such as Syniverse obsolete is rampant.

However, I believe that the analysts are myopic in their focus. Syniverse has not only a global reach, but also a wide suite of services that place Syniverse in a unique position. Other competitors may have one or the other – or even neither. Analysts are focusing too deeply into the developments occurring in North America when the true growth of Syniverse lies in the global development.

Thesis Points

Syniverse's track record is a crucial comparative advantage in a relationship-driven industry

Success in Syniverse's industry is determined by how well one can obtain and maintain relationships. Business is established through long-term contracts averaging three years, and being able to obtain renewals for contracts guarantees a stable cash flow. In that regard, Syniverse has been able to provide 20 years of quality service, although it has only gone public recently in 2005. Adding credence to its service quality was **Syniverse's ability to retain 98% o**ver that time frame.[1] In 2008, Syniverse had successfully obtained renewals from its largest customer, Verizon Wireless, along with extensions from AT&T and T-Mobile.

The success domestically is resounding: Cellular South had signed a contract renewal, announced on November 30, 2009. This adds another to the count of more than 80 North American operators that have renewed contracts with Syniverse since January 2009. And in that same timeframe, Syniverse has succeeded in adding to its existing customer base with 20 new North American customers, consisting of mobile operators as well as cable operators and Internet, VoIP, and applications services providers.[2]

Syniverse amalgamates a wide array of services that provide dual economies of scale

A more subtle comparative advantage of Syniverse is its unique ability to provide a wide array of services. In the industry, competitors may only be able to provide Number

[1] 2008 Annual Report
[2] TMC news, "Syniverse Strengthens Ties with Cellular South"

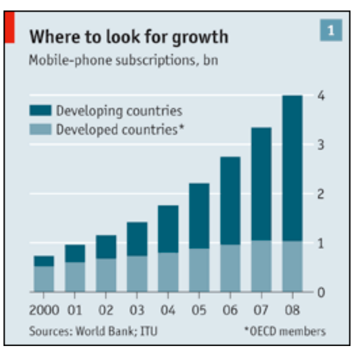
Portability Services or Network Services. There is no other company that competes **with Syniverse's wide array of products on a global scale.** A distinct advantage that Syniverse's global positioning allows is its ability to give 24-hour customer service to its clients. This synergy has allowed the company to enhance the quality of service offered to all its clients.

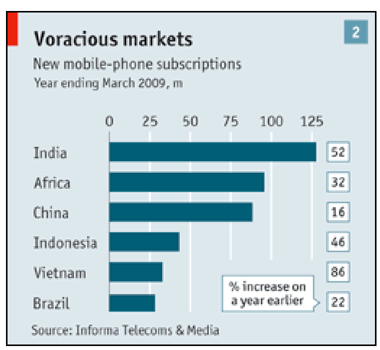
Furthermore, Syniverse's service suite allows clients to settle all their needs with Syniverse alone, as opposed to having to obtain services and products from numerous different sources. This allows both Syniverse and its clientele to circumvent logistical issues that may have occurred with different technologies. As evidence of this point, **Verizon has contracted to continue using Syniverse's comprehensive suite of data** clearing and roaming services. Also, Cellular South followed suit, signing a contract for a broad suite of 11 messaging, roaming, clearing, fraud prevention, and business intelligence solutions.

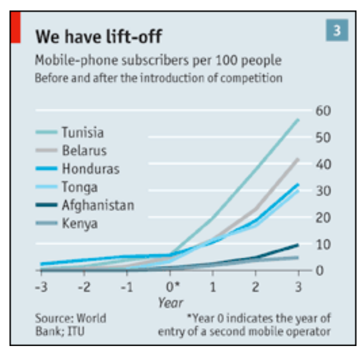
But it is not just the clients that benefit from the suite – Syniverse, likewise, also benefits. Being able to put all its services together allow Syniverse to have specialists perform work in more than one area, allowing for new methods of cost cutting. This was most evident when **Syniverse bought out VeriSign's messaging business to Syniverse in a $175-million cash deal. The strength of Syniverse's balance sheet created in thanks** to its competitive advantages had made the deal possible and the deal will help Syniverse scale its global business.[3]

<u>**Syniverse is extremely well-positioned to take advantage of the global explosion of wireless**</u>

One fact must be reiterated: Syniverse provides its services to more than 650 operators in over 140 countries. The following graphs give an idea of the explosion in wireless technology worldwide.







And Syniverse is right in the middle of taking advantage of that explosion. On November 16th, 2009, Syniverse had announced that it achieved 100 mobile operator customers in the Asia Pacific region. These customers are located in more than 25 countries in the region and represent approximately 900 mobile subscribers.[4] The

[3] Telephony Online, "Syniverse CEO: VeriSign acquisition all about scale"
[4] RTT News, "Syniverse Provides Array of Services to 100 Operators in Asia Pacific"

region has 2 billion total subscribers, so this milestone also signifies Syniverse's dominating market share. **Syniverse's customers are many of the region's major** providers, including four in Hong Kong, three in Japan, and all three in South Korea.

In a different part of the world, in this same month, VIVA, the Kuwaiti operator, has announced that Syniverse's services will be employed. Among the products chosen by VIVA are Data Clearing House for GSM, Financial Clearing House for GSM, Roaming Management Services, Syniverse DataNet NRTRDE solution, SS7 Signaling Transport, SCCP Gateway, and MMS Interworking Gateway. VIVA is the 12th mobile operator in the Middle East to choose Syniverse during the past two years.

The growth in telecommunications technology increase opportunities for Syniverse

The global wireless industry relies on an extensive and complex set of communication standards, technical protocols, network interfaces, and systems that must successfully communicate with one another in order to provide voice and data services to subscribers in their local markets and when roaming. The proliferation of these standards has resulted in technological incompatibilities, which are increasingly difficult to manage as new wireless technologies and services are introduced and deployed.

These realities are Syniverse's opportunities. The mobile phone is no longer used simply for calls. SMS, MMS, and MIM are of course some of the new ways of communication. But another new development has been the VoIP technology spearheaded by Internet services such as Skype. The advantage of these services is the ability to make calls worldwide including video conferencing at a much lower price. This development adds a new type of standard for which phone carriers must adjust their network to and brings new demand to Syniverse's services.

Also, there is a time lag between different countries in terms of technology. While the United States has moved on to the 3G networks, there are still areas domestically that are still 2G. Globally, many areas have not moved on to the 3G network yet, but there is already talks of countries moving towards the 4G standard. Syniverse is able to create compatibility between these networks and allow wireless companies to focus on developing the generation networks.

Risks

- Future consolidation among wireless companies could cause Syniverse to lose transaction volume and reduce prices
- Syniverse depends on a small number of customers for a significant portion of revenues (10 largest customers represented approximately 55.8% of revenues in aggregate)
- Syniverse may be unable to adapt to rapid technological change in the telecommunications industry
- Expansion into international markets is subject to uncertainties

Appendix A: Value Added Research (VAR)

Italics are my thoughts.

Anonymous lawyer in US Telecommunications industry
Deals with trademark, copyright issues

- Internationally, trademarks are very difficult to protect. Many fees are involved including legal fees and it is necessary to register trademarks in majority of countries. Each registration incurs additional fees.
  - This leads to many companies having presence in only a few countries at most.

There are significant barriers to entry for one company to dominate the entire globe and many players will invariably appear. This provides demand for Syniverse's services

Randall Rager, Verizon Sales Engineer
Works primarily in wired telecommunications

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- Verizon is one of the largest carriers in hundreds of countries.
- Networks being standardized makes it easier to maintain
- With regards to companies outsourcing services, believes it's closer to a combination. While companies may prefer to do everything in-house, if it's cheaper to outsource, there's no choice.

Even if companies may prefer to perform services in-house, Syniverse will be able to capture a large portion of demand if it can provide high quality services cheaper than companies can do it themselves

Tom Brooks, Deloitte Technology Consultant.
Previously worked at BearingPoint and Florida state government, with over 30 years of experience in the industry.

- Seen lots of change in telecommunications industry, believes right now is next phase of change
- Companies can overcome economies of scale and entry barriers by riding on backbones of patents and using copyrights to develop niche
- In the United States, government will also be there to regulate companies deemed too large
- In developing countries, technology is moving towards wireless
  - They are adopting newer technology quickly.
  - Lack existing large customer base
  - Advantage of not being caught in old infrastructure, unlike US

The US will not be dominated by a single wireless carrier if only to prevent antitrust. In developing countries, there is huge growth in wireless and opportunities for many companies to succeed because of the lack of a large incumbent telecommunications company.

Kunal Doshi, International student from India

- More and more individuals are using cell phones in India and next opportunity lies in rural areas
- Use of email on cell phones is prevalent in businessmen. SMS is preferred by younger generation. Older generation still prefers to directly call.
- Little brand loyalty – consumers flock towards cheapest plan. Since there is no "family plan", family members usually end up with different phone carriers.

India is one of the largest areas of growth for telecommunications. Because of the inherent environment in place with little carrier loyalty, it will be difficult for one carrier to dominate and competition will keep everyone in check. This also will work to preserve Syniverse's niche in the global market.

Betsy Chapman, Telephia-Nielsen Mobile

As a product manager, my job is to ensure the research we provide meets the business need of our customers, and that the roadmap for product enhancements is aligned with client needs.

Domestically, as operators continue to expand their networks, consumers will be able to use their devices for more and more services, which will bring more and more new competitors into the market. Internationally, in emerging markets like India, China and Brazil, traditional broadband services will be leapfrogged by mobile broadband.

From a service provider perspective, the acquisition of Alltel by Verizon and Nextel by Sprint and Cingular by AT&T indicates that the market is moving towards consolidation. However new technologies like WiMax and VOIP are bringing new competitors like Clearwire and other traditional cable providers, plus Skype into the market. From a services standpoint, the growth of iphones and other smartphones is bringing other new companies into the market like Application Developers, Mobile advertisers etc.

Generally firms are moving towards outsourcing repeatable and process-based activities like call centers and other related services.

The trend of consolidation certainly cannot be ignored, but at the same time, new competitors are rising which will create new demand to replace demand lost. The proliferation of smartphones such as the iPhone with their capabilities for many value-added services is a glowing business opportunity.

Jeffry Abramson, AT&T R&D Department

I work in the R&D branch where I am responsible for designing, building and maintaining a variety of systems used to keep the calls flowing.

Domestically, there have been a number of trends including:

1) An un-doing of the 1984 court ordered breakup of AT&T.
2) A de-emphasis on POTS (Plain Old Telephone Service) and an emphasis on providing wireless and broadband access as well as content itself (witness AT&T's U-Verse and Verizon's FiOS offerings).

There will always be niche firms in outlying areas but, in general, the trend has been more towards consolidation. As with the traditional landline portion of the business, there is AT&T, Verizon and everyone else.

A lot of the outsourcing is the same as the rest of the corporate world. Things that are not core to the business (Human Resources, Benefits, running the cafeterias) generally have been the first to have been outsourced. Things like desktop PC support and PC network maintenance have also been outsourced, which I personally think is a mistake. I think the core part of the business which is actually running and maintaining the communications backbones will remain internal.

Phone service provides will seek to create any competitive advantage possible. Part of this will include any possible cost cutting methods through usage of services like Syniverse's.

Mike Coffey, Telecom Infrastructure Start-up
Leads a program management organization, building Distributed Antenna Systems and sell service to major wireless carriers to augment wireless coverage

In general, the industry has been responsible for some of the most significant cultural and economic shifts in the last century. The advent of inexpensive long-haul voice and data communications has moved jobs around the world and accelerated the speed of business. Wireless services have enabled businesses and individuals instant access to each other and all of the information that's available on the internet. I expect continued growth in the industry as it keeps up with customer demand and as new applications hit the market.

Some areas are trending towards consolidation, for example wireline and wireless carriers that are merging and consolidating due to the massive capital investment required to build networks. Meanwhile, new businesses are being created, such as applications developers/providers, and tower companies or network service companies that enable carriers to share the cost of infrastructure. As the business matures, I expect consolidation of the maturing elements of the industry and the spawning of a wide variety of new businesses that eventually shake out the weak competitors.

Outsourcing is becoming more popular for non-strategic elements of the business, with the intent being to achieve a lower overall cost structure without giving up long-term strategic positioning. For example, my former employer, Sprint Nextel, recently announced an outsourcing agreement with Ericsson to provide network engineering and operations services. I would imagine that Sprint intends to differentiate on products and services, and is leveraging the Ericsson relationship to reduce network cost. Incidentally, this trend has already started to unfold in Europe, where Ericsson and others have large service related contracts with multiple carriers, and within the US in the tower industry. Few carriers own their own towers any longer, since it's not truly a strategic asset, and the cost of a shared tower is lower than owning your own infrastructure.

This is another voice with the belief that with lost demand will create new demand. Syniverse may lose revenue when mergers like Verizon-Alltel occur, but the emergence of new technologies will support Syniverse's growth rate in the future.

Appendix B: Financial Ratios

VALUATION RATIOS

	Company	Industry	Sector	S&P 500
P/E Ratio (TTM)	16.16	8.92	13.90	116.00
Price to Sales (TTM)	2.38	0.93	2.24	2.01

GROWTH RATES

	Company	Industry	Sector	S&P 500
Sales (MRQ) vs Qtr. 1 Yr. Ago	-14.95	-2.46	9.98	-4.11
Sales (TTM) vs TTM 1 Yr. Ago	-3.51	-0.54	3.22	-5.14
Sales - 5 Yr. Growth Rate	13.28	10.43	15.08	15.60

FINANCIAL STRENGTH

	Company	Industry	Sector	S&P 500
Quick Ratio (MRQ)	6.65	0.70	0.62	0.86
Current Ratio (MRQ)	6.65	0.76	0.65	1.02
Interest Coverage (TTM)	3.69	0.02	0.01	26.84

PROFITABILITY RATIOS

	Company	Industry	Sector	S&P 500
Gross Margin (TTM)	64.57	39.54	68.64	27.37
Gross Margin - 5 Yr. Avg.	62.79	75.88	81.09	27.04
EBITD Margin (TTM)	41.07	--	--	--
EBITD - 5 Yr. Avg	36.76	42.83	55.75	15.66
Operating Margin (TTM)	28.96	12.35	30.14	--
Operating Margin - 5 Yr. Avg.	24.77	21.21	35.65	20.01

MANAGEMENT EFFECTIVENESS

	Company	Industry	Sector	S&P 500
Return on Assets (TTM)	5.51	3.55	13.53	3.70
Return on Assets - 5 Yr. Avg.	5.57	7.52	16.18	5.34
Return on Investment (TTM)	5.79	4.55	21.79	5.06
Return on Investment - 5 Yr. Avg.	6.01	9.68	24.50	6.88