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T-Mobile USA’s Push for Subscriber Growth May Lead to Turnover

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By Roger Cheng
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NEW YORK (Dow Jones)--T-Mobile USA's apparent pursuit of customers with weaker credit histories reflects the pressures that the smallest nationwide wireless player faces in the current environment and portends rough times ahead.

T-Mobile - a unit of Deutsche Telekom AG (DT) - declined to comment on any change in credit standards, but industry observers sense the change, noting the aggressive push of its pre-paid service and recent data that suggest the company has loosened its credit standards.

Critics say that by adding lesser-quality customers, T-Mobile's strategy could lead to a spike in customer defections starting in the second half. They point to similar efforts by Sprint Nextel Corp.(S) years ago, which contributed to problems still affecting the company today.

"The net addition quality has really deteriorated," said Patrick Comack, an analyst at Zachary Investment Research. "This is a company that's going to have a couple of turbulent quarters."

T-Mobile, in the midst of losing customers in the first two months of the fourth quarter that wrapped up at the end of December, lowered its standards for contract customers to turn things around in the final month, according to an industry analyst. The carrier ended the fourth quarter with 621,000 net new customers - a 35% decline from a year ago. It reports first-quarter numbers on May 7.

Others, however, point to T-Mobile more visibly touting its Flex Pay program, which is its own version of a pre-paid service, as a contributor.

"With the Flex Pay program, they're blending their credit scores down," said Andy Zeinfeld, chief executive of privately held Simplexity LLC, which runs online mobile phone retailer Wirefly.com.

While Zeinfeld said he did see indications of less stringent credit standards, he said it wasn't a material change. Karen Page, a telecom analyst at marketing firm Compete Inc., said she hadn't seen any changes either.

The credit check is an integral tool that carriers use to keep out deadbeat cellphone users. A lower rating suggests the person is likely to stop paying his bills, and will more often break his contract and leave unpaid cellphone bills. The first signs of trouble typically show up six months after standards drop.

Changing Attitude

The stigma around poor credit is changing as more people lose their jobs and see their ratings fall. Some believe the falling standard will allow T-Mobile to reach younger consumers who don't necessarily have a poor history of credit, but rather no history at all.

T-Mobile is vulnerable to competition. AT&T Inc. (T) and Verizon Wireless monopolize high-end subscribers, while pre-paid carriers nab consumers on the low end, squeezing the middle that T-Mobile occupies.

AT&T has the highest credit standards in the industry, according to the industry analyst. Sprint, having lost millions of customers with bad credit, has raised its standards and is No. 2, followed by Verizon

Wireless, a unit of Verizon Communications Inc. (VZ) and Vodafone Group PLC (VOD). T-Mobile lags behind the others.

Sprint Redux

Sprint faced the same dilemma following its merger with Nextel in 2006. To mask larger fundamental problems, it loosened its own standards to keep up its growth. By the time it began to raise its credit requirements again, the exodus of customers began.

To be sure, T-Mobile doesn't have the myriad problems Sprint did. But the consequences remain the same.

T-Mobile faces pressure to maintain growth. Pre-paid players like MetroPCS Communications Inc. (PCS) have performed well with their cheaper plans, although they endure higher rate of turnover.

Some believe T-Mobile's move is designed to attract younger customers with little credit history. The company has long pushed itself as a youth brand.

"It may be indicative of the types of customers T-Mobile finds itself chasing," said Rory Altman, a director at consulting firm Altman Vilandrie & Co.

He added there were ways of lowering the credit standards in specific areas such as geography or by demographic without hurting the overall metrics.

"If companies are very meticulous about the default of their customers by market or by price level, they may uncover areas where they can lower scores without increasing their churn very much at all," Altman said.