

Specialty Telecommunications Wireless Infrastructure Service Providers

A Middle Market Investment and M&A Update- November 2014

By: Steve Mooney

Recent Trends & Events

The pace of upgrade and construction of the wireless networks of the major MNO's ("Mobile Network Operators") was choppy in 2014. The 2nd quarter slowdown announced by AT&T and the historically bad winter weather presented challenges to the industry. However, the ever-increasing demands of data traffic and the urgency to achieve 4GLTE network performance across their entire footprints remain top priority for all four participants. This is particularly evident as both the primary challengers, (T Mobile and Sprint); continue to press their marketing efforts to take smartphone market share away from the leaders (AT&T and Verizon).

Market Saturation? Many important industry analysts are waving a cautionary flag concerning MNO capital expenditures beyond 2014. Driven by a saturation of mobile devices in the developed world and the potential for a price war among the carriers to gain market share (resulting in declining ARPU), industry analysts (such as the Dell' Oro Group) project as much a 3% decline in overall cap ex worldwide among the MNO's. While we understand the logic of this assessment, we believe it will have more impact on equipment purchases (particularly macrocell gear) and toward the recession prone and the saturated mobile phone markets in Europe. We believe the investments in 4G densification and the performance upgrades (including voLTE) will keep spending with US infrastructure service providers on a growth trajectory through 2016.

Emerging Capital Resource Issues. During 2014, AT&T announced its \$48.5 billion acquisition of DirectTV and Verizon's executed a \$100+ billion buy out of the 45% of Verizon Wireless owned by Vodaphone. These deals will undoubtedly lead to capital allocation issues. We anticipate creative financing plans to be implemented to overcome these capital constraints. One notion under consideration by the MNO's is the continued sale and leaseback of their tower assets to the existing Tower Cos. or special purpose vehicles set up by the MNO's. There is an emerging recognition that there is no real strategic benefit to owning towers. Furthermore, corporate structures such as REIT's can be utilized to take full tax advantage of these "real estate-like" assets that would optimize the cost of capital. In October 2013, AT&T entered into a \$4.5 billion sale-leaseback deal with Crown Castle and we expect additional multi-billion sale-leaseback and other financing transactions in the coming years.

Densification versus Coverage. Overall coverage is still a top priority for wireless carriers throughout the U.S. The signal propagation for LTE (i.e. broadband data) is inherently shorter in distance than classic 3G/2G (narrowband voice) thus leading to an ever-increasing requirement for smaller and denser cells within the established coverage area. This means more antennas and radios on cell towers, and buildings and distributed antenna systems (see discussion below) throughout existing coverage areas.

So despite the apparent perceived maturity and ubiquity of mobile networks and market saturation and the competitive pressure on ARPU, we expect the investment and workload for wireless infrastructure services providers to substantially increase for the next two to four years. Accordingly, we reiterate our projection that US wireless infrastructure cap ex will top \$30 billion and that service provider share of that will top \$7 billion for 2015.

Competitive Differentiators. We reiterate the driving elements for success among the infrastructure service providers:

- Ability to “Self-Perform.”-- Driven by delays and cost overruns and a lack of accountability, the MNO’s are demanding their vendors bring the management, technical and operational personnel on staff. Carriers now want direct relationships with their engineering and construction vendors and have visibility into the quality of their staff, operational processes and procedures. A number of regional contractors are taking business from the major E&C contractors as a result of this trend.
- Ability to Hire Talent and Maintain Crews. There is a severe shortage of trained and certified, RF engineers and technicians (i.e. “tower climbers”) as well as experienced crew managers. The discipline applied and investments made on training and retention programs of key staff and gray collar technical talent will drive significant long-term value among these companies.
- Ability to Scale and Manage Regionally. While the wireless carriers are focused on local management and control, those vendors who can expand within region and out-of-region as customers seek greater coverage will likely see significant revenue growth opportunities. We expect the more successful and skilled wireless infrastructure providers to be acquisitive of the smaller sub-scale players who may have good crews, or a particular market presence that might be of value.
- Supply Chain Management. The MNO’s are increasingly reliant on their infrastructure service providers to manage the entire eco-system of equipment suppliers and subcontractors. Those vendors that have implemented automated project management, e-bonding, and just-in-time inventory systems and practices are going to win more business and be of more value to larger industry players.
- Systems, Training and Safety. In addition to back office infrastructure and integration into customer systems, sophisticated training and safety programs are absolutely essential. Tower climbing is a very dangerous business; a culture of ‘safety first’ is the highest priority for the companies as well as the customers and tower site owners.

Microcell/DAS Integration. As mentioned earlier the drive toward heterogeneous networks or “Hetnet” (i.e. integrated microcell and macrocell technology) networks continues as the capacity demands of LTE- enabled mobile devices continue to challenge the carriers. Distributed Antenna Systems (DAS) are used in locations where a dense and often event driven usage would overwhelm the traditional cellular (macro or small cell) networks of the carriers. This is exacerbated by the need for data driven applications running over LTE in relatively small locations. A dramatic example of these situations is the Arizona University stadium as the venue for the upcoming Super Bowl 2015. The deployment of DAS in this venue and ones like it, represent great technical challenges given the expected smartphone data traffic and the potential for signal interference and capacity constraints. RCR Wireless indicates its professional contacts in the DAS industry estimate that less than 15% of

locations where DAS solutions should be provided (e.g. office parks, commercial buildings, campuses, shopping centers as well as stadium and entertainment venues) have been implemented in the US.

Those contractors that continue to successfully build capable engineers and deployment crews in DAS technology will be increasing more valuable and enable the more traditional E&C firms to pursue greater market share. The ability to program manage these complex implementations, as well as ongoing maintenance will be large drivers of future contract revenue. In May 2012, the largest DAS pure play company- NextG Networks, was acquired by Crown Castle for \$1.0 billion. ExteNet Systems is another large player with thousands of DAS nodes. It has major private equity backing and a \$128 million investment from tower company, SBA Communications. The tower providers view DAS as a natural extension and potential threat to their core macro cell management businesses.

AT&T Network 2.0 Turf Vendor strategies. AT&T Mobility's wireless infrastructure spending gets more attention than other competitors because it tends to issue large territorial or "turf" contracts with six regions (plus Hawaii and Alaska). In the past, AT&T tended to have a single award to a large vendor often a large diversified contractor (e.g. Bechtel, MasTec, GD and Black & Veatch) who would then manage a portfolio of small regional and local subcontractors. Beginning in 2011, AT&T began to split the work with a "minority" vendor within each territory. This "dual vendor" strategy was most likely in response to a desire for more accountability and to inject competition among its prime contractors. New minority vendor entrants include Dynis, Velocitel, Goodman and Jacobs. Furthermore, AT&T implemented its Tower Crew Augmentation Program ("TCAP") requiring vendors to meet certain quality standards in crew quality, training and availability. This program has stirred a trend toward greater consolidation as turf vendors to increase the number and quality of crews (and a cottage industry for training and certification) in order to meet the AT&T requirements.

As mentioned earlier, AT&T's announced its acquisition of Direct TV and used the occasion to announce a "strategic pause" in its plans for broadband wireless deployment (i.e. satellite access) resulting in a partial moratorium on new wireless deployment. This had a major impact on the workload and revenue on all its turf vendors and subcontractors during he year. In fact, MasTec announced a significant shortfall in its wireless services unit in the second quarter of 2014. We believe that this event was only temporary (and more an excuse on AT&T's part to reorganize its 4G deployment effort under the TCAP program). We understand that AT&T's deployments will be back on track in 2015. We will continue to monitor the situation.

The Sprint Challenge After the recent injection of capital from Softbank and consolidation with Clearwire, Sprint is moving aggressively to upgrade its networks to 4G LTE. This is particularly challenging given their legacy PCS (1900 Mhz bands), Clearwire (2.5 Ghz) and the decommissioning of the Nextel networks. Since Sprint is sub-scale (relative to ATT and VZ) it has historically relied on its OEM, Ericsson to manage its network builds. With its latest program ("Spark") the MNO is contracting more directly with infrastructure service providers. There is significant new work to be won by the middle market contractors with Sprint, but they need to be careful that the carrier will be able to sustain their development effort or be constrained by the technical complexity and capital costs associated with their build-outs.

T-Mobile-- the Disruptor. T-Mobile is aggressively going after market share with disruptive smartphone pricing program. In anticipation of a large increase in subscribers, T Mo has been aggressively increasing coverage and the performance of its 4G LTE network while selectively de-commissioning its 2G networks. It has been reported that they are also moving to manage vendors at a local level.

Industry Consolidation

As noted in our previous report (January 2014), the consolidation among wireless infrastructure service providers has been accelerating. In 2014, the larger turf vendors and OEMs acquired certain of the high profile regional service providers. SAC Wireless was purchased by Nokia Siemens Networks (service division) for an undisclosed amount. SAC was on a major a major growth path in the Midwest and had recently won turf contracts with AT&T and taking business from Nsoro (MasTec) with Sprint and T-Mobile.

Jacobs Engineering entered the wireless service provider market as an AT&T turf vendor in the northeast (NJ & PA) in 2013 and acquired Chicago based FMHC in early 2014. FMHC is a full service technical services firm that is a subcontractor to the established to Ericsson, Bechtel and Black & Veatch. With two major regional presences, Jacob represents a major new entrant to the market to compete against the established turf vendors.

In order to extend its reach to the mid Atlantic and its turfing relationship with AT&T, (and allegedly to meet the demands of TCAP) MasTec acquired Dynis a Maryland based providing services. While the terms of the deal were not disclosed it was reported that Dynis had \$117 million in annual revenue and the estimated purchase price was in the \$100 million range.

In August, Bluestream Professional Services affirmed its commitment to growing its DAS business by acquiring the services unit of California-based Tempest Telecom.

Last month, MasTec announced its acquisition of WesTower Communications in a \$199 million all cash transaction. WesTower was owned by a Canadian investment conglomerate-EIC and is a fast growing tower services company with operations with 16 regional offices and 1,600 employees. MasTec disclosed that WesTower was on track to deliver \$450 million in revenue for 2014.

Recent Transactions (\$ Millions)

Closed Date	Target	Acquirer	Enterprise Value	LTM Revenue	LTM EBITDA	EV/ Revenue	EV/ EBITDA
Oct 2014	WesTower Comms	MasTec	\$199.0	\$375.0e	NA	.53X	NA
Aug. 2014	Tempest Telecom	Bluestream	NA	NA	NA	NA	NA
Apr 2014	FMHC	Jacobs Engineering	NA	NA	NA	NA	NA
Mar 2014	SAC Wireless	Nokia Siemens	NA	\$65	\$15	NA	NA
Dec 2013	Netricom - Canada	Telecon Group	NA	NA	NA	NA	NA
Nov 2013	Dynis	MasTec	\$100.0e	\$117.0	NA	.85X	NA
Aug 2013	Multiband	Goodman Networks	\$116.0	\$290.0	\$11.2	.40X	10.4X
July 2013	MUTI	Saber Tech	NA	NA	NA	NA	NA
July 2013	Doty Moore Tower	Velocitel	NA	NA	NA	NA	NA
June 2013	Compass	Jacobs Engineering	NA	NA	NA	NA	NA
Apr 2013	Data Cell	MasTec	NA	\$30.0e	NA	NA	NA
Feb 2013	Custom Solutions (a)	Goodman Networks	\$35.0	\$45.0	NA	.77 X	NA
Nov 2012	Quanta (Telecom)	Dycom	\$275.0	\$550.0	NA	.5X	NA
Nov 2012	DMN (UK)	Gores Group	NA	NA	NA	NA	NA
Oct 2011	Utilimap	Quanta Services	\$35.0	NA	NA	NA	NA
May 2011	EC Source	MasTec	\$128.0	NA	NA	NA	NA
June 2011	Optima Networks	MasTec	\$7.3	\$11	NA	.67X	NA
Apr 2011	Cam Comm	MasTec	\$10.0	\$16.0	NA	.63X	NA

Source: Chessiecap research, 451 M&A Knowledgebase and Merger Stat

NA- Not available or undisclosed; (a) Includes a \$17 million in earn out payments

Public Company Comparable Value Metrics

Telecom & Power Infrastructure Contractors

millions except per share

	Symbol	As of 19/30/14	Shares O/S	Enterprise Value	Market Cap	Net (Cash) Debt	TTM Revenue	TTM EBITDA	EBITDA Margin	EV/ EBITDA	EV/ Rev	
Mastec	MTZ	\$ 29.57	81.8	\$ 3,430.8	\$ 2,418.8	\$ 1,012.0	\$ 4,501.0	\$ 642.0	14.3%	5.3	0.8	
Dycom	DY	30.10	33.8	1,448.4	1,017.4	431.0	1,810.0	176.6	9.8%	8.2	0.8	
Jacobs	JEC	47.35	133.1	6,442.3	6,302.3	140.0	12,620.0	707.0	5.6%	9.1	0.5	
Pike	PIKE	11.87	31.9	574.7	378.7	196.0	810.0	69.3	8.6%	8.3	0.7	
MYR Group	MYRG	23.69	21.3	450.6	504.6	(54.0)	932.0	86.0	9.2%	5.2	0.5	
Unitek	UNTK	0.11	19.2	190.6	2.1	188.5	447.0	31.2	7.0%	6.1	0.4	
Argan	AGX	32.30	14.2	459.0	458.7	0.3	276.1	61.2	22.2%	7.5	1.7	
Emcor	EME	39.07	67.1	2,620.7	2,621.6	(0.9)	6,540.0	338.5	5.2%	7.7	0.4	
WPCS Int't	WPCS	0.78	13.9	16.9	10.8	6.1	23.7	(1.3)	-5.5%	nm	0.7	
Integrated Elec	IESC	8.01	17.8	142.5	142.6	(0.1)	500.3	9.0	1.8%	15.8	0.3	
										Hi	15.8	1.7
										Median	7.7	0.5
										Mean	8.5	0.6
										Lo	5.2	0.3

M&A Outlook

We see significant consolidation activity continuing in the telecommunications infrastructure services segment in 2015 and 2016. The key drivers will continue to be the ability to self-perform and maintain direct contractual relationships with wireless carriers and tower companies. The recent acquisitions of SAC Wireless (Nokia Siemens), Dynis (MasTec) and FHMC (Jacobs Engineering) confirm this trend. We noted these transactions have occurred at what appears to be record valuations for the industry. We reiterate our view that other deals will follow as the majors try to augment their capabilities and gain market share.

For the small service provider, the ability to maintain skilled crew managers, engineers and skilled certified technicians able to keep up with evolving wireless technologies will continue to be of significant strategic value. We expect continuing interest in those companies that have experience and expertise in DAS and other small cell technologies. Obviously, meeting the requirements of AT&T's TCAP program will be essential.

While each situation will be unique, we think premiums for high revenue growth rates and significant prime contract backlog will be at historic highs. For these companies, we see enterprise valuation ranges in the high end of the .5 to .8 times revenue range or 6 to 10 times EBITDA, depending on the circumstances.

About the Author

Mr. Mooney has been in investment banking and corporate finance in the telecommunications and IT sectors for over 25 years. In addition to his focus on telecommunications infrastructure, he specializes in emerging networking and cloud communications services as well as government contractors and business process outsourcing firms. Steve was a senior executive in corporate development, treasury, and finance for Verizon, MCI Communications, WorldCom and Affiliated Computer Services. In addition to strategy development, he led the negotiations of multiple investment, acquisition and divestiture transactions. He has also served as a principal for the MCI WorldCom Venture Fund, investing in advanced communications infrastructure and Internet technology companies. Mr. Mooney played an instrumental corporate finance role in restructuring MCI following WorldCom's bankruptcy and subsequent sale to Verizon. Mr. Mooney has served on the boards of numerous venture-backed companies and currently serves on the board of General Communications, Inc. (NASDAQ:GNCMA). He earned a BA from Mt. St. Mary's University. Contact: steve@chessiecap.com or 301.564.0923/ mob. 301.395.8612

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