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Avaya – Nortel Deal ??

Avaya announced its intention to purchase the assets of Nortel's Enterprise Solutions business. The number thrown out to start off the bidding is \$475 million. The announcement is considered by most of the analysts and bloggers to be but a stalking horse – think of it as the opening bid in an auction scheduled to last 45 days. Bullet points to remember: 1) Avaya was “acquired” by Silver Lake/TPG about two years ago in a leveraged buyout for \$8.2B; 2) this deal would essentially double the size of Avaya's installed base and channel partner network for a sum that is a small fraction of the \$8.2B; 3) Avaya, like everyone else in the PBX-UC industry, needs to bulk up against the onslaught of Cisco and the coming days of Microsoft and yes, even Google. We asked our guru Brent Kelly for his thoughts. Here is what EBK had to say....

The Brave New World of NorVaya

Brent Kelly, bkelly@wainhouse.com

The same day we celebrated the 40th anniversary of man landing on the moon, Avaya announced that it had agreed to purchase Nortel Network's enterprise solutions (ES) business for US \$475M. While not as colossal as a moon landing, this announcement is certainly earth shaking for the enterprise communications market.

Although Avaya has stated it wishes to acquire Nortel's ES business, the stalking horse process means that other companies can bid a higher amount. The process will begin when Nortel takes Avaya's bid to the bankruptcy court, which will take about two weeks. Then, other companies have 45 days in which to bid for Nortel's assets. The Nortel executive who spoke with Wainhouse Research indicated that he expected vigorous bidding activity during the 45 day process. At the end of the bidding process, the judge will look at all of the bids, and determine which one provides the Nortel creditors with the highest total value. Then, the regulatory approvals must be obtained in countries throughout the world. Nortel's management expects this process may take several months. So, Avaya may not be the ultimate high bidder, and we really won't know the outcome of the regulatory approvals till late 2009.



Nortel's enterprise solutions business unit includes Nortel's PBXs, enterprise mobility solutions, contact center, unified messaging, and its data (router/switch) business. It also includes Nortel's very loyal channel partners, its surprisingly loyal customers, and its government systems business unit (Nortel has high penetration in the US government telephony market).

As the table below shows, there is significant overlap in the two companies' product portfolios. Should the acquisition proceed, there must eventually be considerable product rationalization.

Clearly there are pros and cons for Avaya in this bid to take over Nortel. Avaya will clearly be number one in worldwide telephony revenue share with approximately 25% of the market (Cisco follows at 15.3%). The company will try to leverage Nortel's channel and customer base by doing everything it possibly can to keep both channel partners and end users companies within the “NorVaya” family.

Another potential bidder is Siemens Enterprise Communications, now 51% owned by Gores Group. Siemens is strong outside of North America and is the number 3 or 4 player worldwide. Gaining Nortel's customer base in North America must surely make Siemens' mouth water.

Yet, one must ask if either Avaya or Siemens merging with Nortel will ultimately make any difference in the long run. Cisco is still coming on strong. Whereas before the announcement, only Nortel customers wondered what would happen, now Avaya customers must begin to wonder. Avaya has held its own against Cisco in recent quarters, but Cisco is still slowly but surely gaining worldwide market share. In addition, Microsoft OCS 2007 Release 3 will be out in 2010, with the features that will make it a real telephony contender. Can an Avaya/Nortel or Siemens/Nortel merger withstand these two giants?

Avaya has been snuggling up to HP and Juniper networks of late when recommending network data solutions. It is not clear how ownership of Nortel's data assets (which came from Bay Networks), will impact these relationships.

Compounding the issue is the speculation that Avaya's owner, Silver Lake, is also in discussions with Tandberg about acquiring this video company. Would combining the assets of Avaya, Nortel, and Tandberg make a company that could compete among the three unified communications titans: Microsoft, Cisco, and IBM? Time will tell. The stalking horse auction must first run its course, and then we will see who will ultimately own Nortel.

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Item	Nortel	Avaya
PBX	CS1000	Communication Manager
Unified Messaging	Call Pilot	Modular Messaging
Call Center Software	Contact center	Contact center
Vendor Neutral Interface Environment	ACE	Aura
UC Environment	MCS 5100	one-X Desktop
Mobility Products	Mobile Communication 3100	one-X Mobile
Data Products	Routers/Switches	N/A
Worldwide Revenue Market Share	9.3%	15.5%

News in Brief

- Moscow-based SPIRIT DSP, a provider of carrier-grade voice and video software engines, announced support for H.264 SVC (scalable video coding).
- Verizon Business will provide the U.S. Department of Health and Human Services with a comprehensive set of voice, data, collaboration, and professional services under a new agreement through the Washington Interagency Telecommunications System contract. Under the agreement, valued at as much as \$245 million if all options are exercised, Verizon Business will provide HHS with voice and data services, dedicated voice mail systems, and audio, video, and web conferencing. Verizon Business professional services experts will assist the department with conference room design and systems setup.
- My comments in the last WR Bulletin (Volume 10 #15) in the section discussing Tandberg's Q2 results were off base. The company never said that E2 shipments during Q1 were zero. They did say they shipped a bulk quantity to one or more service provider customers in Q1, which was not the case in Q2.

WR Summit Boston 2009 – This week: In person or by WebCast

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What do scalable video coding, virtual meetings, unified communications, managed services, and IP video networks have in common? They are all the focus of presentations, panel discussions, and demonstrations at the Wainhouse Research Summit, July 28-29 at the Royal Sonesta in Cambridge, MA. Come meet with these presenters and scores of your colleagues.



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