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EBay to Acquire Internet Phone Leader; Auction Giant Sees Potential for Growth in Skype, Which Has 54 Million Customers

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Online auction giant eBay Inc. announced a deal yesterday to become one of the world's largest telecommunications companies, buying Internet phone-service leader Skype Technologies SA.

Although Luxembourg-based Skype is relatively unknown in the United States, it has amassed 54 million global customers in less than three years by offering free calls between those who use its software.

EBay became a commerce powerhouse by hosting everything from auctions of grandma's collectibles to retail sales of new furniture and electronics, but its growth has stagnated, and analysts said the Skype deal is an effort to inject new life. The company said it sees Skype's technology as a vital tool for letting buyers and sellers talk to each other, exchange information and close sales more rapidly.

The deal would vault eBay ahead of other technology titans such as Microsoft Corp., Google Inc. and Yahoo Inc. in developing services to make voice calling an additional feature of using personal computers, akin to e-mail or instant messaging. EBay said it would pay \$2.6 billion in cash and stock for Skype, along with future payments that could total an additional \$1.5 billion.

Founded by business partners who developed the Kazaa file-sharing service for online music and videos, Skype quickly dwarfed other Internet-based phone companies such as Vonage Holdings Corp., which recently celebrated its 1 millionth customer.

Large cable and telephone firms, such as AT&T Corp., Verizon Communications Inc. and Comcast Corp., also are starting to offer online phone service. They typically charge \$20 to \$35 per month for unlimited calling in the United States, including free add-ons such as voice mail and call forwarding, and consumers use regular telephone handsets attached to special computer modems that handle the voice calls.

Skype's service and technology differ dramatically from those offerings. Making a Skype call is more like sending an instant message from a personal computer; all that is required is an Internet connection, a microphone for talking, and speakers or a headset for listening.

Skype charges nothing for its software but makes money by charging small fees for making calls to non-Skype users and for talking to people on regular phone networks. Voice mail also is extra.

"By combining the two leading e-commerce franchises, eBay and [online payment service] PayPal, with the leader in Internet voice communications, we will create an extraordinarily powerful environment for business on the Net," eBay chief executive Margaret C. Whitman said in a statement.

In addition to boosting sales, which would earn eBay more commissions, company officials envision Skype accelerating types of electronic commerce that depend heavily on voice conversation, such as personal services, real estate and new cars.

Skype would continue to operate as a separate business, with founders Niklas Zennstrom of Sweden and Janus Friis of Denmark remaining at the helm. The deal would make rich men of the pair, who had been considered outlaws by the U.S. entertainment industry for developing Kazaa, which they sold in 2002.

Zennstrom remains a target of some U.S. litigation accusing Kazaa of facilitating piracy of copyrighted music, videos and software. Skype makes use of the same, underlying "peer-to-peer" technology as Kazaa but carries none of the legal issues.

In an interview, Whitman said Internet telephone service using downloadable software is the future. She cited statistics indicating that by 2009, an estimated 1.5 trillion minutes of voice calls will be Internet-based.

She added that Skype is well ahead of its competition for such systems and already is partnering with such companies as Motorola Inc. for handsets that will work with Skype.

"But we would not have done this if that is all we could see," she said, insisting that integrating Skype, eBay auctions and PayPal would yield significant new revenue for eBay's current businesses.

Closely held Skype had sales of about \$7 million last year and is projected to bring in \$200 million next year, according to the companies, causing some analysts to question the price eBay paid.

"It's a pretty big number and a pretty big gamble," said Carmi Levy, senior research analyst with Info-Tech Research Group of London, Ontario.

But Levy said that eBay's growth had become stagnant and that it needed to find a way to make its auctions more dynamic.

Zennstrom said in a statement that his vision was always "to build the world's largest communications business and revolutionize the ease with which people can communicate through the Internet. We can't think of a better platform . . . than with eBay and PayPal."

Analysts said the deal would accelerate the evolution of two new classes of voice communication providers.

Led by Skype, one group makes voice a part of the suite of applications on the computer "desktop." These include Google, Yahoo and Microsoft.

The other is made up of telephone and cable companies that seek to make voice calling part of the suite of offerings that comes with high-speed Internet access and television services.

Left out in the cold, said Kate Griffin, consumer technologies analyst for the Yankee Group, could be unaffiliated Internet-phone providers such as Vonage or 8x8 Inc.

Whitman said she does not expect Skype to be a substitute for basic telephone service for a long time, in the same way that eBay auctions have not replaced retail stores.

eBay's new competitors reacted cautiously.

A BellSouth Corp. spokesman said that his company takes Skype seriously and that it should be expected to fulfill the same obligations as other carriers, such as providing 911 services.

Whitman acknowledged that joining the ranks of communications companies would require eBay to "get to know a whole new set of players" in Washington and elsewhere.

Staff writer Arshad Mohammed contributed to this report.

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