What's That Ringing in iPod's Ears?

Verizon's V Cast is the phone business' fiercest bid yet to grab away music fans from Apple's iPod and iTunes

No, this is not Steve Jobs's worst nightmare. Not yet, anyway. But with the Jan. 5 launch of Verizon Wireless' long-awaited music download service, the mobile-phone service provider is offering consumers the closest cellular rival yet to Apple Computer's (AAPL) celebrated iPod and iTunes combination.

Verizon's (VZ) new V Cast Music, to be unveiled at the International Consumer Electronics Show in Las Vegas, will give Verizon's 49 million customers an easy way to buy as many as 1 million songs over the air or on a PC at competitive prices. Specifically, Verizon Wireless has signed deals with all four major labels and one independent distributor, and will sell songs over the air for $1.99 a pop, while tunes bought over the PC will cost 99 cents, BusinessWeek has learned.

Sure, the handsets, which start at $99, don't yet hold a candle to the elegant iPod. And the business model is still a work in progress. But with V Cast, the phone giant takes a large stride into the music business. "I think we'll be a very viable competitor to iPod and other players," says Verizon Wireless CEO Dennis F. Strigl. Having spent billions over the past three years to build a high-speed wireless network, Verizon is keen to tap into the growing consumer demand for cellular data services, especially music, games, and video.

MUSIC-CENTRIC. Since it launched a preliminary version of V Cast last February for $15 a month, the carrier has managed to sell a respectable 2 million handsets equipped for music snips and videos. Now, the phone giant is looking to its new music service to turbocharge its digital offerings. Much the way Apple uses the barely profitable iTunes Music Store to help sell iPods, Verizon is branding a music service to entice subscribers into signing up for V Cast. Even if the company fails to sell loads of songs, it will be collecting the $15 a month subscription fee on top of its basic service charges.

That's why Verizon projects that data services -- driven by music, and its already popular ring-tone offerings -- will account for 25% of revenues by about 2011, up from 6% today. "Music is the centerpiece for V Cast," says Verizon Wireless Vice-President and Chief Marketing Officer John Stratton. "I'm a pretty serious iPod fan, but I don't bring it with me everywhere I go."

Verizon's move also provides a boost for the rest of the phone industry. "There is finally starting to be a choice of services for consumers," says Jonas Geust, vice-president for music at handset maker Nokia Corp. (NOK), which is not involved with Verizon's V Cast. "It's good to have some new competition."

TWO-TRACK MODEL. So what exactly is V Cast Music? Like Sprint Nextel Corp.'s (S) service, which launched in late October, V Cast lets consumers download songs over the air. Both the Verizon and Sprint services provide two copies of each tune -- one for the phone plus a higher-quality file that can be zapped to a PC. Verizon is undercutting Sprint on price, though: $1.99 per over-the-air download, vs. Sprint's $2.50.

Still, no one is sure whether Americans will be willing to pay twice what it costs to buy an iTunes download for the novelty of getting a song over the air. Yes, such services are thriving in South Korea and Japan. But those nations are more cell-phone-centric than the U.S., which has tended to put the PC at the center of the online experience.

This may explain why Verizon has adopted a two-track model for its music service. In a first for a wireless carrier, the company will allow consumers to go online and buy songs for 99Â¢, the same as at iTunes. Subscribers will be able to transfer those downloads and songs on CDs from their PCs to their phones through a USB cable.

SONG SELECTIONS. To further hedge its bets, Verizon is mulling a subscription-based music service that could be launched later this year. Many analysts believe the subscription model fits better with the phone because handsets cannot hold as many songs as a single-use device. Subscriptions also have proven popular with wireless callers in South Korea and elsewhere.

"We're well set up to do that if we choose to do so later in the year," says Stratton, who notes that Verizon chose Microsoft's (MSFT) Windows Media Player as the central technology for its V Cast Music service partly because it supports subscriptions.

A broad selection of music is key to drawing in mobile-phone users, and Verizon is clearly aiming to equal iTunes on that front. When the service goes live on Jan. 16, the Verizon store will offer more than 500,000 songs. By the end of the first quarter, it plans to serve up 1 million tunes.

Besides cutting deals with all four major record labels, Verizon, unlike Sprint, is also selling music from an indie distributor, in this case Orchard, which has hundreds of artists ranging from Millie Holland to the punk band Black Flag. While iTunes already has topped 1 million songs, Sprint's service now stands at only 300,000.

LOW-END FIGHT. Matching Apple's snazzy hardware will be the cell-phone industry's biggest challenge. Verizon has worked with three handset makers -- LG Electronics, Samsung, and UTStarcom (UTSI) -- to design phones specifically to handle music. All come with stereo speakers, which sound much better than the speakers typical of cell phones. And the V Cast software is fairly intuitive, including a feature that lets users preview songs for 20 seconds.

The Verizon-branded phones will also offer more bang for the buck than rival phones. Verizon's cheapest -- Samsung's model a950 -- will cost $99 and includes very little memory. For $99 more, customers get a 1-gigabyte memory card that holds 700 songs. Stratton hopes Verizon music phones will compete at the low end of the market, now dominated by cheaper, lower-capacity iPods, such as the shuffle and the nano.

Still, if the iPod is the BMW of music players, then Verizon phones are more like the Honda Accord: They work well and look fine, but they don't yet offer the same hip package of design and performance as the iPod. "You need a strong device to compete with the iPod, and at this point no one has come up with such a thing," says Michael Gartenberg, vice-president of JupiterResearch.

EARLY SALVO. And who knows what Steve Jobs has up his sleeve? He's not talking. But when he presides over the Macworld Conference & Expo in San Francisco from Jan. 9-13, many analysts expect him to announce a new iPod Shuffle and a device that lets consumers manage the digital media in their homes. Some analysts think he could throw the industry for a loop by cutting a deal with a cellular carrier to launch an Apple-branded wireless network -- that would offer over-the-air content and allow Jobs to retain control.

Then again, V Cast Music is only an early salvo in a war that will play out over the next five years. Verizon already plans two new upgrades for V Cast this year. The company is also busily working on new content deals, new handsets, new applications, and new pricing models with the music labels. Says Stratton: "This is the beginning of a series of evolutions."
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