WHY IS CONNECTICUT SO COMPETITIVE?

- Connecticut's largest city ranks 137th in population nationwide.
- Hartford, the main business center, ranks 143rd.
- **So …**
- Why did AT&T make Connecticut its second most important target for local competition (after California)?
- Why did MCI put Hartford on its list of 31 top targets for local entry?
- Why did AT&T and MCI ask the FCC for permission to lower their long-distance rates in Connecticut alone? Why do AT&T and MCI offer flat-rate, 5 cent per minute, in-state toll rates to Connecticut customers?
- Why did TCI choose Hartford as the first U.S. locality in which to offer Internet access and "People Link" local phone service?

LOCAL COMPETITION

<u>Primary objective of 1996 Act</u>: To "open[] all telecommunications markets to competition."

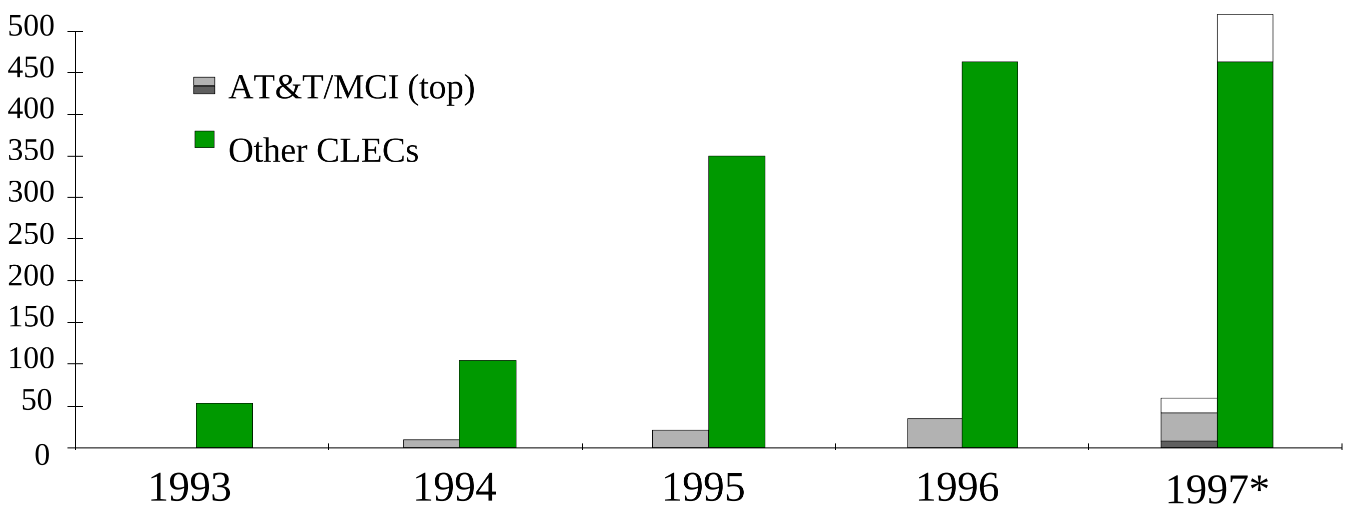
Since passage of the 1996 Act:

- Over 280 companies have signed interconnection agreements to provide competitive local exchange service in over 450 cities.
- Competitors have made significant new capital investment in competitive local facilities.
- CLECs installed over 500 new switches in 1996; 270 more in the first half of 1997.
- Competitors (other than AT&T and MCI) have doubled their installed base of fiber; in the past 20 months they have deployed over half as much new fiber as Bell Companies.
- PCS providers have launched commercial service in markets that serve half of the U.S. population.
- The number of customers able to buy data services from cable operators is growing rapidly, and data traffic is growing much faster than voice.

CITIES SERVED

- Over 280 companies have signed interconnection agreements to provide competitive local exchange service in over 450 cities.

Figure 1. Cities Served by CLECs

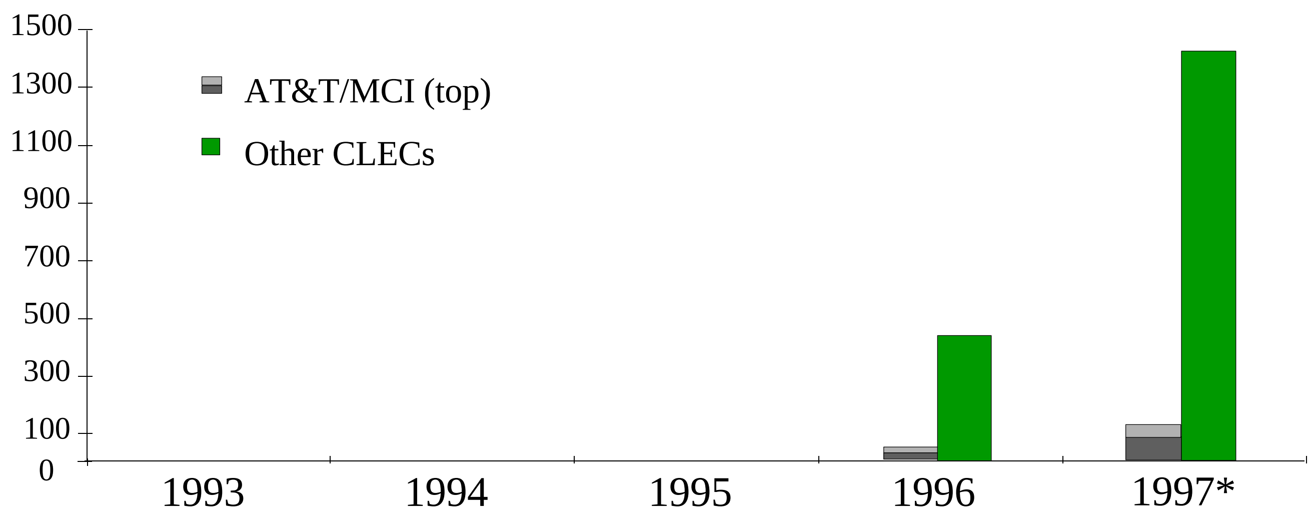


* as of 6/30; year end estimates in white.

INTERCONNECTION AGREEMENTS

- Interconnection agreements are being signed at a rapid pace.
  - Over 100,000 interconnection trunks are operational in SBC's seven-state region; competitors are reselling more than 330,000 lines (180,000 in California and over 115,000 in Texas).
  - BellSouth has over 30,000 interconnection trunks; competitors are reselling 130,000 lines.

Figure 2. Interconnection Agreements

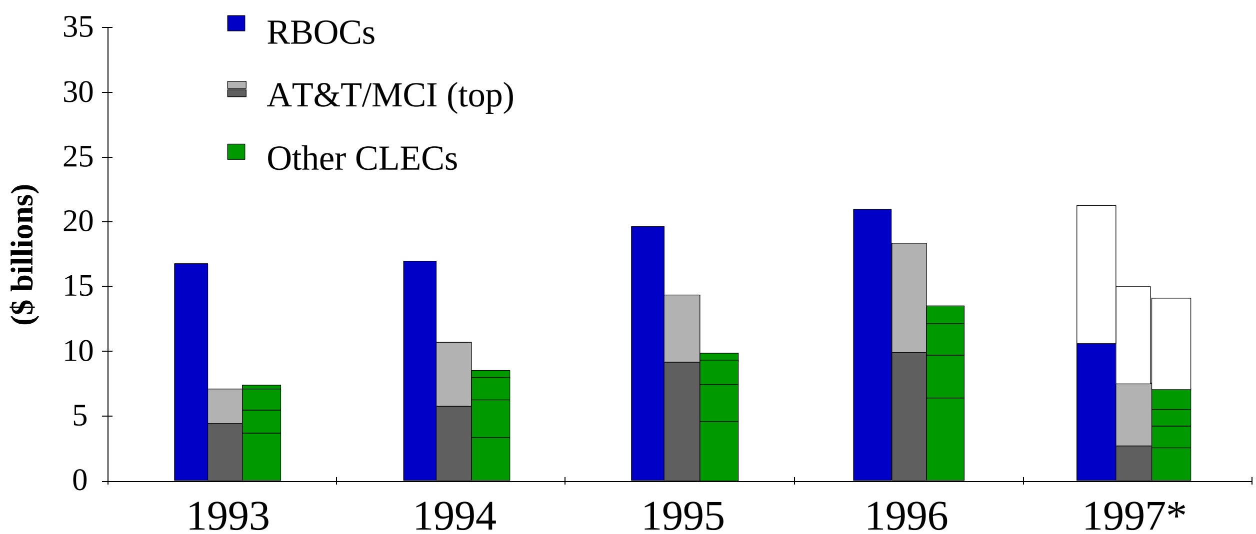


* as of 11/1

CAPITAL INVESTMENT

- Competitors have made significant new capital investment in competitive local facilities.

Figure 3. Capital Expenditures

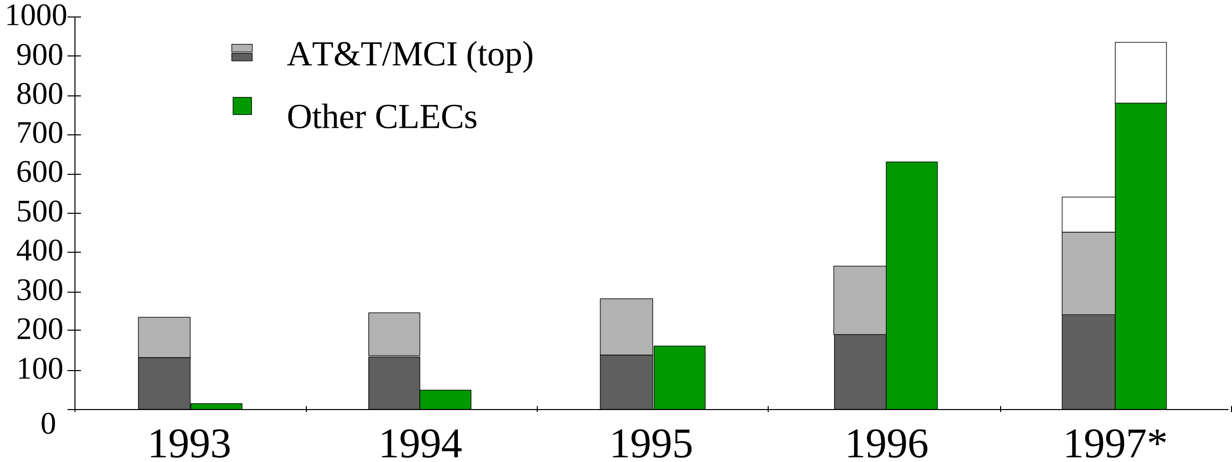


* as of 6/30; year end estimates in white.

NEW SWITCHES

- CLECs installed over 500 new switches in 1996; 270 more in the first half of 1997.

Figure 4. Competitive Switches

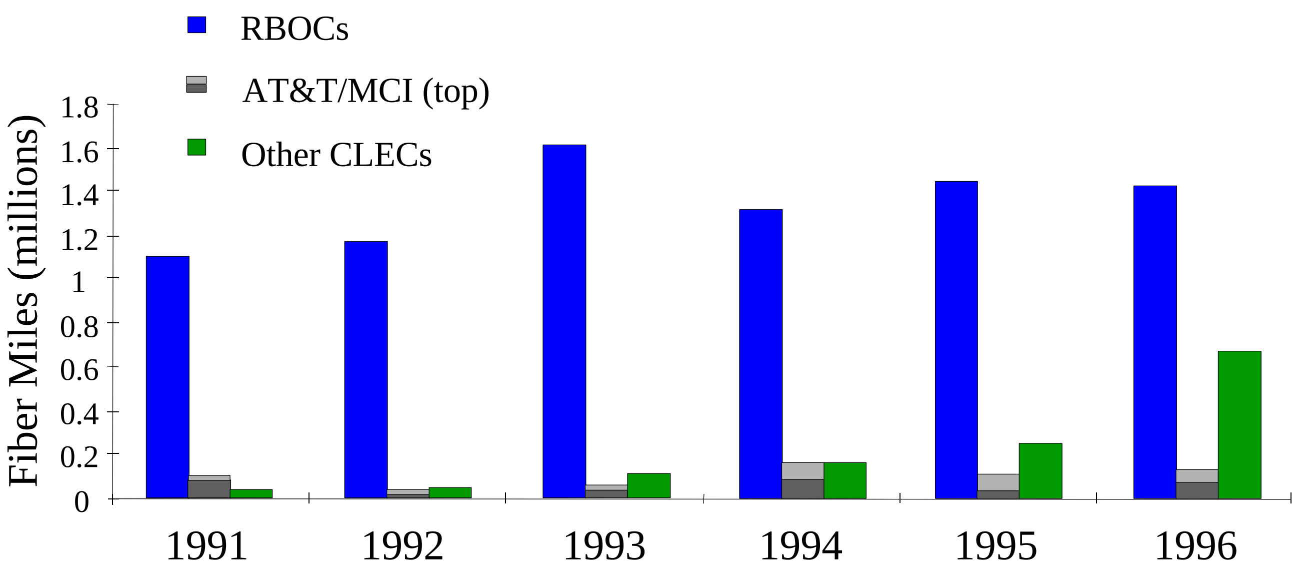


* as of 6/30; year end estimates in white.

FIBER DEPLOYMENT

- Competitors (other than AT&T and MCI) have doubled their installed base of fiber; in the past 20 months they have deployed over half as much new fiber as Bell Companies.

Figure 5. Incremental Fiber Deployment



Competition Is Failing?

"Congress's attempt to open the nation's telecom markets to competition is thus far a failure." (Wall Street Journal, July 3, 1997)

"[T]he rich competition that the bill's proponents predicted would emerge in local telephone and cable television markets has not developed." (New York Times, Sept. 29, 1997)

Competition Is Thriving

"[WorldCom] is the leading provider of alternative local phone services to business customers seeking better prices or services." (New York Times, Aug. 27, 1996)

"Baby Bells and long-distance giants face a new competitor – the combination of WorldCom and MFS Communications." (CNN Moneyweek, Aug. 31, 1996)

"WorldCom is re-creating Ma Bell for the 1990s, with a more aggressive management and business model." (Wall Street Journal, Oct. 2, 1997)

RED-LINING THE LOCAL MARKET

We will build only “where and when it makes economic sense.” (AT&T)

“Not AT&T, not MFS or anyone else, is going to build local telephone facilities to residential customers. Nobody ever will, in my opinion.” (WorldCom CEO Bernard Ebbers)

WHY DO CLECS RED-LINE?

- Residential rates have been set (by regulation) 50-80 percent below business rates.

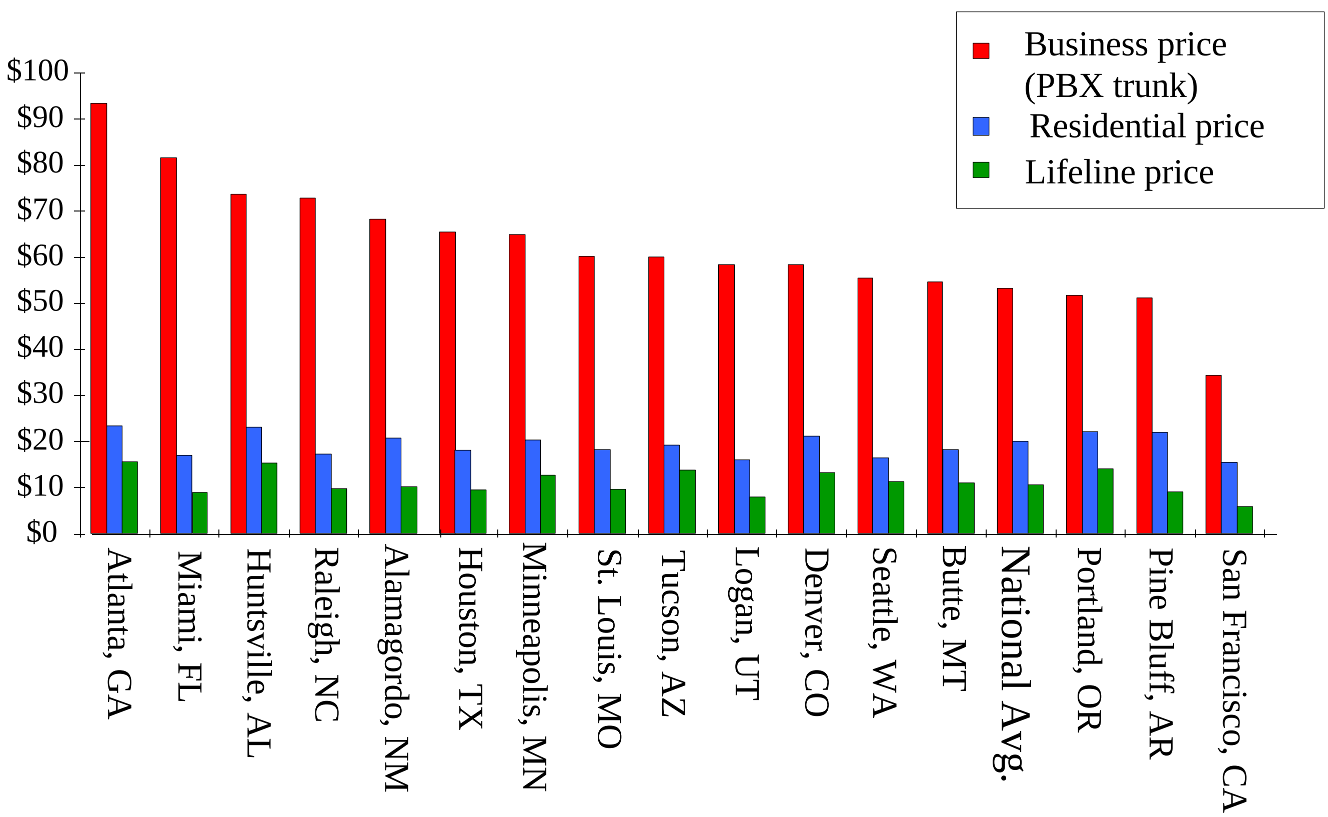
  … while residential service typically costs 50-100 percent more to provide.

- So price-to-cost ratios for CLECs are 2-6 times more attractive in business markets.

BUSINESS VS. RESIDENTIAL SERVICES

- Average business subscriber pays about $27 per month, plus 1.7 cents per minute.
- Average residential subscriber pays a flat rate of about $17 per month.

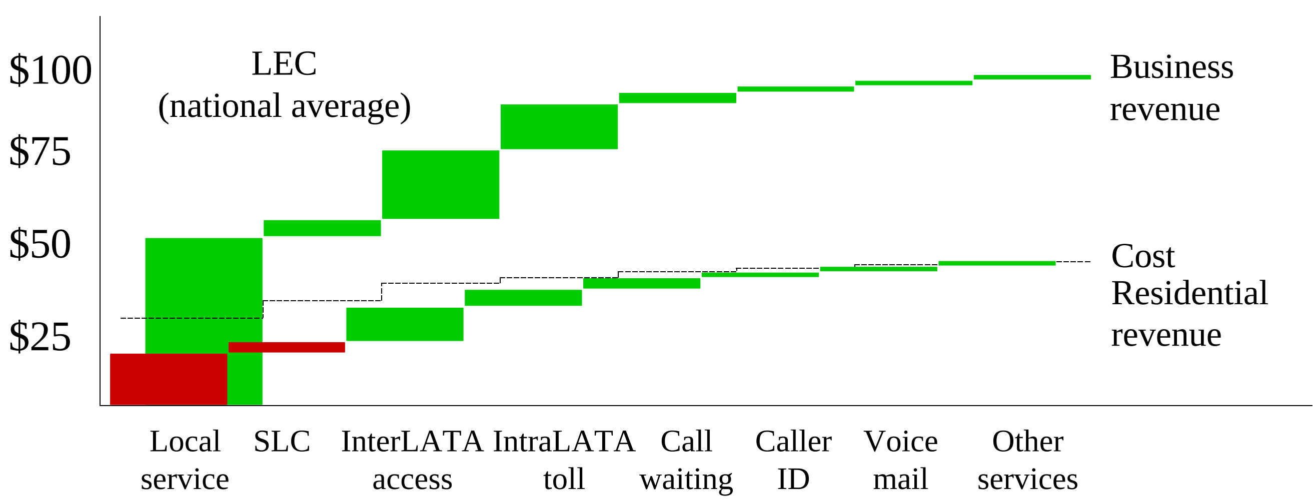
Figure 6. Local Service Prices (selected cities)



HOW INCUMBENTS BREAK EVEN

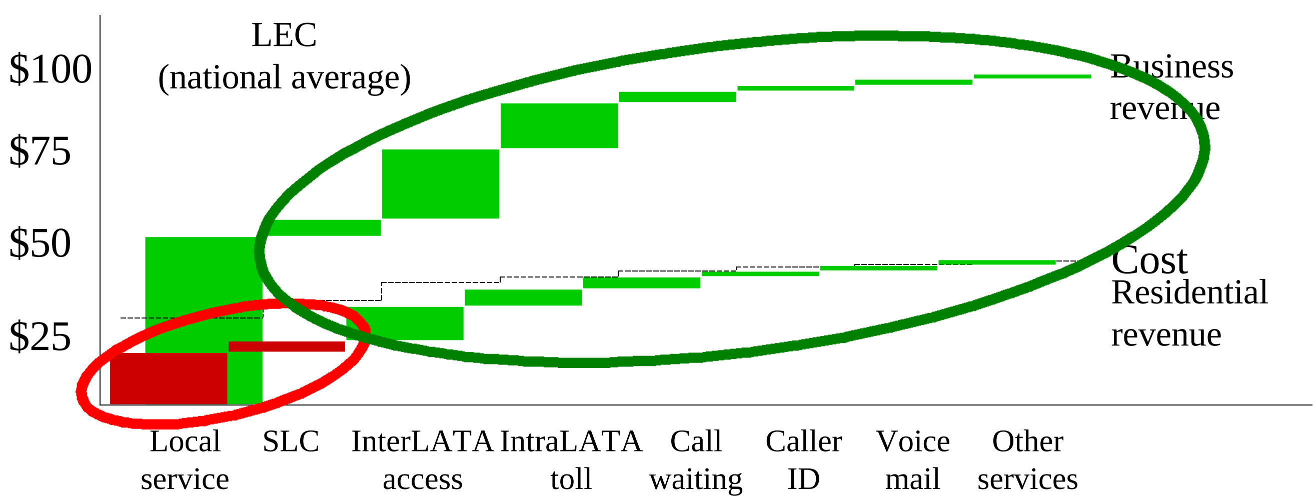
- Local line and dial tone currently cost incumbent phone companies $27-$37 per month to provide.
- Books balance only because above-cost prices charged for business service, access charges, local toll, and vertical services.

Figure 10. Business Monthly Revenue and Cost (per line)



THE RED-LINING STRATEGY

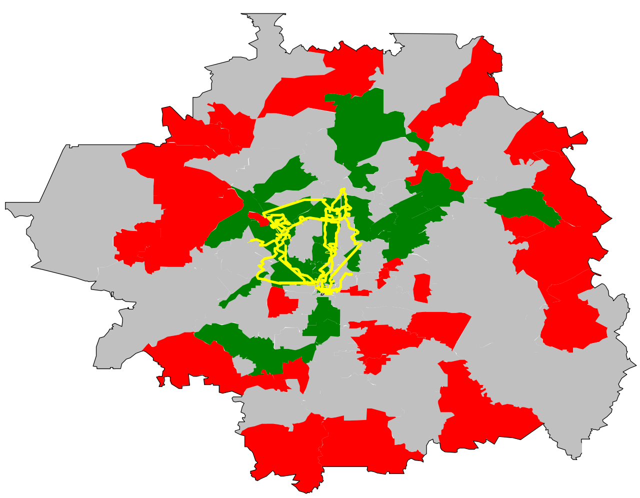
Figure 10. Business Monthly Revenue and Cost (per line)



COMPETITIVE FACILITIES

• Businesses typically cluster in downtown areas and business parks – the areas of highest daytime population. Accordingly, competitors have deployed their fiber networks to areas of high daytime population, while bypassing areas with low daytime population.

Map 1. Competitive Networks In Atlanta

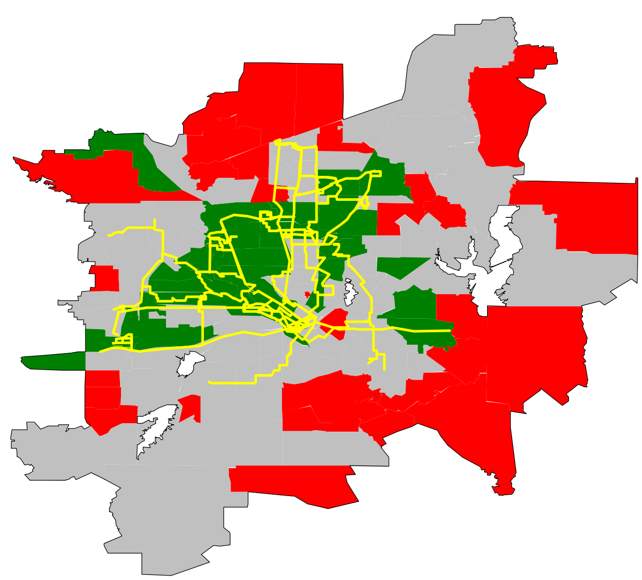


Top 25 percent of Area ZIP Codes in Daytime Population

Bottom 25 percent of Area ZIP Codes in Daytime Population

CLEC Fiber

Map 3. Competitive Networks In Dallas



LOCAL (INTRALATA) TOLL

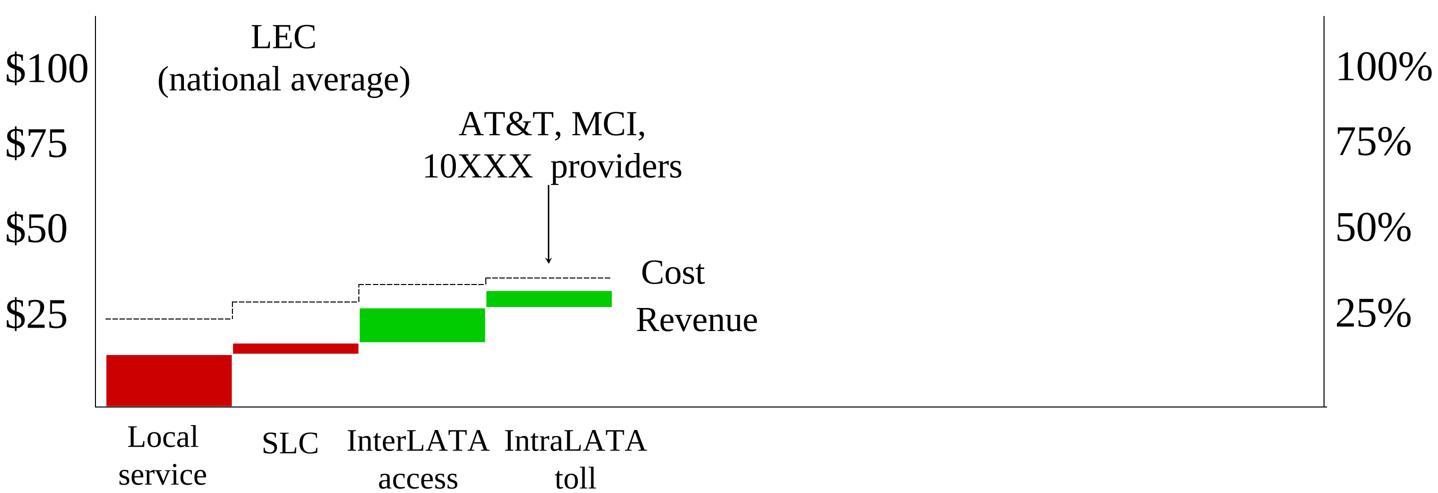
- For business and residential subscribers alike, the highest profits and lowest costs are centered in the market for local toll services.

- In states that have ordered local toll dialing parity – including the two most populous states, California and New York – competitors are already aggressively bundling resold local service with their own local toll services.

- Hundreds of other companies compete in the local toll market using 10-XXX "dial-around" access codes.

- Nationwide, competitive carriers have already captured 15 percent of all local toll traffic, and predict 50 percent capture within three years.

Figure 12. Targeted Competition: IntraLATA Toll (per line)



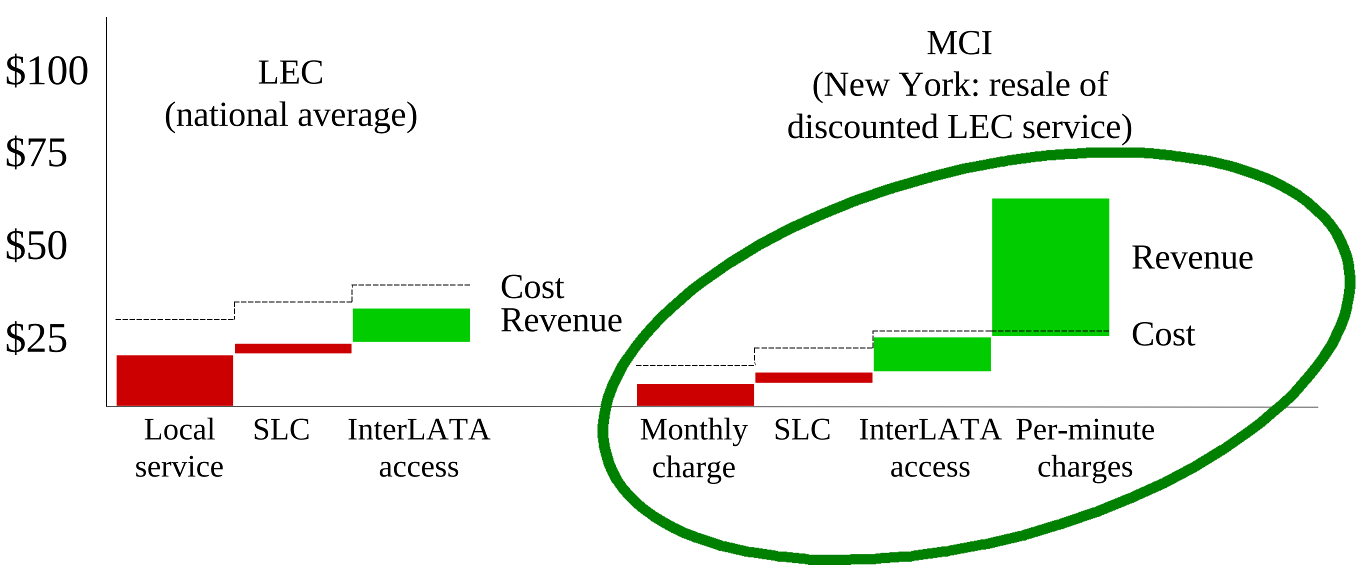
VERTICAL SERVICES

- CLECs offer residential customers the vertical services alone, or a bundle of basic and vertical, but not just basic.
  - AT&T bundles call waiting into its basic local service in some cities in Illinois.
- Providers of shared tenant services offer vertical service packages.
- PCS providers bundle Caller ID, voice mail, and paging: price for entire package is often comparable to wireline.
- MCI resells Bell Atlantic's local residential service in New York: $9.80 a month

  + 10.6 cents per minute for local

  + 10 cents per minute for local toll.

Figure 17. Residential Monthly Revenue and Cost (per line)



WORLDCOM'S RED-LINING STRATEGY

- "Our strategy is not in the consumer business."
- "It's very difficult for us to find a way to make economic sense out of the advertising budgets, the customer service budgets, etc., required to be in the consumer business."
- "[WorldCom's] religious focus is on the business customer . . ."
- CEO Bernard Ebbers: "Not AT&T, not MFS or anyone else, is going to build local telephone facilities to residential customers. Nobody ever will, in my opinion."

COMPETITIVE OPPORTUNITIES

(Or … How to Prove Bernie Ebbers Wrong)

- Customers much prefer to buy a bundled package of telecom services from a single vendor.
- But CLECs have disincentive to bundle local residential markets.
    - CLECs already provide high-margin business, toll, and vertical services … adding below-cost local service is economically unattractive.
    - Regulators reward red-liners! By *not* providing basic local service in residential markets, AT&T, MCI, and other CLECs keep the Bell Companies – their most dangerous potential competitors – caged.
    - AT&T, in particular, is "disproportionately vulnerable to RBOC entry," at risk of losing $8 billion annually to Bell Company long-distance competitors.
- Only ILECs have strong incentives to provide the bundled service that customers want.
- As soon as one vendor begins offering fully bundled local and long-distance service in any major market, others follow. They have no choice. Customers will buy the bundled service as soon as it is offered.

POLICIES TO PROMOTE COMPETITION

- Connecticut: Only state in the continental United States whose main phone company – Southern New England Telephone (SNET) – is permitted to offer complete bundles of service to residential customers.

- April 1994: SNET begins offering Connecticut customers bundle of local and long-distance services.

CLEC RESPONSE: LOCAL MARKETS

- October 1995: AT&T announces Connecticut will be first state in which AT&T offers competitive local exchange service.

- March 1997: AT&T begins offering competitive local service (as a reseller) in Connecticut (AT&T gets to Connecticut second, shortly after California).

- February 1996: MCI includes Hartford on its "Top 31" list of targets for local entry (Hartford is tied for smallest on the list). MCI then rapidly expands its Connecticut network; offers local business service on its own facilities; competitive residential service coming in 1998.

- October 1996: TCI designates Hartford as first U.S. locality in which TCI offers advanced digital telephone, cable, and Internet access services.

- Fall 1996: Connecticut Telephone offers a bundle of wireless, local and long-distance service to business and residential customers statewide.

- 1994-1996: At least 19 other competitors – including Brooks Fiber, Cable & Wireless, WorldCom, Sprint, and Teleport – are certified by the DPUC to offer local exchange service in Connecticut.

CLEC RESPONSE: LONG-DISTANCE MARKETS

- April 1994: SNET begins offering long-distance service; immediately undercuts AT&T by 17 percent. By February 1997 SNET is providing long-distance service to about 35 percent of access lines – mainly residential lines – in Connecticut.

- April 1996: AT&T petitions FCC for permission to reduce its long distance rates in Connecticut alone. MCI joins; requests permission to reduce rates in Connecticut alone. FCC denies both requests.

- SNET price reductions save SNET's long-distance customers an average of $7 per month off an average $40 AT&T monthly bill.

- AT&T's competitive residential service in Connecticut saves AT&T's local customers an average of 25 cents per month off average $18 SNET bill.

THE U.K. EXPERIENCE

(Policies To Promote Competition)

- July 1992: After a decade of deregulatory development, Britain authorized cable operators to provide telephone service over their networks in direct competition with British Telecom (BT).

- U.K. interconnection regulation much less demanding than FCC proposals for U.S. (no attempt to push prices down to long run incremental cost; BT recovers both its fixed and its variable costs; no unbundling; no resale requirement; no electronic processing of service orders).

CLEC RESPONSE

- 1992: SBC, U S West, and other Bell Companies, in conjunction with U.K. cable companies, join with other competitors to challenge British Telecom in the local market.

- TODAY: Nearly 40 percent of U.K. households now have the option to purchase cable telephony, and that figure is projected to rise to 75 percent by 2002.

Figure 24. Competitive Growth in the U.K. Residential Market