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House Energy & Commerce Committee

Wednesday, March 2, 2005

Good morning Mr. Chairman and members of the committee and thank you for inviting me to testify regarding the future of the US telecommunication services industry at this exciting time in its development. I am the Senior Analyst at Sanford C. Bernstein covering the US Telecommunications industry. For those of you not familiar with Sanford Bernstein, we are the oldest and one of the best respected independent sell-side equity research firms in the industry. We do no investment banking, and thus, have no conflicts on that front. I have, however, submitted for the written record a full list of relevant disclosures concerning my and my company's ownership of and business dealings with the all of the companies we will likely discuss today.

In the interest of brevity, I have organized my prepared comments around the various wireline customer segments of consumer, small business, and enterprise and then separately address wireless. I have also submitted for the public record several pieces of research I have authored over the past two years that directly address a few of these topics.

Consumer & Small Business Competition

Looking at the consumer and small business wireline services marketplace, I see no immediate risk to the competitiveness of the marketplace from the proposed mergers. Specifically, the consumer and small business market can be divided into three competitive fronts: the Bells – who, today, dominate the retail voice services market; the large interexchange carriers – AT&T, MCI most notably – that have built positions competing on wholesale connections leased from the Bells; and, the cable multi-system operators or MSOs who have the strongest positions in multichannel video services and broadband data.

Within the past year, the changes in the regulatory landscape surrounding wholesale competition due both to FCC and court actions has fatally eroded the economics for competitors like AT&T and MCI, leading both companies last year to announce their intention to harvest their positions and to actively do so through the cessation of advertising and promotional activity. This competitive capitulation, however, has occurred at the same time that technological advances supporting the carriage of voice services over broadband connections has emerged. This capability, generically referred to as Voice over IP, offers those competitors capable of providing or transiting a broadband connection very favorable economics. By our estimates, over the next five years the cable MSOs as a group will win at least as much share of consumer primary connections as the Bells lost over the past five years to wholesale competitors. And, importantly, the MSOs will compete with the Bells on owned networks not wholesale ones and, thus, will have with far more favorable marginal economics than did the wholesale competitors competing over Unbundled Network Element Platform or UNE-P lines. Thus, it is reasonable to expect that despite the withdrawal either organically or through consolidation of AT&T and MCI from this space, that voice prices in the future could fall at least as rapidly as the 7-8% rate experienced over the past five years. Further supporting this point, I would highlight that where the Bells have already been competing head-to-head against the cable companies, in the consumer broadband market, prices have fallen on average over 10% annually – and at times faster – for the past five years. Thus, while the Bells are proposing to buy their largest consumer market competitors today, we would note that those same companies are doing nothing to pursue new customers or retain existing ones and, thus, we do not believe the mergers are inherently bad for consumer or small business competition so long as the cable companies and, potentially, other facilities-based competitors continue to pursue sales of bundled services.

Enterprise Services Competition

Turning to the enterprise market, we would draw the Committee's attention to two reports we authored over the past few years in a series entitled a Tough Nut to Crack. The title attempts to say it all.

Providers competing for share of the large enterprise and government communication services market must be capable of controlling and delivering high quality of service on their own networks. In addition, they must be able to provide redundancy, custom solutions and, frequently, global connectivity. And, finally, they must have deep sales relationships with the customers and the credibility necessary to convince a customer the size of Citigroup or the Department of Defense that they can secure, monitor and maintain mission critical communications under adverse conditions. To date, the Bells have been scrappy competitors relegated to the provision of only the most commoditized services for this customer segment. AT&T, MCI and Sprint dominate this segment. While backbone providers like Level 3, Global Crossing play the price spoiler role for basic transport. Absent consolidation, the four remaining Regional Bells would need to spend between $5 billion and $7 billion in operating and capital expense over the next five years to build their credibility and competency serving this market and that investment would not even begin to cover the buildout of long-haul transport capacity for which each would still need to contract. In our opinion, for their investment, the Bells would add relatively little to the innovation in the industry and would likely, over the course of the next five to ten years, drive the demise of AT&T and MCI. Thus, while on the one hand I can argue that combining the most likely share gainers (the Bells) with the incumbents and largest share losers (AT&T and MCI) is not pro-competitive, it does, in my opinion, simply hasten the ultimate end-game which would have been the eventual removal of AT&T and MCI from the landscape.

Wireless Competition

Finally, let me turn to wireless. Two years ago, we had six national competitors fighting aggressively for marketshare. Despite that competition, average monthly revenue per user didn't fall. Why? Because demand remained robust and network differentiation drove price stability. Though I know there has been an outcry for quality of service regulation for wireless, I would posit for the committee that wireless, a business built on a capitalistic investment model not a regulated monopoly one, will be far better served allowing market forces to drive quality and innovation than regulation. As evidence, I submit that T-Mobile and Verizon Wireless, the two carriers that have won the greatest number of customer satisfaction awards have also been the leading share gainers, have high customer loyalty and have shown some of the strongest average revenue per user trends. By comparison, AT&T Wireless and Cingular which have received the poorest service marks have been the largest share losers among the big-six carriers over the past three years. As we look at the impact of consolidation, I would say that so long as the US is not allowed to devolve into a duopoly market structure in which the Bells control all of the scale wireless carriers, competition, investment and innovation will remain robust.

Summary

So where does this leave us? My conclusions are four fold:

First, none of the proposed wireline mergers is intuitively a recipe for higher consumer prices or reduced choice;

Second, the SBC-AT&T and Verizon-MCI combinations will likely result in modestly greater stability for enterprise service pricing than we have seen over the past few years but it should also be noted that pricing in that market has been declining at very unhealthy rates since the bursting of the internet bubble unleashed massive overcapacity for transport services.

Third, in wireless, so long as there are three scale competitors and a handful of smaller players, I would not be overly concerned about choice, pricing or service quality; and,

Fourth, if there is concern regarding the longer-term competitiveness of the industry once the cable MSOs and Bells achieve a measure of stability in their consumer market positions, then I would encourage this committee and the FCC to jointly focus attention on fostering the development of additional broadband pipes to the home not once again shackling the incumbents. Further, given the Bells' desire to deploy video services in competition with another former monopoly business, the cable companies, I would encourage this committee to focus efforts on removing the outdated roadblocks currently standing in the way of that innovation and competition.

Thank you, again, for the opportunity to share my thoughts.

<u>Attachments</u>:

a. Research Disclosures

b. Report: "*A Tough Nut to Crack: The Hegemony of AT&T and MCI in the Fortune 1000 Market*," *Jeffrey Halpern et al , March 1, 2002.*

c. Report: "*A Tough Nut to Crack II: Oligopoly Returns to the Enterprise Telecom Market*," *Jeffrey Halpern and Josh Harrington, May 21, 2003.*

d. Report: "*U.S. Telecom: Superior Growth Prospects Make Enterprise Market a Key Battleground for US Service Providers," Jeffrey Halpern, January 6, 2005.*

e. Report: "*Voice over IP: Ripple or Tidal Wave?" Jeffrey Halpern et al, April 26, 2004.*

f. Report: "*SBC: Upgrading to Marketperform; LT Intrinsic Value $32, 12 mo. Target $26; Significant Near-Term Risks Remain," Bernstein Research, February 2, 2005.*

g. Report: *"Verizon & Qwest: Who Will be MCI's Valentine? Verizon Clearly MCI's Preferred Date; Combo Modestly Positive," Bernstein Research, February 14, 2005.*