TECHNOLOGY FUTURES INC.

PCS Poised to Capture Landline Revenues

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To date, wireless cellular service has complemented existing wireline service in the United States. This benign relationship, however, is likely to change as the new PCS providers begin to bring ample capacity online, which can compete directly with the LECs, first for usage and ultimately for access. Over the next decade, continued growth and improvements in wireless communications, coupled with lower prices, mean that wireless will be posed to capture an increasingly larger share of wireline minutes of use, and ultimately wireline voice subscribers. Everything else being equal, this implies significant erosion of LEC landline revenues. Especially at risk is the 50% of LEC revenues arising from usage-sensitive charges, including long-distance access charges and short-haul long distance.

The new PCS providers are building out their networks and improving the quality, capacity, and cost effectiveness of the wireless infrastructure. High-capacity technologies such as CDMA, GSM, and TDMA have been deployed, tested, and adopted by customers. As important, PCS providers are adopting very aggressive and innovative pricing plans, which bring them much closer to being price-competitive with wireline, especially for calls involving per-minute charges. All of this moves us closer to the realization of the scenario outlined above.

In a forthcoming report, *Wireless vs. Wireline for Voice Services: Forecasts & Impacts*, we analyze the competitive threat of emerging wireless services to LEC voice communications. To capture the incremental impact of wireless competition, the economic model we use considers a number of variables including access lines lost and message and non-message revenue lost. The significance of the developments and forecasts to various industry players is clear:

- PCS providers are now defining the wireless industry, especially in terms of vision. They will capture customers and minutes-of-use from cellular and wireline faster than previously thought.

- Cellular providers have no choice but to modernize their networks to digital. The price, capacity, and quality established by PCS is irresistible in all but the short term. Otherwise, consigning themselves to the residual service or to a "carrier of last resort" status would make them the inner-city bus service of the wireless world.

- LECs need to aggressively pursue those opportunities that take best advantage of the strengths of their landline networks and provide high-speed digital access, including Internet access, to the mass market. This, however, is not as much a panacea as might be hoped, since this market will be competitive, willingness-to-pay will be limited, and will require significant investment. For continued growth, LEC owners must continue to expand their range of operations beyond the local exchange to wireless services, long distance, international operations, etc.

- In terms of access lines, LECs could lose 5% market share to wireless by 2001. Furthermore, that loss could grow to over 25% by 2005.

- In terms of voice-minute revenue, nearly 20% of the LEC market share could be lost by 2000 and 50% by 2003.

- Long distance carriers have the opportunity to access local markets without building widespread wireline facilities, relying on resale and unbundling, or paying access charges that currently absorb 50% of their revenue.

- Regulators need to account for the reality of wireless competition in structuring the regulatory environment of the competitive era, including their assumptions about equipment lives and depreciation.

These changes will make life very interesting for people in the telecommunications industry for years to come. From the perspective of all of us as telecommunications customers, the benefits have just begun to be understood.

If you believe that TFI could be of assistance to your organization in developing a fast follower strategy, please contact Ray Hodges at (813) 361-1990 or call John Vanston, Larry Vanston, David Smith, or any other member of the TFI consulting staff.