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Holliday's Holiday Horoscope – 2006

Telecommunications Forecasts for the New Year

{An annual collection of predictions for the New Year by Clifford Holliday, an IGI analyst and author of the Lightwave Series. It is intended for your information and, in some cases, amusement. Many details of these forecasts are available from the author's latest reports ("The Next Generation Network – Will the RBOCs Get Googled Up," and "The Market after the Mergers – The Telecom Economy Today – 2005," which can be obtained from the Information Gatekeeper's web site www.igigroup.com .}

Could it be that another year has gone? It seems just a few days ago, no more than a week or two, that I was thinking about the likely events in 2005. Now here it is time to talk about 2006!

The following is a continuation of our series of annual forecasts for wireline telecommunications (a strange term now that almost no new stuff is wire.) Before we go into our predictions for 2006, we feel compelled (if we had not done well, we probably wouldn't feel so compelled) to cite our results for the last few years. Our Horoscope for 2003 was slightly over half right – batting .500 pays big money in the major leagues! In 2004 we out did ourselves by achieving a better than 70% result. The 2005 result is even better at about 85%. The details of the 2005 forecasts (with my grading) are posted on the Information Gatekeepers' site www.igigroup.com .

Let's look now at our predictions for 2006. (To help those wanting to get a quick look at the actual predictions, and not to be bothered with my reasoning or lack thereof, the actual predictions are underlined.)

We invite you to review the forecasts and let Dr. Polishuk (ppolishuk@igigroup.com) or me (c.holliday@ieee.org) know what you think about the forecast. We may publish the most interesting (or amusing, or both) responses.

Capital Expenditures – Finally, we are seeing an improvement in the capital being expended for growth and new services in telecommunications. The levels of capital expenditure by the major telcos (the others are important, too, but the RBOCs spend so much more than everyone else, the others don't matter much) have been so low for the last several years that basic asset replacement needs are not being met. We predicted an increase last year, and we finally have seen an upward tick. We are again predicting an increase, but not as much as 2005. The RBOCs have started (in varying degrees) several new capital programs that will tend to require more capital expenditures; however, the upfront costs of some of these programs have already been incurred. (Later forecasts will detail some of these programs.) We are therefore forecasting a 10% increase (2006 over 2005) in capital expenditures by the major telcos, cable companies and IXCs. Most of this will be from the RBOCs. Our new report cited above “The Market after the Mergers – The Telecom Economy Today – 2005,” now available from Information Gatekeepers, details this forecast.

High-speed Access – We write a complimentary quarterly report on h-s accesses, also published by IGI, consequently this is an area of great interest. We believe (and we can show the calculations to strongly support that belief) that this is now the main source of traffic growth on our backbone networks. We think that h-s access penetration (percentage of households equipped with h-s access) has reached the part of its ‘S’ growth curve that goes up dramatically. Last year we had predicted that it would reach 45%, and it came close at about 42%. In 2006, we predict an even faster growth rate with h-s access achieving 48% - 50% penetration by year's end.

(Please note that there has been some misleading information published about this rate. The penetration rate refers to the percentage of households in the US equipped with h-s access service. It does not refer to the percentage of people with access to h-s any place, i.e., home, work, etc.)

High-speed Access, Part II – A major battle is in progress between the cable companies and the telcos for dominance in the high-speed access arena. The cable companies achieved a 2-1 lead over the telcos that stood up through 2003. However, in 2004, (might

we be permitted to say, “Exactly as we forecasted,”) the RBOCs began a massive effort to correct this situation, and the 2-1 lead melted to about 61%-39%, still in favor of the cable companies. Last year we predicted that the telcos would cut this led to 55-45, but still in favor of the cable companies. The telcos actually reached about 43%. For 2006, we predict that this trend will continue, with the telcos achieving parity (50-50 including FTTP) by the end of the year.

Network Traffic – We have been forecasting network traffic for several years. This is really a ‘give me’ forecast for several reasons. First, there is no ‘network’ in the sense that one can measure things on it. Then the question of measuring the traffic (if there were a single network) is also problematical. However, in spite of these very formable problems, this issue is very important. Traffic growth is the source of investment need, and profit growth. It is really the basis of our business. Therefore, we try to estimate the increase in traffic on the network every year. Last year we estimated that network traffic would increase by 150%. While it cannot be proven that it achieved that growth (because of the problems noted above,) the increase in h-s accesses for the year alone would be enough to account for that level of increase in traffic. For 2006, we predict that this traffic will go up by another 150%. As noted above we think h-s accesses are going to increase even more rapidly in 2006. Add to that all the things that are being forecast (by the IT/entertainment people) to become even more popular in 2006 – cell phones with high-speed data, more digital music and entertainment, more on-line gaming, more digital pictures – all contributing to more data sources being dumped on the network. These two sources and increases due to the rapid expansion of FTTP with video, add up to faster network growth – we predict it will be as much as 150% for 2006.

Mergers – This is the forecast that we hit out of the ballpark in 2005. We correctly predicted the RBOC – IXC mergers in our 2005 Holiday Horoscope! For this year, we are changing tact a little to the communications manufacturers. We have felt for some time (since the telecom/Internet blowup of 2000) that there are too many major equipment vendors in the US. We just think that the market is too small to support Lucent, Nortel, Siemens, Alcatel, Fujitsu, Ericsson, and the others. We predict that either one or more of the large, traditional telecom vendors will be involved in a major merger, or will leave the US market.

Mergers II or “Who’s Going to be Googled Up?”– There has arisen a new class of telecom competitor in the Googles, Yahoo! and MSNs of the world. These customers/competitors have found ways to profitably use the growth of data traffic in

their basic businesses much more so than any of the traditional telecom companies. While we are not predicting Google will take over an RBOC (at least not this year), we are predicting that these companies will have much more active participation in the telecom market place, and by the end of the year one or more will begin to be viewed as more competitor than customer. Our latest report, “The Next Generation Network – Will the RBOCs Get Googled Up?” deals with this in detail.

Regulation – The 2005 trend towards lighter regulation will continue. With that in mind, we predict that the network access sharing rules will continue favoring the incumbent carriers; that the Internet will continue untaxed; and that any prospective telecom vendor merger will be allowed.

Network Modernization and the NGN– Our existing network, at almost every level, is a conglomerate of various generations and types of technologies. There has been substantial work done on the development (from a standards viewpoint) of a Next Generation Network (NGN.) Capital constraints have previously prevented the initiation of any real replacement program for the older technologies. In addition, while we have been in a deep freeze as to investment, technology and product advancements have continued. While capital may be loosening up a little, there is still a strong pressure for profitability, suggesting the need for expense containment. For all of these reasons, we predict a definitive movement towards a NGN in 2006. This program will be based on elements like ROADMs, next generation DWDM, next generation SONET and optical switches. It will be directed at making the network, more flexible, more reliable, and less labor intensive. Our latest report, “The Next Generation Network – Will the RBOCs Get Googled Up,” outlines this prediction in great detail.

ROADMs – As noted under Network Modernization, we believe that the time has come for Reconfigurable Optical Add Drop Multiplexers (or as we say in Texas, “Rode ‘ems.”) The RBOCs will begin to deploy these elements in metro networks, and the IXC and cable companies will continue to use them in long haul networks. We predict that there will be substantial deployment of ROADMs in 2006.

FTTP – Verizon has started its FTTP program vigorously, and has added to video to its offering. SBC looks ready to begin its program (although it is slightly different from Verizon’s) and BellSouth will be ready by the end of the year. For 2006, we predict that SBC will enter the FTTP arena (with their version) and will be pursuing a strong deployment route by the end of the year and that BellSouth will begin a similar program (to SBC) by the end of the year.

So, there are our predictions for 2006. We hope they will be useful to you, or at least have offered you a laugh or two. Happy New Year to all!

Notes to the media:

For interviews with Dr. Polishuk or Clif Holliday (author of the Lightwave Reports) please contact Dr. Polishuk at 617-782-5033 or at marketing@igigroup.com

Charts and graphs from the latest IGI telecom reports, noted above, can be made available to media outlets as needed, as can information from our latest reports on FTTP, VoIP, and R-OADM.