Columbia Business School

The Private Equity Phenomenon in Telecoms and Media

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Purpose of this (somewhat descriptive) presentation

- Understand some basic trends in the industry
- Provide a taxonomy that allows us to understand investment strategies
- Provide some factual basis to generate a discussion about the issues

Contents

- Assessing size and trends in private equity investment in telecoms and media
- Investment models
- Social and political impacts

Private equity investment in the telecom and media industries is increasing but still remains volatile despite some large deals

1. Investment levels recovering from the dot.com crash but still not reaching historic levels

2. Still primarily focused in North America, but the rest of the world (Europe and Asia) is growing its share of investment

3. Average size of transaction is reaching dot.com levels, with Europe mirroring North America

4. Since 2000, three clearly defined periods in the evolution of PE investment in telecommunications

5. Incumbent targeting in telecommunications is changing the nature of the private equity industry

Private equity investment in telecom and media is recovering from the dot.com crash but exhibits wide shifts in investment allocation

PRIVATE EQUITY TRANSACTIONS IN TELECOM AND MEDIA BY SECTOR(2000-5)
($ '000'000)

	2000-1				2002-3				2004-5			
	All VC/PE Deals		Top 16 PE Firms		All VC/PE Deals		Top 18 PE Firms		All VC/PE Deals		Top 16 PE Firms	
	($)	%	($)	%	($)	%	($)	%	($)	%	($)	%
Broadband	19,270	4.1	260	1.6	85	0.1	0	0.0	3,485	2.5	192	1.5
Cable TV/TV	2,720	0.6	81	0.5	1,030	1.5	451	6.3	3,560	2.6	1,490	11.7
Radio	3,635	0.8	98	0.6	810	1.2	52	0.7	1,035	0.7	19	0.2
Internet	197,825	41.9	4,109	25.4	25,887	37.2	2,007	28.2	23,700	17.2	1,059	8.3
Network / infrastruct. equipment	194,148	41.1	5,930	36.7	35,008	50.3	2,840	39.9	86,060	62.3	7,896	61.8
Wireline services	22,058	4.7	3,086	19.1	4,765	6.8	1,549	21.7	8,875	6.4	1,390	10.9
Wireless services	32,278	6.8	2,605	16.1	2,058	3.0	212	3.0	11,444	8.3	737	5.8
TOTAL	471,984		13,863		69,643		7,120		138,158		12,784	

Source: Thomson Financial; Analysis by the author

North America continues to be the largest destination but the rest of the world is growing its share

PRIVATE EQUITY TRANSACTIONS IN TELECOM AND MEDIA BY GEOGRAPHY (2000-7) (*)

	2000-1		2002-3		2004-5		2006-7 (est.)	
	(‘000 $)	%	(‘000 $)	%	(‘000 $)	%	(‘000 $)	%
North America	404,758,260	85.8	56,635,373	81.3	115,915,737	83.9	106,019,937	80.4
Europe	47,130,093	10.0	9,919,011	14.2	17,435,881	12.6	22,691,984	17.2
Asia	12,738,850	2.7	2,172,904	3.1	4,169,934	3.0	3,083,163	2.4
South America	4,948,164	1.0	322,024	0.5	16,284	0.0	0	0
Rest of World	2,313,914	0.5	593,764	0.9	619,704	0.4	55,499	0
Total	471,934,293		69,643,078		138,157,542		131,850,583	

(*) 2006-7 includes Alltel, Bell Canada, and One

Source: Thomson Financial; Analysis by the author

Average size of transactions has regained "dot.com" levels, while Europe now appears to be as large as North America

PRIVATE EQUITY TRANSACTIONS IN TELECOM AND MEDIA AVERAGE TRANSACTION SIZE (2000-7) (*)

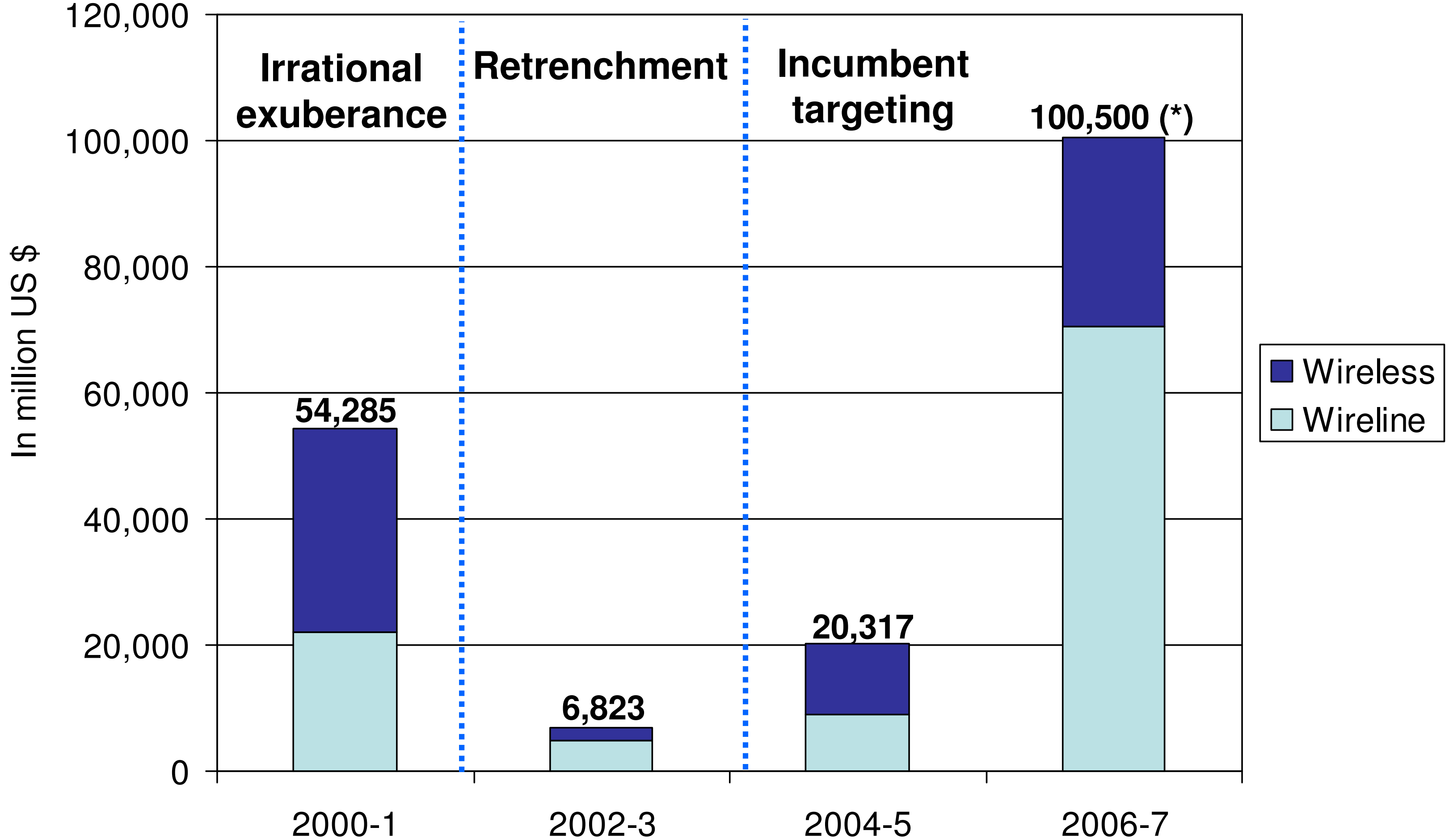
	2000-1 ('000 $)	2002-3 ('000 $)	2004-5 ('000 $)	2006-7 (est.) ('000 $)
North America	44,000	13,699	57,073	40,593
Europe	17,156	9,592	22,015	36,098
Asia	18,995	11,939	43,894	5,900
South America	42,292	8,945	2,035	0
Rest of World	11,398	4,750	9,113	4,624
Total	36,482	12,634	46,144	32,489

(*) 2006-7 includes Alltel, Bell Canada, and One

Source: Thomson Financial; FactSet; Analysis by the author

Private equity investment in telecommunications exhibits three clearly defined periods

PRIVATE EQUITY INVESTMENT IN TELECOMMUNICATIONS



(*) Incumbents with wireless operations have been categorized as fixed telephony

Sources: Thomson Financial; Company and Fund reports; analysis by the author

The “irrational exuberance” period resulted in significant value destruction

LARGEST PE TELECOMMUNICATIONS INVESTMENTS (2000-1)

OPERATOR	INVESTING PE FIRM	AMOUNT INVESTED (in $ millions)
XO Communications	Forstmann Little	1,501
IDT	Hicks Muse	431
Windstream	Welsh Carson	405
McLeod	Forstmann Little	275
BTI	Welsh Carson	270
Birch telecom	KKR	218
Bharti	Warburg Pincus	262
Convergence Communications	TCW	246
Ntelos	Welsh Carson	225
Eircom	Providence	128
IPCS	Blackstone	120
Horizon PCS	Apollo	107
Metrored	Fidelity	90
US LEC	Bain Capital	89
360 Networks	Providence	82

Source: Thomson Financial

In the “retrenchment” period, PE somewhat improved its success rate

LARGEST PE TELECOMMUNICATIONS INVESTMENTS (2002-3)

OPERATOR	INVESTING PE FIRM	AMOUNT INVESTED (in $ millions)
Metro PCS	Flagship, Accel, Primus	1,100
Bharti	Warburg Pincus	805
Vonage	Momentum	396
Diveo	Flagship, Northwest, Alta	353
Citynet	Carlyle, Great Hill	296
Broadview	Opus Capital	296
McLeod	Forstmann Little	278
IP Communications	DLJ, GE, Brookwood	237
IP Wireless	Oak Hill, Doll, Bay	170
FDN Communications	Media Communications Prtnr	143

Source: Thomson Financial

In the “incumbent targeting” period, PE investments focus on “utilities”

LARGEST PE TELECOMMUNICATIONS INVESTMENTS (2004-7)

REGION	DATE	ACQUIRED COMPANY	ACQUIRING PE FIRMS	DEAL SIZE
NORTH AMERICA	2005	Verizon Hawaii (incumbent telco)	•Carlyle	US $ 1.65 billion
	2005	Alltel (wireline)	•Welsh Carson (Valor Communications Group)	US $ 9.1 billion
	2005	Ntelos (incumbent rural)	•Citigroup VC, Quadrangle	
	2007	Alltel (wireless)	•Texas Pacific Capital, Goldman Sachs capital Partners	US $ 24.7 billion
	2007	Bell Canada (incumbent telco)	•Ontario Teachers Union, Madison Dearborn, and Providence Equity	US $ 51.7 billion
EUROPE	2006	TDC (Denmark) (incumbent telco)	•Apax, Blackstone, KKR, Permira, Providence	US $ 13.2 billion
	2006	Eircom (Ireland) (incumbent telco)	•Babcock & Brown	US $ 2.9 billion
	2007	One GmbH (Austria) (wireless)	•Mid Europa Partners, France Telecom	US $ 1.88 billion

Sources: SEC Filings; Company reports; analyst reports

To sum up, each period has a distinct profile

STAGES OF PRIVATE EQUITY INVESTMENT IN TELECOMMUNICATIONS

	PHASE 1 "IRRATIONAL EXUBERANCE"	PHASE 2 "RETRENCHMENT"	PHASE 3 "INCUMBENT TARGETTING"
TIMING	2000-1	2002-3	2004-7
AMOUNT INVESTED	$54.3 Billion	$ 6.8 Billion	$120.8 Billion
AVERAGE SIZE OF INVESTMENT	$ 36 million	$ 11 million	$ 450 million
PRIMARY TARGETS	New entrants (CLECs, 2nd and 3rd wireless licences)	Surviving CLECs and wireless challengers	Incumbents
GEOGRAPHY	84% NA 12% Europe 2% Asia 2% ROW	52% NA 35% Europe 8% Asia 5% ROW	79% NA 20% Europe 1% Asia 0% ROW

Source: Thomson Financial; analysis by the author

Contents

- Assessing size and trends in private equity investment in telecoms and media
- Investment models
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Private Equity investment models appear to be of four types

- Model 1: leveraged buyout/financial engineering
- Model 2: private equity/telco partnerships
- Model 3: rationalization of industry structure
- Model 4: price flipping

Model 1: Leveraged buyout/financial engineering

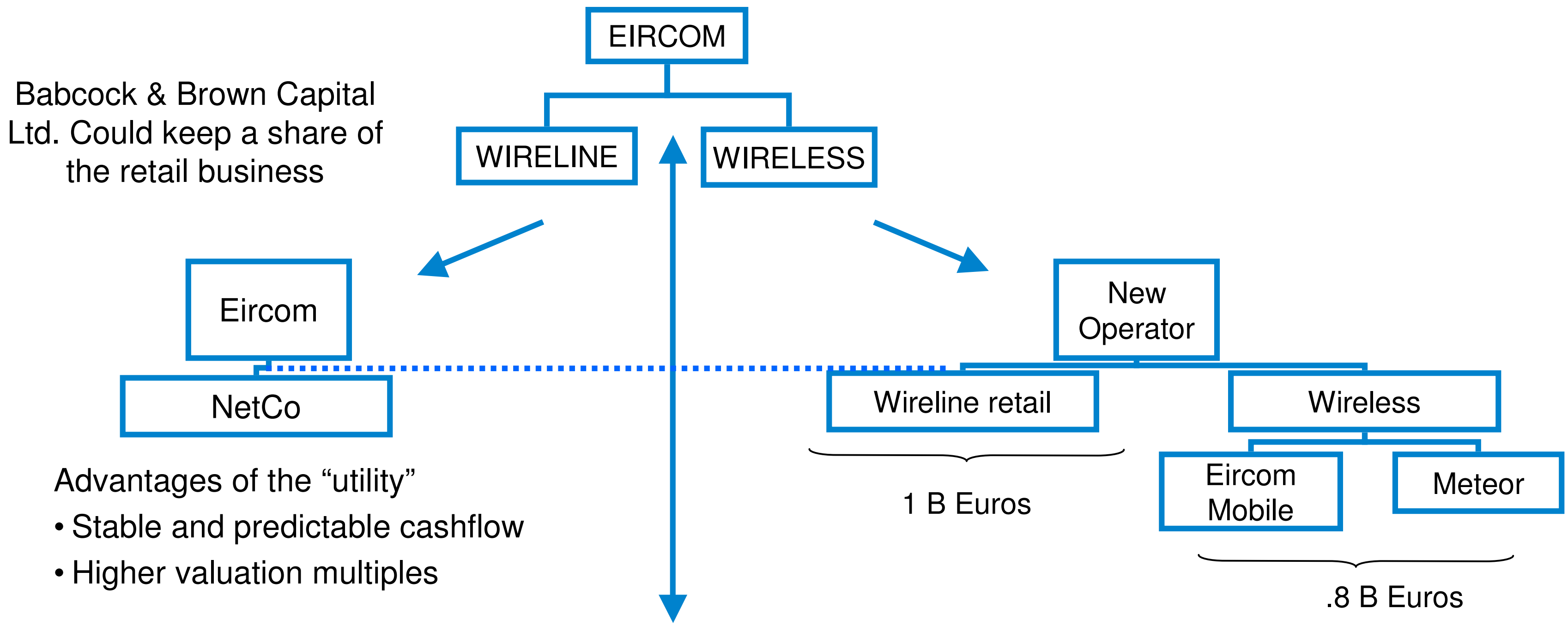
- Buyout of incumbent carrier made in total or partial cooperation with existing management
- Acquisition funds borrowed against the target firm's assets to leverage the buyout
- Value proposition:
  - Efficient long term investment with more extensive time horizons rather than quarterly concerns of publicly-traded companies
  - Operational management
  - Maximization of short-term returns to investors
- Concerns: asset stripping, unsustainable debt structures, postponement of strategic investment, higher risk to investors (e.g. Pension funds), public utility implications
- Performance metrics:
  - Short-term allocation of capital generated from operations
  - Debt as a percent of total capital (debt plus equity)
  - Net debt/EBITDA

Eircom was one of example of this investment model

Carrier Profile	Transaction history	•Privatized in 1998 •Bought through an LBO in 2001 by Valentia •Second IPO in 2004 •Acquired in 2006 by Babcock & Brown
	Size	•Revenues: 1.7 Billion Euros •EBITDA margin: 32% •Employees: 7,000 •75% of wireline market and 20% of wireless
New Ownership	•Eircom Group owned by BCM Ireland Holdings Ltd (Cayman Is.) (57.1%), Employee Share Ownership Trust (35%), other (7.9%)	
Performance between 2001-6	Cost reduction	•Opex: 1,132 m Euros (2001) to 1,097 m Euros (2006)
	Investment	•Late deployment of broadband •Capex: 700 m Euros (2001) to 250 m Euros (2006)
	Debt	•Net debt/EBITDA: <1 (2000); 3 (2001); 6.9 (2006) •Debt/capital: 25% (2000); 70% (2001); 80% (2006) •Cost of debt rose to >8%

Sources: Annual reports; D. Leavy (2006)

The PE exit strategy is based partly on voluntary “structural separation”



- The separation would reduce the regulatory pressure and free up the retail business of debt in order to make it more attractive to investors-with the perspective of a leveraged buyout

TDC in Denmark is another example of this investment model

Carrier Profile	Transaction history	•Partly privatized in 1994, remaining shares sold to SBC in 1998 •SBC sold shares in public market in 2004 •LBO in 2/06
	Size (2006)	•Revenues: 6.4 Billion Euros •EBITDA margin: 29% •Employees: 20,000 •75% of wireline market and 20% of wireless
New Ownership	•88.2% of TDC owned by Nordic Telephone Co. Owned by five PE firms	
Performance between 2001-6	Cost reduction	
	Investment	•High broadband penetration •Weak international expansion •Capex: 1,260 m Euros (2001) to 718 m Euros (2006)
	Debt	•Net debt/EBITDA: <1 (2000); 3.7 (2001); 4.0 (2005); 5.1 (2007) •Debt/capital: 25% (2000); 50% (2001); 27% (2005); 94% (2006)

Sources: Annual reports; Melody (2007)

The payout and exit strategy is a combination of special dividend and assets divestiture

- Special dividend in april 2006 resulted in a total payout of “more than 57% of the share price paid the acquirers, about 47% of TDC total assets, and more than twice the equity investment”
  - It was funded from cash reserves, international divestitures and additional debt
  - It was used to pay down the debt incurred to buy the company
- Most international properties (Hungary, Switzerland, Oman, Poland, Lithuania, Latvia, Germany) will be sold off; so far, Talkline in Germany and One in Austria have been sold
- Sales/lease back of real estate (224 properties already sold)
- At the end, the streamlined company (wireline, cable and domestic mobile) will be sold off

Model 2: private equity/telco partnerships

- Recently emerged in Europe to fit the need for complementary assets/intangible capabilities between private equity groups and debt-laden telcos seeking to achieve a regional footprint
- Example 1: Acquisition of One GmbH, third wireless carrier in Austria
  - Property: One GmbH, 20% market share
  - Seller: E.ON AG (50%), TDC (15%), Telenor (14.5%), France Telecom (14.45%)
  - Buyer: France Telecom (no cash outlay, Orange brand, 35%), Mid Europa Partners (65%)
  - Deal value: US $ 1.88 billion
  - Potential scenario: France Telecom might take control in the future or take a profit if business is sold (less likely)
  - “The partnership constitutes a new approach of co-operation between and operator and a private equity fund which allows to combine the operational expertise of a leading telecom operator and the recognized know-how of a private equity fund strongly active in this sector and this region” (FT statement)

Model 3: private equity as a rationalizer of industry structure

- Private equity group identifies a sector where intrinsic industry economics favor a consolidation with high returns to scale
- Group partners up with management team with experience in succesful acquisitions and integration
- Target identification is conducted in areas with low competitive pressure
- Consolidation is combined with growing the core business driven by capital investments in adjacent businesses (broadband)
- Integration is aimed at generating operational efficiencies and improvements through common systems and processes
- Once the new integrated company is packaged, sell to an operator that benefits from further consolidation

Madison River is an example of this model

1996 — Madison River Capital is formed

1998 — Acquisition of MebTel

1998 — Acquisition of Gallatin River

1999 — Acquisition of Gulftel

2000 — Acquisition of Coastal Comm.

2005 — Acquisition of N. Carolina acc. lines

Madison Dearborn, Goldman Sachs, Providence

Madison River Communications

- 176,000 rural access lines
- 45,000 broadband subscribers
- Residential broadband penetration 38%
- 3,600 route miles of local and long haul network
- $16 million in capex (8.5% of sales
- Total debt: $ 549 million
- 2006 Results:
  - Revenues: $ 189 million
  - Ebitda: $ 99 million (52%)
  - FCF: $ 35 million

Sold to CenturyTel

- $830 million in a combination of cash and the assumption of debt
- Complementary to acquirer

Value added

- From family owned to corporate culture
- Cost controls
- Platform integration
- Economies of scale
- New services to rural consumers

Another one could be the Windstream transaction, although the exit is combined with retention of a cash business

Alltel/Valor/Windstream Transactions

2000

Welsh Carson and Vestar Capital acquire telephone assets of GTE Southwest and creates Valor Telecom

1983-2005

Alltel builds rural wireline business

- Allied Telephone (Ark, Ok, Missouri)
- Mid-Continent Telephone (Ohio)
- Standard Group (Georgia)
- Aliant Communications (Nebraska)
- Verizon Kentucky

7/2006

Valor acquires Alltel wireline business and is renamed Windstream

- 3.4 million customers
- 16 states
- Revenues: $ 3.1 billion
- Capex: $ 380 million
- Total net debt: $ 5.4 billion

12/2006

Welsh Carson exchanges shares of Windstream stock (4.1%) for its directories business

Model 4: private equity as a "price flipper"

- Private equity group identifies or is approached by a company whose shareholders are searching for an exit strategy but cannot find yet a strategic buyer
- Group partners up with existing management team to continue taking care of the company
- After transaction is conducted, ongoing management team continues leading the company, although some search might occur for margin improvement
- After 3-5 years, with industrry consolidation having progressed, private equity group sells to strategic buyer

The Alltel wireless transaction is a classic example of this model

- Original investors put the wireless business up for sale right after spinning off the wireline business
- Strategic buyers were reluctant to close on the company
  - Verizon: largest roaming partner but antitrust concerns and has a build vs. buy option based on the 700 Mhz auction
  - ATT: gsm/cdma conversion would add to the ptice, plus antitrust concerns
  - Sprint: still struggling with the Nextel integration and low stock value reduces currency
- Between February and April, 2007 the company reports agressive repurchase of shares
- Company finally bought by Texas Pacific and the private equity arm of Goldman Sachs at 8.9 x EBITDA estimates, versus 7.1 (Sprint) and 8.3 (Dobson)
- Unclear questions:
  - Leverage (which could link it to model 1)
  - Cost reduction
- Exit strategy: sell to strategic investor?

Each model comprises opportunities and risks for investors as well as consumers

	Investors		Consumers	
	Opportunities	Risks	Opportunities	Risks
Model 1: Leveraged buyout/financial engineering	• More efficient long-term investment and operational management of carrier • Maximization of short-term returns (payouts, asset divestiture, opex reduction, tax avoidance)	• Higher debt and leveraged financing • Exit risk for a smaller residual highly leveraged carrier	• Management focus on core business with consequent impact on service quality	• Reduction in innovation capex • Asset-stripping might lessen benefits of vertical integration • USS at risk
Model 2: private equity/telco partnerships	• Good combination of acquirer capabilities • Huge upside for telco under sale or keep scenarios	• PE bears most of the risk	• Benefit from capability infusion from telco buyer (new services, better quality)	• Some turbulence derived from management changes and post-merger integration
Model 3: private equity as rationalizer of industry structure	• Abundance of low-priced assets	• Management team is not up to the task of post-merger integrating properties	• New services • Better quality from change in corporate culture	• Potential service disruption due to poorly managed integration
Model 4: private equity as "price-flipper"	• Find opportunities for margin improvement	• Strategic buyers do not show up at exit time • Industry enters into slow-down cycle		• Any temptation of short-term cash value maximization might hinder innovation capex

Legend: High Moderate Low

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The entry of private equity in telecommunications has raised strong opposition, primarily in Europe

- "Private equity bosses claim to take over poor performing firms, strip out inefficienies and leave them stronger. But all too often they don't see the long-term advantages of key parts of the business, like research and development. The evidence is that where private equity gets involved, investment plummets, new services decline and broadband networks deteriorate" (Adrian Askew, General Secretary of Connect, UK Communications Union)
- The CWU Ireland has launched a campaign against Babcock & Brown's proposals to split the network and retail divisions and form two separate companies. The CWU points out the proposal does not make economic sense and will undermine employment, pay and conditions of serving eircom members
- Denmark's Eastern High Court supported Danish unions and denied TDC to enforce the Articles of Association that would lead to compulsory redemption of the minority shareholdings and consequent delisting of the company from the Cpenhagen stock Exchange
- PE' funds were described as "locusts" moving across countries and companies (Germany's 2006 political campaign), and "vultures" engaged in asset stripping
- In France, funds are criticized by unions and industrialists for a complete lack of "respect du patriotisme economique" (Claude Bebear, Axa Chairman)

We have attempted to gather evidence which could give us directional answers to some of the issues raised

- Can a reduction in capex be linked to negative innovation impact of PE buyouts?
- Can buyout companies be linked to employment reduction or growth?
- Can the volatility of ownership result in inordinate frictional costs?
- What is the ultimate impact on long term infrastructure investment?
- Are there countervailing forces to undue political influence?

As expected, the European buyouts have increased debt beyond the accepted range

- **TDC:** Since the buyout was financed by approximately 80% debt, TDC's debt jumped from 27% (2005) to 82% (2007) of total capital (debt plus equity) and the net debt/EBITDA from 1.3 to **5.1**; part of it is funded through high yield bonds, maturing in 2014
- **Eircom:** the buyout transaction has resulted in an increase in debt from xx% to 80% (2006) of total capital and the net debt/EBITDA from 3.0 (2001) to **6.9** (2006); average cost of debt is 8%
- **Madison River:** in 7/05, Madison refinanced its debt, reaching **5.5** in tne net debt/EBITDA ratio; weighted average interest rate is 8.1%
- **Windstream:** As a of 5/07, its net debt/EBITDA was **3.1** (partly reduced by sale of directories)
- These ratios are not out of the ranges found in the US industry, although TDC and Eircom are out of the range in Europe

Verizon	1.20
ATT	1.24
Embarq	2.40
CenturyTel	2.53
Qwest	2.63
Windstream	3.03
Citizens	3.48
Cincinnatti Bell	3.83
Level 3	5.02
Madison	5.5

Telenor	1.32
BT	1.63
DT	1.96
Telefonica	1.97
FT	2.07
PT	2.43
TI	2.90
TDC	5.1
Eircom	6.9

Sources: Bear Sterns (2007); analysis by the author

Broadband deployment is not slowing down under PE acquired incumbents

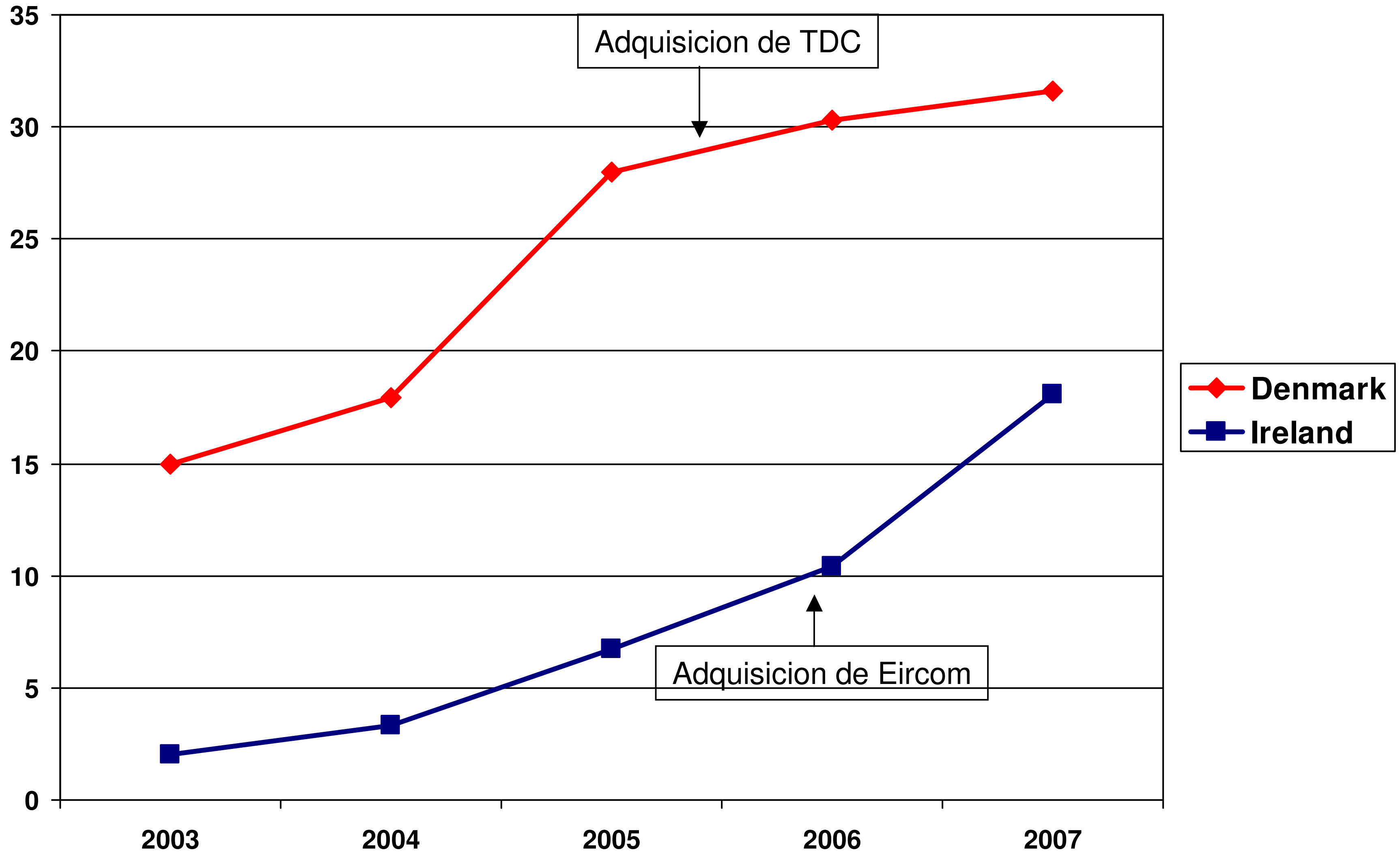
BROADBAND PENETRATION

	2000	2001	2002	2003	2004	2005	2006	2007
Madison River (*)	3.2	8.2	12.2	18.5	32.2	35.7		
Denmark				15.0	17.9	28.0	30.3	31.6
Ireland				2.0	3.3	6.7	10.4	18.1
Windstream		0.9	2.0	4.4	7.5	13.3	20.2	26.6

(*) Residential Penetration

Sources: ECTA; Annuel reports; SEC filings; Surterre Research; CommReg filings

Legend: Change of ownership



35
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Adquisicion de TDC
Adquisicion de Eircom
Denmark
Ireland

Capex continues declining in most cases, but so is that of most carriers

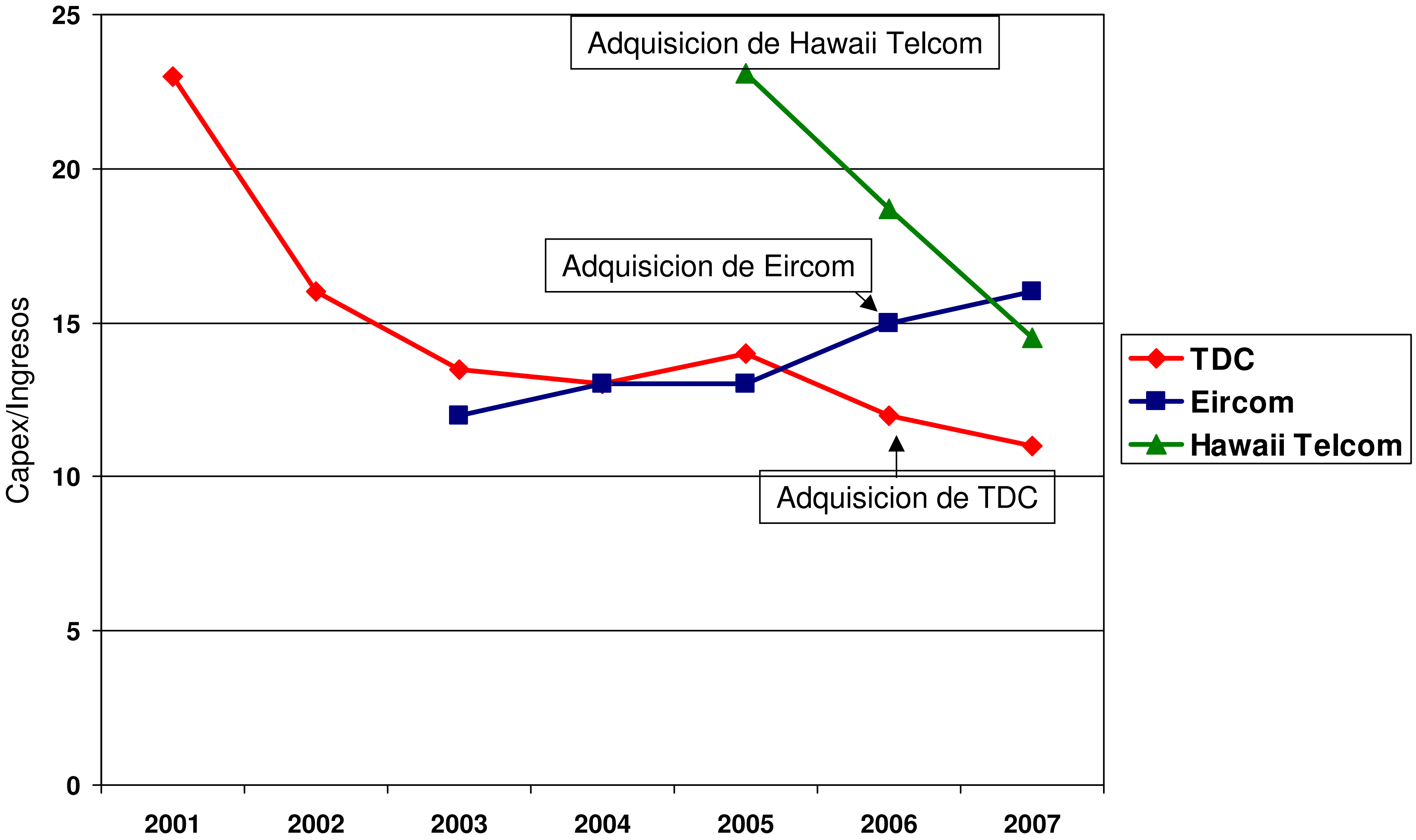
CAPEX AS PERCENTAGE OF REVENUES

	2000	2001	2002	2003	2004	2005	2006	2007
Madison River		21.7	6.7	6.6	7.5	8.5	13 (*)	
TDC		23	16	13.5	13	14	12	11
Eircom				12	13	13	15	16
Windstream		17.3	15.7	13.4	11.9	13.5	13.2	11.8
Hawaii Telcom						23.1	18.7	14.5

(*) CenturyTel

Sources: Annuel reports; SEC filings; Surterre Research; CommReg filings

Legend: Change of ownership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To sum up, some consistent evidence emerges from recent PE acquisition deals

- CAPEX declines but that is somewhat consistent with industry trends; nevertheless, at Eircom is increasing
- Broadband deployment (as a proxy for innovation and consumer benefits) does not appear to slow down
- Debt leverage increases but European deals appear to be way beyond the benchmark

Additional slides

Private equity buyouts in the telecommunications industry have increased in the past three years

REGION	DATE	ACQUIRED COMPANY	ACQUIRING PE FIRMS	DEAL SIZE
NORTH AMERICA	1996-2006	Madison River (then sold to CenturyTel)	•Madison Dearborn, Goldman Sachs, Providence	US $ 830 million
	1998	PriCellular (rural wireless)	•Providence, Spectrum, Sandler	US $ 811 million
	1998	Centennial (rural wireless)	•Welsh Carson, Blackstone	US $ 1.4 billion
	2004	Verizon Hawaii (incumbent telco)	•Carlyle	US $ 1.65 billion
	2005	Alltel (wireline)	•Welsh Carson (Valor Communications Group)	US $ 9.1 billion
	2005	Ntelos (incumbent rural)	•Citigroup VC, Quadrangle	
	2007	Alltel (wireless)	•Texas Pacific Capital, Goldman Sachs capital Partners	US $ 27.5 billion
	2007	Bell Canada (incumbent telco)	•Ontario Teachers Union and others	C $ 51.7 billion
EUROPE	2006	TDC (Denmark) (incumbent telco)	•Apax, Blackstone, KKR, Permira, Providence	US $ 13.2 billion
	2006	Eircom (Ireland) (incumbent telco)	•Babcock & Brown	US $ 2.9 billion
	2007	One GmbH (Austria) (wireless)	•Mid Europa Partners, France Telecom	US $ 1.88 billion

Sources: SEC Filings; Company reports; analyst reports

PRIVATE EQUITY TRANSACTION BREAKDOWN FOR TOP FIRMS (2000-7) (All numbers in $,000)

	2000-1	2002-3	2004-5	2006	TOTAL
Blackstone	N/A	22,703	486,000	1,664,999	$2,173,702.00
Warburg Pincus	1,677,585	2,483,905	2,217,971	783,512	$7,162,973.00
Carlyle Group	N/A	575,953	1,483,908	830,868	$2,890,729.00
KKR	517,728	149,466	420,357	N/A	$1,087,551.00
Goldman Sachs	1,362,299	460,424	792,252	171,945	$2,786,920.00
JP Morgan Partners	1,568,878	446,894	391,967	33,974	$2,441,713.00
Apax Partners	N/A	738,328	1,041,214	72,904	$1,852,446.00
3i Group	N/A	567,107	849,927	139,570	$1,556,604.00
Welsh, Carson	1,657,037	334,995	50,000	N/A	$2,042,032.00
Thomas Lee	N/A	26,262	N/A	N/A	$26,262.00
Hicks, Muse	1,255,499	N/A	155,000	N/A	$1,410,499.00
Apollo Advisors	N/A	119,895	106,700	N/A	$226,595.00
Bain Capital	614,765	321,028	832,599	13,920	$1,782,312.00
Madison, Dearborn	977,521	52,542	384,438	N/A	$1,414,501.00
Texas Pacific	717,094	58,205	659,699	N/A	$1,434,998.00
Providence Equity	N/A	605,369	773,039	999	$1,379,407.00
Morgan Stanley PE	813,927	8,332	5,527	10,000	$837,786.00
TA Associates	386,390	148,972	N/A	4,967,813	$5,503,175.00