CLEC’s Grow Up

Competitive Carriers Come Through with Rapid Asset Deployment, Capital Markets Access and Revenue Growth

By Terry Barnich
Since the enactment of the 1996 Telecommunications Act, observers of competitive local exchange carriers (CLECs) anxiously have awaited the transformation of the fledgling CLECs from their “alternative access” or “bypass” roots into a robust, fully integrated communications services industry.

As we digest the 1998 end-of-year operational and financial statistics from the CLECs, there is clear and convincing evidence to assuage the anxieties of the nervous. Indeed, it is now beyond reasonable debate that CLECs are coming into their own, fulfilling the expectations of even their most enthusiastic boosters.

Examining aggregate industry data from both an assets-based analysis and a revenue perspective, reveals that CLECs are proving wildly successful at executing the construction of the three legs of the CLEC network stool: rapid asset deployment, access to the capital markets and sustained exponential revenue growth.

Network and Asset Growth

The size, reach and scope of the industry has grown rather dramatically since the passage of the Telecom Act. As measured by the sheer number of entrants into what still is a near-monopoly market, we see market aspirants still willing to bear the risk of entering the business.

The growth of facilities-based carriers operating in the United States over the last 11 years has been tremendous (see “CLEC Revenue Growth” chart, this page). What in 1988 was an industry of two companies, MFS Communications Co. Inc., Omaha, Neb. (now part of MCI WorldCom) and Teleport Communications Group Inc., New York (bought by AT&T Local Services), has morphed into more than 160 today. Indeed, it seems to those of us who chart the growth and development of the emerging carriers that, despite well-publicized consolidation trends, new-entrant growth is and remains steady (see “10-Year CLEC Entity Growth” chart, page 63).

Fueling new-player introduction, not surprisingly, has been the constant market opportunity in building working,
revenue-making networks (see "CLEC Network Growth 1998-1999" chart, this page). The most impressive statistic, because it translates directly into the point of the exercise—raising revenue—is that of line growth. If anything represents a leading indicator of industry and company health, it is this data point. Today, facilities-based CLECs account for 5.6 million access lines in service, which, in 1998, produced $10.6 billion in total CLEC service revenue.

As competitors multiply, so too does their reach. In 1996, CLECs reported operating in 303 markets, which largely meant serving tier 1 and tier 2 "NFL cities." (If literally true that would mean a CLEC for Green Bay, Wis., but not for Los Angeles. That clearly is not the case.) Today, CLECs are serving customers in 566 markets around the country and in a growing number of tier 3 and tier 4 cities. It would appear there are few, if any, cities too small to warrant a competitor to the incumbent.
Access to Capital Markets

One fundamental measure of and predicate for success in building communications networks is access to investment capital. To build out networks quickly and execute deployment schedules, CLECs must secure the financing to fuel capital expenditures. Despite the hiccup in the financial markets last summer, the CLECs have been singularly adept, raising $6.1 billion in debt and $3.1 billion in equity from April 1996 through January 1999. Following this, CLECs continue to make substantial investments in building competitive networks (see “CLEC Capital Expenditures” graph, page 63).

Revenue Growth and Analysis

The overall objective for any long-term CLEC strategy is profitability, and the first priority to achieve that goal is to acquire (and retain) paying customers. Accordingly, revenue growth is the leading financial indicator of CLEC health. By that measure, the CLEC industry is “in the pink,” and revenue growth for the over-all market has been exponential (see “CLEC Revenue Growth” graph, this page). In fact, the industry has enjoyed dynamic, triple-figure revenue growth for the last two years. To top it off, the rate of growth has been accelerating since 1996.

Apart from that which we glimpse from measuring aggregate growth, categorizing the sources of revenue by service really enables us to appreciate significant industry drivers and identify emerging trends.

In the days before the regulators opened the local switched exchange to competition, CLECs largely were limited to offering competitive local access to the interexchange carriers (IXCs) and private line services.