Notes to Consolidated Financial Statements—(Continued)

Note 15—Related Party Transactions—(Continued)

Effective September 5, 1995, ITC's President became President and Chief Operating Officer of the Company and certain core management personnel previously provided by ITC also became employees. Concurrently, ITC ceased providing services to the Company under the consulting agreement, and the Company's obligation to pay any future compensation to ITC under such agreement was terminated.

Note 16—Supplemental Cash Flow Information

Cash paid for interest during the ten months ended December 31, 1995, and the years ended December 31, 1996 and 1997 was $1.3 million, $2.1 million and $26.0 million, respectively. During the years ended December 31, 1996 and 1997, the Company capitalized $300,000 and $4.2 million of interest incurred in connection with the buildout of its telecommunications network respectively. No interest was capitalized in the ten months ended December 31, 1995.

During the ten months ended December 31, 1995, the Company completed the following material noncash transactions: (i) the conversion of $3.75 million of convertible notes plus accrued interest thereon; (ii) the conversion of all shares of Preferred Stock Series E; (iii) the acquisition of approximately $7.5 million in property and equipment through various capitalized leases; (iv) the Private Exchange transaction (see Note 14); (v) the settlement of the Company's placement expenses from the gross proceeds of the Debt Placement; and (vi) the acquisition of Avant-Garde.

During the year ended December 31, 1996, the Company completed the following material noncash transactions: (i) the conversion of $3.75 million of convertible notes plus accrued interest; (ii) the acquisition of $8.6 million in property and equipment through various capitalized leases; (iii) the issuance of 100,605 shares and share equivalents, with a value of $1.5 million, and $800,000 in notes payable in connection with certain acquisitions (see Note 2); (iv) the issuance of $17.5 million in notes payable for the acquisition of Locate; and (v) the acceptance of 150,000 shares of the Company's common stock for payment of stock options exercised. Depreciation and amortization includes amortization of deferred compensation.

During the year ended December 31, 1997, the Company completed the following material noncash transactions: (i) dividends-in-kind on the Series A Preferred Stock for the aggregate amount of $5.3 million; (ii) the acquisition of $8.9 million in property and equipment through various capitalized leases; (iii) the issuance of 337,648 shares of common stock with a value of $7.5 million in connection with the acquisition of licenses; (iv) The issuance of 3,594,620 shares of Common Stock with a value of approximately $75 million in connection with the acquisition of Milliwave Limited Partnership.

Note 17—Advertising Costs

Advertising costs are charged to operations when the advertising first takes place. Advertising expense for the ten months ended December 31, 1995, and the years ended December 31, 1996 and 1997 was approximately $500,000, $4.3 million and $11.0 million, respectively.

Notes to Consolidated Financial Statements—(Continued)

Note 18—Business Segments

The Company's continuing business segments are telecommunications and information services. The following table is a summary of the ten months ended December 31, 1995 and the years ended December 31, 1996 and 1997:

	TELECOMMUNICATIONS	INFORMATION SERVICES	TOTAL CONTINUING BUSINESS SEGMENTS	GENERAL CORPORATE	CONSOLIDATED CONTINUING OPERATIONS	DISCONTINUED OPERATION—MERCHANDISING
			(IN THOUSANDS)			
For the ten months ended December 31, 1995						
Net sales	$ 13,137	$ 2,648	$ 15,785	$ —	$ 15,785	
Operating income (loss)	$ (7,288)	$ 217	$ (7,071)	$ (3,861)	$ (10,932)	$ 237
EBITDA	$ (6,358)	$ 241	$ (6,117)	$ (3,758)	$ (9,875)	
Depreciation and amortization	$ 930	$ 24	$ 954	$ 104	$ 1,058	
Capital expenditures	$ 7,458	$ 14	$ 7,472	$ 651	$ 8,123	
Identifiable assets at December 31, 1995	$ 36,998	$20,195	$ 57,193	$217,711	$ 274,904	$ 3,321
For the year ended December 31, 1996						
Net sales	$ 33,969	$14,650	$ 48,619	$ —	$ 48,619	
Operating loss	$ (43,698)	$ (1,409)	$ (45,107)	$ (11,373)	$ (56,480)	$(1,010)
EBITDA	$ (39,206)	$ (890)	$ (40,096)	$ (9,796)	$ (49,892)	
Depreciation and amortization	$ 3,831	$ 469	$ 4,300	$ 202	$ 4,502	
Capital expenditures	$ 46,632	$ 701	$ 47,333	$ 509	$ 47,842	
Identifiable assets at December 31, 1996	$ 101,380	$30,133	$ 131,513	$143,462	$ 274,975	$ 3,814
For the year ended December 31, 1997						
Net sales	$ 38,277	$41,354	$ 79,631	—	$ 79,631	
Operating loss	$(153,139)	$ (4,092)	$(157,231)	$ (30,815)	$(188,046)	$(6,477)
EBITDA	$(128,637)	$ (2,786)	$(131,423)	$ (26,922)	$(158,345)	
Depreciation and amortization	$ 24,502	$ 1,306	$ 25,808	$ 3,893	$ 29,701	
Capital expenditures	$ 219,979	$ 612	$ 220,591	$ 1,709	$ 222,300	
Identifiable assets at December 31, 1997	$ 399,111	$30,376	$ 429,487	$544,809	$ 974,296	$ 2,105

EBITDA represents operating income (loss) plus interest, taxes, depreciation and amortization.

Notes to Consolidated Financial Statements—(Continued)

Note 19—Quarterly Results of Operations (Unaudited)

The unaudited quarterly financial data for 1996 and 1997 for the Company is as follows:

	QUARTER ENDED 1996 (UNAUDITED)			
	MARCH 31	JUNE 30	SEPTEMBER 30	DECEMBER 31
	(IN THOUSANDS)			
Operating revenues				
Telecommunications services	$ 10,217	$ 10,356	$ 7,384	$ 6,012
Information services	771	2,652	4,056	7,171
Total operating revenues	10,988	13,008	11,440	13,183
Operating expenses				
Cost of services and products	6,678	9,175	9,250	13,130
Selling, general and administrative expenses	8,845	14,401	15,816	23,303
Depreciation and amortization	492	679	1,158	2,172
Total operating expenses	16,015	24,255	26,224	38,605
Operating loss	(5,027)	(11,247)	(14,784)	(25,422)
Other (expense) income				
Interest expense	(8,643)	(9,007)	(9,045)	(10,053)
Interest income	3,108	2,664	2,570	2,173
Loss from continuing operations	(10,562)	(17,590)	(21,259)	(33,302)
Discontinued operations	(137)	(526)	47	(394)
Net loss	$ (10,699)	$ (18,116)	$ (21,212)	$ (33,696)
Basic and diluted net income (loss) per share:				
From continuing operations	$ (0.39)	$ (0.63)	$ (0.76)	$ (1.17)
From discontinued operations	(0.00)	(0.02)	0.01	(0.01)
Net loss per share	$ (0.39)	$ (0.65)	$ (0.75)	$ (1.18)

Notes to Consolidated Financial Statements—(Continued)

Note 19—Quarterly Results of Operations (Unaudited)—(Continued)

	QUARTER ENDED 1996 (UNAUDITED)			
	MARCH 31	JUNE 30	SEPTEMBER 30	DECEMBER 31
	(IN THOUSANDS)			
Operating revenues				
Telecommunications services	$ 7,763	$ 7,678	$ 9,169	$ 14,367
Information services	6,014	8,662	11,017	15,661
Total operating revenues	13,077	16,340	20,186	30,028
Operating expenses				
Cost of services and products	12,959	15,908	19,621	32,529
Selling, general and administrative expenses	29,553	39,228	41,135	47,043
Depreciation and amortization	3,501	4,896	7,077	14,227
Total operating expenses	46,013	60,032	67,833	93,799
Operating loss	(32,936)	(43,692)	(47,647)	(63,771)
Other (expense) income				
Interest expense	(10,798)	(20,194)	(22,082)	(24,183)
Interest income	2,235	5,090	3,727	6,525
Other income	—	—	2,219	—
Loss from continuing operations before income tax benefit	(41,499)	(58,796)	(63,783)	(81,429)
Income tax benefit	—	—	—	2,500
Loss from continuing operations	(41,499)	(58,796)	(63,783)	(78,929)
Loss from discontinued operations	(477)	—	(1,500)	(4,500)
Net loss	$ (41,976)	$ (58,796)	$ (65,283)	(83,429)
Basic and diluted net loss per share				
From continuing operations	$ (1.27)	$ (1.85)	$ (1.97)	$ (2.37)
From discontinued operations	(0.02)	—	(0.04)	(0.13)
Net loss per share	$ (1.29)	$ (1.85)	$ (2.01)	$ (2.50)

The financial data presented above reflects certain reclassifications from the amounts presented in the Company's filings on form 10-Q for the periods ending March 31, June 30 and September 30, 1996. The reclassifications principally relate to the breakout of revenues by operating segment and the reclassification of certain telecommunication network costs from the selling, general and administrative caption to the cost of services and products caption.

Note 20—Discontinued Operation—WinStar Global Products, Inc.

On May 13, 1997, a formal plan of disposal for the Company's consumer products subsidiary, Global Products, was approved by the Board of Directors, and it is anticipated that the disposal will be completed within the next 12 months. The disposal of Global Products has been accounted for as a discontinued operation and, accordingly, its net

Notes to Consolidated Financial Statements—(Continued)

Note 20—Discontinued Operation—WinStar Global Products, Inc.—(Continued)

assets have been segregated from continuing operations in the accompanying consolidated balance sheets, and its operating results are segregated and reported as discontinued operations in the accompanying consolidated statements of operations and cash flows.

Information relating to the discontinued operations of Global Products is as follows (in thousands of dollars):

	FOR THE TEN MONTHS ENDED DECEMBER 31, 1995	FOR THE YEAR ENDED DECEMBER 31, 1996	FOR THE YEAR ENDED DECEMBER 31, 1997
Operating revenues	$13,986	$19,429	$ 15,665
Cost of services and products	8,833	13,903	17,534
Selling, general & administrative	4,289	5,323	8,393
Depreciation and amortization	183	245	464
Total operating expenses	$13,305	$19,471	$ 26,391
Operating income (loss)	681	(42)	(10,726)
Interest expense, net	(444)	(968)	(854)
Net income (loss)	$ 237	$ (1,010)	$(11,580)

	DECEMBER 31, 1996	DECEMBER 31, 1997
Assets:		
Accounts receivable, net	$ 4,499	$ 4,383
Inventories	8,606	4,663
Other assets	2,143	1,268
Total Assets	15,248	10,314
Liabilities:		
Current liabilities	3,102	3,570
Other liabilities	8,332	9,951
Total liabilities	11,434	13,521
Net assets (deficit)	$ 3,814	$ (3,207)

During the year ended December 31, 1997, the Company reduced the carrying amount of its investment to $2,105,000 and recorded a loss on discontinued operations of $6,477,000.

Note 21—Condensed Financial Information of WinStar Equipment Corp. and WinStar Equipment II Corp.

The Company's wholly-owned subsidiaries, WEC and WEC II, each of which is a special purpose corporation which was formed to facilitate the financing and purchase of telecommunications equipment and related property ("Designated Equipment"), received $200.0 million and $50.0 million in gross proceeds, respectively, from the issuance and sale of 12.5% Guaranteed Senior Secured Notes in placements of debt in March and August of 1997, respectively (see Note 7). The use of the proceeds of the Guaranteed Senior Secured Notes are to be used to purchase designated equipment and, if such equipment is not purchased within a specified period, WEC and WEC II must apply unused proceeds thereof to redeem the WEC and WEC II Notes, respectively. Both the interest and principal of the WEC Notes are guaranteed by the Company.

WEC and WEC II have no independent operations other than to purchase designated equipment to lease same to the Company's other telecommunications subsidiaries. Given this operating environment, it is unlikely, in the

Notes to Consolidated Financial Statements—(Continued)

Note 21—Condensed Financial Information of WinStar Equipment Corp. and WinStar Equipment II Corp.—(Continued)

opinion of management, that WEC or WEC II will generate sufficient income, after the payment of interest on the WEC and WEC II Notes, to pay dividends or make other distributions to the Company.

Summary financial information of WEC and WEC II, which are included in the consolidated financial statements of the Company, are as follows (in thousands):

Balance sheet information at December 31, 1997:

	WEC	WEC II
Current assets	$ 144,004	$ 48,394
Long-term assets	71,424	2,660
Current liabilities	(25,601)	(2,432)
Long-term liabilities	(200,000)	(50,000)
Stockholders' deficit	$ (10,173)	$ (1,378)

Statements of operations information for WEC for the period from its inception through December 31, 1997, and for WEC II for the period from its inception through December 31, 1997, are as follows (in thousands):

	WEC PERIOD FROM MARCH 13, 1997 (INCEPTION) TO DECEMBER 31, 1997	WEC II PERIOD FROM AUGUST 8, 1997 (INCEPTION) TO DECEMBER 31, 1997
Rental revenues from other WinStar subsidiaries	$ 854	$ —
Interest income from other WinStar subsidiaries	1,207	—
Interest income—investments	7,765	1,105
Selling, general and administrative expenses	(1,470)	—
Interest expense	(18,529)	(2,483)
Net loss	$(10,173)	$(1,378)

Separate financial statements concerning WEC or WEC II are not presented because management of the Company has determined that such information would not provide any material information that is not already presented in the condensed consolidated financial statements of the Company.

Note 22—Employee Benefit Programs

The Company has a defined contribution 401K Plan for substantially all full time employees. The Company makes a 25% matching contribution up to 6% of participant's compensation, subject to certain limitations. The Company contribution vests over a five year period. Company contributions to date have not been significant.

Note 23—New Accounting Pronouncements

The Financial Accounting Standards Board released Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" (SFAS No. 130), governing the reporting and display of comprehensive income and its components, and Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information" (SFAS No. 131), requiring that all public businesses report financial and descriptive information about their reportable operating segments. The Company will implement SFAS 130 and SFAS 131 as required in 1998. The impact of adopting SFAS No. 130 is not expected to be material to the consolidated financial statements or notes to consolidated financial statements. Management is currently evaluating the effect of SFAS No. 131 on consolidated financial statement disclosures.

Note 24—Subsequent Event (unaudited)

In March 1998 the company issued an aggregate of $650.0 million of notes and preferred stock consisting of $200.0 million of 10% Senior subordinated Notes Due 2008, $250.0 million of 11% Senior Subordinated Deferred Interest Notes Due 2008 and $200.0 million of Series D 7% Senior Cumulative Convertible Preferred Stock Due 2010.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS ON SCHEDULE

Board of Directors
WinStar Communications, Inc.

In connection with our audit of the consolidated financial statements of WinStar Communications, Inc. and Subsidiaries referred to in our report dated February 12, 1998, which is included in this Annual Report on Form 10-K, we have also audited Schedule II for the ten months ended December 31, 1995 and the years ended December 31, 1996 and 1997.

In our opinion, this schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information required to be set forth therein.

GRANT THORNTON LLP

New York, New York
February 12, 1998

WINSTAR COMMUNICATIONS, INC. AND SUBSIDIARIES

Schedule II—Valuation and Qualifying Accounts

COLUMN A	COLUMN B	COLUMN C	COLUMN D	COLUMN E
DESCRIPTION	BALANCE AT BEGINNING OF PERIOD	ADDITIONS CHARGED TO COSTS AND EXPENSES	DEDUCTIONS	BALANCE AT END OF PERIOD
Reserves deducted from assets to which they apply:				
Year ended December 31, 1997				
Allowance for doubtful accounts(a)	$851,512	$5,674,018	$2,706,274(b)	$3,819,256
Year ended December 31, 1996				
Allowance for doubtful accounts(a)	$684,355	$1,818,521	$1,651,364(b)	$ 851,512
Ten months ended December 31, 1995				
Allowance for doubtful accounts(a)	$740,688	$ 852,425	$ 908,758(b)	$ 684,355

(a) Deducted from accounts receivable

(b) Uncollectible accounts receivable charged against allowance

WINSTAR

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New York, NY 10169
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Fax: 212.867.1565

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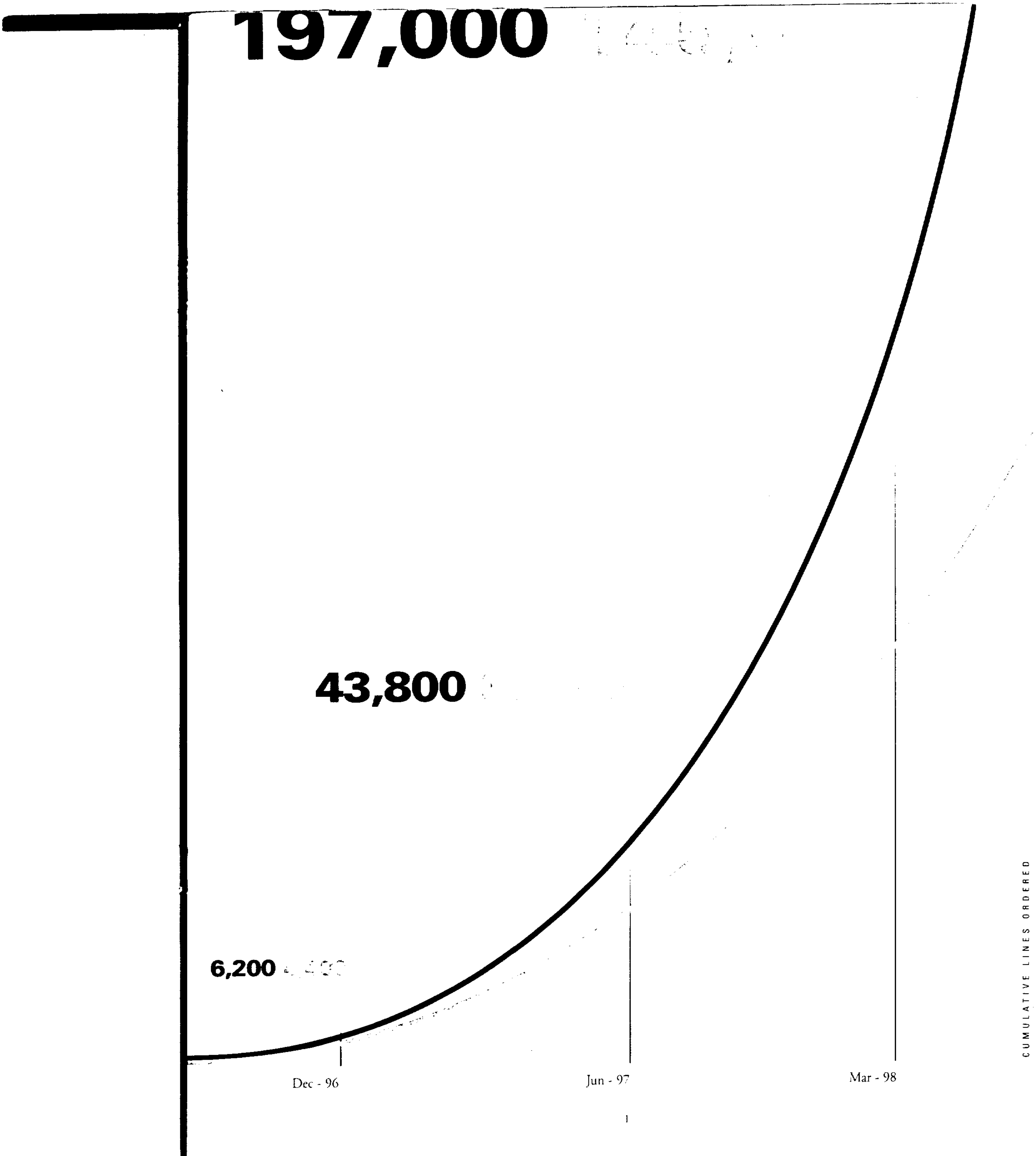
WINSTAR® 1997 Annual Report


197,000
43,800
6,200
Dec - 96
Jun - 97
Mar - 98
CUMULATIVE LINES ORDERED

To Our Shareholders, Employees and

WILLIAM J. ROUHANA, JR.

n 1997, we got our first view of just how vast the demand for broadband telecommunications capacity is in the U.S., and how uniquely positioned WinStar is to meet this demand and translate it into a meaningful business opportunity.

Our accomplishments over the past year extended to every corner of the company. They highlighted the superiority of our Wireless Fiber℠ solution for extending fiber networks, and they propelled us to a position where we are ready to grow our business significantly. By year end, we had gained the critical mass of people, systems, network and marketing firepower necessary to establish a large and successful phone company. The investment community began to take active note of the progress we made, and WinStar's share price has

"Our employees are totally committed to WinStar's mission: bringing people into the information age through high-quality wireless broadband services, and helping our customers use our network to productively share information with each other."

WILLIAM J. ROUHANA, JR.
CHAIRMAN & CHIEF EXECUTIVE OFFICER

more than tripled since I last wrote to you. Although we were pleased by this turn of events, we believe WinStar's current stock price has only begun to reflect the true value of our company.

A Strong Emphasis on Rapid & Robust Growth

The major expansion of WinStar's network over the past year shows our strong emphasis on rapid growth. Today, WinStar is offering services in 21 major metropolitan markets, in contrast to one at the close of 1996. By the end of 1998, we expect to provide switched services in 30 cities, 12 months ahead of our original schedule.

Our network is not only larger than it was a year ago, it's far more robust, providing for the high-speed transport of broadband data and voice traffic. In January 1998, we acquired GoodNet, a Tier I Internet service provider with a national backbone and points-of-presence in 27 cities across the country. We are incorporating its network of ATM data switches into our national local network. We also acquired the PacNet data network the same month, adding 17 frame relay switches plus a direct connection to the Unispan consortium which routes frame relay traffic throughout the U.S. and internationally. Now WinStar can provide customers with a choice of Internet, ATM and frame relay modes of data transmission, in addition to a full complement of local and long distance voice services.

WinStar's network will further evolve in 1998, as we take steps to aggregate voice and data traffic onto a leased long distance fiber backbone that will interconnect *all* our switches. We should realize substantial economies and efficiencies from this integration.

Using a Successful & Superior Networking Model

We believe that our fixed wireless broadband solution for networking customer buildings is clearly superior to the approach used by companies that rely on fiber-based connections. There are several key reasons for this: our lower deployment costs, our ability to reach thousands of buildings that fiber cannot serve economically, and the high percentage of customer traffic we'll be able to carry on our own network. We estimate that, over time, at least two thirds of our lines will be on our own network, and therefore unaffected by provisioning systems and cost issues impacting lines leased from the incumbent local exchange carrier. These on-net lines will give us excellent profitability and greater control over the type and quality of service we provide to customers.

Our recent experience in our first market, New York City, demonstrates that our model works, and works exceptionally well. We began by reselling long distance services while we were building our switch, establishing hub sites and obtaining roof rights. We then gradually moved an increasing percentage of our lines onto our network as it was built. By year-end 1997, 13 months after we launched our service, more than 50% of our New York lines were on our own network; and an even greater percentage of lines were installed on our Lucent 5ESS switch. We expect this experience to be repeated in each of our cities as WinStar extends its network to a total of 40 markets by the end of 1999.

Extending Our Service Capabilities to the 50 Largest U.S. Markets

The value of our radio spectrum holdings, which represent WinStar's core asset, was substantially enhanced in 1997 and early 1998. This came about through the addition of new spectrum licenses, and favorable rulings from the FCC on how we can use our spectrum. In the fall of 1997, the FCC set out new rules permitting 38 GHz licensees to hold up to the full 1,400 MHz of spectrum available in a given market, while also allowing utilization of that spectrum for a wide range of fixed or mobile communications services.

As a result of license acquisitions, grants, and our participation in the LMDS auction, WinStar's potential service area has been extended to include all 50 of the largest U.S. markets. Our bandwidth holdings in those key markets now average approximately 740 MHz. WinStar's coverage area encompasses *more than 200 million people* and over one billion channel pops (covered population times the number of 100 MHz equivalent channels).

Setting a New Standard with a Point-to-Multipoint System

The competitive value and utility of our spectrum holdings will be further enhanced beginning in the latter part of 1998, when we expect to start deploying our point-to-multipoint wireless network on a commercial basis. This is a major development for the company and an entirely new paradigm for our industry.

Point-to-multipoint systems will enable us to install radios with 155 Mbps data rates and higher on a customer building for a capital cost of as little as $4,000 per incremental building as our rollout reaches national scale in 1999. This data rate is triple the speed of current point-to-point radios which have capital costs of about $20,000 per building. Our point-to-multipoint technology has many other important benefits, including an ATM over-the-air interface to carry voice, video and data traffic over a single network, and the ability to provide bandwidth on demand to our customers.

Our successful advanced testing of the technology reenforces our belief that we can deliver a rich blend of essential services, ranging from voice and data communications, LAN-LAN interconnections and MPEG-2 video, to high-speed Internet access and distance learning. This will be the *Information Superhighway* in operation.

Building Toward a Much Bigger Future

The national deployment of services, systems, switches, and people on the large scale and accelerated schedule we are pursuing is expensive. However, the infrastructure we are putting in place today will support the needs of the far larger company we expect to become over the next several years. We have met with great success in raising the capital to build our network. Between January 1997 and April 1998 alone we secured more than $1.4 billion in debt and equity financing. The receptivity to our securities offerings is a solid vote of confidence in our business plans and investment decisions.

During 1997, we also saw significant growth in WinStar's New Media business which develops information content targeted to the business, educational and consumer markets. Their services help drive usage of the bandwidth we provide our customers and differentiate us from other telecommunications companies. They also strengthen the loyalty of our customers by helping them become more productive through our broadband connectivity and improved access to interactive services. This is how we enable the true convergence of broadband connectivity, computer technology and content.

In 1997, we also added significant depth and breadth to our already strong managment team. This led, among other things, to the formation of a stand-alone broadband services unit to spearhead the development of our data business, and to the creation of a new division concentrating on the acquisition of building access rights. In a related vein, the deployment of a new sales force to call on large businesses expanded our focus to a previously unaddressed market segment.

These initiatives gave us three major sources of telecommunications revenues: voice services for small and medium-sized businesses, voice services for large businesses, and broadband data services. WinStar's now broadened universe of potential customers is quickening the pace of our orders and installations.

Addressing Our Business Priorities for 1998

For 1998, our priorities focus on executing our plan to deploy WinStar's network and systems to 30 cities. The valuable lessons we learned in 1997 are being applied in 1998. We expect to increase efficiency as we add sales volume to our growing infrastructure. We will also continue to analyze potential acquisitions that can lead to greater utilization of our network or enhance our service offerings. At the same time, we remain extremely focused on the goal of gradually reducing EBITDA losses from the inflection point we reached in the fourth quarter of 1997.

During 1998, we also expect to begin leveraging our expertise in creating fixed wireless communications networks in markets *outside* the U.S. The demand for bandwidth is a global phenomenon, and our approach to meeting it is not limited to national boundaries. Over the near term, we will likely seek spectrum rights in Canada, Europe and other regions. We could be in a position to launch some operational networks in 1999.

Our employees are totally committed to WinStar's mission: bringing people into the information age through high-quality wireless broadband services, and helping our customers use our network to productively share information with each other. Of the more than 180 million local loop connections that make up the U.S. telecommunications network, only a fraction have been upgraded to broadband status. This means we have an amazingly large business opportunity.

I look forward to keeping you updated on how WinStar is taking advantage of this great opportunity, and transforming it into value for our shareholders, customers, employees and community. In the meantime, I would like to thank all of you, and particularly our employees, for your tremendous enthusiasm and support, and for sharing WinStar's vision of the future, a future we are beginning to turn into a reality.

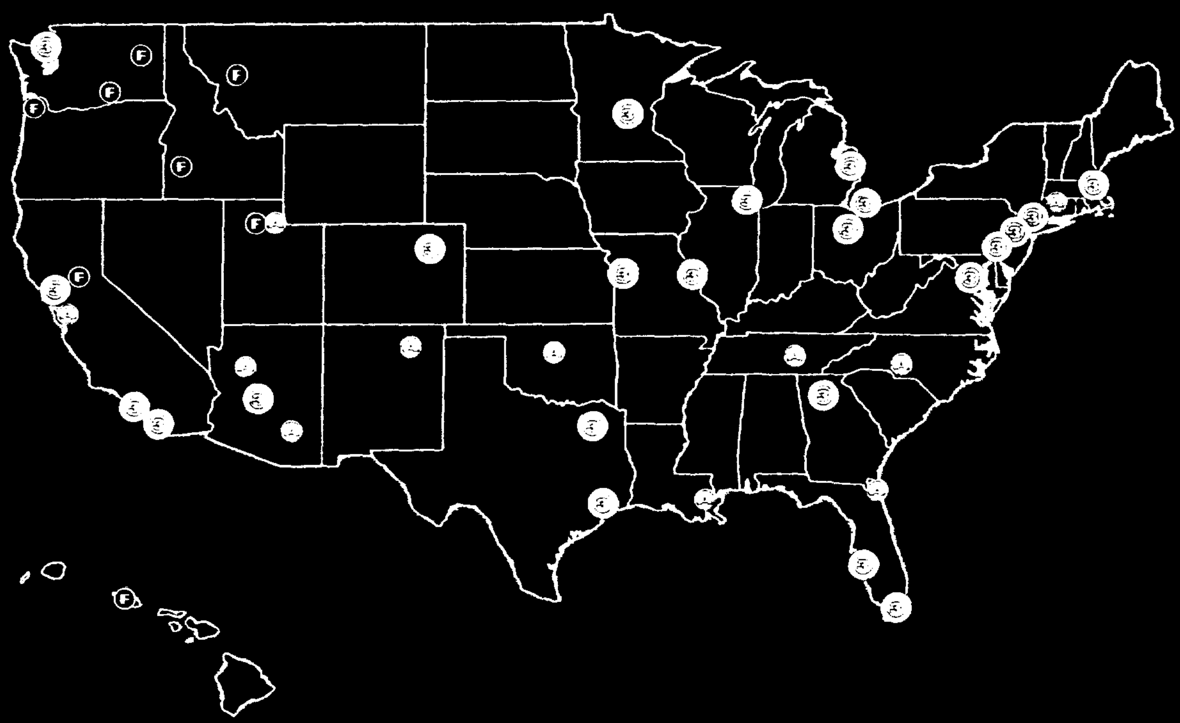
WILLIAM J. ROUHANA, JR.
CHAIRMAN & CHIEF EXECUTIVE OFFICER

April 24, 1998

Report on Operations

WINSTAR'S NATIONAL NETWORK

(Illustration includes switches planned for deployment in 1998)



FRAME RELAY SWITCH

ATM SWITCH

VOICE SWITCH, FRAME RELAY SWITCH AND ATM SWITCH PRESENT

We're Making Excellent Progress with Operations Nationwide

We made excellent progress developing WinStar's nationwide operations in 1997, and equally impressive strides in the first months of 1998. WinStar has extremely ambitious goals, and our employees are rising to these challenges with great enthusiasm and ingenuity.

Looking at revenues, our core telecommunications business began to take on significant scale in 1997: we ended the calendar year at a $62 million annualized revenue run rate, as the growth in CLEC operations more than compensated for an anticipated $21 million decline in our residential long distance business, which is no longer an area of focus for the company.

It was also an outstanding year for WinStar's information services business, where sales soared 182%, or almost $27 million over 1996. This was due to excellent demand for information content developed by our New Media subsidiary, and to the acquisition of Telebase, a leading developer of online business information services.

Total operating revenues reached approximately $80 million, a gain of more than 60% from the prior year. At the end of the 1998 first quarter, the revenue run rate for our consolidated operations had risen to $230 million as a result both of internal growth and acquisitions.

NATHAN KANTOR

WinStar's telecommunications *network* has grown substantially since the installation of our first local network switch only 17 months ago. Looking toward the end of this year, we plan to have 23 Lucent 5ESS switches installed, and an additional 29 ATM switches and 17 frame relay switches in service. This extensive switching capability should increase again in 1999.

We're Fielding a Direct Sales Force of Trained Professionals

To generate traffic for WinStar's expanding network, we've built a professional field sales force to call directly on potential business customers. More than 800 WinStar sales and service representatives have been trained to assist customers with total solutions to their telecommunications needs; including data specialists and salespeople concentrating solely on large businesses.

The rewards of this investment have come in the form of continually rising flows of line orders and installations. Cumulative line orders reached 118,000 at the end of 1997, an encouraging conclusion for a 12-month period that started with only about 6,000 ordered lines. We achieved further gains in the first quarter of 1998, when cumulative orders rose to nearly 200,000. Our base of installed lines expanded over thirty-fold, from 4,400 at the beginning of 1997, to 82,000 as of December 31, to 145,000 at the end of the first quarter of 1998. The cumulative orders and installations reported for March 1998 included some 24,500 lines acquired with our new broadband data businesses. However, WinStar's ongoing rate of installation already exceeds 40,000 lines per quarter. The number of quarterly installations should continue to rise as our services come on stream in additional major cities.

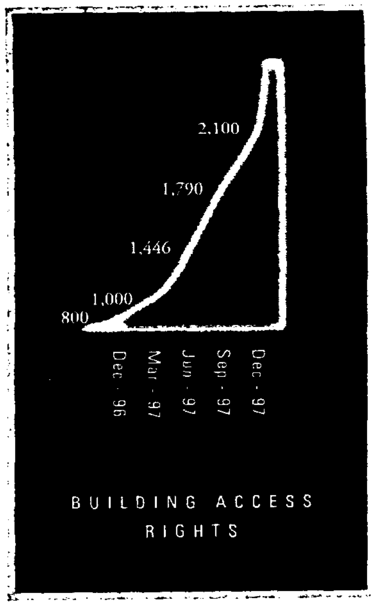
We're Gaining Momentum with Hub Sites, Access Rights & Interconnect Agreements

Creating hub sites, to collect traffic from customer buildings and route it to our switches, is essential to the successful buildout of our network. From no completed hubs at the beginning of 1997, within 15 months we had over 50 in service. Meeting our target for 1998 will bring the total to more than 100.

Wireless connectivity to our hubs hinges on our success in obtaining building access rights to install a small antenna and radio atop customer buildings. This makes access rights a second critical factor in deploying our wireless network nationwide. Accordingly, we're giving this effort a significant amount of focused attention. During 1997, the number of building access rights held by WinStar climbed to 2,100, versus 800 in 1996. We are finding that building owners increasingly recognize the value of having broadband telecommunications services available to tenants within their buildings. In 1998, we're broadening our rights acquisition program to include negotiations with REITs and other property owners and managers who control large numbers of commercial office buildings. By year-end, we expect to have gained access to a total of 4,000 locations.

Clearly, WinStar's network cannot be of true value without connecting it to the national telecommunications system. Doing so requires us to negotiate individual agreements with the Regional Bell Operating Companies (RBOCs) and other established local and long distance carriers. It's well worth noting that WinStar has made interconnect agreements that today cover 44 of the top 50 U.S. markets. Additionally, the company has peering arrangements with more than 130 U.S. and foreign Internet service providers.

CLEC authorizations represent a fourth crucial building block for a national telecommunications provider like WinStar, and our progress here has been very satisfactory. We currently have authorizations applying to 48 of the largest markets in the country. That's up considerably from 30 markets at the end of 1996.



We're Investing Heavily in Customers and the Future

The fact is, WinStar's combination of innovative service offerings, value-based pricing and passion for customer satisfaction is being met with great enthusiasm in the marketplace. We have quickly built a solid base of more than 7,000 customers. Our rate of customer acquisition remains on a strong upswing, and our services are being enhanced by the most advanced operational and business support systems in the industry. This is a critical area for the company, and we continue to make substantial investments in order entry, order provisioning, billing and network management systems. We have also designed new network elements to support the deployment of WinStar's point-to-multipoint technology, commencing later this year. It is equally gratifying to report that WinStar's wireless network achieved a 99.999% ("five-nines") level of availability in 1997. This accomplishment proved that our unique approach to providing broadband connectivity is of the utmost quality and reliability.

WinStar's success is being further supported by an aggressive marketing program which incorporates media advertising and a wide range of special activities conducted inside our target buildings. Our marketing themes differentiate WinStar from other service providers and encourage heightened expectations among our potential customers. Once they experience WinStar's services, we work with our customers to handle an increasing amount of their communications requirements, and integrate WinStar into their business. This approach has been highly effective.

We're looking ahead and working toward even greater achievements in 1998. We're supremely confident about the unique and talented group of employees we have at WinStar, and the bright new people we are attracting, who are delivering on our promise: "See things from a phone company you've never seen before."

NATHAN KANTOR
PRESIDENT & CHIEF OPERATING OFFICER

April 24, 1998

With the deployment of our revolutionary point-to-multipoint (PMP) technology, there are hundreds of thousands of buildings we can reach and connect with high-speed telecommunications servi[illegible] We're going to bring the people in those buildings all the features and benefits of today's and tomorrow's Information Superhighway.

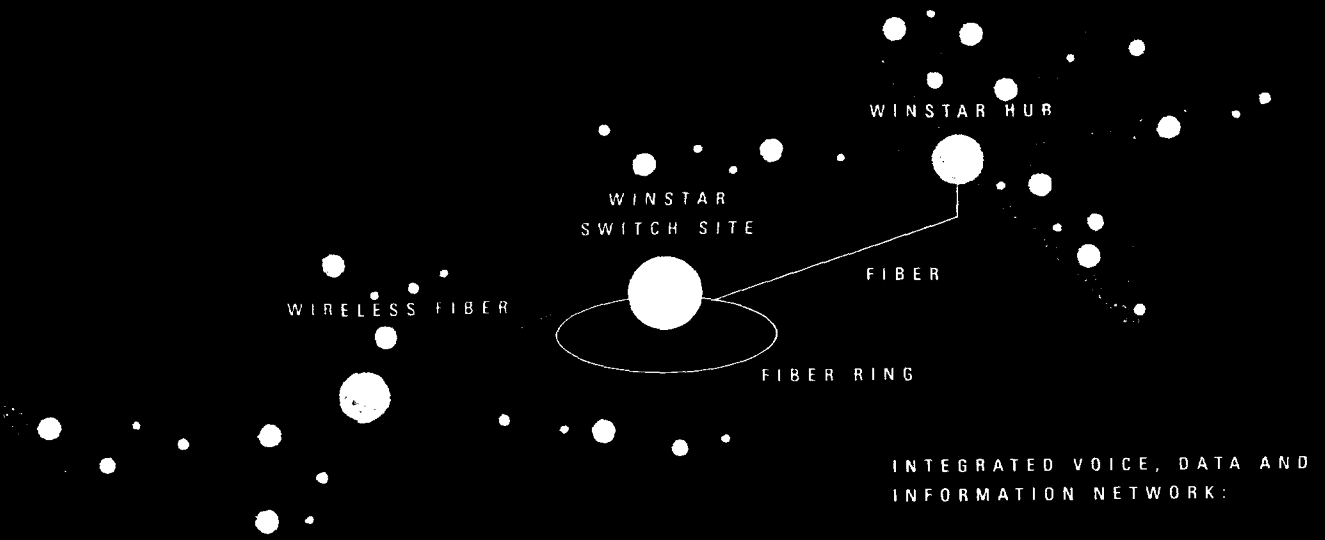
This rich, new and extremely robust networking approach significantly expands our ability to service many more customers, and dramatically lowers the cost of reaching them. It also creates a totally new paradigm for broadband local networks: marking the first time that voice, data and video capabilities have been integrated into one network.

Point-to-Multipoint is a *line-of-sight* technology. It begins at our hub sites, where we have a universe of buildings in our sight, a universe that includes customers located in buildings as small as 20,000 square feet. It's an affordable and relatively easy-to-install alternative to the higher cost, old wireline technology systems offered by the country's entrenched monopoly carriers. When the buildout of the company's hubs is complete in our 50 major target markets, we'll be able to see from our hub sites and reach close to 75% of all commercial office buildings in these cities.

Lacking broadband connectivity, these buildings can be classified as "access disadvantaged." As such, they're perfect candidates to benefit from our PMP "on ramp," which will be able to connect them - with bandwidth-on-demand - to the nation's telecommunications infrastructure, and to the current and future Information Superhighway.

WinStar's hub sites each provide line-of-sight to hundreds of buildings which can be served by the company's wireless broadband network.

Fixed wireless broadband communications is not cellular service. It's a high capacity communications channel that matches the performance and quality of fiber-based networks and systems. Connections are made through the air by way of antennae on building roofs. Service is delivered faster and less expensively than by fiber, and isn't vulnerable to construction-related outages involving cut cables. With point-to-multipoint technology, WinStar doesn't have to build specific pipes to each building, or try to fill them. Our virtual "pipe" can get bigger or smaller as demand increases or lessens; the cost to our customer is based on actual bandwidth use, not on capacity that is unused. These significant cost advantages, coupled with our strong service edge, make a compelling argument for customers to switch to WinStar from other local exchange carriers.



INTEGRATED VOICE, DATA AND INFORMATION NETWORK:

- VOICE TELEPHONE
- FAX
- HIGH-SPEED INTERNET
- FIXED OR VARIABLE-RATE DATA
- NATIVE LAN TO LAN
- VIDEO CONFERENCING
- INFORMATION SERVICES

Students and teachers at The Holy Name of Jesus School in New York City use specialized software developed by WinStar to take maximum advantage of the educational content available through the Internet.

Education in America is undergoing a transformation, aimed at improving children's learning and giving them the skills they need to succeed in tomorrow's world. This transformation represents an evolution from "products of the muscle" to "products of the mind." In the future, the ability to access information, and use the tools of technology to analyze and creatively solve problems, will be the defining factor in determining who succeeds. WinStar is an active part of this big and important picture, guiding schools through the sea of new technology.

The Seven "C's" of Education and the Internet

WinStar has a strong and socially responsible vision for America's schools, intended to build the foundation of a nationwide community of lifelong learners. It begins with *connectivity:* getting schools connected to the Internet. Here, our Wireless Fiber service is an ideal technology, providing high-speed connectivity at a fraction of the price of conventional alternatives. *Content:* once connected, content is the critical issue. Our *NewsNow* program enables children to publish their content on the Web. *Context:* Our *LivingPage* enables schools to create their own electronic library, and students' electronic bibliographies for Web-based research. *Collaboration:* the true power of the Web is connecting minds to other minds. Programs like our *WebBoard, MindsEye Monster Exchange* and *The Journey* are bringing thousands of children from hundreds of schools around the world into collaboration. *Creativity:* essential to creating value. We're building a suite of creative problem-solving tools, and working with top experts in the field to develop an Internet curriculum. *Commerce:* children must learn the fundamentals of electronic commerce. We'll be introducing tools and programs to give them great hands-on experience. *Community:* we're dedicated to improving communities through the creative use of telecommunications. In the nation's capital, we took the lead in forming a broad business and community coalition involving D.C. public schools, the D.C. public library and various foundations and groups, with the goal of making a significant difference, and closing the "digital divide" for inner city families. Vice President Al Gore hailed it as a model for the nation.

Everyone focuses on the content, yet that's only 10% of the equation. 90% is the process of collaboration. It's not about connecting children with other computers and Web pages, it's about connecting their minds with other minds. This is the true power of the Internet.

Creating a Model for America's Communities

We're about to link an inner city housing project in Washington, D.C. with neighborhood elementary, middle and high schools, and a local senior citizens home. The Internet environment we're creating is extending the schools into the home, and opening the door to rich, cross-generational communication between seniors and children. WinStar is today's new phone company not only in terms of its technology, but also in terms of our passionate sense of social responsibility to the country's schools and communities.

Consolidated Statements of

(In thousands, except per share data)

	FOR THE TEN MONTHS ENDED DECEMBER 31,	FOR THE YEAR ENDED DECEMBER 31,	
	1995	1996	1997
Operating revenues			
Telecommunications services — commercial	$ 130	$ 4,487	$ 29,796
Telecommunications services — residential	13,007	29,482	8,481
Information services	2,648	14,650	41,354
Total operating revenues	15,785	48,619	79,631
Operating expenses			
Cost of services and products	12,073	38,233	81,017
Selling, general and administrative expenses	13,617	62,365	156,959
Depreciation and amortization	1,027	4,501	29,701
Total operating expenses	26,717	105,099	267,677
Operating loss	(10,932)	(56,480)	(188,046)
Other (expense) income			
Interest expense	(7,186)	(36,748)	(77,257)
Interest income	2,890	10,515	17,577
Other (expense) income	(866)	–	2,219
Loss from continuing operations before income tax benefit	(16,094)	(82,713)	(245,507)
Income tax benefit	–	–	2,500
Loss from continuing operations	(16,094)	(82,713)	(243,007)
Income (loss) from discontinued operations	237	(1,010)	(6,477)
Net loss	(15,857)	(83,723)	(249,484)
Preferred stock dividends	–	–	(5,879)
Net loss applicable to common stockholders	$(15,857)	$ (83,723)	$(255,363)
Basic and diluted income (loss) per share:			
From continuing operations	$ (0.71)	$ (2.96)	$ (7.49)
From discontinued operations	0.01	(0.04)	(0.19)
Net loss per share	$ (0.70)	$ (3.00)	$ (7.68)
Weighted average shares outstanding	22,770	27,911	33,249

(Please refer to the company's Form 10-K for complete financial information)

Consolidated Balance Sheets

(In thousands)

	DECEMBER 31, 1996	DECEMBER 31, 1997
ASSETS		
Current assets		
Cash and cash equivalents	$ 95,490	$ 402,359
Short term investments	26,997	16,903
Cash, cash equivalents and short term investments	122,487	419,262
Investments in equity securities	688	—
Accounts receivable, net of allowance for doubtful accounts of $852 and $3,819, respectively	13,150	30,328
Inventories	5,009	10,296
Prepaid expenses and other current assets	15,969	8,985
Net assets of discontinued operations	3,814	2,105
Total current assets	161,117	470,976
Property and equipment, net	62,572	284,835
Licenses, net	27,434	174,763
Intangible assets, net	12,955	14,293
Deferred financing costs, net	10,535	27,463
Other assets	4,176	4,071
Total assets	$ 278,789	$ 976,401
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities		
Current portion of long-term debt	$ 19,901	$ 386
Account payable and accrued expenses	29,442	97,714
Current portion of capitalized lease obligations	3,110	6,848
Total current liabilities	52,453	104,948
Capitalized lease obligations, less current portion	10,846	21,823
Long-term debt, less current portion	265,161	768,469
Deferred income taxes	—	24,000
Total liabilities	328,460	919,240
Series C exchangeable redeemable preferred stock, liquidation preference of $175,000 plus accumulated dividends	—	175,553
Commitments and contingencies		
Stockholders' equity (deficit)		
Series A preferred stock issued and outstanding 3,910 shares at December 31, 1997	—	39
Common stock, par value $.01; authorized 200,000 shares, issued and outstanding 28,989 and 34,610, respectively	290	346
Additional paid-in-capital	75,436	255,741
Accumulated deficit	(125,034)	(374,518)
	(49,308)	(118,392)
Unrealized loss on investments	(363)	—
Total stockholders' deficit	(49,671)	(118,392)
Total liabilities, exchangeable redeemable preferred stock and stockholders' deficit	$ 278,789	$ 976,401

(Please refer to the company's Form 10-K for complete financial information)

Consolidated Statements of Cash Flows

(In thousands)

	FOR THE TEN MONTHS ENDED DECEMBER 31,	FOR THE YEAR ENDED DECEMBER 31,	
	1995	1996	1997
Cash flows from operating activities:			
Net loss	$ (15,857)	$ (83,723)	$ (249,484)
Adjustments to reconcile net loss to net cash used in operating activities:			
Net (income) loss from discontinued operations	(237)	1,010	6,477
Depreciation and amortization	1,117	5,977	32,360
Deferred income tax benefit	—	—	(2,500)
Provision for doubtful accounts	855	1,562	5,674
Equity in unconsolidated results of AGT	866	—	—
Non cash interest expense	6,151	35,040	53,506
Decrease (increase) in operating assets:			
Accounts receivable	(4,216)	(3,838)	(24,026)
Inventories	(991)	(1,897)	(9,217)
Prepaid expenses and other current assets	(2,342)	(13,442)	510
Other assets	(865)	(1,940)	(178)
Increase in accounts payable and accrued expenses	4,911	9,795	50,306
Net assets provided by (used in) discontinued operations	90	(1,481)	(4,559)
Other, net	179	186	—
Net cash used in operating activities	(10,339)	(52,751)	(141,131)
Cash flows from investing activities:			
Investment in and advances to AGT	(5,704)	—	—
Decrease (increase) in short-term investments, net	(73,594)	46,597	10,094
Decrease (increase) in other investments, net	(7,497)	6,447	—
Purchase of property and equipment, net	(8,138)	(47,842)	(213,356)
Acquisition of licenses and other	—	(2,121)	(40,190)
Other, net	(499)	(1,619)	2,494
Net cash (used in) provided by investing activities	(95,432)	1,462	(240,958)
Cash flows from financing activities:			
Proceeds from (repayments) of long-term debt, net	224,200	(2,778)	410,585
Net proceeds from redeemable preferred stock	—	—	168,138
Net proceeds from equity transactions	11,259	6,295	104,781
Proceeds from equipment lease financing	6,998	8,345	9,912
Payment of capital lease obligations	(676)	(2,080)	(4,141)
Other, net	(898)	(1,010)	(317)
Net cash provided by financing activities	240,883	8,772	688,958
Net increase (decrease) in cash and cash equivalents	135,112	(42,517)	306,869
Cash and cash equivalents at beginning of period	2,895	138,007	95,490
Cash and cash equivalents at end of period	138,007	95,490	402,359
Short-term investments at end of period	73,595	26,997	16,903
Cash, cash equivalents and short-term investments at end of period	$211,602	$122,487	$ 419,262

(Please refer to the company's Form 10-K for complete financial information)

Delivering the next generation of telecommunications

WinStar Communications provides broadband telecommunications services to customers in major metropolitan markets throughout the United States. The company's integrated data and voice network, utilizing fixed wireless circuits in the 38 GHz band, can deliver high-speed communications to thousands of buildings and customers not being served by other broadband communications carriers.

WinStar's 38 GHz spectrum licenses represent the largest single holding of bandwidth in the U.S. They enable the company to quickly and cost efficiently extend its wireless broadband network to customer buildings. WinStar's spectrum licenses cover all 50 of the largest markets in the country, and more than 100 other cities, encompassing a total population of approximately 200 million.

WinStar's services are marketed through a rapidly growing direct sales force and service organization of more than 800 professionals. The company is passionate about customer satisfaction, and emphasizes individual solutions to telecommunications needs backed by personal service, the most advanced information systems and a network which is establishing new benchmarks for reliability.

Beyond providing local, long distance, broadband data and Internet services, WinStar develops specialized valued-added information content for customers linked to its digital network and for other users. The company's broadband network capacity enables customers to efficiently access this information.

The company employs more than 2,200 people and is headquartered in New York City.

Statistical Profile

March 31, 1998

Annualized Revenues	$230 million
Cumulative CLEC Lines Installed	148,000
Cumulative CLEC Lines Ordered	199,000
Customers with Installed Lines	7,100
Markets Served	21

Corporate Information

Board of Directors

William J. Rouhana, Jr.
Chairman & Chief Executive Officer
WinStar Communications, Inc.

Nathan Kantor
President & Chief Operating Officer
WinStar Communications, Inc.

Steven G. Chrust
Vice Chairman
WinStar Communications, Inc.

James I. Cash, Jr.
The James E. Robison Professor of Business Administration
Graduate School of Business Administration
Harvard University

Steven B. Magyar
Financial Consultant

William J. vanden Heuvel
Of Counsel
Stroock & Stroock & Lavan
Sr. Advisor
Allen & Company

Bert W. Wasserman
Executive Vice President &
Chief Financial Officer (retired)
Time Warner

Officers

William J. Rouhana, Jr.
Chairman & Chief Executive Officer

Nathan Kantor
President & Chief Operating Officer

Steven G. Chrust
Vice Chairman

Charles T. Dickson
Executive Vice President &
Chief Financial Officer

Timothy R. Graham
Executive Vice President &
General Counsel

David W. Ackerman
Executive Vice President
Business Development

Robert K. McGuire
President & Chief Operating Officer
WinStar Wireless

Stuart B. Rekant
President
WinStar New Media

David R. Schmieg
President & Chief Operating Officer
WinStar Telecommunications

Howard E. Taylor
President & Chief Operating Officer
WinStar Broadband Services

Richard J. Uhl
President & Chief Operating Officer
WinStar for Buildings

Ruth A. Shields
Executive Vice President &
Chief Operating Officer
WinStar New Media

SEC FORM 10-K AND STOCKHOLDER INQUIRES

Copies of the Company's Form 10-K for the fiscal year ended December 31,1997, as filed with the Securities and Exchange Commission, can be obtained without charge upon written request to: Manager of Investor Relations, WinStar Communications, Inc., 230 Park Avenue, Suite 2700, New York, New York 10169 Tel. (212) 584-4053 Fax. (212) 867-1565

INDEPENDENT AUDITORS

Grant Thornton LLP, New York, New York

TRANSFER AGENT AND REGISTRAR

Continental Stock Transfer and Trust Company, New York, New York

ANNUAL MEETING

Shareholders are invited to WinStar's Annual Meeting which will be held at 10:00 a.m. on Wednesday, June 10, 1998 at the Hotel Inter-Continental, 111 East 48th Street, New York, New York 10017

Except for any historical information contained herein, the matters discussed in this document contain forward-looking statements that involve risks and uncertainties which are described in the company's SEC reports, including the 10-K for the period ended December 31, 1997.

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Regulatory Counsel

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