

DECLARATION OF ERIC BRUNO

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EXHIBIT 35

REDACTED - FOR PUBLIC INSPECTION

November 11, 2003

United States of America
Telecommunications
Enterprise Telecom Services

Enterprise Telecom Services

Initiation of Coverage

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Enterprise Telecom; A Comeback Begins

Sector View:

New: 2-Neutral

Old: 2-Neutral

Investment conclusion

□ We initiate coverage of Enterprise Telecom Services and are optimistic regarding the industry's financial and operational streamlining, the consolidation that has occurred to date (and more to come), and cautiously optimistic regarding improving demand and pricing over the next year.

Summary

- We expect a cyclical up-tick, improving operational efficiencies, and industry consolidation to drive stabilizing revenues, improving margins and 10% EBITDA growth in 2004 for the commercial units of our covered Enterprise Carriers.
- We favor Carriers with greater high-end Enterprise exposure, particularly wholesale, and less SME. While competition remains intense across Enterprise telecom, we believe it is poised to improve in 2004 within the wholesale segment, while it is likely to intensify within SME.
- We believe the supply/demand imbalance has finally begun to stabilize. On the supply side, due to recent consolidation and selected bidder-ineligibility among the financially weaker carriers, we believe the bidding-group on a given contract has been reduced by almost 50% from '01's 8-10 bidders. On the demand side, we are seeing the early signs of improvement in key employment, technology sales (chips), and a proprietary Lehman Brothers Fortune 500 Survey.
- Enterprise coverage group valuations hover near 10-year lows - LVLT is our top recovery pick, while T is our best value pick.

Enterprise Telecom Services Launch:

We initiate specialized coverage of the Enterprise Telecom Services sub-sector of the US Wireline Telecom Services market, with an emphasis on carriers specializing in the high-end of the market (Wholesale/Large Enterprise), companies designated as "Enterprise Carriers". We are optimistic regarding the industry's financial and operational streamlining, outlook for 2004 revenue stabilization, margin improvement and EBITDA growth, the consolidation that has occurred to date (and much more to come), and cautiously optimistic regarding improving demand and pricing over the next year. *Please see our companion notes on AT&T, Sprint (FON), and Level (3) for company-specific information, as well as our forthcoming industry report (under the same title as this note) and company reports for extensive details developing the themes outlined in this note. We will be hosting an investor call today at 10:30 a.m. EST; the dial-in numbers: (800) 706-8249 (US), (706) 634-5881 (Intl), and 0(800) 953-0406 (UK toll-free), and the conference ID is 3972920.*

Figure 1: Enterprise Telecom Services Coverage Universe

Company Rating, Target & Enterprise Value						
Company	Ticker	Price	LEH Rating	Price Target	Enterprise Value \$B	Investment Thesis Synopsis
AT&T	T	\$19.08	1-OW	\$24	\$23.5	Dominant Large Enterprise Carrier; Good value & further margin improvement likely; Divs & FCF provide strong value support
Level 3	LVLT	\$5.33	1-OW	\$7	\$8.1	A wholesale leader & consolidator; Strong growth opps & dilution manageable; No liq. issues
MCI	MCI AV (when issued)	\$25.26	NR		\$11.7	Restructuring opportunity, with growth upside, but a lot to prove; await audited financials
Sprint	FON	\$15.22	2-EW	\$18	\$13.8	Local business supports FON-Commercial, growth limited; Strong value support at \$16

PLEASE SEE ANALYST(S) CERTIFICATION(S) ON PAGE 32 AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 33

Investment Thesis: Enterprise Telecom; A Comeback Begins

- We expect a cyclical up-tick, improved operational/financial efficiencies, and industry consolidation to drive stabilizing revenues, materially improved margins and 10% EBITDA growth in 2004 for the commercial units of the Enterprise Carriers in our coverage group. These factors are expected to drive increasing cashflows to equity holders via dividend increases, share buybacks, and operating free cashflow.
- In general, we favor Carriers with greater exposure to the high-end of Enterprise telecom, particularly Wholesale, and less exposure to SME. While competition is intense across the sector, we believe it is poised to improve in 2004 within the Wholesale market, while it is likely to intensify within SME, as the RBOCs aggressively attack that market. We believe Wholesale/Large Enterprise revenue comparisons and margins will improve throughout 2004, while SME revenues and margins remain weak.
- We believe that the supply/demand imbalance has finally begun to stabilize – on the supply side, we estimate that North American fiber route miles could be reduced by up to 30% within 1-2 years (already about 11% reduced) – on the demand side, we are seeing early signs of improvement in commercial bandwidth requirements (our Enterprise Demand Index and Fortune 500 Survey).
- Enterprise coverage group valuations hover near 10-year lows, as investor sentiment remains uniformly abysmal. High-end carriers with the most efficient networks and improving sequential revenues and margins offer compelling cyclical/recovery investments – Level (3) is our top pick in this regard – while AT&T is our best value pick.

Enterprise Carrier – Coverage Group Highlights:

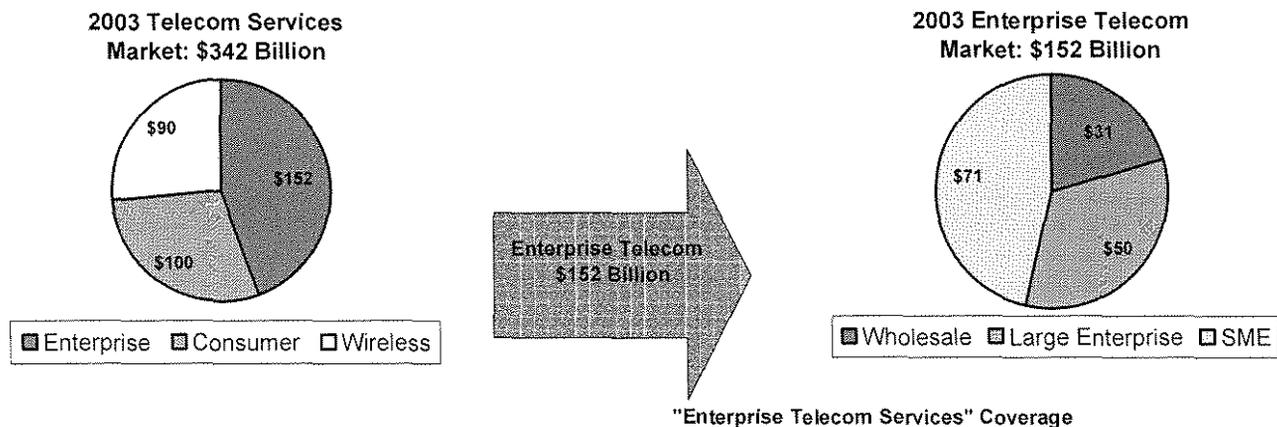
Within our Enterprise Telecom Services coverage universe, we include telecom carriers that derive more than 50% of their total revenues from commercial users, with an emphasis on carriers that specialize in service delivery to Large Enterprises (Fortune 1,000 enterprises) and Wholesale users. This includes the following coverage stocks:

- AT&T (1-OW, PT=\$24): Assumption of coverage with ratings and price target increases from 2-EW and \$22 respectively. AT&T is our top value pick in the group as it trades at a low 3.0x '04 EBITDA, has a 5% dividend yield and a massive \$3.5 billion in expected '04 FCF. We believe BS margins will expand 100 bps in '04, improving BS EBITDA growth to 1% (up from -12% in 2003). While consolidated revenues and EBITDA will still decline in '04, the CS drag is not as much as originally expected. Combined, these factors are driving a greater discounted value of cashflows, driving our upgrade on the stock. Likely further dividend increases or share buybacks in the next few months should also support the stock.
- Level (3) (1-OW, PT=\$7): Initiation of coverage as our top pick in the sector, given its pure-play Wholesale position, operating momentum, liquidity, and improving balance sheet. The company is experiencing sequential revenue growth and delivered 380 bps in sequential Communications EBITDA margin improvement in 3Q. We expect Communications revenues to grow 9% in '04, while EBITDA should grow 29%. Leverage and dilution are less of an issue as the company is FCF-positive, has no material debt maturities until '08, is more modestly 55% debt-to-enterprise value leveraged and no convertible strike prices until \$7.18.
- Sprint-FON (2-EW, PT=\$18): Assumption of joint coverage with its rating maintained at 2-EW, but an increased \$18 price target (up from \$14). We expect FON to cut costs aggressively in '04, which should drive 3% EBITDA growth, despite nearly 3% revenue declines. By 2006 we expect EBITDA margins to expand by more than 400 bps, driving our increased price target. Company has strong value support at \$16, an implied \$1,800 per local access line valuation, and a healthy balance sheet. Revenue growth will remain challenging, however, driving our maintained 2-EW rating.
- MCI (Not Rated): We are initiating coverage on the when-issued equity of MCI Communications, but await audited financials, more insight from management, and an exchange-traded equity before issuing a rating and price target. Operationally, we believe the company has significant upside opportunities, as highlighted in the company's bankruptcy disclosure documents, but also a lot to prove. Facilitating this opportunity is the company's increased financial flexibility, resulting from its restructured and lean balance sheet (approximately \$3.5 billion in net debt).

Enterprise Telecom Services – Defining the Industry:

In evaluating the overall Enterprise Telecom Services market, we include all the assets, financing, revenues and cashflows associated with the units servicing commercial customers. We have constructed our industry compilation using both bottom-up and top-down methodologies, factoring in data from internal sources, company feedback and FCC reports. Importantly, although we include all relevant information from any carrier selling commercial services in our industry compilation, we specifically define "Enterprise Carriers" within this report as carriers that specialize in service delivery to Large Enterprise and Wholesale customers and that receive more than 50% of their revenues from commercial clients. Therefore, the primary Enterprise Carrier segment is comprised of the incumbent IXC group (AT&T, MCI, Sprint), the emerging Network Carriers (Level (3) and its competitors), and the remaining CLECs. We estimate that the broad Enterprise market totals \$152 billion in 2003 revenue, or approximately 45% of the total telecom services market and 60% of the wireline services market. Within Enterprise, we estimate that \$31 billion is Wholesale (20% of Enterprise), \$50 billion is Large Enterprise (33%), and \$71 billion is SME (47%). Our research effort will focus on the Wholesale and Large Enterprise segments, where the Enterprise Carriers are best positioned to create long-term shareholder value. We outline the Enterprise market below.

Figure 22: Enterprise Telecom Services – A Massive Market with Distinct Segments


SME

- * Dominated by RBOCs & LECs
- * Highly fragmented
- * Less sophisticated services
- * Local/Regional Infrastructure Required
- * Key Products (wireline):
 - Local & LD Voice
 - T-1/fractional, DSL, low-end data

Large Enterprise

- * Dominated by AT&T, MCI, Sprint
- * '03 Mkt Shrs: T = 26%, MCI = 14%, FON = 8%
- * National/Global WAN & customer service/support infrastructure req. (many POPs)
- * Fortune 1,000 focus
- * Customized data/voice/network integration
- * Key Products (wireline):
 - Private LAN-to-WAN services
 - Dedicated Hi-cap circuits
 - Public IP access & security
 - LD & Local Voice (PBX)

Wholesale

- * Currently Dominated by AT&T, MCI
- * Sprint, Qwest, Level (3) are next tier
- * National/Global WAN & customer service/support infrastructure req. (fewer POPs)
- * Top 300 global users of bandwidth: IXCs, ILECs, CLECs, ISPs, PTTs, Cable, Sat.
- * Customized data/voice/network integration (with more real-time provisioning & service)
- * Key Products (wireline):
 - Similar to Large Enterprise, only more capacity, faster provisioning

Expected Enterprise Carrier Improvements:

We expect a cyclical up-tick, significant operational/financial improvements, and industry consolidation to drive stabilizing revenues, materially improved margins and 10% EBITDA growth in 2004 for the commercial units of the Enterprise Carriers in our coverage group. These factors are expected to drive increasing cashflows to equity holders via dividend increases, share buybacks, and growing operating free cashflow (OFCF).

- A modest cyclical up-tick, led by estimated 5% growth in 2004 Fortune 500 telecom service budgets (versus 5% declines in 2003), is expected to stabilize 2004 revenues for our Enterprise Carrier coverage group commercial revenues at -1% (versus -6% in 2003).
- A 25% reduction in headcount from 2000 to current has driven an 18% improvement in productivity per employee. Combined with the benefits of other massive network and systems cost/efficiency initiatives, we expect Enterprise Carriers to improve 2004 EBITDA margins 220 bps and grow EBITDA 10%.
- Industry consolidation, and bidding-ineligibility by weaker players, has reduced the number of bidders per contract from 8-10 in 2001 to 4-6 today. We expect increased financial slack resulting from reduced leverage to help drive ongoing consolidation of weaker, cashflow-negative carriers. Industry debt is down 58% from 2001 to 2003 (\$224 billion to \$95 billion) and debt/EBITDA has declined from 6.8x to 3.1x.

Figure 3: Expected 2004 & 2005 Enterprise Carrier Improvements

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003f</u>	<u>2004f</u>	<u>2005f</u>
Enterprise Industry:						
Revenue Growth	13.7%	1.6%	-7.0%	-4.7%	2.1%	4.6%
bp Change		-1210 bp	-860 bp	230 bp	680 bp	250 bp
# of Bidders per Contract	8-10	8-10	8-10	4-6	3-5	3-4
Enterprise Carrier Coverage Group: Commercial Metrics						
Revenue Growth	6.4%	0.6%	-6.1%	-6.3%	-0.6%	3.6%
bp Change		-580 bp	-670 bp	-20 bp	570 bp	420 bp
Headcount (000)	164	150	129	123	123	123
% Change		-8.8%	-13.8%	-4.9%	0.0%	0.0%
Rev. Productivity/Employee (\$ 000)	\$382	\$421	\$459	\$452	\$449	\$466
% Change		10.3%	9.0%	-1.6%	-0.6%	3.6%
EBITDA Margins	30.1%	25.0%	23.8%	21.2%	23.4%	25.5%
bp Change		-510 bp	-120 bp	-260 bp	220 bp	210 bp
OFCF (\$ bil)	(\$9.8)	(\$11.2)	\$6.2	\$6.2	\$4.6	\$5.2
Leverage (Consolidated Debt/EBITDA)	5.6x	6.8x	3.8x	3.1x	2.7x	2.4x

Favor Exposure to High-End Enterprise:

In general, we favor Enterprise Carriers with greater exposure to the high-end of Enterprise telecom and Wholesale, and less exposure to SME. While competition is intense across the Enterprise market, we believe it is poised to improve in 2004 within the Wholesale market, while it is likely to intensify within SME for Enterprise Carriers, driven by the RBOCs. Early signs of this were evident in Enterprise Carrier 3Q03 earnings reports, as renewed point-of-sale long distance and low-speed private line price declines added a discernable drag to revenues.

- The operational and financial improvements expected for 2004 should flow most directly to the high-end of the Enterprise market, due largely to the core nature of the improvements and to the improving competitive landscape within those segments.
- The 2004 growth and margin outlook is better for Enterprise Carriers within the Wholesale segment, driven ironically by increasing competition within the SME and Consumer market segments by traditional and non-traditional carriers that lack a national backbone and rely on wholesalers to provide the wide area networking.
- Despite the much publicized hyper-competition within the Wholesale market, we believe this segment is the one best positioned to see improving competitive dynamics in 2004, as the number of competitors and network miles are expected to decline.
- While SME has better margins and good long-term growth, to the incumbent Enterprise Carriers it represents the segment expected to most intensify competitively in 2004, as competitive threats emerge from well-funded and aggressive RBOCs. SME revenues are expected to cause 100 bps drags to commercial revenue growth for AT&T and MCI in 2004.
- The following table highlights that AT&T and MCI have the largest long distance SME exposure, while Sprint has materially less and Level (3) has none. Of note, Level (3) derives 100% of its revenues from the portion of the market we expect to perform the best in 2004 (Wholesale).

Figure 4: Enterprise Carrier SME Exposure

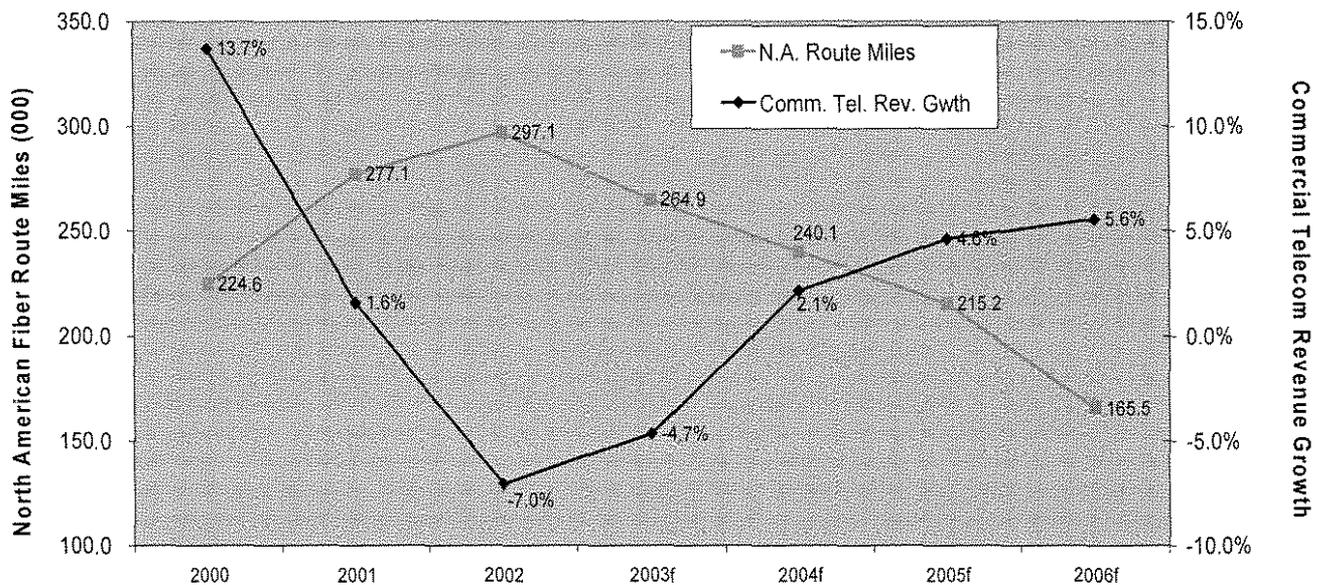
Enterprise Carrier	SME		High-End		
	LD SME	ILEC SME	Total High-End	Wholesale	Large-Enterprise
AT&T Bus. Serv.	24%	0%	76%	24%	52%
MCI Commercial	28%	0%	72%	33%	39%
FON-Commercial	14%	23%	62%	22%	41%
Level (3)	0%	0%	100%	100%	0%
Enterprise Carrier Avg.	23%	2%	75%	30%	45%

Improving Supply/Demand Balance:

We believe that the supply/demand imbalance that has plagued the industry has finally begun to stabilize. On the supply side, we estimate that North American fiber route miles could be reduced by a cumulative 30% within 1-2 years (already about 11% reduced). Additionally, the number of bidders per contract has fallen from 8-10 in 2001 to 4-6 today (and likely 3-5 by 2004). On the demand side, we are seeing the early signs that commercial bandwidth requirements are beginning to improve, as indicated by our Enterprise Demand Index improvements and our Fortune 500 Survey. Currently, we are forecasting a modest recovery, but if job growth and technology sales continue accelerating at current rates there could be upside to our numbers.

- To date, one US-based network carrier has been consolidated and its network decommissioned (Genuity), and a European carrier is scaling back its US operations.
- Another two carriers will likely consolidate within 1-2 years, as they remain cash-flow-negative and have limited access to capital.
- Enterprise telecom is a cyclical business – we believe we have found two reliable leading indicators in terms of forecasting changes in commercial telecom services revenue growth, namely employment growth and semi-conductor revenue growth, and constructed an Enterprise Demand Index (EDI).
- Our EDI score of 0.5 signals an expected moderate improvement to current 4% Enterprise telecom service revenue declines (to begin by 2Q04), while our Fortune 500 Survey indicates an expected 5% increase in 2004 telecom service spending, up from -5% in 2003.

Figure 5: Decreasing Fiber Route Miles Supports Improving Enterprise Telecom Services Industry Revenue Growth

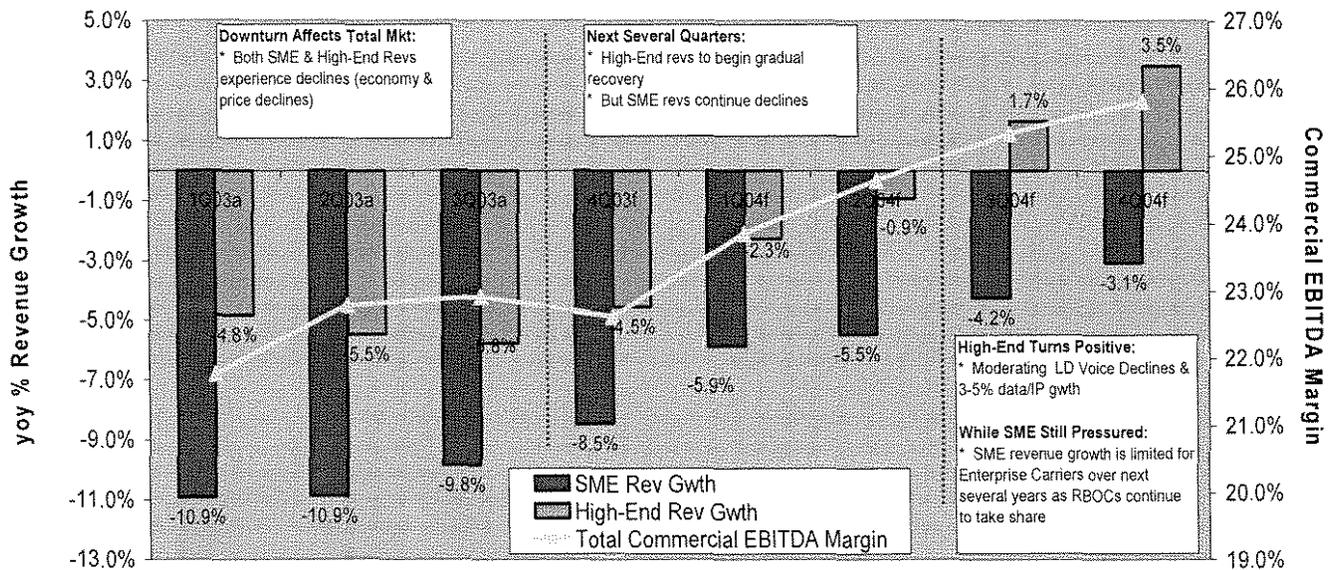


Diverging 2004 Performance – High-End Turning the Corner

While overall revenues for our Enterprise Carrier coverage group are expected to decline 1% in 2004, this masks two diverging trends that we expect to develop throughout the year – improving quarterly Wholesale/Large Enterprise revenue growth and margins versus continued SME revenue declines and pressured margins.

- Expected 1% declines in 2004 Enterprise Carrier revenue masks important underlying trends that favor the high-end of the market, namely improving revenue growth and margins, driven by improving demand and cost reduction initiatives.
- We expect Wholesale/Large Enterprise revenue growth will see improving quarterly yoy growth rates, driven by improving competitive dynamics, better pricing stability and key growth-product opportunities (VoIP and MPLS-enabled LAN-to-WAN services). By 4Q04, we expect high-end revenues will be growing 3.5% yoy for our Enterprise Carriers, while SME is still expected to be declining 3.1%.
- While VoIP does not represent a net growth opportunity to the incumbent market, it does represent a material Wholesale opportunity given that the retail providers of this new service mostly lack a national backbone and will rely on wholesalers.
- Additionally, MPLS-enabled services marketed to enterprises, by RBOCs in particular, provide another such Wholesale growth opportunity .
- We expect Wholesale/Large Enterprise to benefit most from cost-reduction initiatives. Since most of these center around the network core and related systems, the benefits should flow mostly to services that most intensively utilize the core.

Figure 6: Diverging 2004 Performance within Enterprise – High-End Versus SME

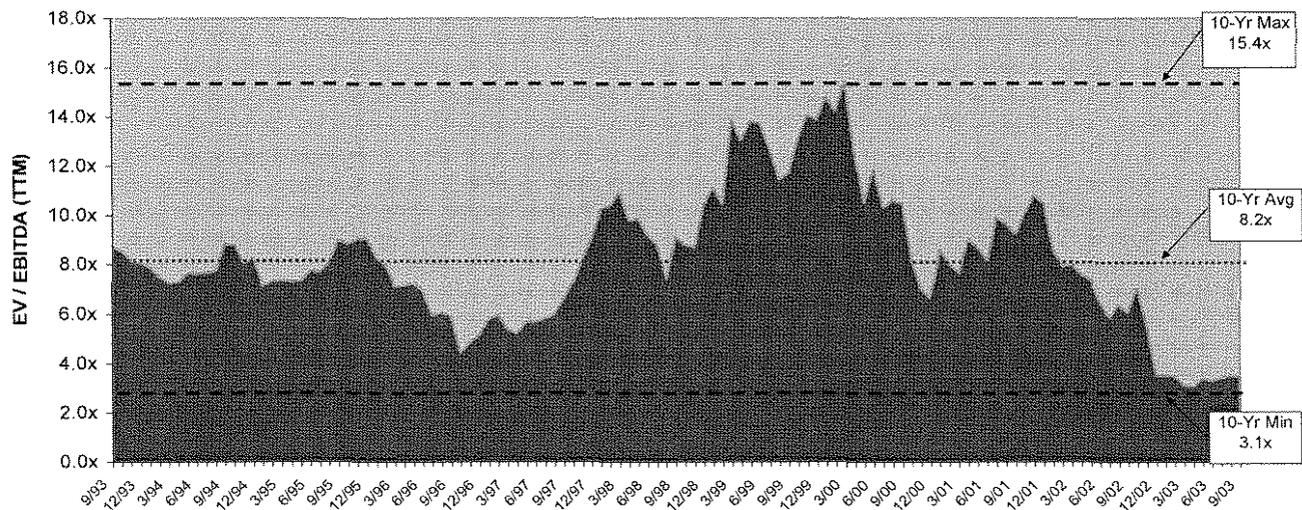


Valuations at 10-Year Lows – Provides Targeted Opportunities:

Enterprise coverage group valuations hover near 10-year lows, creating investment opportunities as the entire sector remains tarred with a broad brush. High-end carriers with the most efficient networks and improving sequential revenues and margins, and less exposure to SME, offer investors the chance to buy at a market-bottom values that do not yet reflect their improving underlying fundamentals.

- Level (3) is our top pick in the space, with its Wholesale pure-play model, its industry leading margins (that continue to improve sharply, up 380 bps in 3Q), its FCF-positive status and improving balance sheet. It is most cleanly positioned to benefit from the improvements we expect in the Enterprise market in 2004. We believe the bear case valuation is \$6 and buy aggressively below this level.
- AT&T, while exposed to SME, is our top value pick, given its dominant position within Large Enterprise, improving margins, and very cheap valuation at 3.0x 2004 EBITDA. While revenue and EBITDA growth will remain pressured due to Consumer/SME drags, we believe the discounted value of cashflows is worth more than current market prices. A 5%+ dividend yield and potential for additional dividend increases and/or share buybacks should provide strong support for the stock.
- MCI offers strong potential upside, given its vast opportunity for margin improvement. Based on the current when-issued trading levels, the company is trading modestly above AT&T, at 3.4x 2004 EBITDA. We await audited financials and more insight from management in order to fully develop our thesis.

Figure 7: Enterprise Carrier Coverage Group's Valuation Hovering at 10-Yr Lows – EV / EBITDA Multiple



Valuations – Enterprise Carriers Low Vs. Rest-of-Telecom:

We believe that the operating environment is beginning to improve for the carriers within our Enterprise coverage group and that valuations do not yet reflect this, providing an opportunity for patient investors to enjoy a favorable risk/return relationship.

- Fortunately, cycles proceed. We believe valuations and multiples are poised to expand as operational and financial improvements have positioned the stronger Enterprise carriers to benefit in a leveraged fashion from improvements in the commercial economy.
- This process of value-expansion should be greatly enhanced by industry consolidation, which we believe is ripe to occur and should be seen as a catalyst for valuation appreciation in the sector. Other catalysts will be continued improvements in employment and technology and productivity increases (with semiconductor chip sales being a reasonable proxy).
- The following table summarizes our new Enterprise Carrier sector in relation to the other telecom service sector stocks covered by Lehman Brothers. The Enterprise group stands out as the having the lowest market valuation, at 3.5x EBITDA versus the next-nearest group (the RBOCs) at 4.8x. To highlight the disparity, we estimate that Enterprise Carriers comprise 25% of Lehman Telecom Services coverage revenue, and 17% of EBITDA, but only 12% of the market capitalization. Given that we believe fundamentals are poised to improve, we believe the sector has good value at these levels.

Figure 8: Enterprise Carrier Valuation Low Relative to Lehman Telecom Services Coverage Universe

	RBOCs	National Wireless	RLECs	Enterprise Tel.	Small Wireless
	BellSouth Qwest SBC Communications Verizon	AT&T Wireless Nextel Sprint PCS	Alltel Century Tel. Commonwealth Tel. Citizens Comm. US Cellular TDS	AT&T MCI Sprint Level (3)	
\$ Bil					
2003 Revs	\$161	\$37	\$16	\$73	\$9
% of LEH-Cvg	54%	12%	5%	25%	3%
2003 EBITDA	\$61	\$12	\$7	\$16	\$3
% of LEH-Cvg	61%	12%	7%	17%	3%
Market Cap	\$225	\$46	\$27	\$42	\$15
% of LEH-Cvg	63%	13%	8%	12%	4%
EV/EBITDA	4.8x	6.6x	6.6x	3.5x	11.8x

Price Target Methodologies:

FON: Our new \$18 price target is based on an average of DCF and EV/EBITDA multiple, versus expected growth methodologies, and implies a modest multiple expansion to 3.6x 2004 EBITDA, still low versus historical averages.

T: We value AT&T shares based on DCF and EV/EBITDA multiples relative to growth. Based on these metrics, we find strong price support levels for AT&T at \$19 per share, based on the EV/EBITDA multiple versus growth method, with a higher DCF-value, at \$32 per share. Our \$24 price target represents a weighted average of DCF and EV/EBITDA multiple methods, with a \$2 per share haircut to account for variability in valuation driven by different CS assumptions in the out years.

LVLT: Our DCF valuation results in a \$7 per-share price target, using a 10.3% WACC and a 4.5% terminal growth assumption. We believe the bear case downside is \$6 per share and the bull case upside is \$8 per share. Our target is based on the assumption that management does not issue significant incremental equity in the near term.

Enterprise Carrier Coverage Group – Improving Commercial Outlook:

We expect a cyclical up-tick, significant operational/financial improvements, and industry consolidation to drive stabilizing revenues, materially improved margins and 10% EBITDA growth in 2004 for the commercial arms of the Enterprise Carriers in our coverage group. These factors are expected to drive increasing cashflows to equity holders via dividend increases, share buybacks, and growing OFCF.

- Estimated 5% growth in 2004 Fortune 500 telecom service budgets (versus 5% declines in 2003) is expected to stabilize 2004 commercial revenues for our Enterprise Carrier coverage group at -1% (versus -6% in 2003). We expect 2005 Enterprise Carrier commercial revenues to grow nearly 4%, and long-term average annual growth of 4%.
- Enterprise Carriers have significantly pared cash operating expenses and are poised to reap meaningful returns as the commercial economy improves. A 25% reduction in headcount from 2000 to current has driven an 18% improvement in productivity per employee. Combined with the benefits of other massive network and systems cost/efficiency initiatives, we expect Enterprise Carriers to improve 2004 commercial EBITDA margins 220 bps and grow commercial EBITDA 10%.
- We expected continued strong margin gains in 2005, at +210 bps, driving expected EBITDA growth of nearly 13%. Between now and 2010, we expect commercial EBITDA will grow at an average annual rate of nearly 9%.
- Capex has also been reigned in and targeted on core efficiency upgrades and success-based spending. We expect it to normalize at 8-10% of revenues, enabling healthy 3-4% commercial OFCF growth rates from 2003 to 2010.

Figure 9: Enterprise Carrier Coverage Group: Improving Commercial Outlook

(\$ Bil)	2000	2001	2002	2003	2004f	2005f	'03 to '10 CAGR
Revenue	\$62.7	\$63.0	\$59.2	\$55.4	\$55.1	\$57.1	3.6%
% Growth	6.4%	0.6%	-6.1%	-6.3%	-0.6%	3.6%	
Opex	\$43.8	\$47.3	\$45.1	\$43.7	\$42.2	\$42.6	1.9%
% Growth	8.0%	8.0%	-4.5%	-3.2%	-3.4%	0.9%	
EBITDA	\$18.9	\$15.8	\$14.1	\$11.8	\$12.9	\$14.5	8.5%
% Growth	20.8%	-16.5%	-10.7%	-16.4%	9.8%	12.6%	
Margin	30.1%	25.0%	23.8%	21.2%	23.4%	25.5%	
Capex	\$22.2	\$17.6	\$6.5	\$5.3	\$5.8	\$6.1	5.9%
% Growth	19.1%	-20.8%	-62.9%	-18.8%	9.8%	4.5%	
% of Rev	35.5%	27.9%	11.0%	9.6%	10.6%	10.6%	
OCF⁽¹⁾	(\$9.8)	(\$11.2)	\$6.2	\$6.2	\$4.6	\$5.2	3.3%
% Growth	16.0%	13.9%	-155.6%	-0.6%	-26.6%	14.9%	
Margin	-15.7%	-17.8%	10.5%	11.2%	8.3%	9.2%	
Commercial Telecom Employees (000s)	164.1	149.6	129.0	122.7	122.7	122.7	n/m

(1) Operating Free Cash Flow is defined as CFFO - capex.

LEHMAN BROTHERS

EQUITY RESEARCH

Enterprise Telecom Services Comparables:

Figure 10: Enterprise Comps

Company & Enterprise Value													
Stock Information				Enterprise Value					Investor Returns				
Company	Ticker	Price	Shares Out	Mkt.Cap	Net Debt	Non-Con. Assets	Enter. Value	Book Equity	Current Yields	Stock Performance: % Return			
									Div Yld	ROA	Week	Month	YTD
AT&T ⁽¹⁾	T	\$19.08	789	15.1	8.5	0.0	23.6	13.6	5.0%	7.6%	1%	-5%	-27%
T Bus. Serv. ⁽²⁾										4.6%			
MCI ⁽¹⁾	MCI AV	\$25.26	326	8.2	3.4	0.0	11.7	8.4	0.0%	6.5%	1%	-5%	-27%
MCI Comm. ⁽²⁾										3.6%			
Sprint ⁽¹⁾	FON	\$15.22	903	13.7	0.0	0.0	13.8	13.3	3.3%	8.7%	-6%	-3%	5%
FON Comm. ⁽²⁾										4.2%			
Level 3 ⁽¹⁾	LVL T	\$5.33	653	3.5	4.5	0.0	8.0	0.3	0.0%	-1.9%	-4%	-1%	9%
L3 Comm. ⁽³⁾										-5.1%			
XO Comm.	XOCM	\$5.30	95	0.5	0.2	0.0	0.7	0.5	0.0%	-6.6%	-2%	-1%	N/A
Time Warner	TWTC	\$10.16	115	1.2	0.8	0.0	2.0	0.5	0.0%	-1.8%	-7%	-13%	382%
Enterprise Avg. (Largecap for Div & ROA)									2.8%	4.2%	-3%	-5%	68%
S&P 500 Avg.											-1%	1%	19%

Operating Statistics													
Stock Information		Revenue				EBITDA				EPS			
Company	LEH Rating	2003		2004		2003		2004		2003		2004	
		\$ Bil	% Gwth	\$ Bil	% Gwth	\$ Bil	Margin	\$ Bil	Margin	\$	% Gwth	\$	% Gwth
AT&T ⁽¹⁾	1-OW	34.7	-8.1%	32.9	-5.4%	8.7	25.1%	7.9	24.0%	\$2.28	-17.2%	\$1.73	-24.3%
T Bus. Serv. ⁽²⁾		25.2	-5.3%	24.5	-2.5%	6.8	26.9%	6.8	27.9%				
MCI ⁽¹⁾	NR	24.5	-16.3%	24.0	-1.7%	2.7	11.2%	3.4	14.3%	N/A	N/A	\$2.76	N/A
MCI Comm. ⁽²⁾		18.2	-11.4%	18.3	0.8%	2.0	11.2%	2.8	15.4%				
Sprint ⁽¹⁾	2-EW	14.1	-7.0%	13.8	-2.6%	4.4	31.1%	4.5	32.9%	\$1.45	7.5%	\$1.55	6.4%
FON Comm. ⁽²⁾		9.3	-5.6%	9.3	-0.6%	2.5	26.8%	2.7	28.5%				
Level 3 ⁽¹⁾	1-OW	3.6	26.6%	3.6	-1.2%	0.4	12.1%	0.6	16.4%	(\$1.18)	N/M	(\$0.98)	N/M
L3 Comm. ⁽³⁾		1.6	2.9%	1.8	9.0%	0.4	27.3%	0.6	32.2%				
XO Comm.		1.2	-7.2%	1.2	6.7%	0.0	1.1%	0.0	1.8%	(\$1.28)	N/M	(\$1.08)	N/M
Time Warner		0.7	-7.0%	N/A	N/A	0.2	28.6%	N/A	N/A	(\$1.06)	N/M	(\$0.89)	N/M
Enterprise Ind.		151.6	-4.7%	154.8	2.1%	31.0	20.4%	32.9	21.3%				

Valuation Multiples & Capital Structure													
Stock Information		EV / Revenue		EV / EBITDA		EV / OFCF		P/E Ratio		Leverage Ratios		Coverage Ratios	
Company	Price Target	2003	2004	2003	2004	2003	2004	2003	2004	Nt Debt / Capital	Nt Debt / '04 EBITDA	Unlev. '04 OFCF / Int.	
AT&T ⁽¹⁾	\$24	0.7x	0.7x	2.7x	3.0x	4.0x	6.9x	8.4x	11.1x	38.5%	1.1x	4.6x	
T Bus. Serv. ⁽²⁾		0.9x	1.0x	3.5x	3.4x	5.6x	8.4x						
MCI ⁽¹⁾	NR	0.5x	0.5x	4.3x	3.4x	5.3x	11.5x	N/A	9.2x	29.0%	1.0x	3.4x	
MCI Comm. ⁽²⁾		0.6x	0.6x	5.7x	4.1x	5.3x	11.5x						
Sprint ⁽¹⁾	\$18	1.0x	1.0x	3.1x	3.0x	8.0x	6.9x	10.5x	9.8x	0.2%	0.0x	9.0x	
FON Comm. ⁽²⁾		1.5x	1.5x	5.5x	5.2x	12.8x	11.5x						
Level 3 ⁽¹⁾	\$7	2.2x	2.2x	18.2x	13.6x	N/A	115.1x	N/A	N/A	93.1%	7.7x	1.1x	
L3 Comm. ⁽³⁾		5.0x	4.5x	18.1x	14.1x								
XO Comm.		0.6x	0.5x	53.2x	30.0x	N/A	N/A	N/A	N/A	23.3%	7.4x	No Cash Int.	
Time Warner		2.8x	N/A	9.8x	N/A	N/A	N/A	N/A	N/A	61.5%	N/A	N/A	
Enterprise Avg. (Largecap)		0.7x	0.7x	3.4x	3.1x	5.8x	8.5x	9.4x	10.0x	22.6%	0.7x	5.7x	
S&P 500 Avg.													

(1) Represents consolidated, total company information (for Level 3, reflects recurring items only - excludes any dark fiber, settlement & termination)

(2) Reflects operating statistics for the commercial portion of the company; valuation statistics reflect total company market valuation as a multiple of the commercial operating unit's cashflows.

(3) Reflects recurring Communications Group items only

MCI Company Report on When-Issued Equity:

We are initiating coverage on the when-issued equity of MCI Communications, but await audited financials, more insight from management, and an exchange-traded equity before issuing a rating and price target. Operationally, we believe the company has significant upside opportunities, as highlighted in the company's bankruptcy disclosure documents, but also a lot to prove. Facilitating this opportunity is the company's increased financial flexibility, resulting from its restructured and lean balance sheet. We include our full company report within this industry report since MCI does not yet have an eligible ticker under which to publish research for its new equity. The most important contributor to MCI's value proposition over the next 12 months should be its ability to shed costs while at least stemming market share losses. It is undertaking a massive network and infrastructure overhaul in order to drive more than 500 bps of margin improvement by 2005. We believe these efforts, assuming disciplined pricing, will be successful in driving significant EBITDA improvements over the next two years. If continuing margin improvement can be sustained, driving margins toward industry levels, EBITDA growth could easily exceed 15% annually, materially outperforming the sector. However, we await audited financials and more insight from management in order to fully develop our view on the stock.

Investment Thesis:

- 2004 Outlook: We believe MCI margins will expand 300 bps in 2004, improving EBITDA growth to positive 26% (up from an estimated 46% decline in 2003), despite forecasted 1.7% revenue declines (improved from a 16.0% decline in 2003). OFCF is estimated to be \$1.1 billion in 2004.
- Productivity & Efficiency: MCI currently lags the Enterprise industry in most operational metrics, but particularly in EBITDA per employee. At a 2004 forecast of \$68k EBITDA/employee, MCI lags the Enterprise industry average of \$105k by 35% and the AT&T level of \$141k by more than 50%. This is largely due to a redundant cost structure, accumulated through multiple acquisitions and a lack of infrastructure grooming. However, management is keenly focused on achieving 500 bps+ of margin improvement by 2005 (MCI lags the industry by as much as 1,000 bps).
- Streamlining the Model: We believe MCI's lower margins are driven by a combination of low pricing and the myriad networks, systems and hierarchical infrastructure built up from its acquisition roll-up/holding-company model over the years. To address this, management is converging its network to a single IP core and eliminating redundant systems. Given the magnitude of the opportunity for improvement, we believe management can achieve its goal of 500 bps+ improvement by 2005, and 50-100 bps per year for some time thereafter.
- Pricing: MCI has historically been among the most aggressive in terms of pricing, partially explaining its low margins. However, with 2003 EBITDA margins at a forecast of 10.9%, and approximately \$1 billion in OFCF per year thereafter, there is not much room to cut prices further, giving us some comfort against fears of an all-out price war, although some cuts at re-emergence are likely.
- Capital Structure & Dilution: At an estimated 326-366 million outstanding shares at re-emergence and \$4.7-\$5.7 billion in debt, MCI will boast one of the best balance sheets in the business. Even at \$5.7 billion in total debt, net debt would only be \$3.5 billion, leaving net debt/EBITDA at a low 1.3x (similar to AT&T). With expected improvements in 2004 EBITDA, we expect leverage to fall to 0.7x and interest coverage to be 3.4x.
- Consumer: We expect ongoing revenue and EBITDA losses within Consumer (-5% annually for revenues and -16% annually for EBITDA over next 7 years), but believe a lower proportion of fixed costs within its Consumer unit will allow MCI to maintain positive FCF over time.
- SME Exposure: MCI maintains the second-largest SME revenue base, estimated at \$5 billion in 2003, but has the largest relative exposure as a percent of commercial revenues of any of the Enterprise Carriers. We estimate that MCI will lose approximately 25 bps of share annually to the RBOCs in this segment (similar to AT&T), causing an estimated 100 bp drag to commercial revenue growth.
- Valuation: Bankruptcy documents value the restructured equity at \$25 per share, however arguments could be made for a range of values, from price support at \$22 per share, to premium-multiple values approaching \$28, for the stock. Fundamental to determining where the stock should trend are assumptions on cost-reduction, pricing and margin-improvement potential over the next 12 months. We await audited financials and more insight from management prior to establishing a price target.

Core Business Model:

MCI is a leading provider of voice and data telecom services to 20 million residential and commercial customers worldwide. The company is structured along customer segment lines, dividing itself primarily into Business, International, and Mass Markets segments. For purposes of this report and our modeling, we have attempted to group revenues and expenses into just two buckets, Commercial (\$18 billion in revenue) and Consumer (\$6 billion in revenue). In this regard, we include International within Commercial since the vast majority of its business involves multinational corporations. While the new corporate structure is not yet totally evident, we believe the Commercial unit will own and operate the fiber network and related POPs and lease capacity to the Consumer unit on a volume basis (we believe that Consumer will own a number of Class 5 voice switches and related network interface devices).

MCI's Commercial unit is second-largest Enterprise telecom services provider in the US and offers a full suite of facilities-based long distance voice and data network services – it maintains a relationship with most of the Fortune 1000 companies and has historically maintained the largest Wholesale business in the US, although estimated share loss due to the bankruptcy process in 2003 has likely driven MCI to a number two Wholesale share spot (below AT&T). As the company re-emerges from bankruptcy, we believe MCI will be particularly focused on regaining share losses within its historic Top 500 accounts (similar to AT&T's increasing focus) and is reconfiguring its network, support and client-facing infrastructure to accommodate this. In this regard, significant network, systems, headcount and bankruptcy-driven restructuring changes are underway in efforts to bring MCI's profitability up to industry levels. This is clearly the number one challenge for management, and without question the central item in MCI's value proposition over the next several years.

Where there is much challenge, there is much opportunity, but the path won't be easy. MCI has historically operated as a holding company that oversees the myriad autonomous companies it has acquired since the 1980s. This has helped lead to the lower margins it maintains versus its peers, due to the layers of inefficient legacy systems, redundancies and parallel network protocols inherent in this structure. By some estimates, MCI maintained at one point more than 400 internal systems (versus AT&T with 140+ at its peak). To address these inefficiencies, MCI announced in April an initiative to overhaul its network, migrate traffic to a single IP core, and streamline its systems. It plans to have 25% of its voice traffic running over its IP core by year-end 2004, but these leaves it somewhat behind the incumbent peers, who are aggressively building out migration paths to a single core in 2003. Nonetheless, success in these areas could lead to significantly faster-than-industry cashflow growth, due to degree of MCI's current margin lag (AT&T Business Services 26.5% 2003 EBITDA margin versus MCI Commercial at an estimated 10.9%).

The Consumer unit is the second-largest provider of residential long distance services in the US and counts an estimated 18 million customers as its client base. The unit is aggressively deploying a non-facilities-based UNE-P local strategy in order to offer a bundled local/long distance, fixed-rate service in efforts to reduce the severity of secular competitive and substitution declines in the mature Consumer long distance voice product. While the local service itself has limited profit potential, its bundled offering with long distance is proving to be effective at reducing competitive losses to RBOCs and substitution to wireless. And while the local/long distance bundle is slowing the rate of customer defection, MCI's smaller overall share within Consumer (versus AT&T), combined with its broader UNE-P scope (48 states versus 35 states for AT&T) is likely to make a thin-margin product even less profitable, making us wonder how long MCI will maintain such a broad deployment. According to our forecasts, MCI's stand-alone UNE-P product will not reach breakeven until 2006 (versus AT&T in 2005), due to its higher costs of service (UNE-P rates), resulting from deployment into less urban areas, and lower effective ARPUs (for similar reasons). Nonetheless, if the product's deployment helps stabilize the overall business in the near-term, we believe it is the best course of action. And if the Consumer infrastructure can be dynamically scaled to match decreasing volumes over time, the current local/long distance strategy may prove the most effective way of maximizing cashflows and harvesting a declining, mature product.

The following table summarizes the relative size of the MCI's Commercial and Consumer units. The table highlights that Commercial revenues (including International) are estimated to be 74% of 2003 MCI total revenues and are expected to grow to 84% of revenues by 2010. Commercial revenues are expected to grow 4% annually over this period, while Consumer revenues are expected to decline approximately 5% annually.

Figure 11: MCI Commercial & Consumer Revenues

Revenue (\$ Bil)	2001		2003f		2005f		2010f	
	Revs	% of Total						
Commercial (Inc. Intl)	\$22.7	67%	\$18.2	74%	\$19.1	78%	\$24.1	84%
% Growth	4.8%		-11.4%		4.6%		4.2%	
Consumer	\$11.2	33%	\$6.3	26%	\$5.3	22%	\$4.5	16%
% Growth	-13.6%		-27.9%		-7.2%		-2.1%	
MCI Consolidated	\$33.9	100%	\$24.5	100%	\$24.5	100%	\$28.6	100%
% Growth	-2.1%		-16.3%		1.8%		3.2%	

A Brief Bankruptcy History:

On June 25, 2002, the Company announced that as a result of an internal audit, it was determined that transfers from line cost expenses to capital accounts in the amount of \$3.9 billion were not made according to GAAP. Subsequent announcements over the course of the summer 2002 indicated that additional improperly recorded transfers and accounting we identified and that the ultimate size of the eventual restatements could exceed \$9 billion and involve 1999, 2000, 2001 and 1Q02.

KPMG is the Company's new auditor and conducted this review and restatement process. It also conducted an internal controls audit, which is being relied upon by the Federal government as the guideline as to when MCI may have its current suspension from new GSA business lifted. It has been alleged that the improper transfers at the core of this matter were intentional and done at the direction of various senior management personnel. As such, the entire senior management team of MCI has essentially been removed and replaced, as has the Board of Directors.

There remain outstanding criminal and civil legal challenges to MCI and some of its former senior management related to these matters, as well as other alleged improper access-charge and call-routing practices. Resolution of these matters are uncertain, but they have not impeded the Bankruptcy Court's decision to approve the restructuring transaction, or the creditors agreement to this restructuring, indicating that that outcome of such legal matters is not perceived by the concerned parties as likely to be catastrophic in nature.

On July 21, 2002 WorldCom, Inc. (the "Company") and most of its direct and indirect domestic subsidiaries filed voluntary petitions for relief in the United States Bankruptcy Court for the Southern District of New York under Chapter 11. On November 8, 2002 43 additional, but mostly inactive, subsidiaries filed Chapter 11 and the cases were all consolidated, while the company continued to operate its business as debtors-in-possession. On April 14, 2003 the Company filed a Plan of Reorganization and on May 28, 2003 the Bankruptcy Court approved the Disclosure Statement, allowing solicitation of creditors' approval. Solicitation began on June 13, 2003, but on July 31, 2003 the Bankruptcy Court postponed the expected August 13, 2003 Confirmation Hearing until September 8, 2003 in order to permit the Company to file an additional Disclosure Statement addressing issues relating to the investigation of its call-routing practices by the US Attorney's Office and the impact of the July decision by the GSA to propose debarment of the Company for the purposes of soliciting and contracting new government business.

There remains a current suspension of MCI's ability to gain new government contracts pending on ongoing review of the Company's internal controls improvements and related items. The Company filed this updated Disclosure Statement on August 4, 2003, which was approved by the Court on August 6, 2003. The final Confirmation Hearing began on September 8, 2003 and on September 9, 2003 agreement was reached with the last major group of creditors, clearing the way for a final agreement.

On September 11, 2003, the Company filed a final Disclosure Statement reflecting this agreement. The final creditor vote was completed on October 7, 2003 and the final Confirmation Hearing reinitiated on October 15, 2003, where it was once again delayed until October 30. The Court gave verbal approval for the deal on October 31, and MCI's when-issued stock began trading under the ticker MCI AV on November 3. Re-emergence will become effective at some point just after the beginning of the 2004, when the Company is expected to complete and file its financial restatements and other documents and distribute its new securities. At this point the new equity will begin trading under its official ticker on an exchange to be determined.

Core Markets and Competitors:

MCI is estimated to hold the #3 market share position in terms of total Enterprise revenues, although among carriers that we designate "Enterprise Carriers" (i.e. – carriers that derive more than 50% of their revenues from commercial customers) it is the second largest (behind AT&T). We estimate MCI's 2004 overall Enterprise market share to be 11.8%, down from an estimated 13.3% in 2001, prior to bankruptcy being filed. We estimate that MCI has lost approximately \$2.6 billion in annual market share over the course of its bankruptcy. However, MCI is re-emerging largely intact, with continued strong competitive positions across the Enterprise market, and particularly so within Large Enterprise, where we believe a patient approach to profitable re-acquisition of market share will lead net share gains over the next 7 years. For example, while we expect MCI as an incumbent to experience overall Enterprise share loss of 10 bps annually (through 2010), we expect the company to experience net share gains of 15 bps per year within the Large Enterprise segment of the market. The most intense competition for MCI will come at the upper and lower ends of the market, with strong emerging competition from Level (3) within the Wholesale segment and RBOC long distance entry within SME, driving estimated 10 bps and 25 bps of annual share loss respectively.

Figure 12: The Enterprise Market

Top 10 Enterprise Market Share Carriers⁽¹⁾ - Total Market

Rank	Carrier ⁽²⁾	2004f		2005f		2010f		
		Rev (\$ bil)	Mkt. Share	Rev (\$ bil)	Mkt. Share	7-Yr Rev CAGR	Market Share	Avg. Annual Share Chg.
1	AT&T Bus. Serv.	\$24.5	15.8%	\$25.1	15.5%	2.6%	14.2%	-30 bp
2	SBC	\$20.2	13.1%	\$21.1	13.1%	4.7%	13.1%	00 bp
3	MCI	\$18.3	11.8%	\$19.1	11.8%	4.1%	11.4%	-10 bp
4	Verizon	\$15.2	9.8%	\$16.3	10.1%	5.5%	10.7%	10 bp
5	Sprint	\$9.3	6.0%	\$9.5	5.9%	2.5%	5.2%	-15 bp
6	Qwest	\$8.7	5.6%	\$9.2	5.7%	5.4%	5.8%	05 bp
7	BellSouth	\$8.5	5.5%	\$8.9	5.5%	5.4%	5.7%	05 bp
8	Level 3	\$1.8	1.1%	\$1.9	1.2%	10.3%	1.5%	05 bp
9	XO Communications	\$1.2	0.8%	\$1.4	0.9%	9.7%	1.1%	05 bp
10	Rest of Industry	\$47.1	30.4%	\$49.3	30.4%	6.2%	31.3%	15 bp
Enterprise industry		\$154.8	100.0%	\$162.0	100.0%	4.9%	100.0%	

(1) Represents commercial local and long distance, voice and data revenues.

Figure 13: The Large Enterprise Market

Top 5 Large Enterprise Market Share Carriers⁽¹⁾

Rank	Carrier ⁽²⁾	2004f		2005f		2010f		
		Rev (\$ bil)	Mkt. Share	Rev (\$ bil)	Mkt. Share	7-Yr Rev CAGR	Market Share	Avg. Annual Share Chg.
1	AT&T Bus. Serv.	\$13.1	25.7%	\$13.5	25.6%	3.5%	25.1%	-10 bp
2	MCI	\$7.5	14.8%	\$8.1	15.3%	5.6%	15.8%	15 bp
3	Sprint	\$3.9	7.7%	\$4.0	7.6%	3.0%	7.0%	-10 bp
4	Qwest	\$2.2	4.4%	\$2.4	4.5%	6.6%	5.1%	10 bp
5	XO Communications	\$0.5	1.1%	\$0.6	1.1%	9.6%	1.5%	05 bp
	Rest of LE	\$23.6	46.4%	\$24.1	45.8%	3.8%	45.5%	-15 bp
Large Enterprise		\$50.9	100.0%	\$52.7	100.0%	4.1%	100.0%	

(1) "Large Enterprise" is defined as the "Fortune 1,000" Enterprises; these users generate \$25 million or more annually, with average over \$50 million.

(2) Represents wholesale local and long distance, voice and data revenues.

Figure 14: The Wholesale Market

Top 5 Wholesale Market Share Carriers⁽¹⁾

Rank	Carrier ⁽²⁾	2004f		2005f		2010f		
		Rev (\$ bil)	Mkt. Share	Rev (\$ bil)	Mkt. Share	7-Yr Rev CAGR	Market Share	Avg. Annual Share Chg.
1	AT&T Bus. Serv.	\$5.9	18.6%	\$6.2	18.4%	3.6%	16.8%	-30 bp
2	MCI	\$6.0	18.7%	\$6.2	18.6%	4.9%	18.3%	-10 bp
3	Qwest	\$2.6	8.0%	\$2.6	7.9%	3.4%	6.9%	-20 bp
4	Sprint	\$1.8	5.8%	\$1.9	5.7%	2.3%	5.2%	-10 bp
5	Level 3	\$1.8	5.5%	\$1.9	5.7%	10.3%	7.0%	30 bp
	Rest of Wholesale	\$13.8	43.3%	\$14.6	43.6%	7.0%	45.7%	40 bp
	Wholesale Market	\$31.9	100.0%	\$33.5	100.0%	5.6%	100.0%	

(1) "Wholesale" is defined as the "Top 300 Telco Users" worldwide; these users generate at least \$75 million annually in telecom revenues

(2) Represents wholesale local and long distance, voice and data revenues.

LEHMAN BROTHERS

EQUITY RESEARCH

Segment Exposure and highlights:

Approximately 26% of consolidated 2003 revenues are Consumer, which are expected to decline 9% in 2004, with EBITDA margins expected to remain steady at 11%, resulting in 9% EBITDA declines. Approximately 21% of 2003 revenues are SME, which are expected to decline 4% in 2004. However, an estimated 260 bp improvement in SME margins, due to the massive cost reduction efforts being undertaken as part of the bankruptcy restructuring, is expected to drive 12% SME EBITDA growth in 2004. We estimate that MCI will lose approximately 25 bps of share annually to the RBOCs in this segment, causing an estimated 100 bp drag to commercial revenue growth. Collectively, the "Drag Revenues" comprise 46% of 2003 revenues and are expected to decline 2% over time, while the "Growth Revenues" comprise 54% and grow 5%.

Figure 15: MCI Segment Exposure & Outlook Highlights

	2003	2004	2005	2006	2010	'03 to '10 CAGR
Revenue: \$ Bil						
"Drag Segments"						
Consumer	\$6.3	\$5.7	\$5.3	\$5.1	\$4.5	-4.7%
% Growth	-27.9%	-9.1%	-7.2%	-4.4%	-2.1%	
% of Consolidated Revs	26%	24%	22%	20%	16%	
SME	\$5.0	\$4.8	\$4.8	\$4.9	\$5.3	0.7%
% Growth	-10.1%	-3.9%	0.3%	1.5%	1.8%	
% of Consolidated Revs	21%	20%	20%	20%	19%	
Total "Drag Segments" (Cons+SME)	\$11.3	\$10.6	\$10.2	\$10.0	\$9.8	-2.1%
% Growth	-20.9%	-6.8%	-3.8%	-1.6%	0.0%	
% of Consolidated Revs	46%	44%	42%	40%	34%	
"Growth Segments"						
Wholesale & Large Enterprise	\$13.1	\$13.5	\$14.3	\$15.2	\$18.8	5.3%
% Growth	-11.8%	2.7%	6.1%	6.2%	4.9%	
% of Consolidated Revs	54%	56%	58%	60%	66%	
MCI Consolidated Revenue	\$24.5	\$24.0	\$24.5	\$25.2	\$28.6	2.3%
% Growth	-16.3%	-1.7%	1.8%	3.0%	3.2%	
EBITDA: \$ Bil						
"Drag Segments"						
Consumer	\$0.7	\$0.6	\$0.5	\$0.4	\$0.2	-16.1%
% Growth	-53.1%	-9.4%	-18.5%	-15.5%	-15.9%	
% of Consolidated EBITDA	25%	18%	13%	10%	4%	
Margin	11.0%	11.0%	9.7%	8.5%	4.5%	
SME	\$0.8	\$0.9	\$1.0	\$1.0	\$1.2	6.1%
% Growth		12.1%	8.6%	5.2%	4.0%	
% of Consolidated EBITDA	30%	26%	25%	24%	22%	
Margin	16.2%	18.8%	20.4%	21.2%	23.3%	
Total "Drag Segments" (Cons+SME)	\$1.5	\$1.5	\$1.5	\$1.5	\$1.4	-0.7%
% Growth		2.2%	-2.5%	-1.9%	0.6%	
% of Consolidated EBITDA	55%	45%	38%	34%	25%	
Margin	13.3%	14.6%	14.8%	14.7%	14.7%	
"Growth Segments"						
Wholesale & Large Enterprise	\$1.2	\$1.9	\$2.5	\$2.9	\$4.3	19.6%
% Growth		55.9%	28.8%	16.9%	8.3%	
% of Consolidated EBITDA	45%	55%	62%	66%	75%	
Margin	9.3%	14.1%	17.2%	18.9%	22.8%	
MCI Consolidated EBITDA	\$2.7	\$3.4	\$4.0	\$4.3	\$5.7	11.1%
% Growth	-45.6%	26.2%	14.8%	9.8%	6.2%	

Core Products and Competitors:

As shown in the following table, MCI maintains strong product positions across the Enterprise space, but particularly strong positions within the retail Large Enterprise market, a market totaling an estimated \$50 billion in 2003 and representing about 33% of the total Enterprise market. In long distance voice, MCI is the second-largest US carrier, behind AT&T; when including local voice revenues, MCI's estimated share position is 6th. Across the legacy data products such as private line, FR, and ATM, MCI generally maintains the second market share position. Historically, MCI held a lead in Large Enterprise DIA, but we believe the disruption of the past few years, both in terms of its client base being particularly hard hit from the Internet crash, as well as the company's own bankruptcy filing, has pushed AT&T into the lead spot in this product. Conversely, this decline leads to opportunity going forward. We believe network overhauls to migrate toward a single IP core as well as intense sales focus within Large Enterprise will drive faster-than-industry growth for MCI in these core products, with IP-LAN/WAN driven products such as IP-VPNs and MPLS-enable services leading the way

Figure 16: The Core MCI Products and Competitors

Core MCI Wholesale-Focused Markets & 2003 Estimated Sizes - \$31.0 b		
Voice - \$13.8 b		
1	AT&T	
2	MCI	
3	Qwest	
4	Sprint	
5	RBOCs	
DIA - \$3.6 b		
1	Sprint	
2	Level 3	
3	MCI	
4	AT&T	
5	Qwest	
Dial & DSL Wholesale - \$2.0 b		
1	Level 3	
2	MCI	
3	Sprint	
4	Qwest	
5	Regional Players	
Core MCI Retail-Focused Markets & 2003 Estimated Sizes - 121.0 b*		
Voice - \$55.7 b		
1	SBC	
2	AT&T	
3	Verizon	
4	Sprint	
5	BellSouth	
6	MCI	
7	Qwest	
Packet Svcs⁽¹⁾ - \$26.0 b		
1	AT&T	
2	MCI	
3	Sprint	
4	Qwest	
5	RBOCs (in-region)	
		(1) FR, ATM & IP LANs, WANs and VPNs
Private Line: Retail⁽²⁾ - \$16.0 b		
1	AT&T	
2	MCI	
3	RBOCs	
4	Sprint	
5	Network Carriers	
		(2) DS-3 & below; market includes ILEC/IXC last-mile links since most end-users are retail-based
DIA - \$4.6 b		
1	AT&T	
2	MCI	
3	Qwest	
4	Network Carriers	
5	Regional Players	
Managed Svcs⁽³⁾ - \$9.0 b		
1	AT&T	
2	Network Integrators⁽⁴⁾	
3	Qwest	
4	MCI	
5	RBOCs	
		(3) Includes network management outsourcing fees, hosting, e-services & colocation revenue.
		(4) The large network design integrators such as IBM, EDS & others.
Network Integration⁽⁵⁾ - \$18.5 b		
1	Network Integrators⁽⁶⁾	
2	AT&T	
3	Regional/Other Consultants	
4	RBOCs	
		(5) Includes outsourced network design and integration
		(6) The large network design integrators such as IBM, EDS & others.

* \$130 b of gross Retail Large Enterprise & SME revenues less \$9 b of intercarrier eliminations

Bold = A dominant market share position

Competitive Advantages:

MCI's core competencies are anchored by its top-tier market share position and reputation within Large Enterprise, its rejuvenated balance sheet and its product mix, which has the heaviest weighting in favor of data revenues of any incumbent carrier. MCI has established itself, in conjunction with AT&T, as one half of the dominant "duopoly" in terms of the retail Large Enterprise telecom services market. The merging of WorldCom and its leading Internet business, UUNet, with MCI's corporate customer list pushed the company to years of accelerated growth, as it was successful in penetrating the old MCI commercial customers with increasing amounts of IP-centric products. While the Internet downturn was particularly impactful to UUNet, which had a heavier than average exposure Internet-centric companies, we believe MCI's established reputation and corporate customer list will continue to be its number one competitive advantage, with the share loss of the last two years ironically providing upside opportunity over the next several years. Additionally, thanks to the fresh-start procedures of bankruptcy, MCI is eliminating more than \$28 billion in term debt, leaving it with only \$4.7-\$5.7 billion of total debt at re-emergence, and only \$2.5-\$3.5 billion of net debt. This leaves its estimated 2004 leverage at only 0.7x net debt/EBITDA and its interest coverage at 3.4x (somewhat lower than AT&T's due to MCI's lower margins). This increased slack should give the company more flexibility to invest capital in efficiency-improving areas. Finally, MCI maintains a revenue mix that is easily the most data-weighted among the incumbent carriers. We estimate that 53% of its 2004 revenues will be data/IP, versus an industry average of 45%, and AT&T's weighting of 40%. We believe this weighting differential alone gives MCI an average 100 bp total revenue growth advantage versus AT&T.

Figure 17: Competitive Advantage – Product Mix Favors Data

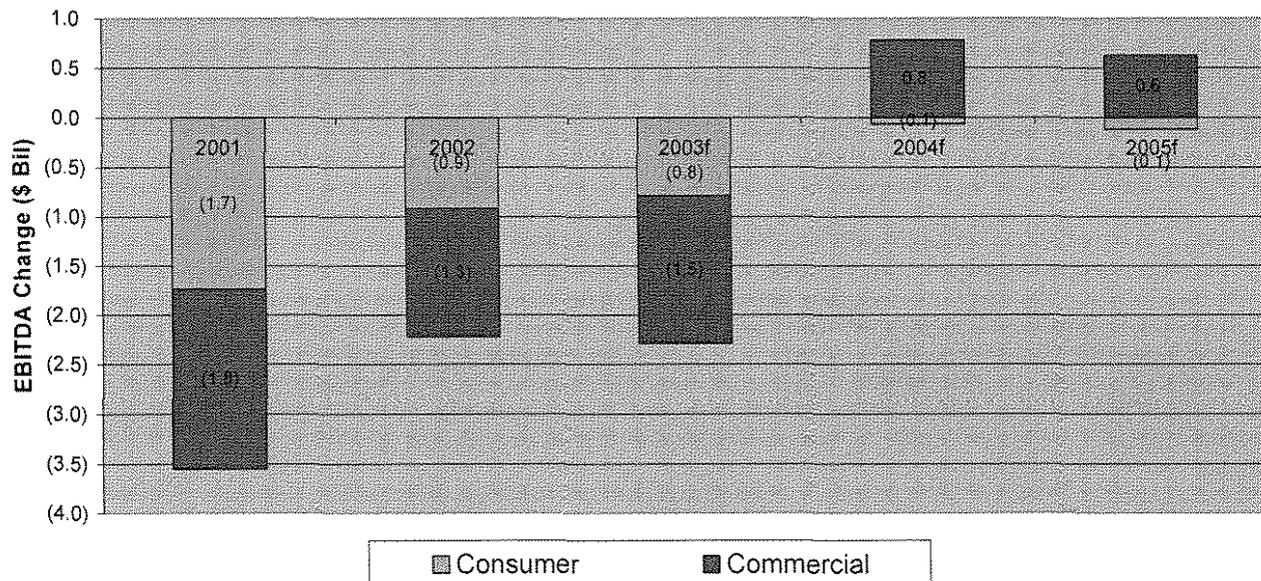
Mix Weighted in Favor of Data			
2004f Revenues (\$ Bil):	MCI Commercial Serv.	Enterprise Coverage Group Average	MCI Mix Vs. Enterprise Group Average
Voice	\$5.3	\$24.3	
Growth	-5.3%	-3.9%	
% of Total	29%	44%	-1500 bp
Data	\$9.7	\$24.8	
Growth	3.8%	3.2%	
% of Total	53%	45%	800 bp
Other (Inc. Intl)	\$3.3	\$6.0	
Growth	2.9%	-1.3%	
% of Total	18%	11%	
Total	\$18.3	\$55.1	
Growth	0.8%	-0.6%	

Competitive Challenges:

MCI is facing a number of challenges as it re-emerges from bankruptcy, including low margins (large cost structure and low pricing), continuing drag from its Consumer unit and some technical volatility that is likely to impact the stock upon initial trading. We believe MCI's low margins are driven by a combination of lower pricing and the myriad networks, systems and hierarchical infrastructure built up from its acquisition process over the years. MCI has historically operated as a holding company that oversees the numerous autonomous companies it has acquired since the 1980s. This has helped lead to the lower margins it maintains versus its peers, due to the layers of inefficient legacy systems, redundancies and parallel network protocols inherent in this structure. Additionally, MCI faces ongoing drag from its Consumer unit as it suffers under technological substitution losses to wireless and Internet, as well as competitive losses to RBOCs. Over the past two years, despite the fact that Consumer is only approximately 25% of revenues, it has accounted for approximately 45% of total EBITDA declines (shown in the following figure). We expect ongoing declines in this unit, estimated at 5% annual revenue declines over the long run, and 16% annual EBITDA declines. Additionally, we estimate that due to its broader deployment of UNE-P, the margins on its local product are lower, and will take longer to reach breakeven than AT&T's.

Finally, we expect there to be technical volatility in both the when-issued share price, as well as the initial exchange trading of the stock due to issues of dilution-concern and ownership redistribution from restructuring (credit) investors into new equity investors.

Figure 18: Competitive Challenge – Consumer Drag



While MCI's low margins represent a current disadvantage, costs are one thing that management can truly control. Therefore, we believe this actually represents tremendous upside for the company – the key will be management's dedication to *ongoing* margin improvements. The drag from Consumer revenue declines is more problematic, but we believe MCI benefits from a lower proportion of fixed costs within its Consumer unit, which should allow the company to better eliminate expenses as volumes decline, allowing cashflows to remain positive strategically, albeit at very low margins. This is highlighted by the fact that we estimate that SG&A as a percent of revenues in 2003 is 33% for MCI, but 43% at AT&T.

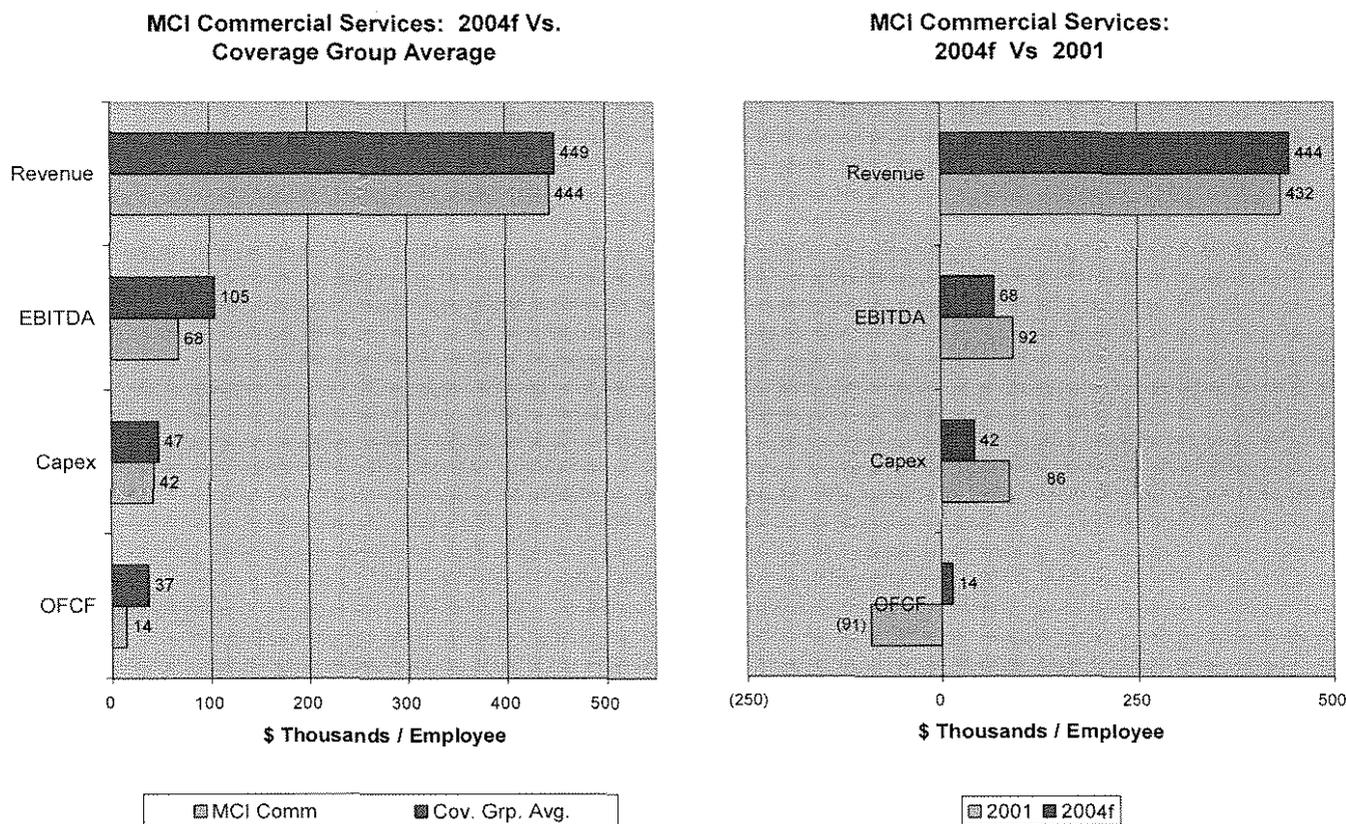
Network:

MCI owns and operates an estimated 75,000 global route-mile (ex-undersea), IP-MPLS over DWDM at the core fiber backbone reaching an estimated 4,500 IP POPs in 130 markets in 65 countries worldwide. It represents one of the most extensive networks in the US and claims the most dial IP modems of any US carrier (3.2 million). Management is aggressively overhauling the legacy components of this network, consolidating its protocols to a single IP core and deploying MPLS switching throughout as part of its initiative to improve network efficiency and performance, and lower costs. This initiative will allow MCI to significantly reduce its estimated 400+ total systems as well as eliminate redundant overlay networks and consolidate all traffic (including voice) to a single IP core. Management intends to migrate approximately 25% of its voice traffic to this core by the end of 2004, leaving it somewhat behind incumbent competition, which spending the bulk of their 2003 capital budget to begin a migration of traffic to a single packet-switched core this year. We believe this "lost year" in terms of capital spending as a result of the bankruptcy process is the likely to be the largest friction to the company as it recovers from its financial distress. Having said that, MCI's market share, reputation and scale provide strong assets to carry it while such efficiencies are achieved, and we believe there are material opportunities for improved cashflows deriving from such improvements.

Productivity and Efficiency:

MCI is estimated to lag the Enterprise industry in most operating metrics, but particularly in EBITDA per employee. At a 2004 forecast of \$68k EBITDA/employee, MCI lags the industry average of \$105k by 35% and the AT&T level of \$141k by more than 50%. We believe this is driven by a combination of lower pricing and a redundant cost structure accumulated through multiple acquisitions. However management is keenly focused on achieving 500 bps+ of margin improvement by 2005 (MCI lags the industry by as much as 1,000 bps), which we believe is achievable given the magnitude of opportunity for improvement, the network and systems overhaul and hierarchical restructuring taking place.

Figure 89: Operating Metrics Per Employee



OCF is defined as CFFO - Capex; All metrics reflect commercial telecom services operating information divided by estimated commercial telecom services employees.

Capital Structure and Financial Strength:

MCI should re-emerge from bankruptcy with 326-366 million shares of new equity and \$4.5-\$5.5 billion in new senior term debt (plus \$275 million in capitalized leases). Of the 15 classes of claimants to MCI's assets, five can or will be receiving equity in the newly reorganized company, including the following classes:

	<u>Est. Claim Amount (\$ bil)</u>
■ Class 5 WorldCom Senior Debt Claims	\$27.3
■ Class 6 WorldCom General Unsecured Claims	n/a
■ Class 11 Intermedia Senior Debt Claims	\$0.9
■ Class 12 Intermedia General Unsecured Claims	n/a
■ Class 13 Intermedia Subordinated Debt Claims	\$0.3

Of these classes, we estimate that Class 5, the WorldCom Senior Debt Claims, will receive nearly 90% of the new stock, with Class 11 receiving approximately 8%, with the balance spread among the rest, representing 100% equity ownership of the company at the moment of reorganization. However, management has established a restricted stock and options program through which shares and options on shares will be distributed, diluting the re-emergence owners over time. Our analysis makes no assumptions or estimations regarding such dilution from restricted stock or options. We have assumed the bankruptcy plan capital structure of 326 million in new equity shares, valued at \$25 per share, to yield an initial \$7.2 billion market cap, and \$5.7 billion of total debt (\$3.5 billion in net debt), resulting in an initial enterprise value of \$11.6 billion. This represents a 4.4x multiple of our 2003 MCI EBITDA forecast and 3.4x multiple of our 2004 forecast, which is in-line with current trading levels of AT&T). The following table highlights various potential prices and implied EV/EBITDA multiples.

Figure 20: MCI Stock Price & Implied EBITDA Multiples

Assumed NewCo Share Price	NewCo Total Enterprise Value	EBITDA & Multiples			
		2003	2004		
		\$2,731	\$3,250	\$3,448	\$3,690
\$22.50	10,772.7	3.9x	3.3x	3.1x	2.9x
\$23.00	10,935.7	4.0x	3.4x	3.2x	3.0x
\$23.50	11,098.7	4.1x	3.4x	3.2x	3.0x
\$24.00	11,261.7	4.1x	3.5x	3.3x	3.1x
\$24.50	11,424.7	4.2x	3.5x	3.3x	3.1x
\$25.00	11,587.7	4.2x	3.6x	3.4x	3.1x
\$25.50	11,750.7	4.3x	3.6x	3.4x	3.2x
\$26.00	11,913.7	4.4x	3.7x	3.5x	3.2x
\$26.50	12,076.7	4.4x	3.7x	3.5x	3.3x
\$27.00	12,239.7	4.5x	3.8x	3.5x	3.3x
\$27.50	12,402.7	4.5x	3.8x	3.6x	3.4x
\$28.00	12,565.7	4.6x	3.9x	3.6x	3.4x

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EQUITY RESEARCH

At our base case assumptions of the maximum debt and minimum equity (\$5.7 billion in debt and 326 million equity shares), MCI will still boast one of the best balance sheets in the business. The following table highlights this strength. At re-emergence, we expect MCI to have leverage of 1.3x (net debt/EBITDA). With expected improvements in 2004 EBITDA, we expect leverage to fall to 0.7x and interest coverage to be 3.4x. This financial slack should give MCI the flexibility to invest capital in efficiency-improving areas.

Figure 21: MCI Capital Structure Outlook – Pre & Post Restructuring

MCI Capital Structure & Cashflow Outlook: 2003 Pre & Post Reorg. & Forecasts								
(\$ bill):	2003		Proforma Projections - Reorganized Company					
	Pre-Reorg.	Reorganized Company	2004	2005	2006	2007	2008	2009
Cash Balance	\$4.7	\$2.3	\$3.1	\$4.2	\$5.1	\$6.1	\$7.2	\$8.3
Total Assets	\$20.0	\$20.9	\$21.8	\$23.1	\$24.5	\$26.2	\$28.0	\$30.0
Total Debt	\$34.2	\$5.7	\$5.6	\$5.5	\$5.5	\$5.5	\$5.5	\$5.5
Net Debt (Net of Adjustments)	\$29.4	\$3.4	\$2.5	\$1.3	\$0.4	(\$0.6)	(\$1.7)	(\$2.8)
Debt Mat./Paid-down this Period ⁽¹⁾		\$28.4	\$0.1	\$0.1	\$0.0	\$0.0	\$0.0	\$0.0
OFCF ⁽²⁾		\$2.2	\$1.0	\$1.2	\$0.9	\$1.0	\$1.1	\$1.1
Total Incremental Financing Required		\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Portion Assumed as Debt		\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Portion Assumed as Equity		\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Leverage (Net Debt / EBITDA)	10.3x	1.3x	0.7x	0.3x	0.1x	-0.1x	-0.3x	-0.5x
Coverage (Unlev. OFCF /Cash Int.)	not paying coupons in '03		3.4x	4.0x	3.5x	3.8x	4.1x	4.3x

Comments

Represents the least levered, large-cap telecom services company

(1) 2003 debt reduction represents the debt forgiven as part of fresh start accounting under Chapter 11.

(2) Operating Free Cash Flow is defined as CFFO - capex.

MCI as a Consolidation Play?

Upon re-emergence from bankruptcy, MCI will present itself as an extremely attractive commercial telecom services company, with minimal debt, strong coverage ratios and the second-leading market share among the Enterprise carriers, but slowed by a high cost structure and a consumer unit that is in sharp decline. If a potential suitor could solve the consumer overhang by somehow selling off the consumers that are out of the suitor's local footprint (if it has any), and get comfortable with its ability to materially rationalize MCI's commercial cost structure, MCI could be attractive at its estimated \$10-\$12 billion valuation upon re-emergence. There is significant execution risk however in such a transaction, as paring off the unwanted portions of the consumer arm could be highly complex, require extensive regulatory approvals, receive very low valuations and take a long time.

Additionally, the only deal structures that are likely to receive regulatory approval are the ones that are the most economically unattractive. For example, in order for an RBOC to win regulatory approval for an MCI acquisition, it would likely have to divest the consumer business in-region (which would be the only customers the RBOC would want to keep to begin with) and agree to do one of the following: (1) operate MCI's consumer long distance and local UNE-P business out of region, or (2) sell it intact to another company that would. All of this makes for an especially messy transaction with unattractive economics. The only consumers that are efficient for an RBOC to keep would be the in-region ones, which they'd have to divest. And the out of region ones, served with low-margin UNE-P would be extremely unattractive and dilutive. Additionally, we do not see many other buyers out there that would be interested in owning and operating the consumer business – there simply aren't enough local customers for it to make sense for a cable company to buy (and the cable companies would likely have the same incentives to divest the out-of-footprint consumers and keep the in-footprint ones, again flying exactly in the opposite direction of what would likely gain regulatory approval). In our opinion, all of this makes an acquisition unlikely in the near term.

Business Units and Forecasts:

As the following table shows, we believe that 2004 will mark the last consolidated revenue decline for MCI as it pulls itself out of bankruptcy and the economy stabilizes and begins to improve. We expect total revenues to decline approximately 1.7% in 2004, but EBITDA to grow a material 26%+, driven by the significant cost reduction efforts discussed previously and the forecast 310 bp improvement in EBITDA margins. Operating free cashflow declines are also expected to bottom out in 2004 at around \$1 billion, and then grow approximately \$100-200 million per year. As the Commercial unit refocuses its efforts on regaining profitable market share, and demand begins at least a modest recovery, we expect consolidated revenue growth to approach the 2-3% range. However, we believe EBITDA can grow at more healthy rates due to the significant cost reduction opportunities and management's intense focus in this area – we expect to see consolidated EBITDA grow approximately 11% annually through 2010.

Figure 22: MCI Consolidated Summary Forecasts

(\$ Bil)	2001	2002	2003f	2004f	2005f	2010	'03 to '10 CAGR
Commercial (Inc. Intl)	\$22.7	\$20.5	\$18.2	\$18.3	\$19.1	\$24.1	4.1%
% Growth	4.8%	-9.7%	-11.4%	0.8%	4.6%	4.2%	
Consumer	\$11.2	\$8.7	\$6.3	\$5.7	\$5.3	\$4.5	-4.7%
% Growth	-13.6%	-21.8%	-27.9%	-9.1%	-7.2%	-2.1%	
Corp.	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	#DIV/0!
Total Revenue	\$33.9	\$29.2	\$24.5	\$24.0	\$24.5	\$28.6	2.3%
% Growth	-2.1%	-13.7%	-16.3%	-1.7%	1.8%	2.4%	
EBITDA	\$7.2	\$5.0	\$2.7	\$3.4	\$4.0	\$5.7	11.1%
% Growth	-32.9%	-30.7%	-45.6%	26.2%	14.8%	6.2%	
Margin	21.4%	17.2%	11.2%	14.3%	16.2%	20.0%	
Operating Income	\$5.5	\$3.4	\$1.3	\$1.8	\$2.1	\$3.5	15.8%
% Growth	-41.8%	-38.2%	-62.9%	40.8%	18.3%	8.6%	
Margin	16.4%	11.7%	5.2%	7.4%	8.7%	12.4%	
Net Income	\$2.7	\$1.5	\$1.2	\$0.9	\$1.1	\$2.0	7.9%
% Growth	-49.3%	-42.2%	-25.0%	-24.6%	24.6%	10.2%	
Margin	7.9%	5.3%	4.7%	3.6%	4.4%	6.9%	
Capex	\$4.8	\$1.5	\$1.2	\$1.8	\$2.0	\$2.8	13.1%
% Growth	-30.3%	-69.5%	-18.6%	48.9%	13.7%	5.1%	
% of Rev	14.1%	5.0%	4.9%	7.4%	8.2%	9.8%	
OFCF⁽¹⁾	(\$5.3)	\$3.4	\$2.2	\$1.0	\$1.2	\$1.1	-9.3%
% Growth		-163.7%	-35.0%	-53.7%	17.0%	1.9%	
Margin	-15.6%	11.5%	9.0%	4.2%	4.9%	3.9%	

(1) Operating Free Cash Flow is defined as CFFO - capex.

Commercial:

We believe the ability for MCI management to strip away significant cost structure is the most important value driver for the company over the next 1-2 years. In this regard, given its importance, the vast opportunity (MCI Commercial's estimated margins lag the industry by 1,000 bps and AT&T's by as much as 1,500 bps), and management's focus and current initiatives, we believe MCI - Commercial will be successful in driving more than 680 bps of EBITDA margin improvement over the next 2 years, with approximately 420 bps of this coming in 2004 and 260 bps in 2005. This would still leave MCI Commercial's estimated EBITDA margins at only 18% in 2005, which would still represent a 450 bp disadvantage versus the industry forecast and a 1,000 bp discount to AT&T Business Services' margins. A key question in forecasting margin improvements of this magnitude is pricing. As we've discussed earlier, given the already slim margins at the company, we believe aggressive across-the-board price cuts are not in store, but would clearly wipe out forecasted margin improvements if they were to occur.

The following table summarizes our Commercial forecasts, which are characterized by recovering but still-moderate revenue growth and but sharply improving margins and EBITDA. Commercial revenues are expected grow 0.8% in 2004, driven by 4% growth in data revenues, moderated by a 3% decline in voice revenues. We expect EBITDA to grow 38% in 2004 as margins are expected to improve by approximately 420 bps. We believe 2004 should also mark the low-mark in terms of OFCF at approximately \$0.6 billion, which should begin healthy growth from that point forward. Strategically, we expect the Commercial unit will grow revenues 4% annually, due to a greater weighting of data revenues (53% of 2003 MCI Commercial revenues versus an industry average of 45%) and market share recapture-opportunities within Large Enterprise. With ongoing improvements in margins, back toward the low end of industry averages, we believe EBITDA will grow 15% annually, on average, through 2010.

Figure 23: MCI Commercial Summary Forecasts

							'03 to '10
(\$ Bil)	2001	2002	2003f	2004f	2005f	2010	CAGR
Total Voice	\$7.9	\$6.6	\$5.6	\$5.3	\$5.3	\$5.7	0.3%
% Growth	-16.0%	-17.1%	-15.0%	-5.3%	-0.8%	1.9%	
Data & IP	\$11.8	\$10.4	\$9.4	\$9.7	\$10.4	\$14.3	6.2%
	19.6%	-11.6%	-10.1%	3.8%	7.6%	5.4%	
<u>Other</u>	<u>\$3.0</u>	<u>\$3.5</u>	<u>\$3.2</u>	<u>\$3.3</u>	<u>\$3.4</u>	<u>\$4.1</u>	3.7%
Total Revenue	\$22.7	\$20.5	\$18.2	\$18.3	\$19.1	\$24.1	4.1%
% Growth	4.8%	-9.7%	-11.4%	0.8%	4.6%	4.2%	
EBITDA	\$4.8	\$3.5	\$2.0	\$2.8	\$3.4	\$5.5	15.3%
% Growth	-27.3%	-26.9%	-42.4%	38.4%	22.3%	7.3%	
Margin	21.3%	17.3%	11.2%	15.4%	18.0%	22.9%	
Capex	\$4.5	\$1.4	\$1.1	\$1.7	\$1.9	\$2.7	13.3%
% Growth	-27.9%	-69.9%	-18.5%	57.1%	10.1%	9.2%	
% of Rev	19.9%	6.6%	6.1%	9.5%	10.0%	11.0%	
OCF⁽¹⁾	(\$4.8)	\$1.7	\$1.3	\$0.6	\$0.9	\$1.2	-1.5%
% Growth	129.8%	-136.7%	-26.4%	-53.5%	50.9%	-2.8%	
Margin	-21.0%	8.5%	7.1%	3.3%	4.7%	4.8%	

(1) Operating Free Cash Flow is defined as CFFO - capex.

Consumer:

MCI faces ongoing drag from its Consumer unit as it faces technological substitution losses to wireless and Internet, as well as competitive losses to RBOCs. Over the past two years, despite the fact that Consumer is only approximately 25% of revenues, it has accounted for approximately 45% of total EBITDA declines. We expect ongoing declines in this unit, estimated at 5% annual revenue declines over the long run, and 16% annual EBITDA declines. Additionally, we estimate that due to its broader deployment of UNE-P, the margins on its local product are lower, and will take longer to reach breakeven than AT&T's. For example, we believe MCI's 2003 local UNE-P EBITDA margins are -30%, while AT&T's are -26%. This should improve over the next several years, but at slow rates and with limited profit potential. On the plus side, we believe MCI benefits from a lower proportion of fixed costs within its Consumer unit, which should allow the company to better eliminate expenses as volumes decline, allowing cashflows to remain positive strategically, albeit at very low margins. This is highlighted by the fact that we estimate that SG&A as a percent of Consumer revenues in 2003 is 33% for MCI, but 43% at AT&T. We summarize our MCI local UNE-P forecasts in a subsequent table.

The following table summarizes our Consumer forecast, which is characterized by 7-9% annual revenue declines losses through 2005, easing to mid-single single digit declines longer-term as wireless substitution matures, RBOC penetration slows, voice-rate declines ease, and UNE-P local bundling helps boost customer retention. On average, we are expecting revenues to decline nearly 5% annually through 2010, with EBITDA staying positive throughout. Ultimately, the Consumer unit should shrink to a size that is small relative to the Commercial arm, such that its ultimate resolution would not have dramatic effects. The challenge for MCI in the interim is to build wholesale replacements for the network volume that Consumer currently uses, which should be aided by a gradual migration of voice to VoIP.

Figure 24: MCI Consumer Summary Forecasts

		2001	2002	2003f	2004f	2005f	2010	'03 to '10 CAGR
	(\$ Bil)							
Stand-Alone LD Voice		\$7.1	\$5.0	\$2.8	\$1.5	\$0.7	\$0.1	-37.9%
% Growth		2.1%	-29.3%	-43.2%	-46.4%	-55.9%	n/m	
Bundled Voice		\$0.2	\$1.0	\$2.4	\$3.2	\$3.9	\$4.0	7.9%
		n/m	576.1%	125.6%	37.4%	18.5%	-1.8%	
Other		\$4.0	\$2.7	\$1.1	\$1.0	\$0.8	\$0.4	-14.5%
Total Revenue		\$11.2	\$8.7	\$6.3	\$5.7	\$5.3	\$4.5	-4.7%
% Growth		-13.6%	-21.8%	-27.9%	-9.1%	-7.2%	-2.1%	
EBITDA		\$2.4	\$1.5	\$0.7	\$0.6	\$0.5	\$0.2	-16.1%
% Growth		-42.0%	-38.2%	-53.1%	-9.4%	-18.5%	-15.9%	
Margin		21.5%	17.0%	11.0%	11.0%	9.7%	4.5%	
Capex		\$0.3	\$0.1	\$0.1	\$0.0	\$0.1	\$0.2	10.1%
% Growth								
% of Rev		2.4%	1.1%	1.3%	0.5%	1.8%	3.5%	
OF CF⁽¹⁾		(\$0.5)	\$1.6	\$0.9	\$0.4	\$0.3	(\$0.0)	-165.7%
% Growth			-402.6%	-44.2%	-53.8%	-31.3%	n/m	
Margin		-4.8%	18.6%	14.4%	7.3%	5.4%	-1.1%	

(1) Operating Free Cash Flow is defined as CFFO - capex.

Figure 25: MCI Consumer Local UNE-P Forecasts

MCI Consumer - Stand-Alone Local UNE-P Forecasts				
Subscribers: (000)	2003f	2004f	2005f	2006f
Eligible Consumer HHs	96,513	93,394	92,221	91,396
% of US	78.0%	85.0%	85.0%	85.0%
Gross Adds	3,496	3,829	3,704	3,574
- Churn (Annual)	<u>50.2%</u>	<u>47.2%</u>	<u>39.6%</u>	<u>37.4%</u>
Net Adds	2,041	1,496	1,153	733
Year-End Subs	4,941	6,437	7,590	8,322
Penetration of Eligible HHs	5.1%	6.9%	8.2%	9.1%
Revenue:				
Effective ARPU/Mo.	\$29.6	\$28.2	\$27.6	\$27.6
Local UNE-P Revenue (\$mil)	\$1,411	\$1,941	\$2,333	\$2,646
% Growth	115%	38%	20%	13%
Expenses:				
CGS: UNE-P Rate/Sub/Mo.	\$18.2	\$19.0	\$19.3	\$19.3
Gross Margin	38%	32%	30%	30%
SG&A (Inc. Acq. Costs)/Sub/Mo.	\$20.7	\$13.4	\$9.7	\$8.0
EBITDA (\$mil)	(\$419)	(\$273)	(\$107)	\$36
Margin	-30%	-14%	-5%	1%

Valuation – Bankruptcy Plan Capital Structure:

We have assumed the bankruptcy plan base-case capital structure of 326 million in new equity shares and \$5.7 billion of total debt (\$3.5 billion of 2003 net debt). The following table summarizes our estimation of the impact of higher amounts of equity (and thus lower amounts of debt) in the initial capital structure. We estimate that for each incremental 20 million shares of equity issued at the time of reorganization, the dilution per share is estimated to be \$0.50. Therefore, if the maximum amount of 366 million shares is issued, we believe the equity value would be \$1.0 less than if the minimum 326 million shares are issued. The table also shows that no matter what the ultimate blend of debt and equity are under the reorganized capital structure, the leverage of the company is extremely modest. Additionally, even under the maximum 366 million share scenario, the implied P/E on estimated 2004 EPS is still a modest 10.0x, below the 2004 industry average of 11.5x.

Figure 26: Capital Structure & Value Implications

MCI - Valuation & Balance Sheet Effects of Different Re-emergence Capital Structures					
Debt Scenario	Bankruptcy Base Plan	Range of Bankruptcy Plan Debt Scenarios		Versus Bankruptcy Plan Base Case	
	Maximum of Possible Debt	Mid-Range of Possible Debt	Lowest-End of Possible Debt	Mid-Range Vs. Base Case	Lowest-End Vs. Base Case
(\$ bil):					
Total Assets	\$20.9	\$20.9	\$20.9		
Total Debt	\$5.7	\$5.2	\$4.7	(\$0.5)	(\$1.0)
Debt / Assets	27.5%	25.1%	22.7%	-240 bp	-479 bp
Book Equity	\$8.4	\$8.9	\$9.4	\$0.5	\$1.0
Debt / Equity	0.7x	0.6x	0.5x	-0.1x	-0.2x
"New-Co." Shares (mil)	326	346	366	20.0	40.0
"New-Co." 2004 EPS	\$2.76	\$2.64	\$2.50	(\$0.12)	(\$0.26)
Implied P/E (on Assumed \$25 Price)	9.1x	9.5x	10.0x	0.4x	0.9x
Unlevered FCF / Share	\$4.41	\$4.15	\$3.93	(\$0.25)	(\$0.48)
Implied \$25 Share Price / FCF	5.7x	6.0x	6.4x	0.3x	0.7x
DCF- Value / "New-Co." Share	\$25.1	\$24.6	\$24.1	(\$0.5)	(\$1.0)

(1) Consolidated tracking stock information reflecting the current capital structure for Sprint. Corp.

Potential Trading Range:

The following table outlines what we believe to be a potential trading range for the new stock, given three views on the company. Our Base Case assumes that the stock's value is viewed on a discounted cashflow, as well as on relative EV/EBITDA multiple basis, and that management is reasonably successful in achieving its stated EBITDA goals for 2004. At an assumed maximum number of 366 million new shares, we believe a Bull-Case premium valuation could be \$27-\$28. Our Bear Case analysis assumes that only a EV/EBITDA multiple valuation gets applied and that the 10-year industry low multiple value is assigned to a 2004 MCI EBITDA amount that is only 50% as improved as management forecasts. This results in a \$22 value per share. We believe the near-term equilibrium range should be between these two points, roughly in the \$24-\$26 range.

Figure 27: Potential Trading Range

MCI Potential Trading Range Arguments

<u>New MCI Equity Valuation:</u>	<u>Bear Case</u>	<u>Base Case</u>	<u>Bull Case</u>
Market Assumptions	Stock gets valued at the 10-yr low-tick of industry EV/EBITDA multiples and market believe 2004 MCI EBITDA will only improve 50% of mgmt's forecasted \$1 billion amount. No intrinsic value (DCF) credit is given.	Stock gets valued both intrinsically and by peer EV/EBITDA target multiples. Market believes 2004 MCI EBITDA will achieve 80% of mgmt's forecasted improvement, reaching \$3.5 b.	Stock gets valued both intrinsically and by peer EV/EBITDA target multiples. Market believes 2004 MCI EBITDA will achieve 100% of mgmt's forecasted improvement, reaching \$3.7 b.
Valuation Metrics: \$ Bil			
Intrinsic Value:			
DCF - Public Equity Value	No Credit	\$8.2	\$8.2
EV / EBITDA Valuations:			
10-yr Low Industry Multiple	3.0x		
Industry Target Multiple		3.4x	3.4x
2004 EBITDA	\$3.2	\$3.4	\$3.7
Enterprise Value	\$9.5	\$11.8	\$12.6
- Net Debt	\$2.5	\$2.5	\$2.5
Equity Value	\$7.1	\$9.3	\$10.2
Equity Value Per Share⁽¹⁾ at...			
326 million shares (lowest)	\$22	\$27	\$28
346 million shares (mid-range)	\$22	\$27	\$28
366 million shares (max)	\$22	\$26	\$27

<u>Assumes 366 million Shares:</u>	<u>Price Support</u>	<u>Mid-Range Equilibrium</u>	<u>Premium Multiples</u>
Potential Trading Range:	\$22	\$24 - \$26	\$27 - \$28

(1) Equity Value per Share represents an equal weighted average of the DCF and EV/EBITDA multiple values for the Base Case and the Bull Case. For the Bear Case it only represents the EV/EBITDA multiple value.

Enterprise Telecom Services Comparables:

Figure 28: Enterprise Carrier Comparables

Company & Enterprise Value													
Stock Information				Enterprise Value					Investor Returns				
Company	Ticker	Price	Shares	Mkt.Cap	Net Debt	Non-Con. Assets	Enter. Value	Book Equity	Div Yld	ROA	Stock Performance: % Return		
			Out								Week	Month	YTD
AT&T ⁽¹⁾	T	\$19.08	789	15.1	8.5	0.0	23.6	13.6	5.0%	7.6%	1%	-5%	-27%
T Bus. Serv. ⁽²⁾										4.6%			
MCI ⁽¹⁾	MCI AV	\$25.26	326	8.2	3.4	0.0	11.7	8.4	0.0%	6.5%	1%	-5%	-27%
MCI Comm. ⁽²⁾										3.6%			
Sprint ⁽¹⁾	FON	\$15.22	903	13.7	0.0	0.0	13.8	13.3	3.3%	8.7%	-6%	-3%	5%
FON Comm. ⁽²⁾										4.2%			
Level 3 ⁽¹⁾	LVLT	\$5.33	653	3.5	4.5	0.0	8.0	0.3	0.0%	-1.9%	-4%	-1%	9%
L3 Comm. ⁽³⁾										-5.1%			
XO Comm.	XOCM	\$5.30	95	0.5	0.2	0.0	0.7	0.5	0.0%	-6.6%	-2%	-1%	N/A
Time Warner	TWTC	\$10.16	115	1.2	0.8	0.0	2.0	0.5	0.0%	-1.8%	-7%	-13%	382%
Enterprise Avg. (Largecap for Div & ROA)									2.8%	4.2%	-3%	-5%	68%
S&P 500 Avg. SPX									\$1.047		-1%	1%	19%
Operating Statistics													
Stock Information		Revenue				EBITDA				EPS			
Company	LEH Rating	2003		2004		2003		2004		2003		2004	
		\$ Bil	% Gwth	\$ Bil	% Gwth	\$ Bil	Margin	\$ Bil	Margin	\$	% Gwth	\$	% Gwth
AT&T ⁽¹⁾	1-OW	34.7	-8.1%	32.9	-5.4%	8.7	25.1%	7.9	24.0%	\$2.28	-17.2%	\$1.73	-24.3%
T Bus. Serv. ⁽²⁾		25.2	-5.3%	24.5	-2.5%	6.8	26.9%	6.8	27.9%				
MCI ⁽¹⁾	NR	24.5	-16.3%	24.0	-1.7%	2.7	11.2%	3.4	14.3%	N/A	N/A	\$2.76	N/A
MCI Comm. ⁽²⁾		18.2	-11.4%	18.3	0.8%	2.0	11.2%	2.8	15.4%				
Sprint ⁽¹⁾	2-EW	14.1	-7.0%	13.8	-2.6%	4.4	31.1%	4.5	32.9%	\$1.45	7.5%	\$1.55	6.4%
FON Comm. ⁽²⁾		9.3	-5.6%	9.3	-0.6%	2.5	26.8%	2.7	28.5%				
Level 3 ⁽¹⁾	1-OW	3.6	26.6%	3.6	-1.2%	0.4	12.1%	0.6	16.4%	(\$1.18)	N/M	(\$0.98)	N/M
L3 Comm. ⁽³⁾		1.6	2.9%	1.8	9.0%	0.4	27.3%	0.6	32.2%				
XO Comm.		1.2	-7.2%	1.2	6.7%	0.0	1.1%	0.0	1.8%	(\$1.28)	N/M	(\$1.08)	N/M
Time Warner		0.7	-7.0%	N/A	N/A	0.2	28.6%	N/A	N/A	(\$1.06)	N/M	(\$0.89)	N/M
Enterprise Ind.		151.6	-4.7%	154.8	2.1%	31.0	20.4%	32.9	21.3%				
Valuation Multiples & Capital Structure													
Stock Information		EV / Revenue		EV / EBITDA		EV / OFCF		P/E Ratio		Leverage Ratios		Coverage Ratios	
Company	Price Target	2003	2004	2003	2004	2003	2004	2003	2004	Nt Debt / Capital	Nt Debt / '04 EBITDA	Unlev. '04 OCF / Int.	
AT&T ⁽¹⁾	\$24	0.7x	0.7x	2.7x	3.0x	4.0x	6.9x	8.4x	11.1x	38.5%	1.1x	4.6x	
T Bus. Serv. ⁽²⁾		0.9x	1.0x	3.5x	3.4x	5.6x	8.4x						
MCI ⁽¹⁾	NR	0.5x	0.5x	4.3x	3.4x	5.3x	11.5x	N/A	9.2x	29.0%	1.0x	3.4x	
MCI Comm. ⁽²⁾		0.6x	0.6x	5.7x	4.1x	5.3x	11.5x						
Sprint ⁽¹⁾	\$18	1.0x	1.0x	3.1x	3.0x	8.0x	6.9x	10.5x	9.8x	0.2%	0.0x	9.0x	
FON Comm. ⁽²⁾		1.5x	1.5x	5.5x	5.2x	12.8x	11.5x						
Level 3 ⁽¹⁾	\$7	2.2x	2.2x	18.2x	13.6x	N/A	115.1x	N/A	N/A	93.1%	7.7x	1.1x	
L3 Comm. ⁽³⁾		5.0x	4.5x	18.1x	14.1x								
XO Comm.		0.6x	0.5x	53.2x	30.0x	N/A	N/A	N/A	N/A	23.3%	7.4x	No Cash Int.	
Time Warner		2.8x	N/A	9.8x	N/A	N/A	N/A	N/A	N/A	61.5%	N/A	N/A	
Enterprise Avg. (Largecap)		0.7x	0.7x	3.4x	3.1x	5.8x	8.5x	9.4x	10.0x	22.6%	0.7x	5.7x	
S&P 500 Avg.													

(1) Represents consolidated, total company information (for Level 3, reflects recurring items only - excludes any dark fiber, settlement & termination)

(2) Reflects operating statistics for the commercial portion of the company; valuation statistics reflect total company market valuation as a multiple of the commercial operating unit's cashflows.

(3) Reflects recurring Communications Group items only