

TechnoNetworking Hardware

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Between 70 and 100 per cent of all North American telecom service providers will go bankrupt within two years from Sept 2000 (15 months from today).
Which ones on your targeted customer list will still be there ?

Richard



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Nortel, JDS Uniphase, 360networks a cross-section of troubled telecom sector
DAVID PADDON

TORONTO (CP) - A year ago, Nortel Networks, JDS Uniphase and 360networks were flexing their high-tech muscles, boasting stellar share prices, double-digit revenue growth and the respect of both Wall Street and Bay Street.

Today, the entire telecommunications sector is in a shambles - brought down by a sudden slowdown in revenues, a lack of new money from investors and crushing debts amassed during the boom years.

"Basically, when everyone stopped spending, they did it all at once," said Brian Acker, chief investment officer with Acker Finley, a Toronto money manager. "Now there's a huge domino effect."

In essence, Nortel, JDS and 360networks provide a good cross-section of the industry.

Vancouver-based 360networks, which announced Friday it wouldn't make a scheduled \$11-million US interest payment because of a cash crunch, is one of about 14 North America companies that have spent billions to build high-speed fibre-optic networks in recent years.

Nortel Networks of Brampton, Ont., which is cutting another 10,000 jobs by the end of 2001, has seen its revenues drop dramatically this year because telecom carriers are suddenly unable to buy more equipment.

And because companies like Nortel need fewer components, suppliers like JDS Uniphase of Ottawa are seeing revenues dry up. JDS Uniphase warned Thursday that revenues in the current quarter will be \$100 million US less than expected.

One reason for the telecom industry's boom and bust, experts say, was the easy money available in the late 1990s and early 2000.

"For the last three years, the access to capital was really relatively wide open. Money was almost free. It has been an unprecedented time in telecommunications," said Rick Schafer, a Denver-based research analyst with CIBC World Markets.

As a result, a whole new generation of communications carriers sprang up, particularly in the United States. Among the bigger U.S. names were Global Crossings, Level 3 and Williams Communications.

Canadian-based companies like 360networks and Teleglobe, now a subsidiary of Montreal-based BCE Inc., were seen as late arrivals, although they each had ambitious plans to build their own global fibre-optics networks.

But when money for capital expenditures began to dry up in mid-2000 - a delayed effect of higher U.S. interest rates phased in over several months by the U.S. Federal Reserve - the telecom industry began to hurt.

For a while, some people believed the telecom sector would be immune to the slowdown, TD senior economist Marc Levesque said Friday.

"That was a very misguided view because what higher interest rates do is slow down demand in the overall economy for everything from fibre optic cables to toothpaste," Levesque said.

Yet, because telecommunications was perceived to be a high-growth area, investors were willing to buy stock and lend money to companies in that sector.

"If you believe the economy is going to slow (because of higher interest rates) but these companies are going to be immune to the slowdown, where are you going to put your money?" Levesque asked rhetorically.

Signs of trouble for Nortel began to emerge in October when it announced it had slightly missed its revenue target for the July-September quarter. The next day, the Toronto Stock Exchange had its second-worst day in history as investors bailed out of Nortel.

"In an environment like that, it doesn't take much in terms of bad news for investors to realize that their expectations were overblown and start bidding the stock down. And in the case of Nortel, it came down to earth very dramatically," Levesque said.

On Friday, Nortel shares traded as low as \$13.42 and closed at \$15.17 on the Toronto Stock Exchange. JDS fell \$1.37 to \$12.44 US on the Nasdaq stock market, where it is most widely traded. And shares of 360networks closed at 46 cents Cdn on the TSE, down 19 cents for the day and just above an all-time low of 41 cents set earlier in the day.

Schafer, who primarily follows optical components companies like JDS Uniphase and Nortel, said their fortunes won't improve until there's an end to the credit crunch crippling communications carriers.

"The carriers will have to feel comfortable spending money again, which will in turn lead to orders for Nortel, which will in turn lead to orders for components from JDS Uniphase," Schafer said.

Schafer shares the widely held view that few of the telecom carriers will survive that long.

"I think you'll see a shakeout in that group," Schafer said. "I think we have too many long-haul carriers."

Richard Prytula, president of Montreal-based TechnoCap, venture capital fund with \$250 million under management, has an even more pessimistic view of the industry - particularly for the new telecom carriers that have come into the market since the mid-1990s.

Somewhere between 70 and 100 per cent of all North American telecom service providers will go bankrupt within two years, Prytula predicted Friday, noting the U.S. rail and airline industries have undergone similar shakeouts.

"You're going to have even more difficulty in companies like JDS and Nortel as all these service providers start going under," Prytula said.

"What's going to happen is that they're all going to go bankrupt, one at a time. And someone's just going to go pick up the fibre (optic networks) and use the fibre that's there."

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