**EXHIBIT 8**
**Stone Container's Monthly Closing Stock Prices, 1989–1993 ($ per share, except index)**

| Month | Stone Container Stock Price | S&P 500 Index | Month | Stone Container Stock Price | S&P 500 Index |
|---|---|---|---|---|---|
| **1989** | | | **1991** | | |
| January | 31.859 | 297.47 | January | 13.109 | 343.93 |
| February | 31.625 | 288.86 | February | 14.344 | 367.07 |
| March | 29.531 | 294.87 | March | 15.563 | 375.22 |
| April | 30.516 | 309.64 | April | 16.547 | 375.34 |
| May | 28.922 | 319.05 | May | 21.328 | 389.83 |
| June | 24.875 | 317.98 | June | 21.203 | 371.16 |
| July | 26.719 | 346.08 | July | 20.594 | 387.81 |
| August | 31.375 | 351.45 | August | 21.453 | 395.43 |
| September | 28.547 | 349.15 | September | 18.500 | 387.86 |
| October | 25.609 | 340.36 | October | 22.297 | 392.45 |
| November | 24.016 | 345.99 | November | 19.609 | 375.22 |
| December | 23.406 | 353.40 | December | 25.375 | 417.09 |
| **1990** | | | **1992** | | |
| January | 21.078 | 329.08 | January | 28.313 | 408.78 |
| February | 20.344 | 331.89 | February | 26.469 | 412.70 |
| March | 20.828 | 339.94 | March | 26.953 | 403.69 |
| April | 18.016 | 330.80 | April | 27.453 | 414.95 |
| May | 19.859 | 361.23 | May | 24.266 | 415.35 |
| June | 16.047 | 358.02 | June | 24.625 | 408.14 |
| July | 15.563 | 356.15 | July | 18.500 | 414.22 |
| August | 11.891 | 322.56 | August | 16.750 | 414.03 |
| September | 10.047 | 306.05 | September | 15.000 | 417.80 |
| October | 8.828 | 304.00 | October | 16.875 | 418.68 |
| November | 9.797 | 322.22 | November | 19.125 | 431.35 |
| December | 11.156 | 330.22 | December | 16.750 | 435.71 |
| | | | **1993** | | |
| | | | January | 16.000 | 438.78 |
| | | | February | 15.375 | 443.38 |

**EXHIBIT 9**
**Selected Interest Rates, 1990–1993**

| | Government Bonds | | Corporate Bonds | |
|---|---|---|---|---|
| Interest Rate Data | Short Term | Long Term | Aaa | Baa |
| 1990 | 7.51% | 8.55% | 9.32% | 10.36% |
| 1991 | 5.42 | 7.86 | 8.77 | 9.80 |
| 1992 | 3.45 | 7.01 | 8.14 | 8.98 |
| January 1993 | 3.06 | 6.60 | 7.91 | 8.67 |
| February 1993 | 2.95 | 6.26 | 7.71 | 8.39 |
| March 1993 | 2.97 | 5.98 | 7.58 | 8.15 |
| April 1993 | 2.89 | 5.97 | 7.46 | 8.14 |

# MCI Communications Corporation (1983)

In April 1983, Wayne English, chief financial officer of MCI Communications Corporation, faced the problem of setting financial policy in an environment characterized by a large potential demand for external funding and great uncertainty concerning MCI's future. MCI, which provided long-distance telecommunications services in competition with AT&T, had seen its revenues grow from almost nothing in FY 1974 (ending March 31, 1974) to more than $1 billion in FY 1983. During that period, the company climbed from a loss of $38.7 million in FY 1975 to a profit of $170.8 million in FY 1983. In the last 2 years, its stock price had increased more than fivefold.

Nevertheless, the antitrust settlement between AT&T and the U.S. Department of Justice in January 1982 had significantly altered the economic landscape for MCI. The settlement, providing for the breakup of AT&T by early 1984, would affect MCI in two important ways. On the one hand, it offered the opportunity for greatly increased growth, since AT&T would be required, for the first time, to compete on equal quality-of-service terms with MCI. On the other hand, the settlement posed new uncertainties, since it promised to eliminate certain MCI cost advantages and to increase AT&T's competitive flexibility.

Even in the face of intensifying competition from AT&T, however, MCI was committed to extending the reach and capacity of its network. According to Brian Thompson, senior vice president for corporate development: "Economies of scale and scope are everything in this business. In the long term, the strategic high ground lies in owning your own facilities for basic call services and then leveraging off this to provide value-added services."

## Company Background

MCI was organized in August 1968 under the leadership of William McGowan as the Federal Communications Commission (FCC) appeared willing to allow increased competition with AT&T in the long-distance market. In June 1971, the FCC formally adopted a policy of allowing qualified new companies to enter the market for specialized long-distance services, which consisted chiefly of *private line* (i.e., dedicated telephone line) services for large telephone users. By June 1972, MCI was ready to begin construction of its telecommunications network.

To provide the necessary funds, MCI sold 6 million shares of common stock to the public at $5 per share.[1] Net proceeds after expenses and commissions were $27.1 million. MCI also obtained a $64 million line of credit from a group of four banks headed by the First National Bank of Chicago and further loan promises of $6.45 million from private investors in the form of 7½% subordinated notes (with attached warrants) of up to 5-year maturities. The bank loans carried an interest rate of 3¾% above prime, plus a commitment fee of ½% per annum on the unborrowed balance.

[1]This and subsequent prices and numbers of shares have been adjusted for all stock splits on or before April 1, 1983.

By March 31, 1974, the MCI communications system bad grown to 2,280 route-miles of transmission circuits, linking 15 major metropolitan areas. Still, this was far short of the 11,600 route-mile system originally planned in 1972. MCI had to rely on AT&T facilities to carry calls from its subscribers to MCI transmission centers in each metropolitan area. Since AT&T had successfully resisted providing a full range of these interconnection services, MCI was unable to generate significant subscriber revenues. Late in 1973, MCI suspended all construction activity as it pursued legal and regulatory remedies. As part of this process, it filed an antitrust suit against AT&T in March 1974 (Exhibit 1 presents this sequence of events schematically). The FCC ordered AT&T to provide MCI with the full range of interconnection facilities as of May 1974; MCI then resumed construction of its network.

In FY 1975, MCI had revenues of $6.8 million but losses of $38.7 million. By September 1975, despite a network consisting of 5,100 route-miles connecting 30 major metropolitan areas, MCI had a negative net worth of $27.5 million, an accumulated operating deficit of $87.3 million, and a stock market price just below $1 per share (see Exhibit 2 for MCI's financial and operating history). MCI had exhausted its line of credit from the banks, had been forced to renegotiate the previous credit agreement to defer interest payments, and was in technical default of many provisions of the revised credit agreement. In the midst of this crisis, MCI managed a public sale of 9.6 million shares of common stock in December 1975, each share having an associated 5-year warrant with an exercise price of $1.25. The net proceeds of this offering, which amounted to $8.2 million (or about $.85 per share-plus-warrant, compared with a then prevailing market price of $.875 per share), enabled MCI to survive.

MCI reached a turning point in 1976. "Execunet" service, which had been introduced in the winter of 1974, began to yield substantial revenues and changed the nature of the company. Execunet provided a service comparable to standard long-distance calling, with customers having random access to MCI's transmission lines. This enabled MCI to attract small business subscribers who could not afford the expense of dedicated private lines between particular cities (private line customers tended to be large corporations with large call volumes). Partly as a result, revenues increased to $28.4 million in FY 1976 and $62.8 million in FY 1977 (about half of which came from Execunet). Interest payments to the consortium of lending banks, which had been previously suspended, were resumed in August 1976. Just as MCI made its first profit of $100,000 in September 1976, the FCC won a court order that restricted Execunet to existing subscribers; this order was not lifted completely until May 1978.

The order restricting Execunet slowed, but did not halt, MCI's progress. Revenue growth slowed to 18% between FY 1977 and FY 1978 but quickly returned to annual rates of more than 50% once the order was lifted. The number of employees tripled from 605 in March 1977 to 1,980 in March 1981; plant grew from $136.6 million to $410.0 million over the same period. More important, MCI's profitability improved rapidly. After-tax earnings from continuing operations rose from a loss of $1.7 million for FY 1977 to a profit of $21.1 million in FY 1981 (see Exhibit 2). As a result, MCI had exhausted its tax loss carry-forward by the end of FY 1981, and stockholders' equity was a positive $148 million.

This record paled, however, in comparison to MCI's growth in subsequent years. In March 1980, MCI offered Execunet service to residential customers (hitherto it had been available exclusively to businesses) on a trial basis in Denver, Colorado. The results were so striking that within a week plans were made to offer Execunet to households nationwide. MCI's growth was then constrained only by a lack of investment capital, which soon became available in substantial quantities (see Exhibit 3). Revenues more than doubled to $506 million in FY 1982 and, with the acquisition of Western Union International from Xerox for $195.1 million in June 1982, revenues doubled again to $1,078 million in FY 1983. Income from operations was $295.1 million, with net earnings of $170.8 million. A range of new products such as MCI Mail (an electronic mail service) and the results of AT&T's settlement with the Department of Justice offered dramatic opportunities for further growth. (Income statements and balance sheets for MCI for 1981–1983 are presented in Exhibits 4 and 5.)



## Financial Policy

Until 1976 the need to obtain funds to continue operations dominated MCI's financial policy. The court's 1976 order preventing the extension of Execunet service to new customers restricted opportunities for growth and consequently reduced the need for investment funds. At the same time, restrictive covenants associated with the bank loans from the syndicate headed by the First National Bank of Chicago severely limited MCI's ability to raise new capital for expansion. Between 1976 and the summer of 1978, lease financing of new fixed investment was the only substantial source of funds available. This went largely into expanding capacity in MCI's existing markets.

Withdrawal of the court's Execunet order in May 1978 opened the way for accelerated growth if the required investment funds could be obtained. Wayne English, who had arrived as chief financial officer in February 1976, spent the summer of 1978 preparing to do this. First, he obtained agreement from the majority of the lending banks to a public offering of securities whose proceeds would retire their loans. Second, he arranged for the loans of those banks that refused this accommodation to be bought out by private investors. Finally, he bought up or converted a number of outstanding warrants and loans held by earlier investors. Consequently, in December 1978, MCI was able to enter the public capital markets for the first time since the equity issue of December 1975, with an offering of convertible preferred stock which raised $25.8 million—net of all issue expenses (see Exhibit 6). A second convertible preferred offering in September 1979 raised $63.1 million and a third in October 1980 netted $46.7 million.

The choice of convertible preferred stock was dictated on the one hand by the need for some form of equity capital, and on the other hand by the fact, as expressed by Mr. English, that "it was always our conviction that issuing more common would knock the props out from under the stock." As it was, the conversion price on the preferred stock rose with each offering, from $2.1875 in December 1978 to $5 in September 1979 to $9 in October 1980. In addition, the dividend on the preferred stock would be 85% tax-deductible to corporate purchasers without costing MCI a significant loss of tax benefits, since MCI's earnings were still sheltered by the carry-forward of past losses.

An additional feature of these preferred issues was a *call* provision that enabled MCI to force investors to convert to common stock, thus eliminating the drain of preferred dividends on cash flow. This provision typically specified that if the market price of MCI's common stock exceeded the conversion price by more than a stated margin (e.g., 25%) for 30 consecutive trading days, MCI could call the unconverted preferred shares in question for redemption at 110% of their issue value. Owners of preferred stock would, of course, voluntarily exchange their shares for common at the conversion price rather than allow them to be repurchased. A steadily rising stock price enabled MCI to use this mechanism to convert all three preferred issues to common stock by November 1981.

Proceeds from these preferred offerings allowed MCI to retire its short-to-intermediate term bank debt and to issue longer-term debt. Leasing activity decreased and, in July 1980, MCI raised $50.5 million through the public sale of 20-year subordinated debentures.

In FY 1981, as the demand for investment funds intensified, the direction of MCI's financial policy shifted slightly from offerings of convertible preferreds to convertible debt. After obtaining $102.1 million in April 1981 through a straight subordinated debenture issue, MCI raised $98.2 million in August 1981 and $245.9 million in May 1982 with convertible debentures.

These convertible debentures carried forced conversion (i.e., *call*) provisions similar to those of the earlier preferred stock issues. As a result, MCI was able to force conversion of the May 1982 issue in December 1982 and of the August 1981 issue in February 1983. The consequent additions to common equity enabled MCI to take on a still greater debt burden. Thus, a straight debenture issue in September 1982 yielded $209.9 million, and a further convertible debenture in March 1983 produced almost $400 million.

In all, MCI raised about $1,050 million from the public sale of securities in FY1982 and FY1983. As with all MCI offerings, the initial issues were oversubscribed. Interest costs were relatively high (see Exhibit 7), but in the words of Mr. English, "Availability of funds [was] the paramount consideration"; cost was "secondary." Moreover, since profitability was increasing more rapidly than interest expense, interest coverage actually increased during this time. Considering the situation in 1975, and in comparison to other companies (see Exhibit 8), this was a remarkable achievement.

However, as details of the FCC s response to the AT&T antitrust settlement began to emerge, the resulting uncertainty cast doubt on MCI's continued ability to raise funds in these amounts. MCI would have to proceed with care, agility, and imagination.

## The AT&T Antitrust Settlement and Other Developments

Historically, AT&T provided a necessary part of the MCI system—and its most serious competition. One part of AT&T—the local telephone operating companies (e.g., Illinois Bell, New England Telephone)—supplied MCI with connections to subscribers through their local telephone networks. MCI paid for these services at a rate negotiated in 1978, under the FCC's supervision, between MCI and the local telephone companies (predominantly AT&T subsidiaries). This charge was about $230 per month per access line, or $172.7 million a year by FY1983, MCI also used AT&T and other long-distance facilities to enable its customers to reach areas not already served by the MCI network. In FY1983, MCI paid at the standard commercial rate $137.2 million for these services.

MCI's principal competitor in the market for interstate long-distance services was AT&T's Long Lines division, with about 95% of the market in March 1983. AT&T Long Lines also reimbursed local operating companies for access lines, but at a rate about three times that charged MCI and the other competing carriers, such as GTE, Sprint, and ITT. This discrepancy was justified by the fact that MCI customers usually had to dial 20 digits to reach a long-distance number, compared with 11 digits (1, plus area code, plus 7-digit number) for an AT&T customer. Thus, AT&T Long Lines was expected to pay more for "superior access."

The settlement of the antitrust suit between AT&T and the Justice Department in January 1982 would separate AT&T from its local operating subsidiaries. AT&T would retain the Long Lines division and the intrastate long-distance facilities of the local companies. After separation occurred in January 1984, the long-distance operations would be consolidated in a new AT&T subsidiary named AT&T Communications. AT&T Communications would eventually compete on a more or less equal basis with MCI and the other long-distance companies (GTE, ITT, and so on). To ensure this result, the settlement required that by 1986 the newly independent local telephone companies provide *equal* quality of *access* to all competing long-distance providers. To implement equal access, a series of elections would be held in communities nationwide in which consumers would be asked to select a long-distance provider. Simultaneously, an FCC plan would phase out the differential in access charges between AT&T and its competitors by increasing the fees paid by MCI and others. Although equal access would be phased in over 2 to 3 years, the FCC plan in its original form called for an initial increase of about 80% in MCI access charges in 1984. Thus, on the one hand, MCI would eventually gain by acquiring equal access but, on the other hand, would immediately lose much of its existing cost advantage over AT&T.



The value of equal access to MCI was difficult to measure precisely. Some customers already enjoyed effectively equal access, since electronic switchboards had features that would automatically route calls via MCI lines whenever the usual 10- or 11-digit long-distance number was dialed. However, these tended to be large business customers who made up only a small fraction of MCI's revenue. A trial of equal access in part of Iowa led to an almost immediate increase in MCI's share of the long-distance market from less than 5% to about 20%. In this case, however, competition from MCI's non-AT&T competitors was not severe, and AT&T still paid more in access fees.

The impact of equalized access charges on market share was also difficult to judge. Under the FCC plan, AT&T's access pricing flexibility was expected to increase as deregulation of the long-distance market—the FCC's ultimate goal—proceeded. In principle, therefore, AT&T would be able to reduce its prices to prevent further erosion of its market share. In practice, however, it would make little economic sense for AT&T, with 95% of the market, to cut prices for the sake of preventing anything less than massive losses of market share to MCI and its other competitors. The outcome would depend on the direction taken by AT&T's management, which had been surprisingly aggressive in the past.

In the face of these uncertainties, it was difficult to predict MCI's growth in revenues and earnings in FY1984 and beyond. Forecasting the need for fixed and working capital was equally difficult; nevertheless, a consensus forecast is presented in Exhibit 9. Against these contingencies, MCI held about $550 million in cash in the spring of 1983. At the beginning of April 1983, its stock price stood at $47, and long-term interest rates had declined dramatically.

**EXHIBIT 1**
**Chronology of Significant Events, 1971–1984**

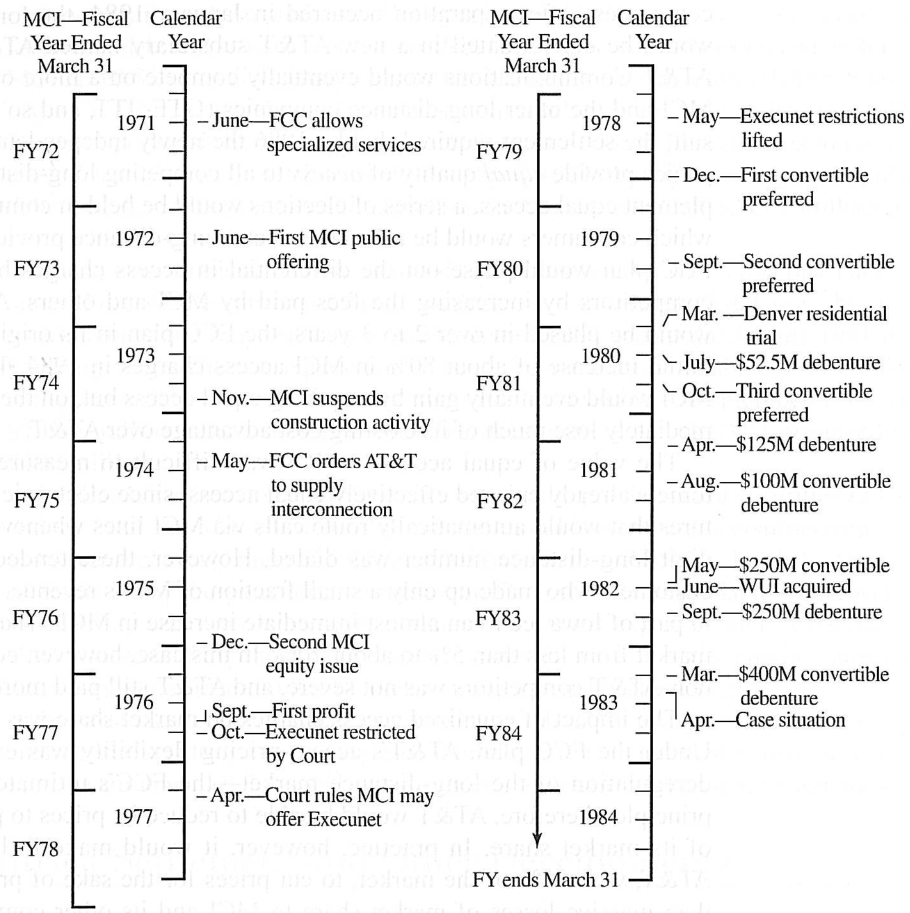


**EXHIBIT 2** **MCI Operating History for Years Ending March 31, 1974–1983 (millions of dollars except per share data)**

Sources: MCI annual reports; 10-K reports; and prospectuses.

| | 1974 | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 | 1981 | 1982 | 1983 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenues | $ .7 | $ 6.8 | $ 28.4 | $ 62.8 | $ 74.0 | $ 95.2 | $144.3 | $234.2 | $506.4 | $1,073.2 |
| Operating income | (15.0) | (17.3) | (10.6) | 17.7 | 25.0 | 30.6 | 37.2 | 51.3 | 167.0 | 295.1 |
| Net interest | 3.8 | 11.6 | 15.5 | 18.4 | 20.5 | 23.1 | 24.1 | 27.4 | 35.1 | 54.1 |
| Net after-tax earnings | (20.1) | (38.7) | (27.2) | (1.7) | 5.2 | 7.1 | 13.3 | 21.1 | 86.5 | 170.8 |
| Cash, cash equivalents | 1.2 | 1.4 | 3.7 | 2.8 | 4.3 | 10.3 | 7.9 | 12.7 | 144.8 | 542.0 |
| Working capital[a] | .3 | (7.4) | (12.7) | (18.3) | (21.7) | (26.9) | (34.1) | (24.8) | 42.5 | 391.8 |
| Plant, equipment | 60.0 | 81.0 | 120.8 | 136.6 | 148.9 | 188.9 | 282.0 | 410.0 | 619.5 | 1,324.2 |
| Total assets | 71.8 | 90.1 | 131.2 | 147.7 | 161.2 | 209.5 | 309.8 | 466.9 | 860.4 | 2,070.5 |
| Short-term debt[b] | 1.2 | 4.0 | 9.8 | 17.0 | 20.2 | 25.8 | 31.6 | 39.9 | 40.3 | 48.0 |
| Long-term debt | 48.4 | 95.2 | 144.3 | 149.7 | 152.8 | 153.3 | 172.9 | 242.7 | 400.0 | 895.9 |
| Stockholders' equity | 19.1 | (14.4) | (29.1) | (32.2) | (22.7) | 11.5 | 78.8 | 148.0 | 240.8 | 765.6 |
| Million shares outstanding[c] | 27 | 30.6 | 41 | 40.2 | 40.6 | 43.4 | 65.8 | 75.6 | 97.4 | 117.2 |
| Earnings per share[d] | $ (.74) | $(1.42) | $ (.81) | $ (.06) | $ .05 | $ .04 | $ (.01) | $ .09 | $ .91 | $ 1.69 |
| Price range—common stock | 1½–4½ | ½–2½ | ½–2½ | 1–2 | 1–2½ | 1½–3½ | 2–4½ | 2½–7 | 7–18 | 16–47 |

[a]Current assets less current liabilities (current assets include cash, cash equivalents).
[b]Includes long-term debt payable within 1 year.
[c]At year-end. MCI has never paid any dividend on its common stock.
[d]Earnings per common share after preferred dividends, before extraordinary items.

## EXHIBIT 3 Sources and Uses of Funds for Years Ending March 31, 1978–1983 (millions of dollars)

Sources: MCI annual reports; 10-K reports.

| | 1978 | 1979 | 1980 | 1981 | 1982 | 1983 |
|---|---|---|---|---|---|---|
| *Sources of Funds* | | | | | | |
| Funds from operations | | | | | | |
| Retained earnings[a] | $ 2.5 | $ 1.6 | $ (1.1) | $ 7.2 | $ 83.1 | $ 170.8 |
| Depreciation | 11.2 | 13.6 | 18.3 | 27.2 | 60.8 | 108.6 |
| Other[b] | 2.7 | 3.5 | 7.0 | 6.1 | 35.2 | 57.1 |
| Total | 16.4 | 18.7 | 24.2 | 40.5 | 179.1 | 336.5 |
| Funds from external financing | | | | | | |
| Net increase in lease obligations | 10.2 | 35.0 | 65.4 | 47.7 | (5.0) | (18.3) |
| Other net borrowing, sale of securities | (4.6) | (.8) | 19.3 | 85.1 | 158.8 | 842.2 |
| Total | 5.6 | 34.2 | 84.7 | 132.8 | 163.8 | 823.9 |
| Total sources | $22.0 | $52.9 | $108.9 | $173.3 | $342.9 | $1,160.4 |
| *Uses of Funds* | | | | | | |
| Investment in plant, equipment | $22.2 | $52.5 | $110.3 | $155.7 | $271.5 | $ 623.0 |
| Acquisitions | — | — | — | — | — | 195.1 |
| Increase in adjusted working capital[c] | (1.7) | (5.6) | 1.0 | 12.8 | (60.4) | (55.2)[d] |
| Change in cash holdings | 1.5 | 6.0 | (2.4) | 4.8 | 131.8 | 397.5 |
| Total uses | $22.0 | $52.9 | $108.9 | $173.3 | $342.9 | $1,160.4 |

*Note:* Numbers may not add exactly because of rounding.
[a]Net income less preferred dividends.
[b]Deferred taxes, employee stock purchase plan.
[c]Working capital excluding cash and short-term debt.
[d]Not including working capital of WUI.

## EXHIBIT 4
**MCI Income Statements for Years Ending March 31, 1981–1983 (millions of dollars)**

| | 1981 | 1982 | 1983 |
|---|---|---|---|
| Revenues | $234 | $506 | $1,073 |
| Operating expenses (excluding depreciation) | 157 | 283 | 674 |
| Depreciation | 26 | 56 | 104 |
| | 183 | 339 | 778 |
| Operating income | 51 | 167 | 295 |
| Interest expense | 28 | 54 | 75 |
| Interest income (less other expense) | 1 | 16 | 21 |
| | 27 | 38 | 54 |
| Profit before taxes | 24 | 129 | 241 |
| Provision for income taxes | 5 | 43 | 70 |
| Net income | 19 | 86 | 171 |
| Extraordinary item | 2 | 0 | 0 |
| Adjusted net income | 21 | 86 | 171 |
| Preferred dividends | 11 | 3 | 0 |
| Income available for common stock | $ 10 | $ 83 | $ 171 |



## EXHIBIT 5
**MCI Balance Sheets at March 31, 1981–1983 (millions of dollars)**

| | 1981 | 1982 | 1983 |
|---|---|---|---|
| Cash, cash equivalents | $ 13 | $144 | $ 542 |
| Accounts receivable | 32 | 79 | 162 |
| Other | 4 | 5 | 9 |
| Current assets | 49 | 228 | 713 |
| Plant, equipment (net) | 410 | 619 | 1,324 |
| Other | 8 | 13 | 33 |
| Total assets | $467 | $860 | $2,070 |
| Accounts payable, accrued liabilities | $ 34 | $137 | $ 251 |
| Accrued taxes | 0 | 8 | 22 |
| Debt due within 1 year | 40 | 40 | 48 |
| Current liabilities | 74 | 185 | 321 |
| Long-term debt | 243 | 400 | 896 |
| Deferred income taxes | 2 | 34 | 88 |
| Total liabilities | 319 | 619 | 1,305 |
| Preferred stock (par value) | 1 | 0 | 0 |
| Common stock (par value) | 4 | 5 | 12 |
| Surplus capital paid in | 220 | 230 | 576 |
| Retained earnings (deficit) | (77) | 6 | 177 |
| Total liabilities and net worth | $467 | $860 | $2,070 |

## EXHIBIT 6 Public Sales of Securities by MCI, 1972–1983

Source: MCI prospectuses.

| Date | Instrument | MCI Price on Issue Date | Amount/Price | Net Proceeds | Date Called for Conversion |
|---|---|---|---|---|---|
| June 1972 | Common stock | IPO | 6,000,000 shares @ $5 | $ 27,070,000 | na |
| Nov. 1975 | Common stock plus 5-year warrant attached (exercise price—$1.25) | $ ⅞ | 9,600,000 units @ $1 | $ 8,165,000 | na |
| Dec. 1978 | $2.64 convertible cumulative preferred stock (conversion price—$2.1875 per share of common) | $ 1⅞ | 1,120,000 shares @ $25 | $ 25,760,000 | Mar. 1980 |
| Sept. 1979 | $1.80 senior convertible cumulative preferred stock (conversion price—$5 per share of common) | $ 3¼ | 4,500,000 shares @ $15 | $ 63,125,000 | May 1981 |
| July 1980 | 15% subordinated debentures due August 1, 2000 | — | $52,500,000 @ 100% of face value | $ 50,545,000 | na |
| Oct. 1980 | $1.84 cumulative convertible preferred stock (conversion price—$9 per share of common) | $ 6 1/16 | 3,300,000 shares @ $15 | $ 46,725,000 | Nov. 1981 |
| Apr. 1981 | 14⅛% subordinated debenture due April 1, 2001 | — | $125,000,000 @ 84.71% of face value | $102,055,000 | na |
| Aug. 1981 | 10¼% convertible subordinate debenture due August 15, 2001 (conversion price— $12.825 per share of common) | $10⅞ | $100,000,000 @ 100% of face value | $ 98,200,000 | Feb. 1983 |
| May 1982 | 10% convertible subordinated debenture due May 15, 2002 (conversion price—$22.50 per share of common) | $18⅝ | $250,000,000 @ 100% of face value | $245,925,000 | Dec. 1982 |
| Sept. 1982 | 12⅞% subordinated debenture due October 1, 2002 | — | $250,000,000 @ 85.625% of face value | $209,922,500 | na |
| Mar. 1983 | 7¾% convertible subordinated debenture due March 15, 2003 (conversion price—$52.125 per share) | $43⅜ | $400,000,000 @ 100% | $393,675,000 | — |

*Note:* All prices and share figures adjusted for subsequent stock split. Amounts are initial offering levels. In each case, the offerings were oversubscribed and additional funds were raised.
na = not available.





## EXHIBIT 7 Comparative Interest Rates, 1978–1983

| | Industrials | | | | Utilities | | | |
|---|---|---|---|---|---|---|---|---|
| | Bonds[a] | | Preferred Stock[b] | | Bonds[a] | | Preferred Stock[b] | MCI[c] Bonds, Preferred Stock |
| Issue Date | A | BBB | Medium | Speculative | A | BBB | Medium | at Issue |
| Dec. 1978 | 9.17% | 9.76% | 9.45% | 10.34% | 9.50% | 9.78% | 10.48% | PS 10.56% |
| Sept. 1979 | 9.74 | 10.41 | 9.76 | 11.53 | 10.05 | 10.51 | 10.97 | PS 12.00 |
| July 1980 | 11.35 | 11.74 | 10.56 | 10.91 | 11.54 | 12.60 | 12.32 | D 15.00 |
| Oct. 1980 | 12.92 | 13.03 | 11.43 | 11.98 | 12.79 | 14.14 | 14.32 | PS 12.27 |
| Apr. 1981 | 13.29 | 14.18 | 13.19 | 13.65 | 14.01 | 15.17 | 15.12 | D 16.80 |
| Aug. 1981 | 16.25 | 17.25 | 13.46 | 14.99 | 17.50 | 18.00 | 15.85 | CD 10.25 |
| May 1982 | 15.50 | 16.50 | 13.16 | 14.62 | 16.25 | 17.00 | 14.93 | CD 10.00 |
| Sept. 1982 | 13.75 | 14.63 | 13.21 | 14.49 | 14.00 | 15.13 | 14.11 | D 15.17 |
| Mar. 1983 | 12.50 | 13.00 | 11.36 | 12.67 | 12.75 | 13.25 | 12.51 | CD 7.75 |

PS = convertible preferred stock; D = straight debenture; CD = convertible debenture.
[a]Standard and Poor's rating.
[b]Rates are for nonconvertible preferred stock.
[c]MCI bonds are nonrated for most of this period.

## EXHIBIT 8 Comparison of Companies, 1983 (billions of dollars)

Source: Standard and Poor's reports; Moody's.

| | MCI[a] | AT&T | GTE | IBM | ITT |
|---|---|---|---|---|---|
| Revenues | $ 1.1 | $ 65.1 | $12.1 | $ 34.4 | $16.0 |
| Net income | .17 | 6.99 | .90 | 4.41 | .70 |
| Assets | 2.1 | 148.2 | 21.9 | 32.5 | 14.1 |
| Return on | | | | | |
| Sales | 15.9% | 10.7% | 7.4% | 12.8% | 4.4% |
| Assets | 11.0 | 8.6 | 4.1 | 14.1 | 4.8 |
| Equity | 32.4 | 12.2 | 15.6 | 22.9 | 12.7 |
| Payout ratio | 0 | 67 | 61 | 47 | 54 |
| Debt ratio[b] | 55 | 43 | 57 | 14 | 38 |
| Current ratio | 2.2 | .9 | 1.0 | 1.6 | 1.3 |
| Interest coverage | 4.2 | 3.6 | 2.4 | 18 | 25 |
| Bond rating | NR | Aaa | Baa | Aaa | A |
| Price-earnings range | 8–27 | 6–8 | 6–10 | 8–13 | 5–7 |

NR = not rated.
[a]Fiscal year ending March 31.
[b]Total debt to capital.

**EXHIBIT 9** **Baseline Forecast of Anticipated MCI Operating Characteristics for Years Ending March 31, 1983–1990 (millions of dollars)**

Source: Casewriter's estimate based on security analysts' forecasts.

| | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 | 1990 |
|---|---|---|---|---|---|---|---|---|
| 1. Interstate long-distance market | $27,000 | $29,800 | $32,800 | $36,000 | $39,700 | $43,600 | $48,000 | $52,800 |
| 2. MCI market share[a] | 4.0% | 6.2% | 9.6% | 13.5% | 18.6% | 19.8% | 20.0% | 20.0% |
| 3. MCI revenues [(1) × (2)] | $ 1,073 | $ 1,850 | $ 3,160 | $ 4,870 | $ 7,380 | $ 8,660 | $ 9,600 | $10,560 |
| 4. Access charges (% of sales) | 16% | 23% | 29.5% | 29.5% | 29.5% | 28.5% | 27.5% | 26.5% |
| 5. Operating margin[b] | 27.5% | 20.5% | 12.0% | 12.0% | 12.0% | 13.0% | 14.0% | 15.0% |
| 6. Operating earnings (EBIT) [(3) × (5)] | $ 295 | $ 380 | $ 390 | $ 590 | $ 890 | $ 1,125 | $ 1,345 | $ 1,580 |
| 7. Interest paid | $ 75 | $ 100 | $ 100 | $ 100 | $ 100 | $ 100 | $ 100 | $ 100 |
| 8. Other income | $ 21 | $ 13 | $ 3 | $ 4 | $ 4 | $ 5 | $ 5 | $ 5 |
| 9. Provision for taxes | $ 70 | $ 83 | $ 58 | $ 123 | $ 206 | $ 299 | $ 400 | $ 475 |
| 10. After-tax net income [(6) – (7) + (8) – (9)] | $ 171 | $ 210 | $ 235 | $ 371 | $ 588 | $ 731 | $ 850 | $ 1,010 |
| 11. Increase in deferred taxes | $ 53 | $ 65 | $ 88 | $ 106 | $ 120 | $ 140 | $ 146 | $ 140 |
| 12. Incremental investment factor | 1.15 | 1.15 | 1.12 | 1.10 | 1.08 | 1.06 | 1.04 | 1.0 |
| 13. Capital expenditures for new capacity [Change in (3) × (12)] | $ 623 | $ 890 | $ 1,467 | $ 1,881 | $ 2,710 | $ 1,357 | $ 980 | $ 960 |
| 14. Capital expenditures for replacement | — | — | — | $ 50 | $ 50 | $ 100 | $ 100 | $ 100 |
| 15. Total capital expenditures [(13) + (14)] | $ 623 | $ 890 | $ 1,467 | $ 1,931 | $ 2,760 | $ 1,457 | $ 1,080 | $ 1,060 |
| 16. Depreciation | $ 104 | $ 173 | $ 272 | $ 412 | $ 601 | $ 749 | $ 800 | $ 826 |
| 17. Net plant, equipment (end of year) | $ 1,324 | $ 2,041 | $ 3,236 | $ 4,755 | $ 6,914 | $ 7,622 | $ 7,902 | $ 8,136 |
| 18. Additional working capital required | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |

[a]This is total MCI revenue as a fraction of long-distance revenues and includes non-long-distance revenues. MCI's actual share of the interstate long-distance market would be slightly lower.
[b]Includes depreciation as a cost.



**EXHIBIT 9** *(concluded)*
**Assumptions Underlying the Forecasts**

1. The interstate long-distance market, which amounted to about $27 billion in FY1983, would grow at 10% per year through FY1990.
2. MCI's revenues would increase from 4% of total long-distance revenues in FY1983, to 20% in FY1990. The increase would be rapid in the years immediately following the advent of *equal access*, but would subsequently slow down as AT&T began to defend its reduced share of the market, other competitors developed their networks, and the market itself adapted to the shock of competition. This pattern is shown on line 2. In each year, 10% of MCI revenues would come from other than long-distance growth. Thus, in FY1990, MCI was projected to hold 18% of the long-distance market. MCI's management was believed to be committed to a growth program of the dimensions shown on line 3 and would, if necessary, sacrifice profit margins to achieve it.
3. Access charges paid by MCI would almost double between FY1983 and FY1985. They would then taper off to about 26.5% of total revenues in FY1990. This was consistent with announced FCC intentions at the end of March 1983. However, there was a great deal of uncertainty in this area. AT&T currently paid access charges amounting to more than 50% of revenues, and reductions to the levels on line 4 would depend on the imposition of *direct* access charges on households and businesses. Legislation in Congress with a reasonable chance of passage forbade the imposition of such direct access charges.
4. MCI's operating margin (operating earnings as a fraction of revenues) would shrink under the dual pressure of higher access charges and increased competition from both AT&T and other long-distance suppliers. Ultimately, however, as access charges fell and the market stabilized, margins were expected to recover to a level of about 15%. Anticipated yearly margins are shown on line 5. However, as noted, these were subject to substantial uncertainty. In the best case, favorable regulatory and legislative action, coupled with restrained competitor behavior, might increase margins by as much as 7% (up to 22% of sales) from these levels. In an unfavorable situation, severe competition and high access charges could reduce margins by an equal amount.
5. Interest payments on MCI's outstanding debt were running at an annual rate of about $100 million at the end of FY1983 (for the year as a whole, interest payments were only $75 million because the debt level increased during the year) and, with no net change in indebtedness, would remain stable at this level through FY1990.
6. Other income, shown on line 8, represents interest on holdings of cash equivalents. As *excess* cash is used up, this figure is expected to decline to $3 million and then grow roughly with sales. This projection does not include interest on the proceeds of any future security offerings that are added temporarily to cash.
7. Provision for taxes, shown on line 9, amounts in 1984 to 25% of net income, which is below the 46% base rate because of investment tax credits and other special credits. As growth and investment slow in later years and reduce the available credits, taxes as a percentage of net income should increase.
8. Increases in deferred taxes, shown on line 11, accumulate at a rate related to present and past capital expenditures. As growth slows, so does the rate of accumulation of deferred tax credits.
9. In March 1983 each extra dollar of revenue required about $1.15 worth of investment in fixed plant and equipment. This factor was expected to fall to about $1.00 by FY1990, as improved electronic technology reduced equipment costs. The expected yearly pattern is shown on line 12. It was possible, however, that in the latter part of the period (post-FY1987) this factor would fall substantially below $1.00.
10. Replacement of older equipment would require the investments described on line 13.
11. Depreciation would be charged at an annual rate equal to 9.8% of the value at plant and equipment in place at the beginning of each year plus 4.9% of the value of total new investment.
12. No additions to working capital would be required throughout the period and any cash on hand at the end of FY1983 could be devoted to investment programs.
13. MCI would not penetrate the intrastate toll market.