

Cox Communications, Inc. (1999)

Summer in Atlanta, Georgia, home of Cox Communications, Inc. (Cox), was usually quite warm, but the summer of 1999 was especially hot for Dallas Clement, Cox's 34-year-old treasurer. At the beginning of 1999, Clement and his team (Susan Coker and Mark Major, co-assistant treasurers) anticipated that Cox would be making several major acquisitions over the next three to five years, probably spending \$7–\$8 billion in the process. However, unexpectedly aggressive competition by rivals seeking to lock up valuable cable systems had brought a number of important properties into play sooner than expected. From a strategic viewpoint, Cox could not afford to lose these cable properties, especially those that could be combined with its existing systems to yield substantial market presence and attendant cost savings. By the beginning of July, the firm had already committed to over \$7 billion in acquisitions to be completed by the end of the year, which would add over 1.6 million new subscribers in eight states. These deals would put stress on the firm's complicated balance sheet, requiring Clement's team to scramble to fund several years' of acquisitions in little more than six months.

Then, in mid-July, Cox learned that Gannett Co. would put its cable properties up for sale. Cox's parent, Cox Enterprises, Inc. ("CEI"), and Gannett were both approximately 100-year-old newspaper companies that had branched out into other communications businesses, including television and radio broadcasting, print media, production, and cable. There had been little indication that Gannett would sell its cable system, but the high prices being paid for cable subscribers apparently convinced Gannett to part with its cable assets. The Cox team estimated that, based on comparable recent transactions, Cox would need to bid about \$2.7 billion to win the right to serve Gannett's 522,000 customers. With this acquisition and the others to which it had recently committed, Cox's subscriber base would grow 60% from the levels at the beginning of the year. This newest acquisition, however, would put even more pressure on the firm's funding ability, and Clement's team had to recommend how to fund it.

Clement's team had to figure out how much debt, equity, or equity-linked securities to issue, or how many of its appreciated non-strategic assets to sell, to fund these acquisitions. Their recommendation for funding the Gannett acquisition had to be consistent with the firm's long-run capacity to fund future activities. Specifically, they had to be mindful of the impact of their actions on the firm's investment-grade bond rating, which its board was keen to protect. At the same time, their recommendation had to respect the preferences of the Cox family, who owned more than two-thirds of Cox through their ownership of the privately held CEI, and who sought to maintain their super-majority ownership of Cox. The heat outside the Cox headquarters was nowhere as blistering as the heat within Clement's organization as his team worked late into the night.

Professors George Chacko and Peter Tufano and Research Associates Matthew Bailey and Joshua Musher prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

Copyright © 2000 President and Fellows of Harvard College. To order copies or request permission to reproduce materials, call 1-800-545-7685, write Harvard Business School Publishing, Boston, MA 02163, or go to <http://www.hbsp.harvard.edu>. No part of this publication may be reproduced, stored in a retrieval system, used in a spreadsheet, or transmitted in any form or by any means—electronic, mechanical, photocopying, recording, or otherwise—without the permission of Harvard Business School.

Cox Communications, Inc. and the Cable/Broadband Industry

Since its establishment in 1898 until 1962, Cox Enterprise's main business had been newspapers. The firm first entered the cable television business in 1962 with the purchase of cable systems in California, Oregon, Pennsylvania, and Washington. These cable systems carried television signals to homes via coaxial landlines, offering subscribers clear reception and new programming choices. By 1977, Cox's cable division operated in nine states and served 500,000 subscribers. By 1990, it served 1.5 million subscribers, and by the beginning of 1999, it was serving almost 3.7 million subscribers. In 1995, the cable business was partially spun off by CEI in the form of Cox Communications (Cox), with majority control and economic ownership retained by CEI.

Technological innovations, including the Internet, fiber optics, and wireless communications, as well as deregulation, made the late 1990s a period of tremendous change for cable operators. Cable operators spent billions of dollars replacing coaxial cables with fiber optic bundles, which provided 1000 times more capacity. This extra capacity allowed cable companies—now labeled “broadband” companies reflecting the breadth of services they offered—to provide consumers with pay-per-view and digital cable television services, high-speed Internet access, and digital telephony. Cable operators anticipated these and other new services (video-on-demand, interactive TV, video gaming, etc.) would drive much of the profit growth for at least the next several years. Increasing the breadth of services brought broadband companies into competition with a wider range of rivals, including satellite systems, telephone companies, and wireless companies, as part of the telecommunications convergence. Deregulation, in the form of the Telecommunications Reform Act of 1996, made this convergence possible by allowing cable operators and telephone companies to enter each other's businesses. While the traditional part of the cable industry was quite regulated, the growth of the broadband industry—and the competitive battles that would ensue—would take place in less-regulated territory.

Cox prided itself on delivering high-quality technology and services and was very aggressive in upgrading its network and introducing new services. By mid-1999, close to 60% of Cox's cable systems had been upgraded to 750 megahertz¹ (MHz) of capacity. Since analog video services took up only 550 MHz of capacity, this upgrade allowed Cox to offer high-speed Internet access to its cable television customers through Cox@Home, telephone service under the Cox Digital Telephone brand, and advanced digital television programming under the Cox Digital TV brand. Digital video was expected to drive the growth of Cox's core video revenues, which were otherwise anticipated to grow at an annual rate of 6%–8% for the next five years. This growth came from expected rate increases of 3%–5% and natural growth of the subscriber base. Revenues from high-speed Internet access and digital telephony, however, were anticipated to grow at significantly higher rates. (See Table A.) On an aggregate basis, these additional services were expected to raise operating cash flow growth from 8% to 15% annually. Not included in these estimates were additional services, such as Home Security Monitoring, that were still in the concept stage. Total capital expenditures, including those for network upgrades and expansion of services, were expected to be \$1.3 billion in 2000 and close to \$1.1 billion in 2001.

¹Megahertz (MHz) in this context is a measure of bandwidth for high-speed digital data transfer. The bandwidth of a cable line is the maximum data speed that the line can transmit. Generally, the higher the bandwidth, the higher the maximum data transfer speed of the cable line. A 750 MHz line can transmit data at a rate of 750 million bits per second, where a bit is a 1 or a 0, representing one piece of information.

TABLE A
Gross Margins
and Growth Rates
for Cable Services

Source: Case writer estimates
and Cox Communications, Inc.

	Monthly Cash Flow	Gross Margin ^a	Current Subscriber Penetration ^b	Target Penetration ^c
Analog TV	\$30	75%	67%	67%
Digital TV	16–18	55	2	30
High-speed Internet	35–40	30	2	25
Digital telephony	55–60	55	1	25

^aGross margin is defined as revenue minus direct costs of the service.

^bAs a percentage of homes passed.

^cCox expected to reach these target levels within eight years.

Cable operators realized that they had to expand to spread the fixed costs of their operations and networks over as large a number of customers as possible. High *local* market share through consolidation led to tangible cost savings in the form of local scale economies, such as sharing the same cables and fleets of service technicians and vans. On a *national* scale, consolidation provided bargaining power when dealing with content providers, such as firms like HBO or Fox, that produced and distributed programming. Expansion also allowed cable operators to realize increasing returns by bundling services to more households.

As a result, Cox, as well as its competitors, rapidly expanded their customer bases via acquisitions. (See Exhibit 1 for some recent cable mergers and acquisitions, and Exhibit 2 for data on the largest operators that resulted.) For example, in 1995 Cox acquired Times Mirror Cable Television, which increased Cox's subscriber base by 1.3 million customers. In the first half of 1999 alone, Cox announced its intentions to purchase cable systems from Media General (April), merge with TCA Cable (May), and acquire certain AT&T cable properties. These acquisitions were expected to close by the end of 1999, but were by no means guaranteed to occur. They were contingent on regulatory approval, and the transfer of franchise rights by local communities. Obtaining the necessary approvals could take 3 to 15 months. These acquisitions would bring Cox's customer base to 5.5 million in 18 different states, making Cox the fifth-largest cable operator in the United States.

Competition among cable companies for customers had driven up the cost of new customers. Some analysts felt that the race became heated when Charter, owned by Paul Allen of Microsoft, purchased Marcus Cable in April 1998. As a result, while cable firms had paid approximately \$2,000 per subscriber to expand their cable operations throughout most of the 1990s and as recently as 1998, this figure had risen to well over \$4,000 per subscriber by 1999. With the number of available cable assets rapidly shrinking, incumbents in the industry had no choice but to pay these prices or face the prospect of becoming second-tier competitors.² Forrester Research estimated that the top five cable companies would serve 70% of subscribers in four years, up from around 56%.³

Achieving scale was expensive. The deals Cox announced in the first half of 1999, if consummated, would require nearly \$7.6 billion in gross funding. Media General would cost \$1.4 billion in cash, TCA would cost \$4.1 billion (\$2.0 billion in cash, \$1.9 billion in Cox common equity, and \$190 million in assumed debt), and AT&T would cost \$2.1 billion (paid for with 50.3 million shares of AT&T. Cox, through subsidiaries, would acquire cable systems and other assets, including \$750 million cash).

²Some of the recent acquisitions were swaps of subscribers being served by competing companies. The main reason for this was that there were economies associated with having clustered subscribers.

³T. Rhinelander, C. Mines, and K. Kopikis, “Cable's Multiservice Future,” Forrester Research, February 1999.

The possible acquisition of Gannett's cable properties would make 1999 an extraordinary year for Cox. Gannett Co., founded in 1906 by Frank E. Gannett, was a diversified media company. Its 75 newspapers (including *USA Today*, the largest-selling daily newspaper in the United States) made it the nation's largest newspaper group, and its 21 television stations reached 17% of the United States. In 1995, the company had purchased Multimedia Inc., which gave Gannett cable systems in Indiana, Illinois, Kansas, North Carolina, and Oklahoma, and in 1999 reached about 522,000 subscriber households. Gannett's properties were attractive to Cox not only because of the number of subscribers, but also because they fit in well with its own strategy of concentrating subscribers in geographical areas to achieve economies of scale and scope. The Gannett systems, however, would not be cheap. Gannett would sell its cable properties by auction and Cox estimated that it would have to pay \$2.7 billion, or over \$5000 per subscriber, to win.

Financing Cox's Growth and the Gannett Acquisition

James Kennedy, the chairman of Cox's Board, and James Robbins, the firm's president and CEO, wrote in the annual report, "We constantly review potential growth opportunities and weigh them against a very clear litmus test: Will they create significant shareholder value? . . . Cox has the flexibility to [pursue these growth opportunities] in part because of our strong balance sheet." A key issue for Clement and his team to consider as they struggled with the current financing decision was how to retain sufficient financial flexibility to continue to fund planned and unexpected business opportunities.

Surely, funding the acquisitions would affect Cox's balance sheet. Even without the Gannett acquisition, internal cash flow would not be sufficient to fund the acquisitions that had been announced to date. Cox had financed its capital expenditures for network upgrades, acquisitions, capital investments, and new products through \$1.9 billion from internal cash flow in conjunction with \$1.9 billion of net issuance of debt, \$370 million of equity (including its IPO in 1995), and \$900 million from sales of non-strategic assets. The funding and asset sale choices were complicated by a variety of factors that Clement, Coker, and Major had to consider. In particular, the team was acutely aware of changing market conditions that could materially affect their ability to execute the transactions needed to fund the Gannett acquisition.

Issuing Common Shares

Cox could issue shares to the public for all or part of the required amount of funding. The firm's first and only share issuance had been almost four years earlier, in June 1995, when it raised a little under \$400 million through public and private placements of equity. Any recommendation, however, to sell equity had to be mindful of the firm's unique ownership structure. CCI had two classes of common stock outstanding: class A shares were entitled to one vote each, and class C shares had super-voting privileges with 10 votes each. Neither class of common equity paid dividends. Through CEI, the Cox family owned 379.2 million out of 533.8 million class A shares, and all of the 27.6 million class C shares outstanding. After the anticipated issuance of 38.3 million shares as part of the TCA transaction in the next fiscal quarter, CEI would own 67.3% of Cox's common shares and would control 76.8% of Cox's voting stock.⁴ The chairman and CEO of CEI, James Kennedy, was also the chairman of the board of Cox and was the grandson of CEI's founder.

⁴The number of shares was calculated on a fully diluted basis, assuming that 6.1 million outstanding stock options were exercised and that 5 million outstanding convertible preferred shares were converted. The convertible preferred shares had voting privileges, and did not receive dividends.

Cox had a number of financial objectives. The first was to double the size of the company every five years. The second was to preserve the family's economic ownership of Cox. The firm's initial public offering of Cox's equity in 1995 had allowed Cox to expand via acquisitions, but CEI did not want its ownership interests further diluted. To ensure that their interests as management were consistently aligned with those of the other shareholders, the family considered it appropriate to maintain a supermajority stake in conjunction with their control of the firm. This preference constrained the amount of equity financing Cox could undertake, as any equity issuance would have reduced the percentage ownership of CEI. Finally, there was a reluctance to increase the leverage of the firm, as discussed below.

Also on Clement's mind was his tactical ability to place a large block of Cox equity in the market. Charter Communications was expected to make its initial public offering in the fall. Because Charter and Cox appealed to similar investors, Clement was concerned that these investors would have less of an appetite for Cox shares after the Charter deal had been placed. Were he to issue equity, he might want to do so before Charter's IPO. Clement also had to consider overall market condition. The equity markets had enjoyed, for almost a decade, a long period of high returns as part of a prolonged economic expansion in the United States, but many pundits warned of an imminent correction in the markets. (See Exhibit 5.)

A minor consideration was the direct costs of an equity issue, including underwriting fees and expenses, which would likely be between 2%–3% of the amount raised. In addition, there might be some "market impact" of a large equity issue, as the market typically greeted new shares by reducing the price of the firm's outstanding equity (and thereby the price at which the new shares could be offered). Academic studies suggested that this response usually amounted to an additional 3%–4% reduction in the price of a firm's stock, although this discount varied across firms and over time.⁵

Issuing Debt or Borrowing

Alternatively, Cox could issue debt to fund the Gannett cable acquisition, whether in the form of a public debt issue or bank borrowing. The structure of the debt could take many forms determined by the source of the debt, the maturity structure, the level of cash coupons, and various options (such as the right to redeem or call the debt at par). Since 1995, Cox had raised \$1.9 billion in debt. This debt had maturities ranging from 5 to 30 years, with yields ranging from 65 to 115 basis points above the yields on U.S. Treasury obligations of similar maturity.

The Cox executives, however, were concerned about increasing financial leverage. The Cox family was very conservative about the use of debt. Cox already had the highest level of debt financing of all the CEI subsidiaries. Furthermore, Cox had a publicly articulated goal of maintaining a high debt rating. Cox executives had stated, "We want to get the right balance of debt and equity. We obviously are continuing to be investment grade and that's important." Maintaining that rating required careful monitoring of several financial variables, the most important of which being Debt/EBITDA. Currently, Cox was targeting a Debt/EBITDA ratio of no greater than 5 going forward, the maximum that senior management felt would retain an investment-grade rating. Externally, the debt markets for companies rated investment grade seemed larger and more stable than for noninvestment grade firms.⁶ Noninvestment grade firms could find it

⁵See Grinblatt, Mark, and S. Titman, "Financial Markets and Corporate Strategy," Irwin/McGraw-Hill, 1998, pp. 15–16 and the references therein for more information regarding the direct and indirect costs of issuing equity.

⁶An investment-grade rating was one of the four top ratings awarded by the national debt rating agencies.

difficult to obtain access to credit at times, as had happened in the late 1980s when Drexel, Burnham, Lambert, the premier underwriter of noninvestment grade debt, went out of business, and more recently during the Asian currency and Russian debt crises in 1998. Additionally, sub-investment grade debt cost more, as indicated by the BBB-to-BB yield spread versus the BBB-to-A spread. Such circumstances could severely limit future flexibility.

In addition to the risk that credit spreads might widen in the fall, Clement had to consider the fact that the 30-year Treasury yield had increased more than half a percent over the past six months. (See Exhibit 6 for current interest rates.)

The direct and indirect costs of a debt issuance would be less than that for issuing equity. Clement anticipated that the transaction costs would be less than 2%. Academic studies estimated the market impact of issuing debt (on Cox's stock price) to be around 1%–2%.⁷

Hybrid Security Issuance

Another possibility was to issue hybrid securities, which had characteristics of both debt and equity. The most common examples of this class are preferred stock or convertible bonds.⁸ A more recent innovation in the hybrid market was “mandatory convertible” structures and “trust preferred” products that sought to combine the best features of both debt and equity. Many investment banks offered these products, but one particular variety that had recently been proposed to Clement was an equity-linked hybrid product developed by Merrill Lynch called FELINE Income PRIDES.⁹

This security had elements of both debt and equity. Each Income PRIDES was a unit consisting of (i) an obligation by the investor to purchase a fixed dollar amount of Cox's Class A Common Stock in three years, and (ii) preferred equity. Payments made by Cox to the preferred equity component of the Income PRIDES would be essentially deductible for tax purposes, but the security was treated like equity for financial reporting purposes due to the obligation of the holder to purchase equity in the future.

The legal structure that delivered this treatment was somewhat complicated.¹⁰ Essentially, Cox would establish a legal entity (a Trust) that would issue preferred equity and common equity. Cox would purchase all the common equity and exercise full control of the Trust. The preferred equity of the Trust was bundled together with the purchase obligation described above and sold to investors as Income PRIDES.¹¹ For

example, an investor would pay \$50 for an Income PRIDES unit and receive a 7% preferred dividend yield for three years, on a principal amount of \$50. At the end of three years, the investor could satisfy the purchase obligation detailed above (to purchase the Class A Common Stock) by (a) exchanging the preferred equity for shares or (b) exchanging cash for shares. In either case, the number of shares Cox delivered to the Income PRIDES holder for this \$50 varied depending on the market value of Cox's common shares at maturity. Generally, the higher the stock price in three years, the smaller the number of shares that the Income PRIDES holder would receive. (See Exhibit 7.)

After issuing the preferred equity, the Trust would use the proceeds to purchase new Cox debt. The 7% interest on this debt matched the payment terms of the preferred equity, so the Trust effectively served to pass through payments from Cox to the holders of the preferred equity. In effect, therefore, Cox would sell its debt to the Trust, which in turn would sell its preferred equity to investors. Cox would own the residual portion of the Trust through the Trust's common equity.

The financial reporting advantage of this structure to Cox was that its debt would not appear on the balance sheet as debt. Because Cox owned the Trust, Cox would have effectively issued debt to itself, which cancelled out when the two balance sheets were rolled up. Instead all that would appear on Cox's financial statements would be a line item for “Minority Shareholder Interest” reflecting the preferred equity issuance. This account would appear between debt and shareholders' equity on the balance sheet. For tax purposes, however, Cox would be able to deduct the interest payments it made on the debt issued to the Trust. Thus, for financial reporting purposes the FELINE Income PRIDES would appear to be equity, but for tax purposes the payments on the back-to-back debt would be treated like ordinary interest payments. Furthermore, ratings agencies would give equity credit to the debt due to the contractual obligation of investors in FELINE Income PRIDES to purchase Cox common stock in the future. Thus, the FELINE Income PRIDES allowed Cox to simultaneously issue debt and receive the tax benefits of deducting the interest payments, while receiving equity credit from ratings agencies and for accounting purposes.

Asset Sales

Cox could also sell, swap, or monetize some of the firm's non-strategic equity investments, as was anticipated with the AT&T transaction. For example, Cox held equity in Sprint PCS worth approximately \$4.1 billion. Similarly, Cox held substantial equity investments in Discovery Communications (\$2.5 billion), @Home (\$1.5 billion), and Flextech (\$300 million), along with smaller stakes in other firms. Simply selling these investments into the public markets would have meant a considerable tax burden for Cox.¹² Monetizing, or obtaining equivalent cash to, some of the non-strategic investments in a tax-efficient manner was an ongoing effort within the Cox Treasury.

Clement could sell some of these equity investments directly into the public market and use the proceeds to pay for some or all of the Gannett properties. One disadvantage of an outright sale was that Cox would have to pay taxes on the capital gains. Tax efficient disposals of these appreciated assets were also possible, such as in the AT&T transaction, where Cox had effectively swapped its AT&T shares for shares in AT&T subsidiaries that owned cable assets without triggering a taxable event. Through other types of monetizations, Cox might be able to receive the cash equivalent in value in these assets, yet defer the capital gains taxes from any sale for

⁷See Grinblatt, Mark, and S. Titman, “Financial Markets and Corporate Strategy,” Irwin/McGraw-Hill, 1998, pp. 15–16 and the references therein for more information regarding the direct and indirect costs of issuing debt.

⁸A preferred stock pays a fixed dividend and has seniority between that of common equity and junior debt. Failure to pay dividends on preferred stock does not trigger bankruptcy, but sometimes leads to actions such as giving the preferred shareholders seats on the firm's board. A convertible bond is debt where the investor has the right to use the debt to purchase equity at a fixed price. In contrast, in mandatory convertible securities, the investor has the obligation to purchase equity in the future, although the price may not be set in advance.

⁹The description provided in this section of the FELINE PRIDES product issued by Cox and its associated structure has been greatly simplified, and at times deviates from the actual product, for pedagogical reasons. As with most hybrid products, there was a great deal of detail, critical to the accounting and tax treatment of the transaction, which this thumbnail description does not capture.

¹⁰This trust structure had been introduced first in an earlier set of products in the early to mid-1990s. These products went by many banks' acronym-labeled servicemarks such as MIPS, QUIPS, and TOPrS.

¹¹Simultaneously with the issuance of the Income PRIDES, Cox issued FELINE Growth PRIDES and Capital Securities independent of the Income Prides. Growth PRIDES are similar to Income PRIDES except that instead of bundling the purchase obligation with a Capital Security, the purchase obligation is bundled with U.S. Treasury zero-coupon securities of the same maturity. There were also a few other contractual differences between Growth and Income PRIDES in terms of obligations/options retained by Cox and the holders of these securities.

¹²Cox faced a marginal tax rate of 35% on its gain on the sale of assets. The gain is the difference between the sale price of the assets and Cox's “tax basis,” roughly the amount it had paid to acquire the assets less accumulated depreciation. The respective taxable bases were \$0, \$34 million, \$7 million, and \$48 million. Cox's shares in AT&T had a tax basis of zero.

a number of years.¹³ There were a number of practical limitations, however. The Sprint PCS investment could not be sold or hedged until November. Additionally, the stakes in Sprint, @Home, and Flextech were large relative to average daily trading volumes in those stocks. Hence, actually trading these positions would be difficult.

Market Conditions

Apart from the policy issues surrounding the firm’s capital structure choices, there were substantial execution concerns as well. As mentioned above, the team was worried that an IPO by its rival might make it harder for Cox to issue equity. More generally, there was considerable anxiety about the outlook for the markets in the fall. In the fall of 1998, the capital markets had almost melted down when Russia defaulted on part of its debt. The Dow Jones Industrial Average, a barometer equity market index, fell more than 10% in the following two weeks. Credit spreads (the difference between a corporate bond yield and an equivalent-maturity Treasury yield) roughly doubled over the next five months. For A-rated borrowers, spreads rose from 56 basis points to a high of 135 basis points, while for BBB-rated issuers, spreads increased from 95 basis points to 181 basis points.¹⁴

This had led to a dearth of debt issues in late 1998. While the markets recovered somewhat in the first part of 1999, more recent weakness in the bond markets had already led to the cancellation of some previously announced deals. For example, on May 21, Great Lakes Power Inc., a Canadian utility rated Baa3/BBB-, had postponed a \$200 million 10-year issue, and further postponements of more than \$1 billion of issuance had followed. Hardest hit were noninvestment grade issuers, and Internet and telecommunications companies.

The other major concern for the fall was the potential impact of Year 2000 issues. Many feared that computer systems that used two digits for tracking years would malfunction when the year 2000 began. While the risks for catastrophe seemed exaggerated, there was a real possibility that the markets would be inhospitable to new issues until some of the risks had been resolved.

The Recommendation

Regardless of whether Cox completed the acquisition of Gannett’s cable operations, the other acquisitions of 1999 would materially change Cox’s balance sheet. Any action Clement took would have to take into account ownership dilution on the one hand and the reaction of ratings agencies on the other. Additionally, Clement’s team needed to evaluate the appropriate long-term financial policy for Cox and the specific financing of the potential Gannett acquisition and the other acquisitions Cox had recently announced in the context of this policy. Exhibit 8 shows various pro forma financial statements under different financing policies, with and without the Gannett purchase.

¹³See the case “Times Mirror Company PEPS Proposal Review” (Harvard Business School Case No. 296-089), written by Peter Tufano and Cameron Poetzsch, for more on the issue of equity monetizations.

¹⁴Source: Bloomberg.

EXHIBIT 1 Cost per Customer of Cable Acquisitions, 1994–1999

Source: Assorted Bloomberg News stories

Announcement Date	Acquirer	Seller	Total Value of Acquisition	Price Paid per Cable Customer
June 94	Comcast	Maclean Hunter	\$1.27 billion	\$2,300
October 95	Comcast	E. W. Scripps Co.	\$1.49 billion	\$1,900
April 98	Paul Allen	Marcus Cable	\$2.78 billion	\$2,200
June 98	Cox	TCI	\$250.2 million	\$2,176
June 98	AT&T	TCI	\$59.4 billion	\$2,700
July 98	Paul Allen	Charter	\$4.5 billion	\$3,750
October 98	Cox	Prime South Diversified ^a	\$1.325 billion	\$3,329
February 99	Adelphia	FrontierVision	\$2.0 billion	\$2,900
March 99	Adelphia	Century	\$5.7 billion	\$3,600
March 99	Adelphia	Harron Communications	\$1.2 billion	\$4,100
April 99	AT&T	Media One ^b	\$62.5 billion	\$4,700
April 99	Cox	Media General ^c	\$1.4 billion	\$5,380
May 99	Charter	Avalon Cable	\$845 million	\$3,250
May 99	Charter	Falcon	\$3.6 billion	\$2,250
May 99	Comcast	AT&T ^d	\$3.4 billion	\$4,500
May 99	Cox	TCA Cable TV ^e	\$4.1 billion	\$4,600
June 99	Comcast	Greater Media	\$292 million	\$3,700
June 99	Charter	Bresnan	\$3.1 billion	\$4,500
July 99	Cox	AT&T ^f	\$2.15 billion	\$4,350

^aThis deal included access to 105,000 hotels, together with interests in various nonconsolidated operations, and thus is not directly comparable to wholly residential transactions.
^bAgreed to a swap of cable subscribers with MediaOne, including payment of cash.
^cAgreed to buy cable systems covering 260,000 customers from Media General for \$1.4 billion.
^dAs part of the deal Comcast also had an option to acquire from AT&T, in three years, additional cable systems covering between 1.0 million and 1.4 million subscribers for \$4.8 billion to \$6.7 billion. Comcast also agreed to supply AT&T-branded telephony in its cable systems, provided AT&T concluded telephony deals with two other non-AT&T cable companies.
^eMerger with TCA Cable TV, serving 883,000 customers. TCA stock either converted into \$62.50 cash, 0.7418 Cox shares plus \$31.25 in cash, or 1.4836 Cox shares. Cox paid \$4.1 billion.
^fCox and AT&T agreed that Cox would exchange its holding in AT&T for stock in AT&T subsidiaries that own cable TV systems. The swap consisted of 50.3 million AT&T shares (worth \$2.8 billion), for which Cox acquired subsidiaries with approximately 495,000 customers and \$750 million cash and other assets.

EXHIBIT 2 Comparative Financial Data for Major Cable Operators, 1998 (in millions of dollars, except ratios)

Source: Bloomberg Financial Analysis and Global Access

	AT&T	Cox	MediaOne	Time Warner	Comcast	Charter
Total assets	59,550	12,878	28,192	31,640	14,817	4,335
Equity market value ^a (7/99)	178,390	20,436	45,111	90,571	26,839	NA
Debt book value	6,727	3,920	5,422	10,944	5,577	NA
Operating cash flow	10,309	666	5,517	1,845	1,078	30
Cable subscriber base ^b	15.5	6.0	NA	12.9	8.0	6.2
Net income/total assets	0.11	0.14	1.48	0.01	0.07	NM
ROE	26.0%	33.3%	235.3%	−6.0%	43.4%	NA
ROA	8.7%	13.1%	5.2%	0.5%	7.7%	−1.0%
Total liabilities/total assets	0.57	0.58	0.47	0.70	0.68	0.50
Debt-to-equity ^c	0.26	0.74	0.38	1.24	1.42	NA
Total debt/EBITDA ^d	0.6	5.1 ^e	5.7	4.1	3.7	87.6
EBITDA interest coverage ^f	19.4	3.0	1.9	2.3	3.1	1.2
Bond rating	AA−/Aa3	A−/Baa2	BBB/Ba1	BBB/Baa3	BBB−/Baa3	NA
Equity beta	0.61	0.68	1.08	0.87	0.88	NA

^aAs of August 1999, Charter had not yet sold shares to the public.
^bAs of July 1999, the data for AT&T included the MediaOne subscriber base.
^cAs measured by the ratio of the book value of long-term debt to book value of shareholders’ equity.
^dRatio of Total Debt to Earnings Before Interest, Taxes, Depreciation, and Amortization. This is a commonly used ratio for analysis of debt capacity.
^eAs reported by Cox on pro forma basis to credit agencies.
^fEBITDA divided by the interest expense (for the same period) is a common ratio used for debt analysis. It approximates ability to repay on the basis of cash availability.

EXHIBIT 3 Financial Summary for Cox Communications (in millions of dollars unless noted)

Source: Bloomberg Financial Analysis and Global Access

	1996	1997	1998	99Q1	99Q2
Revenue	1,460	1,610	1,717	499	510
Cost of goods sold	468	496	540	168	159
Selling, general, and administrative	436	505	518	142	156
EBITDA	557	610	659	189	196
Depreciation and amortization	335	405	458	123	159
Nonoperating income (expense)	(104)	(193)	2,115	384	890
Interest expense	146	202	223	54	69
Income tax expense (refund)	23	(54)	883	144	352
Net income (loss)	(52)	(137)	1,271	251	506
Cash and marketable securities	42	28	31	90	23
Total current assets	165	377	197	265	210
Total assets	5,785	6,557	12,878	14,727	16,169
Current liabilities	250	245	336	334	362
Deferred taxes	294	722	2,887	3,668	4,152
Long-term debt	2,824	3,149	3,920	3,383	3,587
Other liabilities	155	84	359	485	439
Total liabilities	3,523	4,199	7,502	7,870	8,539
Total shareholders' equity	2,261	2,357	5,377	6,857	7,629
Capital expenditures	(579)	(708)	(809)	(225)	(277)
Cash flow from operations	309	555	666	176	18
Cash flow from investing activity	(552)	(1,108)	(1,600)	515	(292)
Cash flow from financing activity	246	539	937	(631)	207
Shares outstanding (all classes, millions)	540	541	545	555	555
Long-term debt / EBITDA ^a	5.1 ×	5.2 ×	5.9 ×	4.5 ×	4.6 ×
EBITDA interest coverage	3.8 ×	3.0 ×	3.0 ×	3.5 ×	2.9 ×
Free cash flow/long-term debt	-9.6%	-4.9%	-3.7%	-1.4%	-7.2%
Long-term debt/(long-term debt + equity)	55.5%	57.2%	42.2%	33.0%	32.0%
ROE (%)	-2.3%	-5.8%	23.6%	3.7%	6.6%
Price/book	2.76 ×	4.61 ×	3.64 ×	3.11 ×	2.72 ×
Debt-to-equity ^b (book value)	1.25 ×	1.34 ×	0.73 ×	0.49 ×	0.47 ×
Debt-to-equity (market value)	0.45 ×	0.29 ×	0.20 ×	0.16 ×	0.17 ×

^aSource: Cox Communications. As reported pro forma numbers that include EBITDA of new acquisitions when debt is already on the balance sheet.

^bAs measured by the ratio of long-term debt to shareholders' equity.

EXHIBIT 4A Monthly Issuance of Nonconvertible Debt by Credit Rating, July 1988–July 1999

Source: Securities Data Corporation. Represents the face value of public offerings of nonconvertible debt. For example, the dark line represents the monthly issuance volume of bonds rated BBB.

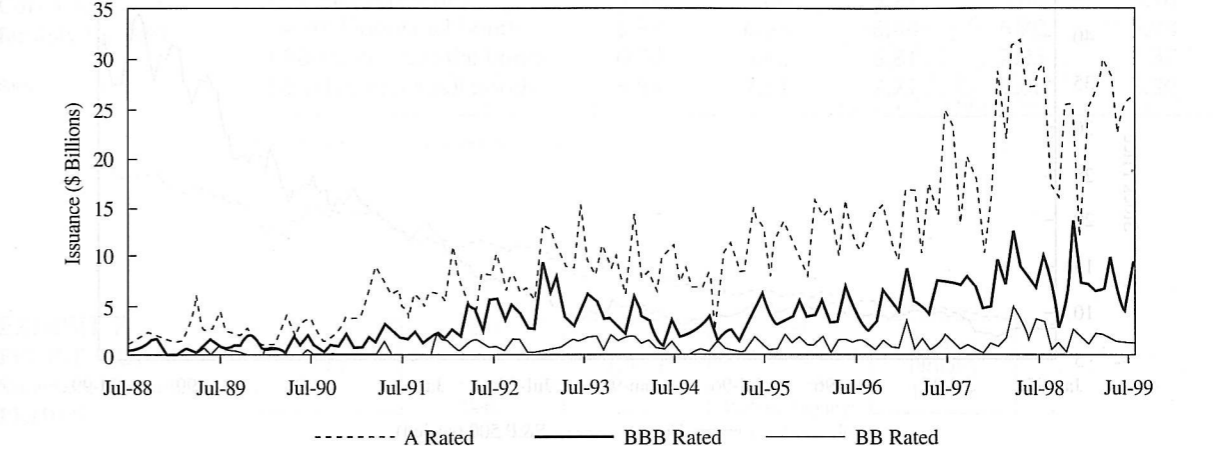


EXHIBIT 4B Credit Spreads for Long-Maturity Bonds, July 1992–July 1999

Source: Securities Data Corporation. Represents the face value of public offerings of nonconvertible debt. For example, the dark line represents the monthly issuance volume of bonds rated BBB.

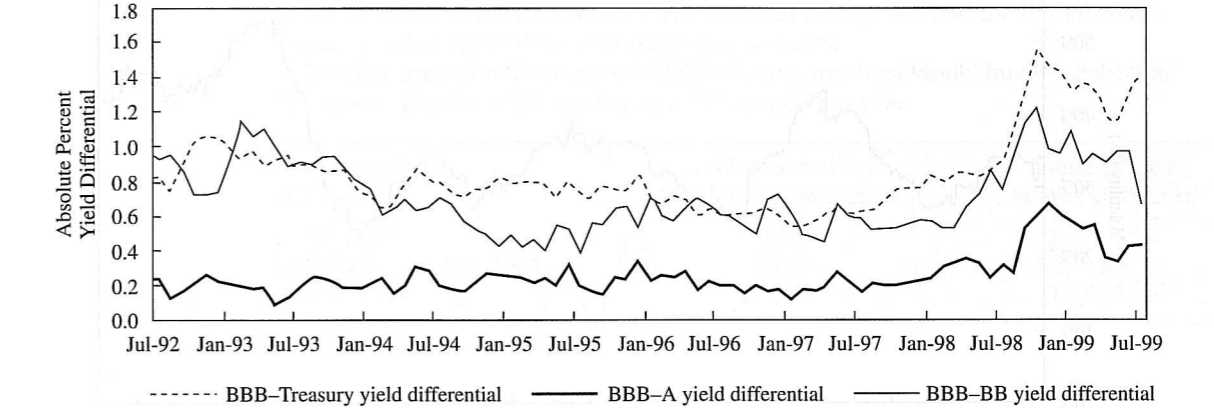


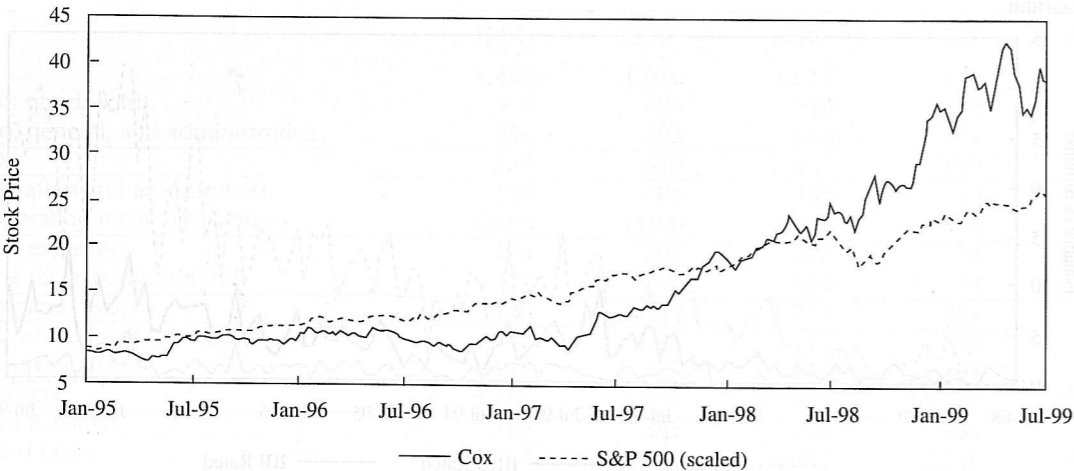
EXHIBIT 4C Supplementary Monthly Statistics for Exhibits 4A and 4B, July 1992–July 1999

Source: Securities Data Corporation

	A Issuance (\$ MM)	BBB Issuance (\$ MM)	BB Issuance (\$ MM)	BBB–Treasury Spread (%)	BBB–A Spread (%)	BB–BBB Spread (%)
Minimum	2,628	791	100	0.54	0.09	0.38
Average	14,503	5,248	1,299	0.85	0.26	0.71
Maximum	32,007	14,149	5,126	1.57	0.68	1.23
Standard deviation	7,279	2,638	919	0.23	0.12	0.20
Standard deviation /Average	50%	50%	71%	44%	28%	27%

EXHIBIT 5A Share Price of Cox Communications' Common Stock, January 1995–July 1999

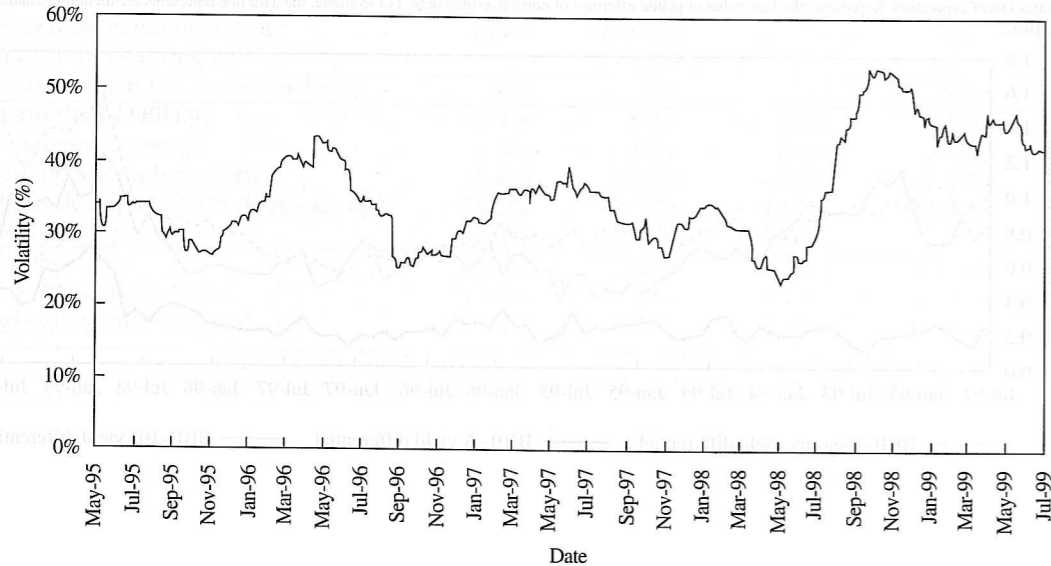
Source: Datastream International



Note: These prices are corrected for stock splits. The price of Cox Communication Common stock as of 8/9/99 was \$34.6875.

EXHIBIT 5B Historical Volatility of Cox Communications' Common Stock, June 1995–July 1999

Source: Bloomberg Financial Markets



Note: The historical volatility is measured by the annualized standard deviation of the log of daily stock price returns over the previous 90 days. The historical volatility as of 8/9/99 was 42%. Implied volatilities on options on Cox Communications were about 47% as of 8/9/99.

EXHIBIT 6 Yields for Government and Corporate Bonds for July 15, 1999

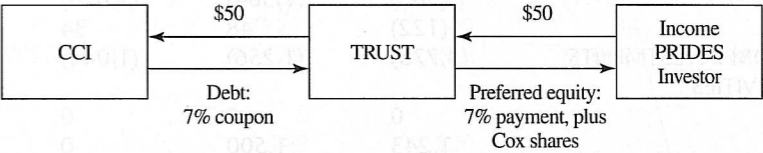
Source: Bloomberg

	1 Year	2 Year	3 Year	5 Year	10 Year
Treasury bonds	5.38	5.64	5.70	5.83	5.83
U.S. Treasury strips	5.38	5.66	5.71	5.88	6.16
A-rated industrial bonds	5.99	6.33	6.44	6.70	6.93
BBB-rated industrial bonds	6.30	6.62	6.81	7.05	7.37
BB-rated industrial bonds	6.84	7.51	7.71	8.00	8.80

Note: All yields quoted on a semi-annual basis.

EXHIBIT 7 FELINE PRIDES Structure: Income PRIDES

Source: Cox Communications, Inc.



Under the Income PRIDES structure, the holders would receive a 7% cash payment for three years. At the end of the three years they were required to purchase a certain number of Cox's shares in exchange, at their option, for cash or their preferred equity in the Trust. The number of shares would be determined by Cox's share price in three years (S), as shown in the first column. The second column shows the number of shares delivered to the holder of a Feline PRIDE in three years, and the third column shows the value of the shares delivered in three years.

Simultaneous with the Income PRIDES offering, the Trust would buy the debt that Cox issued. The Cox debt would pay a 7% coupon per year.

Cox Share Price in 3 Years	Number of Cox Shares Delivered	Value of Cox Shares Delivered
$S \leq \$34.6875$	1.4414	$1.4414 * S$
$\$34.6875 < S < \41.7984	50/S	\$50
$S \geq \$41.7984$	1.1962	$1.1962 * S$

EXHIBIT 8A Pro Forma Cash Flows^a for Cox Communications If It Did Not Purchase Gannett, But If Other Proposed Acquisitions Were Undertaken (figures are in millions of dollars)

Source: Cox Communications, Inc.

	1999 E	2000 E	2001 E	2002 E	2003 E
OPERATING ACTIVITIES					
EBITDA Cox + Acquisitions	878	1,344	1,490	1,697	1,913
EBITDA Gannett	0	0	0	0	0
Interest Expense	(312)	(540)	(443)	(472)	(432)
TOTAL CASH FROM OPERATIONS ^b	566	804	1,047	1,225	1,481
INVESTING ACTIVITIES					
Acquisitions ^c	(2,673)	0	0	0	0
Gannett Acquisition	0	0	0	0	0
CapEx	(983)	(1,304)	(1,078)	(822)	(734)
Total Other	(122)	48	34	10	10
TOTAL CASH FROM INVESTMENTS	(3,778)	(1,256)	(1,044)	(812)	(724)
FINANCING ACTIVITIES					
Equity Issued	0	0	0	0	0
Monetization ^d	1,243	1,500	0	0	0
Beginning Debt	4,091	6,249	5,202	5,198	4,786
Maturing Debt		(431)	(341)	(200)	(277)
New Debt Financed (Retired) ^e	1,968	(617)	337	(212)	(480)
Ending Total Debt	6,249	5,202	5,198	4,786	4,029
TOTAL CASH FROM FINANCING	3,401	452	(4)	(412)	(757)
CONDENSED INCOME STATEMENT					
EBITDA	878	1,344	1,490	1,697	1,913
Depreciation	(197)	(261)	(216)	(164)	(147)
Interest	(312)	(540)	(443)	(472)	(432)
Taxes	(85)	30	10	10	10
Net Income	285	573	842	1,070	1,344
DEBT RATIOS					
Pro Forma Annualized EBITDA ^f	1,201	1,344	1,490	1,697	1,913
Leverage Ratio ^g	5.2 ×	3.9 ×	3.5 ×	2.8 ×	2.1 ×
EQUITY INTEREST					
Cox Family Economic Equity ^h	67.3%	67.3%	67.3%	67.3%	67.3%
Cox Family Voting Equity ⁱ	76.8%	76.8%	76.8%	76.8%	76.8%

^aAssumes that planned monetizations of \$500 million in 1999Q3 and \$1.5 billion in 2000Q1 are implemented.

^bAs a result of significant accumulated tax losses to carry forward, Cox did not anticipate paying any cash taxes for the years shown here.

^cThis figure included \$2.023 billion for cash portion of TCA merger, \$1.4 billion for Media General acquisition, less \$750 million in cash and other assets Cox was supposed to receive as part of the AT&T transaction.

^dMonetization included \$743 million raised in the first quarter, and \$500 million scheduled for the third quarter of 1999. Both of these transactions were independent of the Gannett transaction. Cox also planned to raise \$1.5 billion in 2000Q1 by monetizing a portion of the Sprint PCS position.

^eDebt was treated as a plug, or balancing figure in this pro forma.

^fPro forma Annualized EBITDA is 4 × the Quarterly EBITDA results.

^gLeverage ratio defined as the Ending Total Debt divided by the Pro Forma Annualized EBITDA.

^hEconomic equity was the percentage of the firm owned by the Cox family. Were the firm to be sold, they would receive this percentage of the proceeds. Calculation assumes maximum dilution from FELINE PRIDE conversion.

ⁱVoting equity was the percentage of the firm controlled by the Cox family. They cast this percentage of the votes in any question that came before the shareholders.

EXHIBIT 8B Pro Forma Cash Flows for Cox Communications If It Purchases Gannett by Issuing Debt (figures are in millions of dollars)

Source: Cox Communications, Inc.

	1999 E	2000 E	2001 E	2002 E	2003 E
OPERATING ACTIVITIES					
EBITDA Cox + Acquisitions	878	1,344	1,490	1,697	1,913
EBITDA Gannett	0	151	163	176	190
Interest Expense	(312)	(540)	(657)	(667)	(640)
TOTAL CASH FROM OPERATIONS	566	955	996	1,207	1,463
INVESTING ACTIVITIES					
Acquisitions	(2,673)	0	0	0	0
Gannett Acquisition	0	(2,700)	0	0	0
CapEx	(983)	(1,334)	(1,103)	(847)	(759)
Total Other	(122)	48	34	10	10
TOTAL CASH FROM INVESTMENTS	(3,778)	(3,986)	(1,069)	(837)	(749)
FINANCING ACTIVITIES					
Equity Issued	0	0	0	0	0
Monetization	1,243	1,500	0	0	0
Beginning Debt	4,091	6,249	7,781	7,854	7,484
Maturing Debt		(431)	(341)	(200)	(277)
New Debt Financed (Retired)	1,968	1,962	414	(169)	(437)
Ending Total Debt	6,249	7,781	7,854	7,484	6,770
TOTAL CASH FROM FINANCING	3,401	3,031	73	(369)	(714)
CONDENSED INCOME STATEMENT					
EBITDA	878	1,495	1,653	1,873	2,103
Depreciation	(197)	(267)	(221)	(169)	(152)
Interest	(312)	(540)	(657)	(667)	(640)
Taxes	(85)	30	10	10	10
Net Income	285	718	785	1,047	1,322
DEBT RATIOS					
Pro Forma Annualized EBITDA	1,201	1,495	1,653	1,873	2,103
Leverage Ratio	5.2 ×	5.2 ×	4.8 ×	4.0 ×	3.2 ×
EQUITY INTEREST					
Cox Family Economic Equity	67.3%	67.3%	67.3%	67.3%	67.3%
Cox Family Voting Equity	76.8%	76.8%	76.8%	76.8%	76.8%

EXHIBIT 8C Pro Forma Cash Flows for Cox Communications If It Purchases Gannett by Issuing Equity (figures are in millions of dollars)

Source: Cox Communications, Inc.

	1999 E	2000 E	2001 E	2002 E	2003 E
OPERATING ACTIVITIES					
EBITDA Cox + Acquisitions	878	1,344	1,490	1,697	1,913
EBITDA Gannett	0	151	163	176	190
Interest Expense	(258)	(310)	(413)	(420)	(377)
TOTAL CASH FROM OPERATIONS	620	1,185	1,240	1,453	1,726
INVESTING ACTIVITIES					
Acquisitions	(2,673)	0	0	0	0
Gannett Acquisition	0	(2,700)	0	0	0
CapEx	(983)	(1,334)	(1,103)	(847)	(759)
Total Other	(122)	48	34	10	10
TOTAL CASH FROM INVESTMENTS	(3,778)	(3,986)	(1,069)	(837)	(749)
FINANCING ACTIVITIES					
Equity Issued	2,700	0	0	0	0
Monetization	1,243	1,500	0	0	0
Beginning Debt	4,091	3,495	4,797	4,625	4,010
Maturing Debt		(431)	(341)	(200)	(277)
New Debt Financed (Retired)	(785)	1,732	170	(415)	(700)
Ending Total Debt	3,495	4,797	4,625	4,010	3,033
TOTAL CASH FROM FINANCING	3,348	2,801	(171)	(615)	(977)
CONDENSED INCOME STATEMENT					
EBITDA	878	1,495	1,653	1,873	2,103
Depreciation	(197)	(267)	(221)	(169)	(152)
Interest	(258)	(310)	(413)	(420)	(377)
Taxes	(85)	30	10	10	10
Net Income	339	948	1,029	1,293	1,584
DEBT RATIOS					
Pro Forma Annualized EBITDA	1,201	1,495	1,653	1,873	2,103
Leverage Ratio	2.9 x	3.2 x	2.8 x	2.1 x	1.4 x
EQUITY INTEREST					
Cox Family Economic Equity	59.0%	59.0%	59.0%	59.0%	59.0%
Cox Family Voting Equity	69.9%	69.9%	69.9%	69.9%	69.9%

EXHIBIT 8D Pro Forma Cash Flows for Cox Communications If It Purchased Gannett with a Combination of Debt, Equity (\$680 million), and PRIDES (\$720 million) (figures are in millions of dollars)

Source: Cox Communications, Inc.

	1999 E	2000 E	2001 E	2002 E	2003 E
OPERATING ACTIVITIES					
EBITDA Cox + Acquisitions	878	1,344	1,490	1,697	1,913
EBITDA Gannett	0	151	163	176	190
Interest Expense	(310)	(473)	(580)	(591)	(521)
TOTAL CASH FROM OPERATIONS	568	1,022	1,074	1,283	1,582
INVESTING ACTIVITIES					
Acquisitions	(2,673)	0	0	0	0
Gannett Acquisition	0	(2,700)	0	0	0
CapEx	(983)	(1,334)	(1,103)	(847)	(759)
Total Other	(122)	48	34	10	10
TOTAL CASH FROM INVESTMENTS	(3,778)	(3,986)	(1,069)	(837)	(749)
FINANCING ACTIVITIES					
Equity Issued	1,400	0	0	0	0
Monetization	1,243	1,500	0	0	0
Beginning Debt	4,091	4,847	6,311	6,306	5,861
Maturing Debt		(431)	(341)	(200)	(277)
New Debt Financed (Retired)	566	1,895	336	(245)	(556)
Ending Total Debt	4,847	6,311	6,306	5,861	5,028
TOTAL CASH FROM FINANCING	3,399	2,964	(5)	(445)	(833)
CONDENSED INCOME STATEMENT					
EBITDA	878	1,495	1,653	1,873	2,103
Depreciation	(197)	(267)	(221)	(169)	(152)
Interest	(310)	(473)	(580)	(591)	(521)
Taxes	(85)	30	10	10	10
Net Income	287	786	863	1,123	1,440
DEBT RATIOS					
Pro Forma Annualized EBITDA	1,201	1,495	1,653	1,873	2,103
Leverage Ratio	4.0 x	4.2 x	3.8 x	3.1 x	2.4 x
EQUITY INTEREST					
Cox Family Economic Equity	65.1%	65.1%	65.1%	63.0%	63.0%
Cox Family Voting Equity	75.0%	75.0%	75.0%	73.3%	73.3%