

Growth Leadership of the Year Award Retail/Enterprise DIA Services North America, 2011

Frost & Sullivan's Global Research Platform

Frost & Sullivan is in its 50th year in business with a global research organization of 1,800 analysts and consultants who monitor more than 300 industries and 250,000 companies. The company's research philosophy originates with the CEO's 360 Degree Perspective™, which serves as the foundation of its TEAM Research™ methodology. This unique approach enables us to determine how best-in-class companies worldwide manage growth, innovation and leadership. Based on the findings of this Best Practices research, Frost & Sullivan is proud to present the 2011 North American Growth Leadership of the Year Award in Retail/Enterprise DIA Services Market to XO Communications

Key Industry Challenges

Service Providers Find It Challenging To Differentiate Their Dedicated Internet Access Offerings

The DIA services market is a fairly commoditized market as service providers have traditionally offered just pure bandwidth. This has resulted in a significant reduction of pricing levels for the DIA service. However, the past 4-5 years have seen some shift in the market space with carriers emphasizing value-added services and managed services to counter the revenue decline. VoIP (CPE/network-based), IP VPN, and managed security services are examples of the value-added services being offered along with DIA. Frost & Sullivan's research shows that this challenge is acting as a driver for companies willing to provide managed services and as a restraint to those who see the Dedicated Internet Access space as selling pure bandwidth.

Economic Downturn Has Impacted Multiple Components of the Sale Cycles

Economic constraints definitely affected company renewals, installs, and usage rates in 2009, with many companies reluctant to renew contracts. A concern over financial commitments associated with new contracts has caused many enterprises to simply not renew but operate off of previous contract obligations, thus leading to continuation in usage of traditional services. However, in 2010 the market did witness a noticeable increase in spending with customers shifting from T3 or SONET circuits to Ethernet. Service providers report that a number of deals that were put on hold in 2009 due to the economic downturn finally materialized in 2010.

Service Providers Struggle with Revenue Cannibalization of Legacy System

A majority of carriers in today's DIA market continue to rely on investment in traditional infrastructure to maximize return on investment. However, with increasing adoption of

Ethernet, carriers need to manage the revenue decline for traditional services. A large percentage of carriers' installed base remains in the T1 space, with a significant portion of the T3 and SONET customer base gradually migrating to Ethernet. As enterprises demand more bandwidth and as Ethernet becomes more widely available, market migration to Ethernet will be more rapid. Frost & Sullivan expects that carriers who are not prepared with viable solutions to facilitate market migration will experience a loss of market share. Those carriers who have invested in new technology are better positioned to compete against price compression factors.

Best Practice Award Analysis for XO Communications

The Frost & Sullivan Award for Growth Leadership is presented to the company that has demonstrated excellence in capturing the highest annual compound growth rate for the last 3 years.

XO Communications' Performance in Retail/Enterprise DIA Services Market

XO Communications, through a combination of facilities-based Tier 1 internet backbone, early strategic investment in Ethernet technology and an enviable bundling marketing strategy has experienced a commendable growth in revenues in the retail/enterprise DIA services market. Frost & Sullivan's recent research proves the market share growth of XO Communications in the services market, thus resulting in the company being chosen for 2011 Growth Leadership Award.

Key Performance Drivers for XO Communication

XO Communications offers one of the broadest set of DIA services in the retail/enterprise space backed by its Tier 1 nationwide IP network, with a choice of bandwidth options, multiple access technologies (T1, SONET, Ethernet) options, robust service level agreements, and web-based monitoring and reporting tools. The company has a strong Ethernet strategy with significant investments in Ethernet over Copper offerings, enabling the company to effectively address the small and midsize business segments.

With the demand for high speed bandwidth across multiple industry verticals increasing, it is in turn driving market spending on high-speed dedicated Internet access services. In particular, next-generation services (such as Ethernet) which offer high bandwidth ports at a fraction of the cost of traditional services (such as SONET) are seeing good demand. Several factors are influencing enterprises decision to migrate from TDM-based services to Ethernet - the relatively lower cost of Ethernet compared with TDM service, ease of service management, and straightforward migration to higher performance levels without disruption. Ethernet also provides more flexibility and ease of management for WAN

administrators. Its ability to scale easily and smoothly for higher bandwidths compared with TDM-based services is also driving migration.

As customers add voice/video applications to their Internet pipes, there is a growing demand in the market for managed Internet services where the service provider offers a richer set of offerings that add value to the overall service experience/framework/component. Examples of the services offered include: managed router, network security services (CPE or cloud-based), network management (manage updates or any sort for error resolution, software updates) and physical maintenance as covered in the SLAs.

The T1 customer base in the enterprise markets has been the most difficult segment to migrate to Ethernet as these customers are extremely dependent upon the reliability of TDM circuits. Also, the bandwidth needs of this segment - SMB - are usually below 3 to 5 Mbps, thus hindering adoption of 10 Mbps services. However, as mid-band Ethernet services delivered over copper/fiber/microwave become more widely available in the market, Frost & Sullivan expects a greater migration of the T1 customer base to Ethernet. Also, the need for migration often depends on the applications that the customer typically runs—VoIP is one application that clearly is driving adoption of Ethernet services. Currently, the market demand for sub 10 Mbps speeds is quite significant, and service providers are investing in networks to extend Ethernet services to their existing T1 customer bases.

An interesting observation in the Frost & Sullivan's 2010 and 2008 DIA market share charts is the shifting of aggregate share top 3 large carriers' decrease with a respective market share increase for competitive carriers, such as, XO Communications. Frost & Sullivan expects future adoption of Ethernet services to further alter the competitive market shares. The market has been showing clear signs of downward adoption trending for traditional services, and the decline will only be more rapid as enterprises spending on technology bounces back. Frost & Sullivan firmly believes that Carrier Ethernet as a service has arrived and is here to stay, and only those CSPs who have a clear Ethernet strategy and the ability to support layering of applications/services on top of Ethernet will continue to perform well in the market. Today, having Ethernet services in the portfolio is no longer a competitive advantage by itself; rather, it is a necessity to be well positioned in the competitive landscape.

Frost & Sullivan feels that XO Communications with its early investment in Ethernet over Copper technology has successfully captured a significant share of revenues in the market, taking advantage of the market migration. The company also has a great bundled services offering - DIA + MPLS IP VPN, DIA + VoIP + MPLS IP VPN, managed services (managed router, managed security services) - that has led to its DIA services revenue market share increase from 3.6 percent in 2008 to 4.4 percent in 2010, which is significant considering the market is just emerging out of a recession.

Conclusion

XO Communications with its early investment in Ethernet over Copper technology has successfully captured a significant share of revenues in the market, taking advantage of the market migration. The company also has a great bundled services offering – DIA + MPLS VPN, DIA + VoIP + MPLS VPN, managed services (managed router, managed security services) – that has led to its DIA services revenue market share increase from 3.6 percent in 2008 to 4.4 percent in 2010, which is pretty significant considering the market is just emerging out of a recession.

Frost & Sullivan commends XO Communications' growth in the retail/enterprise DIA services market and bestows its 2011 Growth Leadership of the Year Award in recognition of the company's impressive performance.

About XO Communications

XO Communications is a leading nationwide provider of advanced IP communications, managed network and IT infrastructure solutions for businesses, enterprises, government, carriers and service providers. Its customers include more than half of the Fortune 500, in addition to leading cable companies, carriers, content providers and mobile network operators. Utilizing its unique combination of high-capacity nationwide and metro networks and broadband wireless capabilities, XO Communications offers customers a broad range of services with proven performance, scalability and value in more than 85 metropolitan markets across the United States. For more information, visit www.xo.com.

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