

### Abstract

America Online Time Warner is the nation's largest Internet service provider (ISP), even though serving as an ISP was not the original intent. Along with the growth of the Internet has come expanded opportunities for revenues based on access fees. As the leading player in the effort to attract Internet service subscribers, AOL Time Warner faces ongoing competition. The percentage of American households that own computers is still increasing with a proportional rise in Internet usage at home. Changing technologies, emerging e-commerce practices and the desires of the consumer are some of the drivers that are causing the online environment to evolve. Thus AOL Time Warner must put forth an effort to not only to compete for customers, but adapt their strategies to meet the unforeseen demands that their marketplace will continue to present.

### Competition and Strategy for America Online Time Warner.

America Online Time Warner (AOLTW) is the leading Internet service provider in the United States in terms of total subscribers. Started in 1985, America Online began as an online service, creating a 'private' marketplace for buyers and sellers of selected goods and services. In the mid 1990's, AOL responded to pressure from their customers who desired to use the internet and began to offer access to the web. Since that time, the growth of Internet usage forced to AOL to de-emphasize their online service and expand their offerings as an ISP. AOL gained market share by saturating the market with a low cost product and providing a vast network of dial up numbers, even in remote rural areas. AOL made it easy to sign up and the vast majority of customers did not have to pay telephone tolls to access the service point.

There was a point where AOL gained customers so quickly that demand outpaced the capacity of their infrastructure. Subsequently, AOL was able to catch up with the demand and restore the reliability of their service. In turn, Internet usage has not only increased, but changed. Companies like Amazon revolutionized retailing by introducing the concept of ordering goods across the Internet. Forms of communication like e-mail and chat became more popular. Technologies like telephony and DSL have emerged. To satisfy the desires of their burgeoning and ever more sophisticated customer base, AOL has responded with technologies like AOL Instant Messenger (AIM). AOL acquired the faltering Netscape in order to provide their customers with a top rate web browser and break their dependence on Microsoft's Internet Explorer. With the Netscape purchase, AOL could modify the browser software to fully integrate the Internet experience with other offerings in the AOL stable. In January of 2001, AOL completed a merger with Time and Warner Brothers. AOL had a large customer base, and wanted to revisit their beginning as an online service. By acquiring Time and Warner Brothers,

AOL now had exclusive rights to quality audio and visual content that could be made available only to AOL Time Warner customers. The strategy of acquiring Time Warner should prove fruitful once broadband access is in place for the majority of AOLTW customers.

The competition for AOLTW is varied. One rival is Earthlink. As the number 2 ISP in the US, Earthlink has embarked on an ambitious strategy of acquiring smaller ISP's in an effort to gain subscribers and catch the AOLTW market share. Earthlink offers better web hosting and ASP options than AOLTW. However, the cost of acquisitions has reduced Earthlink's earnings. Another strong competitor is MSN. Controlled by Microsoft, MSN benefits from the deep pockets and technological resources of its parent company. It also helps to be associated with a strong brand. Juno and NetZero have combined forces and now offer a major alternative to AOLTW. The early Juno/Netzero strategy has been simply to offer service equal to AOLTW at half the price. Yet another major competitor for AOLTW is AT&T WorldNet. The WorldNet service has the unique distinction of being associated with a leading telecommunications carrier. Thus AT&T can leverage their huge telephone network resources and operate the WorldNet service at a lower cost than AOLTW, again passing the savings on to customers in the form of lower fees than what AOLTW charges.

The future for AOLTW lies in the broadband market. In order to deliver the content now available within Time and Warner Brothers, high-speed access for subscribers is warranted. The size of the files and the quality of streaming media prohibit connections at the 56-kilobaud speed range. The broadband market has 3 segments in digital subscriber lines (DSL), cable and satellite. There are broadband Internet vendors who own the communication infrastructure, like SBC Direct TV, and those who operate as resellers, like Covad. America Online Time Warner offers DSL and cable Internet access through its broadband subsidiary. The competing players

against AOLTW also offer broadband options. Complicating the issue are resellers like Covad who specialize in DSL access. In general, the threat of new entrants in the ISP market is currently low. Communications networks carry a high initial investment price. Also, it is expensive to operate and maintain the infrastructure. For DSL resellers, however, there is a lower barrier to entry since they do not have to maintain the infrastructure. Nowadays, any ISP venture must deal with an economy of scale to be profitable. There are also regulatory issues administered by the FCC to adhere to. Access is access. Regardless who the provider is, there is little differentiation between the various choices in the current market.

Returning to the competitors for AOLTW, though the ISP market is still growing, it has slowed. In addition, the cost for a customer to switch ISP is low. The Internet runs on standardized protocols, so there is no re-investment in hardware or software necessary upon changing providers. As described above, the major ISP players have various strategies for overtaking AOLTW. In the case of resellers, strategic alliances must be formed with the companies that own the communications networks. Further, the various ISP entities have entered agreements with vendors offering ancillary services that enhance the core access service. For the owners of the networks, exit barriers are high since Internet access networks have no alternative uses. It is not a simple thing to sell off a telecommunications infrastructure.

The bargaining power of buyers of Internet access is strong. They are many and, again, switching costs are low. To hold the customer, companies like AOLTW must offer low cost, reliable access along with value added options like instant messaging, chat, Usenet and web mail. In contrast, the bargaining power of the suppliers differs depending on whether they own the network or act as resellers. There are regulations requiring asset owners to provide resellers access to the network. The companies that control vast communication networks act both as

suppliers to the resellers and direct access providers, especially in the DSL market. The network owners can affect the quality of service allowed resellers and affect market share. As far as content, the network owners have the advantage again since they can deal directly with content providers while resellers have the more complex task of coordinating access and content through the firms that controls the networks.

When considering the Internet, the threat of substitution is limited to narrow band and broadband access. Within broadband there are the options of DSL or cable access. AOL Time Warner offers every type of access. Though the future opportunity lies in broadband, the current major source of revenue is the modem dial up customer base. Another form of Internet access is via wireless devices. Wireless Internet access is not as widespread domestically as in Europe or Asia due to the influence of the established wire-based telephone industry. A competitor offering widespread wireless broadband has the potential to offer a viable alternative not only to AOLTW, but the entire market. Cell phone providers like Sprint offer wireless Internet access, but it is limited in features and function and is expensive. There are technologies like the Ricochet® wireless modem and Intel's® Access Point, but the performance of Ricochet® is lower than that of DSL or cable while Access Point is limited to home network use.

Other stakeholders have an influence over the fortunes of AOLTW. The FCC regulations could change drastically and reduce the competitive advantage that AOLTW holds. Shareholders of AOLTW stock could become disgruntled and relay their feelings to the Board of Directors, in turn affecting the execution of carefully formulated plans. The owners of the network resources that AOLTW relies on could be acquired by a rival resulting in AOLTW losing bandwidth. In an economic downturn, those same asset owners could raise access fees for AOLTW, cutting into revenues.

America Online Time Warner is at the top of the ISP heap and will have to fight to stay there. The competition is varied, and constantly trying to take customers away from AOLTW. The fortunes of AOLTW ride partially on the highly unpredictable horse of technological innovation. The acquisition of Time Warner will only give AOLTW an advantage once broadband access is prevalent.

### References

1) Margaret Kane, 2002, AOL Gains Cable Broadband Access

<http://zdnet.com.com/2100-1105-954607.html>.

2) David McClure, 2002, Internet Service Providers in the 21<sup>st</sup> Century, US Internet Industry Association.

3) Yves Cornaz, Talissa Hollander, Sajeel Malani, 2002, AOL Time Warner.

4) Josephine Giordano, Yen-Tsung Lin, Anita Lopez, Arlene McNear, 2002, America Online.