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Sprint Corp. (S)

Q3 2014 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and thank you for standing by. Welcome to the Sprint Fiscal Third Quarter 2014 Conference Call. During today's conference, all participants will be in a listen-only mode. Following the opening remarks, the conference will be open for questions. I would now like to turn the conference over to Mr. Jud Henry, Head of Investor Relations. Please go ahead, sir.

Jud Henry
Director - Investor Relations, Sprint Corp.

Thank you, Janika. Good morning and welcome to Sprint's quarterly earnings call. Before we get underway, let me remind you that our release, quarterly investor update and presentation slides that accompany this call are all available on the Investor Relations website at www.sprint.com/investors. Slide two is our cautionary statement. I want to point out that remarks this morning will – we will be discussing forward-looking information, which involves a number of risks and uncertainties that may cause actual results to differ materially from our forward-looking statements. We provide a comprehensive list of our risk factors in our SEC filings, which I encourage you to review.

Turning to slide three, throughout our call we will refer to several non-GAAP metrics. Reconciliations of our non-GAAP measures to the appropriate GAAP measures for the quarter can be found on our investor relations website.

Now let's move on to earnings for the third fiscal quarter of 2014 on slide four. Our financial results include a predecessor period related to the results of operations of Sprint Communications, Inc., which is formerly Sprint Nextel, prior to closing the SoftBank transaction on July 10, 2013 and the applicable successor periods. In order to present financial results in a way that offers investors a more meaningful comparison of the year-to-date results, we have combined the results of operations for the predecessor and successor periods of fiscal 2013.

Trended financial information metrics on a combined basis can be found at our investor relations website. Basic and diluted net loss per common share for the third quarter was $0.60, compared to $0.26 in the year ago quarter. The change in net loss per share is primarily related to non-cash impairment charges of $2.1 billion related to wireline network assets and wireless trademarks, which amounted to a loss of $0.54 per share.

During the quarter ended December 31, 2014, we tested the recoverability of the Wireline asset group, and as a result of that test, we reported an impairment loss of $233 million to reduce the carrying value of Wireline's property plant and equipment to its estimated fair value. In addition, due primarily to the decline in revenue from the loss of postpaid phone customers since the merger with SoftBank, we also recognized an impairment to our indefinite-lived intangible assets.

This non-cash impairment was applied to the carrying value of the Sprint trademarks in the amount of $1.9 billion. Net tax benefit in the third quarter was $657 million, largely related to a $726 million, or $0.18 per share, non-cash benefit from the aforementioned impairment charge. We expect net tax expense for the fiscal fourth quarter to be approximately $50 million to $70 million. When adjusting for the non-cash impairment charge and related tax benefit, net loss per share would have improved $0.02 year-over-year.

Lastly, although Clearwire's financial results are now consolidated with Sprint's and included in today's presentation, its standalone quarterly financial results will be available on our website in the next several weeks as required by its debt covenants. I will now turn the call over to Sprint CEO, Marcelo Claure.

R. Marcelo Claure

President, Chief Executive Officer & Director

Thank you, Jud, and good morning, everyone. As I'll share with you in more detail shortly, we made good progress this quarter but we have more work to do to reach the goals that we have set to turn around Sprint. I've been here six months and in that time, I have been able to get my arms around the business and see not only the challenges that we face, but also the great potential that Sprint has.

It is clear that for us to win in the marketplace, it takes a great network, a compelling value proposition and good distribution. We are becoming more aggressive competitors on all fronts, focused on acquiring and retaining quality customers, improving our network and customer experience and reducing costs. I'm very excited about the progress we've made in these few months. The momentum that we built exiting 2014 will provide the foundation for future growth. If you have a good network, have good offers, and treat customers right, then customers will come and they will stay. And I'm happy to report we're making progress on all fronts.

This quarter, we added nearly one million connections to the Sprint platform, or highest net adds in two and a half years and up 42% year-over-year. Our Wholesale business grew for the sixth consecutive quarter. We had industry-best prepaid net adds, and we delivered in our commitment to return to postpaid growth. However, our goal remains to return to growth in postpaid phones.

We lost another 205,000 this quarter, which is a great improvement considering we had lost a total of 1.8 million in the prior three quarters. It was a record sales quarter with our highest ever retail gross adds and highest retail sales on records across postpaid and prepaid brands, with sales up nearly 20% year-over-year. And we have improved our network, as noted by RootMetrics and other reputable third parties. We now cover more than 770 million people with LTE, including 125 million POPs on 2.5 GHz.

This six months also provided the time needed to evaluate the operational model and identify the fundamental issues we must overcome to be successful in our turnaround. But I couldn't be more confident that now we have the right plan to be successful. Let me walk you through the foundational pillars that we're addressing to turn around Sprint.

Turning to slide six. The first priority is to continue to enhance our network by fully leveraging our spectrum portfolio to build a network that delivers a consistent reliability, capacity, and speed that our customers demand. We're executing on a clear three-point plan to create a great network that deliver the service and experience that our customers want.

First of all, we continue to optimize and tune the network to improve the customer experience. Network Vision provided us with a new network infrastructure and enhanced backup platform from which we can continue to innovate and efficiently deploy new capabilities across our network. We have also successfully deployed voice services on the 800 MHz spectrum nationwide, which has greatly improved not only rebuilding coverage, but also the key performance metrics of the voice network.

That enhancement immediately benefits more than 75% of our postpaid phone base that have 800 MHz voice-enabled devices. This improvement was further validated by independent third party data provided by Nielsen, which showed that Sprint's drop call rate as being the lowest ever and improved by more than 50% year-over-year. You can probably guess from the graph which carriers continues to have the worst drop call rate in the industry.

In addition, our LTE network reached over 270 million people at the end of December and a continued expansion and optimization of our 3G and LTE network has greatly improved the overall network performance. In fact, Sprint Network was recently recognized for its improvement by independent mobile analytics firm RootMetrics. Sprint was the operator with the highest net gain among all carriers in first or shared first place RootMetrics network award wins in the second half of 2014, with 133 RootScore Awards for reliability, call or text performance in cities across the country. Results for second half 2014 show Sprint moved up RootScore award rankings in almost every market measure. For example, Sprint ranked second for overall performance in Chicago. This result give us the confidence that the plan is working and we will work to replicate the Chicago success story across the country.

Our second focus area for the network is a continued build-out of LTE on the 800 MHz band. We already have 800 MHz LTE on air across more than 60% of royalty footprint and we're focused on completing the other 40% by the end of this year when rebanding is complete. This would greatly enhance our LTE coverage and in building performance, and it also provides us with an additional layer of capacity across the network. We have already seen immediate improvements in the consistency and reliability of LTE performance as we turn up 800 MHz in several markets already.

Thirdly, we're continuing to invest to unlock the true potential of our network infrastructure and spectrum portfolio. In other words, we intend to fully leverage our low band 800 MHz solid mid back position on 1.9 GHz and [ph] deep (09:01) 2.5 GHz spectrum holdings of more than 120 MHz. This includes significantly densifying our network by increasing the number of sites across all spectrum bands, including macro and small cells, to increase the coverage and capacity of the network. Make no mistake, while we focus on the fundamentals to improve consistency and reliability of the network, we have not lost sight of speed and capacity capabilities that we have with a rich spectrum portfolio. We remain full speed ahead with our 2.5 GHz LTE deployment, and now have 125 million POPs on air.

Moving forward, we expect to transition our network to an IP-based platform, including a clear path to deploying [ph] vaulting (09:43). Also, we will leverage technology development, such as carrier aggregation, that allow us to combine TDD and FDD LTE across all of our spectrum bands, to maximize the coverage and capacity capabilities of our portfolio. For example, this gives us the flexibility to use our 1.9 GHz FDD spectrum for up-link and our 2.5 GHz TDD spectrum for down-link. This means the 2.5 GHz, essentially, will have the same coverage as the 1.9 GHz. These technology advancements allows for improved [ph] capital efficient (10:15) to truly make the value for us much greater than the sum of the parts.

Moving to slide seven. Another critical component to Sprint's turnaround is to significantly increase the number of quality customers by continuing to deliver an industry leading value proposition. We have repositioned Sprint by providing simple offers that save customers money with unlimited plan for individuals, and family plans that allow customers to save money by sharing data. This applies to prepaid as well, with Boost Mobile industry leading data plans, and expanded availability for compelling offers on a newly created Sprint prepaid brand. Put simply, we want customers to know that Sprint can save them money.

In December, we launched a Cut Your Bill in Half event, which invited customers of AT&T and Verizon to come to Sprint to cut their monthly service plan charges in half. The response to Cut Your Bill in Half has been great, and is a very clear message for AT&T and Verizon customers to take a real look at Sprint. Traffic in our retail stores was up more than 10% year-over-year in December. What is interesting is that when AT&T and Verizon customers come in and see the great offers that our customers are benefiting from, many of them elect to take our standard offers instead of cutting their overpriced bills because our plans offer them more value and more flexibility.

We will continue to focus on marketing programs that deliver clear, simple and powerful methods to potential customers. We intend to continue our successful Cut Your Bill offer through 2015, and we will be aggressive in delivering that message to the market. Sunday's Super Bowl ad was just the latest example.

Furthermore, we continue to expand Sprint's innovative and industry exclusive leasing program. Beginning with the iPhone for Life program that launched in September with the iPhone 6. We have since enhanced that program with 12 month, 24 month and 30-month options to give customers more flexibility with how often they want to upgrade their iPhone. In addition, we have created a Sprint leasing program for select high-end Android devices, such as the Samsung GALAXY S5, Samsung Note Edge, and LG G3.

Furthermore, this week, we launched our first leasing bundle, combining unlimited data for iPhone and 2 gigabytes of data for iPad for only $100, including the lease of both devices. Sprint's leasing options have been very well received by consumers. They like the clear and simple value proposition that provides the latest high end devices with no out-of-pocket costs at point-of-sale for qualified customers, with the lowest monthly cost and the opportunity for perpetual upgrades.

We're also providing great value in the prepaid market with the September launch of the Data Boost Plans in Boost Mobile. These plans raise the bar for the industry by offering unlimited talk and text and more high speed data than competitors offer at comparable price points. In January, we announced the launch of the industry's first no-contract data sharing plan with Virgin's Mobile Data Done Right. This is available exclusively at Walmart, which is a major distribution channel for prepaid. We're also excited about expanded distribution on devices we rolled out this quarter for the Sprint prepaid brand.

These simple and innovative offers clearly resonated in the marketplace, as shown in our record sales numbers for December quarter. Our total Sprint platform retail sales in the quarter were the highest on record and I'd like to highlight a few of those. Postpaid gross adds were the highest in three years. A 50% increase in our share of postpaid phone gross additions in the quarter, compared to [ph] August (13:53). Highest postpaid upgrades on record, highest ever postpaid gross adds, and highest ever iPhone sales in a quarter, even higher than when Sprint got the iPhone in 2011, supported by our iPhone exclusive rate plan and our iPhone for Life Plan.

Most importantly, while this is scale business and we want to grow the volume of customers, we're pleased with the quality and long-term profitability of the customers we're adding. Our prime mix of postpaid customers in the quarter was the highest on record for both gross adds and for the base. Furthermore, the volume of new consumer account gross additions with three or more lines more than doubled from the year ago period.

Also, our sales strategy prioritizes the most profitable devices, as postpaid phone gross add were up 20% year-over-year. And we're driving through our most profitable channels as postpaid phone gross adds in our branded doors are up more than 60% year-over-year. As a result, the high quality customers we're now attracting or estimated lifetime value of the customers we brought on in this quarter is more than 3 times the value of customers we brought a year ago this time. While we offer great prices to customer, our estimated long-term profitability actually improves, because these prime multi-line accounts have lower churn characteristics and have lower support costs because they tend to [ph] call care less often (15:19), consume less data, and combine more lines per bill.

Shifting gears to customer retention. While we're pleased that the gross add momentum helped us achieve 30,000 postpaid net adds in the quarter, our postpaid churn rate remains higher than our competitors. We're now placing a stronger focus on customer retention, and our goal is to reduce churn by fundamentally transforming our customer experience. We want our base to enjoy the best value as well, and we plan to be very targeted, utilizing proactive real-time and individualized offers to make sure our high-value customers are on plans that are best suited for them.

Fortunately, there are a number of indicators that give me confidence that we will bring our churn rate down in 2015 and beyond. First of all, we had our highest upgrades on record in the December quarter, with 11.5% of our base recommitting to Sprint. We will continue to embrace upgrades as customers become eligible and want to get the latest devices and stay with Sprint. Also, the quality of the customers we're adding with higher prime and multi-line mix should lead to lower churn in the future, as these customers are much stickier. Our significant improvement in the network and our commitment to make it even better will also help reduce churn.

Lastly, we have already seen the impact of tightening our credit policies beginning last August. Involuntary churn is coming down this quarter and we expect it to improve as we remain disciplined in our credit policies. As a matter of fact, we expect churn to decline significantly this coming quarter to get back to levels we saw last year at this time, if not better, and we believe that we have the opportunity to continue to reduce churn going forward.

Turning to cost structure. We continue to rapidly reduce our operating costs to achieve a more competitive cost position in the industry. As I committed to you last quarter, we're working to eliminate at least $1.5 billion of operating costs on an annualized basis compared to our 2014 levels. We have clear line of sight to these reductions and a high degree of confidence, and many of the initiatives have already started ramping up.

These cost reductions will come from every line in the P&L as we drive simplification of our operating model; continue to rationalize our workforce and optimize our vendors. We have implemented a zero-based budgeting process, where every business unit must justify why they need to spend each dollar. And we drive the initiatives home by having biweekly governance meetings to track the progress of each cost take-out initiative.

Most importantly, this is not a one-time exercise, but a fundamental change in our operating philosophy and a cultural shift on how every employee thinks about the spending impact. While $1.5 billion is a significant reduction, it is just a near-term goal and we're already looking at how we can meaningfully take additional costs out of the business in future periods.

While we're also focused on significant cost reductions, we will also be selectively reinvesting in areas of the business that are key to our turnaround. Last quarter, we noted one example, where we're opening a call center here at our headquarters to have our best and highest level customer service reps. Other examples would include investment in growing distribution and additional offers to attract more high-quality customers to Sprint to improve our operating leverage and grow margins.

To be successful in our turnaround, we're building a stronger management team by attracting and retaining some of the best talent in the industry. We're driving leadership accountabilities through cross-functional meetings, where all parties are present to identify and resolve issues in real-time. We're changing the employee culture through more open and transparent communications, inclusive decision-making, and injecting a more entrepreneurial spirit that encourages our people to innovate more and execute faster.

We're seeing a renewed sense of energy in our employee base, particularly in our front-line employees who see first hand our turnaround in momentum. I made some changes to my leadership team that includes some new faces as well as promoting and expanding the roles of key talent. To better understand our customer needs and experience interacting with Sprint, I have asked my lead team to periodically sell in our retail stores and take customer service calls directly. This should improve insights on how we manage our business, I'm confident that we're building the leadership team and a culture to be successful in our turnaround.

Moving to slide 11, all of these initiatives come together to improve the customer experience as we aim to consistently delight our customers by delivering a simplified experience across all customer touch points. This starts with the customer is first culture and that is why I have appointed Bob Johnson, one of Sprint's longest tenure and successful executives as our new Chief Experience Officer. We will listen to customers and front-line employees to understand customer pain points, address them head on, and proactively identify ways to provide a great experience to our customers.

We are already seeing positive early signs, ending the year with the lowest ever postpaid calls per subscriber and the lowest percent of the base calling into Care as well as higher close rates our stores. In addition, we have set aggressive goals to improve our Net Promoter Score and are tying our executive compensation to that. When I got here, we had more detractors than promoters, but we have seen that trend reversing in just a few months, demonstrating the momentum we're rebuilding.

This includes a continued optimization and rapid improvements in the network, making sure we have great offers for new and existing customers, and having simple and positive experience with the consumers at every touch point. Ultimately, this should lead to improved brand loyalty and lower churn, which will improve the profitability of the business. I will now turn the call over to Joe to take you through our financial results.

Joseph J. Euteneuer
Chief Financial Officer

Thank you, Marcelo. I'll now walk you through our financial and operating results for the December quarter. Total Sprint platform net additions were 967,000 in the December quarter, which was up significantly from 590,000 last quarter and 682,000 a year ago. Retail net additions of 440,000 improved by 60,000 year-over-year, and 677,000 sequentially as postpaid and prepaid each improved by more than 300,000.

Wholesale and affiliate net additions were 527,000, with connected devices driving the majority of the gains. As Marcelo mentioned, Sprint platform postpaid net additions were 30,000 in the December quarter, driven by the highest gross additions in three years, partially offset by elevated churn levels. Postpaid phone net losses were 205,000 in the quarter, which is an improvement of 200,000 compared to last year, and nearly 300,000 better than last quarter, driven by the success of our new offers.

Finally, tablet net additions were 189,000 in the quarter, down 276,000 year-over-year and down 72,000 sequentially. Sprint platform postpaid churn was 2.3% in the December quarter, up from 2.18% last quarter and 2.07% a year ago, driven by higher involuntary and voluntary churn in a highly promotional quarter. As Marcelo mentioned, we expect churn this quarter to drop to levels similar to last year at this time. As involuntary deactivations come down as a result of our tightened credit policy, involuntary churn improves as a result of network improvement and the high quality customers we are acquiring.

Smartphones represented 97% of postpaid phone sales in the quarter and now account for over 87% of our postpaid phone base. In addition, we now have 69% of our Sprint platform postpaid base on LTE devices, including 81% of our Sprint platform postpaid smartphone base. Also, postpaid devices financed through Sprint Easy Pay and leasing increased to 46% this quarter, and reached 50% in the month of December. We expect to maintain the December run rate in the near term with only modest uptake in financing throughout 2015. Sprint platform prepaid experienced net additions of 410,000 in the quarter compared to 322,000 a year ago, and 35,000 last quarter, driven by continued momentum on the Boost brand. In addition, Sprint platform prepaid churn in the quarter was 3.94%.

Moving to revenue, consolidated net operating revenue of $9 billion was up nearly $500 million or 6% sequentially, and down less than 2% year-over-year. Wireless operating revenue was up more than 6% sequentially and flat year-over-year, as declines in postpaid service revenues due to losses of high ARPU phone connections over the course of the year was offset by higher equipment revenue from significantly higher sales, and a higher take rate on Sprint Easy Pay.

Wireline operating revenue declined 2% sequentially, driven by declining voice and Internet revenue. Year-over-year, Wireline operating revenue declined 19% as a resulted of cable voice over IP migrations as we've noted in prior quarters, voice rate and volume declines and the annual inter-company rate refresh, with the inter-company impact being neutral to consolidated adjusted EBITDA.

Sprint platform postpaid average total billings per user, if you add monthly equipment billings to service revenue, were $62.16, which was down less than 1% from the $62.75 last quarter and down 3% year-over-year, primarily driven by tablet mix. In fact, we estimate that phone-only average total billings per customer actually increased slightly year-over-year. This underscores our discipline to maintain the actual monthly cash flow stream from our phone customers.

Sprint platform prepaid ARPU of $27.12 was relatively flat sequentially and up more than 1% year-over-year, primarily due to the improving mix of the base towards the higher ARPU Boost brand.

Please turn to slide 14. Consolidated adjusted EBITDA of $1.04 billion was down $110 million from the year ago period, driven by Wireline declines, and down $342 million sequentially, driven by significantly higher sales volumes in the Wireless business. Wireless adjusted EBITDA of $1.03 billion remained relatively flat year-over-year and declined by $336 million sequentially on record sales volume.

Wireless cost of service of $1.9 billion continued to improve as it was down $346 million year-over-year, driven by lower roaming expenses, lower backhaul expenses with the migration to Ethernet and lower labor with declining network upgrade activity compared to the year ago period. Sequentially, cost of service is down $86 million, mainly due to lower roaming volumes. These continued expense reductions and cost of service help offset the impact of record sales.

Wireless cost of product or equipment expense was $2.95 billion in the quarter, which was up $221 million year-over-year, primarily driven by a higher mix of high-end phones. Sequentially, the high retail sales volume on the Sprint platform was a significant driver of the $580 million cost increase in addition to the mix shift towards higher end devices. I would note that this does not reflect roughly $600 million of equipment cost related to leased devices that is instead captured in PP&E. This is balanced by the fact that we recognize no revenue upfront for leased devices.

Wireless selling general and administrative expenses in the December quarter were $2.5 billion, which was up $101 million from the year ago period and an increase of $346 million sequentially. The sequential increase in SG&A was again mostly driven by the record retail sales in the quarter along with the seasonal increase in marketing spend. The year-over-year increase also includes higher bad debt as a result of an increased volume of sales on installment billing, as the higher sales volume expenses were partially offset by rate favorability as a result of increased mix of sales in our direct and branded channels.

Wireline adjusted EBITDA was $11 million in the quarter, representing a $94 million decline year-over-year, primarily associated with the loss of high margin cable voice over IP customers, lower international voice rates, lower inter-company rates and lower voice volumes.

Turning to CapEx and cash flows on slide 15. Capital expenditures of $1.8 billion in the quarter were down slightly year-over-year, but up approximately $300 million sequentially. This was driven by Wireless CapEx of $1.6 billion, which was up approximately $250 million sequentially, but down $100 million year-over-year as Network Vision expenditures in the year ago period were partially offset by the growing momentum this year on the 2.5 GHz build, which is less capital intensive on a rate basis. The sequential increase in capital expenditures was associated with leased device transactions in our indirect channels where we purchased the title to the devices back from the third parties.

Free cash flow was negative $1.8 billion for the December quarter compared to negative $2.8 billion in the year ago quarter, and negative $75 million in the prior quarter. The year-over-year improvement was due to better cash flow from operations and lower cash CapEx. The decrease in cash used in operating activities compared to the year ago quarter was primarily due to the interest payments in call premiums paid on the early retirement of Clearwire debt in the year ago period and favorable changes to other working capital.

Sequentially, the decline is related to lower cash flow from operations, primarily driven by increased cash paid for inventory and other unfavorable changes to working capital, and higher cash paid for CapEx. Within working capital, we did have $1 billion included in accounts and notes receivable related to installment billing.

Total net receivables related to installment billing were $1.5 billion, up from $1.2 billion at the end of last quarter. As a result, we ended the quarter with a total liquidity position of $7.5 billion including cash, cash equivalents and short-term investments of $3.7 billion, as well as $3.8 billion of undrawn borrowing capacity under our revolving bank credit facility, and eligibility under our undrawn service receivables financing agreement at the end of the quarter. In addition, as I committed to last quarter, we recently closed on $1.8 billion in network vendor financing to provide us greater flexibility and liquidity options as we invest in our network.

As we look ahead, we have no significant maturities due until December of 2016. We will continue to manage our capital structure and position ourselves to have adequate liquidity to grow the business and fund investments in the network. We expect to leverage the capacity under our service receivables facility and the vendor financing on the 2.5 GHz build and continue to work towards entering into installment billing financing facility.

We strive to leverage the assets on our balance sheet to diversify and lower the cost of financing, including maintaining a lower minimum cash balance. All together, the changes that we have made in the last few months as part of our turnaround are starting to build momentum going into 2015, and will support our mission of building long-term value

When we spoke to you last quarter, we expected EBITDA to be flat to slightly up in 2015. However, we now have better insight into the trends of the business with a full quarter behind us, and now expect that EBITDA could increase 5% to 7% year-over-year in calendar 2015 compared to 2014 results.

With regard to capital spending, we expect CapEx in the March quarter to be slightly up compared to the same quarter last year, excluding the impacts of leasing. We plan to provide full year guidance for fiscal 2015 on next quarter's call.

I'll now turn the call back over to Jud to begin the Q&A.

Jud Henry
Director - Investor Relations, Sprint Corp.

Thanks, Joe. In just a moment, we will begin the Q&A. Janika, Please inform our participants on how to queue up for the question-and-answer session.

QUESTION AND ANSWER SECTION

Operator: [Operator instructions] Your first question comes from Kevin Smithen.

Kevin Smithen
Macquarie Capital (USA), Inc.

Q

Can you talk a little bit about the network improvements that we've seen through some of the third party, like RootMetrics, et cetera? How can you begin to get the message out to consumers that the network is improving?

R. Marcelo Claure
President, Chief Executive Officer & Director

A

That's one of the challenges that we have and the fact that it takes time for consumers to realize there is a time effect to that. All we can do is just continue to build every day a better network. And I personally watch the performance of our network across all of the markets on a weekly basis, and we have seen a tremendous improvement in pretty much everything that we measure. And it's nice when a third party is the one who recognizes those achievements.

We might start looking at, potentially, including in our advertising, some stuff that relates around the network improvement. I think what is remarkable is the first market that we put a lot of focus on, on doing the basics, tuning the network, was Chicago, and it's great when an independent firm recognizes that we have the second best network in Chicago. And what you can expect is a pretty aggressive marketing message, recognizing that our network is ahead at a local level in Chicago

And I believe that RootMetrics is going to release their second half 2014 rankings pretty soon and we're going to be watching all the results. And then based on those results, we expect to do a lot more marketing, especially around the markets that we have seen a great improvement.

Kevin Smithen
Macquarie Capital (USA), Inc.

Q

Marcel, there's been a lot of talk about, in the press, about you potentially monetizing some of your excess Spectrum. Can you talk a little bit about how you think about spectrum sales, kind of a leasing, JV and/or MVNOs with Google or others?

R. Marcelo Claure
President, Chief Executive Officer & Director

A

So like we said, it is a responsibility to continue to look in the value for assets. And I told – we were very surprised with the value that the spectrum option generated. And one of the things that I pay special attention is to technology and how technology today, through carrier aggregation, through TDD-FDD carrier aggregation, makes our 2.5 GHz spectrum pretty much be able to provide the same coverage at 1.9 GHz.

So therefore when you look at our spectrum holdings, they become, I would say, very valuable. So we're always looking in terms of what would the value be. And we're always running different analyses that says how much spectrum do we need. So we are always open and looking at potential offers. That doesn't mean that we're out there marketing the sale of our spectrum. As it relates to Google, we are both binded by a confidentiality agreement. So at this point in time, we're not able to comment anything as it relates to the news that has been reported around a Google MVNO.

Kevin Smithen
Macquarie Capital (USA), Inc.

Q

Thank you.

Operator: Your next question from Jennifer Fritzsche.

Jennifer M. Fritzsche
Wells Fargo Securities LLC

Q

Great. Thank you for taking the call. On the CapEx comment, Joe, I know you said you expect March CapEx to be up slightly year-over-year. With -that brings in the question about the build. I mean, I think some are wondering why, given the amount of spectrum you have and realizing the limits of your balance sheet, but why don't you aggressively kind of back up the trucks here and move forward more aggressively on that CapEx? It seems like more of a measured approach and maybe that – can you comment on that? Is there any thought as you get more momentum under the operations and the fundamentals, is that something we could see?

Joseph J. Euteneuer
Chief Financial Officer

A

Yeah. We'll give you a full capital plan on our next call. But remember, seasonally, the first quarter is always a little light because we make that big hard push in the calendar fourth quarter. But I think Marcelo made the comments about how we are going to fully utilize that 2.5 GHz, not only from the capacity standpoint, but its speed and its characteristics of – with carrier aggregation of getting down to 1.9 GHz characteristics. So, yeah, I think there's more to hear. But rest assured that we are going to fully utilize our assets with a capital program that supports that philosophy.

Jennifer M. Fritzsche
Wells Fargo Securities LLC

Q

Great. Thank you.

Operator: Your next question comes from Amir Rozwadowski.

Amir Rozwadowski
Barclays Capital, Inc.

Q

Thank you very much. And good morning, Marcelo, Joe, and Jud.

Joseph J. Euteneuer
Chief Financial Officer

A

Morning.

Amir Rozwadowski
Barclays Capital, Inc.

Q

In thinking about sort of the competitive landscape, certainly, it seems as though some of your larger competitors have made some suggestions about focusing on very specific areas of the market, being the high end or the enterprise customers. I was wondering what you make of those commentaries as related to your potential runway and potential opportunity. And then I've got a quick follow-up post that.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

I think each one of our competitors are focusing on the areas of strength. I think we are focused on providing a great value to our customers. We have been very successful at attracting AT&T and Verizon customers to come to Sprint Network. And we will continue to do so by, basically, continuing with your – Cut Your Bill in Half or Cut Your Rate Plan in Half promotion.

And what that does, as I explained in the call, is it attracts a large number of customers. Our traffic was significantly up year-over-year. And when they come into our stores, the vast majority of them realize that Sprint has very attractive rate plans and they're signing up to our standard rate plans. They're happy with the amount of data we're providing them and we're happy with the price flexibility that we provide to them. So we're going to continually focus on attracting AT&T and Verizon retail customers.

Same thing we've seen from a prepaid perspective. We've put together a compelling value proposition and it's great. I was looking at the numbers in terms of the rankings that we came in and Sprint, our prepaid brands came in first as the carrier – the national carrier with the highest net add. So we feel very good for our value proposition which today is saving money to customers

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Amir Rozwadowski
Barclays Capital, Inc.

Q

Great. Thank you very much, Marcelo. And then in looking at sort of your revised outlook for your EBITDA guidance going forward, how should we think about the different moving pieces here? Is this sort of increased comfortability around the cost execution plans that you have in place and the ability to achieve those? Is it sort of some of the shifting in terms of the value proposition you're providing via leasing plans? Would love to get a little bit of color on sort of what's giving you that comfortability.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

When we spoke in our last earnings call, we said that it was going to be neutral to modestly higher. We're starting to get a lot more comfortable in understanding the drivers of the business. And that is why we say that we believe that EBITDA this year is going to increase between 5% to 7% year-over-year in calendar 2015. It's a combination of many things. A combination of taking cost out of the business to combination of growing our business. It's a combination of moving customers to lease and installment billing, so it's a combination of putting an aggressive focus on churn. So we have a very clear turnaround plan that is up to us to execute. And as we do, we believe that our EBITDA will continue to grow and every single quarter we're going to update on where do we stand as it relates to EBITDA

Amir Rozwadowski
Barclays Capital, Inc.

Q

Thank you very much for the incremental color.

Operator: Your next question comes from Michael Rollins.

Michael I. Rollins
Citigroup Global Markets, Inc. (Broker)

Q

Hi, thanks for taking the questions. A couple, if I could. One is how important is RadioShack as a distributor to you, and can you talk about maybe your distribution strategy more broadly as it relates to stores and doors? And I'll just follow up after that.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

Sure. As you can imagine, we cannot comment on RadioShack, but I'll be more than happy to comment on our distribution growth. There are three basic fundamental principles that would allow you to attract customers. And that is you've got to have a great network, you've got to have a compelling offer, and you've got to have distribution, meaning places where a consumer can go and shop for mobile phones or connected devices.

Today, we are the carrier with the smaller amount of stores. We are, I think, 500 stores or 600 stores less than T-Mobile and we're like 3,000 stores less than Verizon. So our goal is to continually grow distribution. And we made it publicly that we intend to grow at least 500 stores this year. And we are looking at many different opportunities in terms of growing our stores. But distribution growth is one of the key imperatives that are needed to continue to attract more customers to the Sprint brand

Amir Rozwadowski
Barclays Capital, Inc.

Q

And just a second question. Within the Wireline segment, can you just give us a sense of today, what part of the revenue is contributed from Sprint and how important that asset is strategically to the way that you operate and monetize the Wireless business over time?

R. Marcelo Claure
President, Chief Executive Officer & Director

A

So the Wireline business is strategic in helping the Wireless business compete on a multi-element proposal in the business space. About 20% of the Wireline revenue in the quarter was generated for more Wireless business.

Cable, voice over IP migration were the biggest driver of the year-over-year decline. But going forward, we expect to place a greater focus and emphasis on our MPLS and IP solutions.

Amir Rozwadowski
Barclays Capital, Inc.

Q

Thanks very much.

Operator: Your next question comes from Brett Feldman.

Brett Joseph Feldman
Goldman Sachs & Co.

Q

Thanks for taking the question. Joe, you gave us a little bit of color about the financial impact of financing devices. I was hoping we could just come back to that and just a few questions. So one, can you give us a breakdown in terms of the Easy Pay which is the installment plan, relative to the leasing, just from mix standpoint?

And then you noted that you don't think in aggregate the percentage of sales on financing is likely to increase much from roughly the 50% level. I'm curious why not, if there's anything that's a headwind to that or is that something that you're intentionally managing?

Joseph J. Euteneuer
Chief Financial Officer

A

No this is – answer your questions in reverse order. No, there's no headwind. I mean, actually, our installment billing and lease options did very well and we're happy exiting the year at 50%. We're watching it and we're trying – you see a number of offers that we're putting out there and we're trying to sort of land the plane of what's the right balance on consumer demand between financing and non-financing options. But we're very favorable on it, but didn't want to get ahead of our skis.

Brett Joseph Feldman
Goldman Sachs & Co.

Q

And then just the mix in the quarter, is that something you're breaking out in terms of leasing versus...

Joseph J. Euteneuer
Chief Financial Officer

A

Yeah, we haven't broken that out yet. I mean leasing was our first quarter and did very well. We provided you some color on the total value of the leases. You'll see that in the Q. But that's really all we've done to date. As we get more, you'll probably get more additional information.

Brett Joseph Feldman
Goldman Sachs & Co.

Q

And just one last one. Is there a number in terms of like what the actual net use of cash was, in terms of all financing sales over the course of the quarter? And then maybe just as an extension of that, for how long do you think it's going to be a use of cash?

Joseph J. Euteneuer
Chief Financial Officer

A

Well, I mean, look, I think the easiest way to do is just look at cash flow from operations. That's probably the easiest way to do it because, otherwise, you end up with looking at things on a myopic basis and misconstruing what our real results are. So, I mean, obviously, our goal right now is to continue to try to grow EBITDA, especially on a cash basis, to ultimately get to self-sustainability. And the good news is, with maturities not being due until December of 2016, provides us a little runway room to build up some momentum.

Brett Joseph Feldman
Goldman Sachs & Co.

Q

All right, thanks for taking the question.

Operator: Your next question comes from Jonathan Chaplin.

Jonathan Chaplin
New Street Research LLP (US)

Q

Thanks. Two quick questions. Marcelo, I was very interested in your comments around using 1.9 GHz in conjunction with 2.5 GHz. I'm wondering if you could go into a little bit more detail on what your thoughts are in that regard. Are you moving away from using TD-LTE on 2.5 GHz? Would that cause a delay in your deployment of 2.5 GHz as you switch technologies? And then I'm also wondering if you can give us some more context around where churn is in Chicago at the moment? So we've got an idea where the business trends as your network improves in other markets also.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

I'll take the second question, and then I'm going to ask Stephen Bye to take the 2.5 GHz question. As it relates to churn, we don't disclose churn on a market-by-market basis, but I can tell you that, as the network gets better, net churn starts decreasing pretty nicely. And I don't want to elaborate too much on this specific quarter, but we feel extremely good about what churn will be this quarter.

As we've closed January, we've seen a really nice trend forming, and we have many ways to measure this. And that is, percentage of customers are churning because of network, that has reduced as a total percentage. So we feel good, but as we improve our network, customers are going to want to stay longer time with Sprint. The only problem is it takes a little time for that to come to realization. As it relates to our 2.5 GHZ deployment and TDD-FDD, I'll let Stephen Bye comment on that.

Stephen J. Bye
Chief Technology Officer

A

Yeah, hi, Jonathan. It really doesn't change kind of the path that we're on, because we continue to deploy the TDD-LTE at 2.5 GHz. And given the spectrum depth that we have at 2.5 GHz, we can actually complement that with FDD-TDD carrier agg. We're also looking at carrier agg across 800 MHz and 1900 MHz and 2.5 GHz. So it doesn't really change the trajectory or the path that we're on because of the depth of spectrum that we have. So we can actually do a combination and a complement with that solution.

Jonathan Chaplin
New Street Research LLP (US)

Q

And when do you think the carrier agg for 1.9 GHz and 2.5 GHz with an [ph] FD (47:32) configuration will be deployable?

Stephen J. Bye
Chief Technology Officer

A

Yeah, we're not actually talking about a specific timeframe at this point, but it's under development and we're working with device vendors as well as network vendors in terms of the timing for that.

Jonathan Chaplin
New Street Research LLP (US)

Q

So it's still a few years off, Stephen?

Stephen J. Bye
Chief Technology Officer

A

It's certainly not a few years off. It's more in the near term.

Jonathan Chaplin
New Street Research LLP (US)

Q

Okay, thank you.

Operator: Your next question comes from Philip Cusick.

Philip A. Cusick
JPMorgan Securities LLC

Q

Hey, guys. Thanks. So I wanted to try and get some clarity here. Marcelo, when you and I talked in September, and I asked you, this was too early tell, but at this point, as you look at EBITDA, so pulling out all of the handset accounting and I know that's hard, but do you expect EBITDA to grow on a real basis in 2015 versus 2014, as you think of that combination of the huge revenue headwind you have but versus the big cost reductions? Thanks.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

We're changing the fundamentals of the business, and that is when you go from a very low financing or lease percentage and start moving to a big percentage, then obviously, you've got to start looking at the business different and start looking at the business maybe from an EBIT perspective. And I can tell you that when we look at our future projections of EBITDA and EBIT, the business looks – once you start breaking churn into more favorable trend, once you start increasing your number of net adds, we start seeing EBITDA and EBIT start moving in the right direction. So we feel very good about it.

Philip A. Cusick
JPMorgan Securities LLC

Q

Okay. And then, Joe, I'm getting a lot of questions about the lease accounting, both direct and indirect, and how that flows from cash to inventory to PP&E. And I know this is a little bit of minutiae, but there's a lot of questions on this.

Joseph J. Euteneuer
Chief Financial Officer

A

Sure. [indiscernible] (49:32)

Philip A. Cusick
JPMorgan Securities LLC

Q

Can you expand what happened in the fourth quarter? Thanks.

Joseph J. Euteneuer
Chief Financial Officer

A

Yeah, sure. Basically, what happens is on our own stores, basically, the devices get purchased, go into inventory and then is sold, they move into fixed assets. On an indirect basis, we're buying the device back, so it comes in through capital expenditures and then gets depreciated. So one doesn't show up in CapEx, the other does.

Philip A. Cusick
JPMorgan Securities LLC

Q

And so I think you said the EBITDA sequentially was up essentially because of the capitalization from the indirects?

Joseph J. Euteneuer
Chief Financial Officer

A

Yeah, I mean – so you're right. So there was roughly $290 million.

Philip A. Cusick
JPMorgan Securities LLC

Q

Got it. Okay. Thank you.

Joseph J. Euteneuer
Chief Financial Officer

A

Of CapEx. There was $290 million of CapEx related to the indirect, where we're buying these phones back and it hits CapEx versus the stuff that we have through our own stores.

Philip A. Cusick
JPMorgan Securities LLC

Q

Got it. Thanks, Joe.

Joseph J. Euteneuer
Chief Financial Officer

A

Yeah.

Operator: Your next question comes from Simon Flannery.

Simon Flannery
Morgan Stanley & Co. LLC

Q

Okay. Thanks very much. Good morning. You had some nice improvement on the gross add side and you talked about the expectations for churn in Q – in the following I guess, March quarter. Can you talk about what you're doing on the retention side given that a lot of the offers are available only to the new customers coming in? How are you thinking about targeting or migrating some of those customers on to the new sort of pricing plans? Where are you on that? Thanks.

R. Marcelo Claure
President, Chief Executive Officer & Director

A

So one of our main area of focus is on retention and we have a lot of different initiatives. One is we are becoming extremely good at understanding our customers, call it a high propensity to churn customers. And we are going to them very aggressively. We're contacting them, we're sending them letters, we're moving them to the rate plan, so we're looking to the rate plan that will suit them most. Secondly is we're going through a technology upgrade. We're targeting all of the customers that are still on 3G or that do not have a Spark device. And we're contacting proactively and basically moving them to a 4G Spark device so they can have a better experience.

The thing that makes us feel good about retention is we have the highest upgrade rate on record on last quarter. So we had 11.5% of our base who basically signed up to continue to be with Sprint. We're having better quality customers, meaning we have dramatically increased our multi-line accounts. Multi-line accounts churn is significantly lower than single line accounts because it's an entire family that will have to churn.

In network performance improvements, I mean, customers are having a better experience, and therefore, choosing to stay. We have a focus on customer experience. We have a customer experience officer. We're rolling out a new software that the leading carriers around the world use, which is called [indiscernible] (52:33) called Next Best Action. And that is you're treating your customer on an individualized software, and an offer that basically is suitable for them.

So I can go on and on. I mean, the amount of focus that we have on retention, and we started focusing on this on the previous quarter, and you're going to see a great improvement and it's like anything else. You put a lot of focus into it. You drive your executive compensation towards that, and you make everyone in the company understand that churn is actually the best indicator of how we're performing. And suddenly, I think you're going to be very pleased with our churn results that we're going to present this quarter.

Simon Flannery
Morgan Stanley & Co. LLC

Q

And is the Framily related churn, is that pretty much done by next quarter?

R. Marcelo Claure
President, Chief Executive Officer & Director

A

You've got to look at churn into two pieces, voluntary and involuntary churn. Right? On involuntary churn, we have tightened our credit in August, and that takes six months to clean up. So you can start seeing, at the end of this quarter and beginning of next quarter, a nice reduction in voluntary churn. And voluntary churn, this quarter was a little high because there was a lot of promotions from all of the different carriers. But we expect it to just continually going better. So it's fair to say that the elevated Framily churn is going to start coming down.

Simon Flannery
Morgan Stanley & Co. LLC

Q

Thank you.

Jud Henry
Director - Investor Relations, Sprint Corp.

So that's all the time we have for questions. But before we end the call, I'd like to turn it back to Marcelo for some closings comments. If you have additional questions following the call, please contact the Sprint Investor Relations team at 800-259-3755 or investor.relations@sprint.com. Marcelo?

R. Marcelo Claure

President, Chief Executive Officer & Director

Thanks, John. I want to thank everyone for joining us today and for your interest in Sprint. It has been a very busy six months and we have made some significant changes across the business in a very short period of time. I think the employees are excited with the positive early signs we're seeing in the quantity and quality of our customer position and the network continues to make great strides.

At the same time, we recognize that we're only in the beginning of our turnaround and have a lot of hard work ahead of us to meet the aggressive goals we have as a management team. As I said before, I'm confident that we have our arms around the issues that we need to address and we now have the right plan to be successful in reaching our goals. I look forward to providing you an update on our progress in our next quarter. Thank you.

Operator: Thank you for participating in today's conference call. You may now disconnect.