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Sprint Corp. (S)

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and thank you for standing by. Welcome to the Sprint Fiscal Third Quarter 2018 Conference Call. During today's conference call, 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, Vice President of Investor Relations. Please go ahead, sir.

Jud Henry

Vice President, Corporate Strategy & Head of Investor Relations, Sprint Corp.

Good morning, and welcome to Sprint's Third Quarter Fiscal 2018 Conference Call. Joining me on the call today are Sprint's President and CEO, Michel Combes; our CFO, Andrew Davies; and our CTO, Dr. John Saw.

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 Sprint Investor Relations website at www.sprint.com/investors.

Slide 2 is our cautionary statement. I want to point out that in our remarks this morning 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 risk factors in our SEC filings, which I encourage you to review.

Throughout our call, we will refer to several non-GAAP metrics as shown on slide 3. Reconciliations of our non-GAAP measures to the appropriate GAAP measures for the quarter can be found on our Investor Relations website.

Lastly, like last quarter, we have included reconciliations and qualitative disclosures in the tables that accompany our release and investor update to provide additional clarity regarding the adoption of the new revenue recognition standard on our quarterly results.

For the remainder of this call, we will discuss results excluding the impact of this accounting change to provide clear comparability with prior periods unless otherwise noted.

I will now turn the call over to Michel to provide an update on our results.

Michel Combes

Chief Executive Officer, President & Director, Sprint Corp.

Thank you, Jud, and good morning, everyone. Our fiscal third quarter results on slide 4, demonstrate our focus on executing our strategy as we work towards government approval of our merger with T-Mobile. First, we delivered year-over-year growth in wireless service revenue for the second consecutive quarter. We generated the highest adjusted EBITDA for a third quarter in 12 years, as we continue to execute on our cost reduction initiatives.

Meanwhile, we delivered operating income for the 12th consecutive quarter. We delivered postpaid net additions for the 6th consecutive quarter. We continued our digital transformation, increasing our digital sales and the

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implementation of artificial intelligence. In addition, we doubled our network CapEx year-over-year, and our network continued to improve as we have more LTE coverage and faster download speeds year-over-year.

Turning to slide 5, we continued to make good progress in our Next-Gen Network deployment to provide customers a Network Built for Unlimited. As I've said previously, we remained full steam ahead on our Next-Gen Network deployment during the merger review process as shown by the doubling of our capital spending year-over-year in the quarter.

First, we upgraded thousands of our existing macro sites to add LTE on 800 MHz, 1.9 GHz, and 2.5 GHz to sites that lacked those bands previously as we work to deploy all three of our spectrum bands to provide improved coverage and capacity across our footprint.

We now have 2.5 GHz deployed on roughly 75% of our macro sites compared to about 50% a year ago. In addition, we have added 800 MHz to thousands of sites, primarily in the southwest market as we completed additional rebanding which will provide additional coverage for our customers.

In addition, we have deployed thousands of outdoor small cells in the quarter and now have 27,000 small cells on air compared to only 3,000 this time last year. This ramp in small cells includes more than doubling the number of mini macro sites on air year-over-year, and a very successful rollout of strand mounts, which are delivering significant improvements in coverage, capacity and time on LTE to improve the customer experience in specific locations.

We also continued our small cell innovation with the recently announced Sprint TREBL Magic Box, the world's first Smart Home small cell solution providing enhanced LTE coverage, integrated Alexa voice assistance and exceptional Harman Kardon sound quality.

Sprint TREBL Magic Box continues a winning streak for the company's all-wireless Magic Box portfolio with a prestigious CES Innovation Award for 2019 in the Smart Home product category.

As a pioneer in unlimited data plans, it's important that we deliver a network that stays ahead of the demand curve. With download downloading traffic growing more than 50% in the last two years, we are proud to have met this demand by adding more capacity and speed to our network, resulting in national average download speeds of 93% over the past two years, as seen in Ookla Speedtest Intelligence data through the end of December.

We were also recognized for fastest download speeds in major markets such as Manhattan, where many of you are likely joining from today, as well as Los Angeles, Boston, Seattle and Denver, according to RootMetrics VOC testing for the second half of 2018.

The indoor and outdoor testing was conducted during peak usage hours during the day in the busiest areas of the cities to see how well carriers perform. While expanding our 2.5 GHz footprint, is delivering positive results. We have recently rolled out what most carriers call LTE Advanced or 5G E as AT&T wrongly calls it, which will further enhance the customer experience.

More and more Sprint customers with capable devices are benefiting from faster data speeds than before as we utilize some of the most advanced technologies in wireless such as High Performance User Equipment, 256 QAM, 4X4 MIMO, multiple carrier aggregations and more.

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Our Massive MIMO deployment continues to be on momentum, delivering significant improvements in LTE performance and providing the building block for our Mobile 5G launch in the coming months.

We now have hundreds of Massive MIMO sites commercially on air in a few markets where we are seeing a very promising results, including a four times average increase in capacity and speed with peak increases up to 10 times over traditional LTE.

In the world's first independent benchmark study on Massive MIMO, Signals Research Group recently found the benefits of our Dallas-area 64T64R commercial deployments. And I quote, "real and meaningful generating significant increases in downlink and uplink throughput." Also, as you may recall, Atlanta is one of our Massive MIMO markets preparing for 5G launch in the coming months. That means fans in town for the big game will see exceptional network performance in the highest traffic locations, whether they are inside or outside the stadium, to a nearby museum or hotel, or traveling around the city to one of the many special events planned this weekend.

We're also preparing to launch our Mobile 5G network in the first half of 2019. Our Massive MIMO radio, the software upgradable to 5G NR as you know, allowing us to fully utilize our spectrum for both LTE and 5G simultaneously, while we enhance capacity even further with 5G and begin to support new 5G use cases.

We celebrated an important milestone earlier this month on our path towards launching Mobile 5G service in the first half of this year, when we completed the world's first over-the-air 5G data transition using 2.5 GHz and Massive MIMO on Sprint's live commercial network.

We've also announced three 5G devices including smartphones from both LG and Samsung, as well as a feature-rich mobile hotspot from HTC. The other carriers are not standing still, but our significant work investments, spectrum resources and cutting-edge technologies will help us continue to improve our network and we expect to deliver robust 5G experience in major metro areas.

Nevertheless, we're hopeful to complete our merger with T-Mobile, which is the only path to deliverings of breadth and depth of spectrum which will allow us to provide a truly consistent national-wide 5G experience to Americans.

As a stand-alone company, we [ph] love to scale (09:30) to keep pace with the bigger carriers, AT&T and Verizon, in sustained capital investments. And without additional low-band spectrum we will face challenges to provide customers with coverage comparable to that of the big two carriers.

Turning to slide 6. We continued our Unlimited for All approach to deliver retail net additions for the sixth consecutive quarter. Our postpaid net additions were 309,000 in the third quarter, improving 53,000 year-over-year. This is a result of executing our strategy to grow our relationship with customers, for data devices such as tablets, watches and the successful launch of our Sprint Drive connected car product, which was partially offset by slight losses in phones.

Postpaid gross adds were up slightly year-over-year as we increased sales of data devices. Postpaid phone gross adds were down year-over-year as Sprint was less promotional in our service plans compared to a year-ago, competitor offers were more aggressive, particularly the Retro device offers from AT&T and Verizon, as well as some impact on sales from the merger.

Postpaid churn was up year-over-year as we had foreshadowed last quarter, as customers rolling off introductory promotions have been the primary driver of the year-over-year increase in churn this year. We recently launched

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the My Sprint Rewards app to put discounts on the products and services customers love right at their fingerprints as our way of saying thanks for choosing Sprint.

We believe that investments we are making in our network and customer experience will improve churn and help to lessen the perception gap that impact gross adds today, but it takes time to shift perception.

As we're undocking on a multiyear capital program on our Next-Gen Network to improve LTE and prepare for 5G, it's important for Sprint to be able to deliver service revenue growth over time. In addition to selling additional data services to customers, we're also executing our strategy to grow revenue from smartphones by providing customers the option to upgrade to our feature-rich Unlimited Plus and Unlimited Premium plans.

We have seen more than 20% lift in postpaid phone monthly recurring charges on new account gross adds coming to Sprint compared to last year. At the same time, we're also focusing on selling value-added services such as Sprint Complete, our industrial-leading equipment protection plan and our innovative Safe & Found service. The ARPU stabilization from both base customers and new gross adds has helped to deliver year-over-year growth in wireless service revenue for the past two quarters.

Optimizing the balance of gross adds, churn and ARPU is expected to deliver a better financial outcome over the long-term. We have stabilized our total number of postpaid accounts year-over-year while growing both the number of lines per accounts and the average revenue per account year-over-year.

However, if AT&T and Verizon continue with the aggressive promotional activity we have recently seen, it may slow our path to reduce churn, drive new accounts, gross adds to Sprint and stabilize ARPU which will make it difficult to continue our current year-over-year growth in wireless service revenue in fiscal 2019.

In addition, our business segment continues to be a growth engine with gross adds up year-over-year for the seventh consecutive quarter and the third lowest churn on record delivering postpaid net additions from business for 10 consecutive quarters.

Likewise, we're excited about the future of our Curiosity IoT platform with over 150 million of total contract value signed year-to-date after launching the Curiosity Core and Operating System in addition to [indiscernible] (13:50) in the fiscal third quarter.

Turning to prepaid, we faced pressures in the quarter both from industry decisions continuing to shift to postpaid and aggressive offers from bigger competitors in the market. Boost continued to deliver positive net adds before migrations to postpaid driven by year-over-year growth in gross additions for the sixth consecutive quarter. The strength in Boost was offset by losses from our other prepaid brands.

Turning to slide 7, we are driving a digital transformation of our company as I highlighted last quarter in detail. Because we lack the scale of the biggest wireless carriers, we must be more innovative by leveraging digital capabilities and employing advanced analytics, artificial intelligence and intelligent automation in our operations to further optimize our cost structure.

Our digital transformation is based on three main pillars, increase digital revenue for improvements in gross adds and upgrades for digital channels; provide intelligent customer experience by leveraging AI analytics and data-driven decisions; and improve digital engagements with our in-house digital marketing agency and enhanced app functions.

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From a digital sales perspective, benchmarks show that we're the leading wireless carrier in the U.S. in terms of both the mix of sales for digital and the conversion of web traffic. Postpaid gross adds for digital were up nearly 70% year-over-year in the third quarter. This is driven by best-in-class traffic conversion, for a complete redesign of the end-to-end digital customer experience. In addition, we saw one in every six upgrades coming for digital in the third quarter.

Likewise, we are ramping our rollout of a cutting-edge intelligent customer experience leveraging AI and analytics. We're seeing growth in digital customer engagement for chats and on top of that, we have ramped to 30% of chats being handled by virtual agents and the experience continues to show improving SPS or customer satisfaction.

We have even enabled artificial intelligence within the My Sprint app creating a simple and seamless experience from start to finish, so customers can easily and quickly complete a device upgrade.

Furthermore, connecting with Sprint recently got even easier with the availability of Apple Business Chat. More than 50% of customers engage with service providers through live chats or mobile apps and now consumers can chat directly with Sprint 24/7 by sending a message through the Messages App on iPhone and iPad.

Sprint customers can use Apple Business Chat to message an agent, learn about Sprint plans and more any time of the day. Customers can even start and stop a message any time and pick up right where they left off. This is complementary to our overall customer experience as the automation of the simple customer request allows our live agents to spend more time helping customers resolve their more complex issues.

Lastly, our in-house digital marketing agency is delivering solid early results compared to our previously-outsourced model with web conversions up year-over-year, while online media spend and cost-per-click are down significantly. This digital transformation and data-driven culture is expected to contribute to the evolution of our customer experience and the next wave of cost reductions for the future.

I will now turn the call over to Andrew to take you through our financial results.

Andrew Mark Davies

Chief Financial Officer, Sprint Corp.

Thank you, Michel. As Jud mentioned in his opening remarks, for better comparability I'm going to discuss results based on prior Revenue Recognition Standards beginning with revenue on slide 8.

Consolidated net operating revenues were $8.5 billion for the quarter, an increase of approximately $250 million year-over-year. Wireless service revenue of $5.6 billion in the quarter increased year-over-year for the second consecutive quarter, mostly due to growth in our retail customer base and stabilizing ARPU trends.

Additionally, postpaid service revenue inflected this quarter growing year-over-year for the first time in five years. While the near-term trends are encouraging, the pressure we are currently seeing in retail customer growth will likely start to impact wireless service revenue growth in fiscal 2019 as Michel has already mentioned.

Postpaid ARPU of $44.60 remained relatively stable as the 1% year-over-year decline was the smallest in nearly five years and was impacted by our strategy of driving more data device net additions, which generate additional service revenue for the company, but do put some pressure on ARPU.

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Postpaid phone ARPU was essentially flat year-over-year as base customers rolling off promotions and increasing their monthly spend with us, together with other pricing actions, offset the impact of other promotional discounts.

Prepaid service revenue of $1 billion grew year-over-year for the fifth consecutive quarter as our prepaid ARPU remained flat and we saw continued customer growth within our Boost brand.

Now, let's turn to costs and profitability on slide 9. We continued to execute on our cost transformation in the quarter, as we realize nearly $100 million in net reductions year-over-year in combined operating expenses across cost of services and SG&A costs, when adjusted for $67 million of merger-related costs that were included within SG&A expenses.

Cost of services of $1.7 billion in the quarter were down $62 million year-over-year as lower wireline network expenses were partially offset by some incremental costs associated with our increased network investment.

SG&A costs were $2.1 billion in the quarter. When adjusting for merger costs which are not included within adjusted EBITDA, SG&A was down $30 million year-over-year, mostly due to more efficient marketing spend.

Excluding the impact of the new Revenue Recognition Standard and merger costs, we have delivered approximately $800 million of combined year-over-year gross reductions in cost of services and SG&A costs in the first three quarters of fiscal 2018 and net reductions of about $300 million year-to-date.

For the full fiscal year, we continue to expect to deliver gross reductions of more than $1 billion for the fifth consecutive year, with net reductions of just less than $500 million after reinvestments in our Next-Gen Network, digital capabilities and other initiatives.

Adjusted EBITDA of $2.8 billion for the quarter was the highest fiscal third quarter result in 12 years and improved by $126 million year-over-year.

Turning to slide 10, operating income was $223 million in the quarter, marking the 12th consecutive quarter of positive operating income. The current quarter had several non-recurring items, including $105 million related to a loss on asset dispositions, $67 million related to merger costs, $50 million related to a litigation settlement and $30 million of severance and lease exit costs. These led to a net loss of $343 million compared to net income of $7.2 billion in the year-ago quarter. However, as a reminder, we had a $7.1 billion non-cash benefit from tax reform included in last year's results.

Turning to slide 11, on CapEx and free cash flow, network cash capital expenditures of $1.4 billion more than doubled year-over-year and were up roughly $150 million sequentially as we continued to execute our Next-Gen Network plan.

As expected, adjusted free cash flow dipped into negative territory, a $908 million this quarter as network investments continued to ramp, and we had unfavorable working capital outflows associated with a seasonally heavy sales quarter. As a reminder, the year-ago period also included more than $300 million of benefit related to a cash settlement of a patent infringement lawsuit.

We continue to have strong liquidity with nearly $9 billion of general purpose availability, including about $6.8 billion of cash, cash equivalents and short-term investments. We continued to optimize the capital structure this

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quarter as we repaid $1.8 billion of higher coupon debt and raised $1.1 billion of lower interest rate debt via an [ph] add-on to our (22:41) existing Term Loan B.

Importantly, as a part of this transaction, we also amended the credit agreement to allow a significant upsize to the [ph] spectrum note program (22:51) if the merger with T-Mobile is not approved.

Going forward, we will continue to be optimistic and looking at the capital markets and will certainly maintain flexibility through the duration of the merger review process.

Let's move to our latest outlook on slide 12. The team remains focused on executing our operating plan for fiscal 2018. As a result, we are not making any changes to our guidance for the year. We continue to expect adjusted EBITDA to be in the range of $12.4 billion to $12.7 billion for the full year. However, excluding the impact of the new revenue recognition standard, we expect adjusted EBITDA to be in the range of $11.7 billion to $12 billion.

With regard to network cash capital expenditures, we continue to expect $5 billion to $5.5 billion for the year, as we continue to ramp our investments and prepare for our Mobile 5G launch in the first half of 2019.

Additionally, we continued to expect adjusted free cash flow to be in the range of negative $500 million, to negative $1 billion for the full year.

Thank you. And with that, I will now turn the call back to Jud to begin the Q&A.

Jud Henry

Vice President, Corporate Strategy & Head of Investor Relations, Sprint Corp.

Thanks, Andrew. In just a moment we'll begin the Q&A. Bernard, please inform our participants on how to queue up for the question-and-answer session.

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QUESTION AND ANSWER SECTION

Operator: Absolutely. [Operator Instructions] First question is from Jonathan Chaplin from New Street. Your line is open.

Vivek Stalam
Analyst, New Street Research LLP (US)

Q

Hey, there. It's Vivek on for Jonathan. Just real quick on the churn side, churn increases slowed this quarter year-over-year, but you're still quite a bit higher than peers. It seems like 2019 is the year that churn really starts to drop off. Should we think about this as just sort of winning back what you've seen over the last year in terms of increases? Or is it more about a underlying network reduction to get in line with peers?

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So good morning, Jonathan. In terms of churn, so as you rightly highlighted, we posted postpaid phone churn of 1.84%, which is up sequentially and year-over-year, as it was expected and flagged. Sequentially increase is mostly due to seasonality that we see every year in Q3. And year-over-year increase is mostly due to customers rolling off promotions.

You know that we have those promotions which have been introduced in our base in the past few quarters and which now let's say allows the customers or makes the customers [ph] running (25:44) out of them, and so which trigger a bit of churn.

Keep in mind as we have discussed also in the past, that leasing, which is our value proposition, has structurally higher churn than [ph] ID (25:57), and so that's one of the reasons why our churn is higher than the competitors.

The market remains active and competitive, and Verizon and AT&T have also experienced a year-over-year increase in churn this quarter. So I guess that we're more or less on track with the market in terms of evolution quarter-on-quarter. Of course, if AT&T and Verizon continue with aggressive promotional activity as we have seen recently, it may slow our path to reduce churn, which is what I have flagged for the past few quarters. Our aim is to reduce churn moving forward, and I believe that our increased network investments plus our investments in customer experience will help to reduce the churn moving forward. Of course, we have to take care also of the competitive environment. So that's where we are, and that's let's say the way we are going to move forward.

Vivek Stalam
Analyst, New Street Research LLP (US)

Q

Got it. Thanks.

Operator: Next question is from John Hodulik from UBS Securities LLC. Your line is open.

John C. Hodulik
Analyst, UBS Securities LLC

Q

Great. Thanks. Maybe just some clarifications on the prepared comments. Maybe first for Andrew, you mentioned some pressure on retail I think postpaid customers. And then I think earlier Michel talked about some lower sales

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from the deal. Could you talk about those two issues? I mean, so at this point are you guys trying to say that you've seen a change in trend in terms of your postpaid handset adds?

And then could you sort of – if possible sort of maybe disaggregate sort of the what's really being impacted? Are we seeing – can you quantify maybe how much lower the gross adds might have been from the deal? Or are we talking – and is that just driven by customer decisions, or churn in your retail workforce? And then I guess just lastly, are you guys at this point expecting service revenues to return to negative, given what you've seen sort of thus far through the quarter? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So let me remind you, so what is our strategy? Our strategy this year was to stabilize our postpaid account base while growing both lines and revenue-per-accounts. And I would say that we see as a positive results of this strategy as we have stabilized our total number of postpaid accounts year-over-year and we have grew the lines per-account and the ABPA year-over-year, which means that we are just on track with our strategy to optimize the balance of growth, that's churn and ARPU to deliver a better financial outcome over the long-term.

What we'll say is that from a gross adds perspectives, we are up year-on-year in terms of total postpaid gross adds, which means that we have been able to offset some pressure that we have had on phone gross adds, by strong improvements in non-phone gross adds, whether it's tablets, watches and/or our Sprint Drive value proposition. So that's what we have seen.

On top of that, I should say that we have also seen a good momentum in the business market from a postpaid gross adds point of view, so which has also helped. So that's where we stand. So strategy is just right, and we are just where we were expecting to be.

It's safe to say that the market remained competitive, so that's what is putting some pressure on our phones, gross adds and net adds, meaning that we have been slightly less competitive than previous year from a service plan point of view, when our major competitors have elected to be much more competitive in Q3 compared to last year. So of course, that has put some pressure on our ability to drive gross adds, as well as on our churn as I have already mentioned, so that's what you've seen in our figures.

What you have just mentioned, it's obvious that the deal has kind of let's say a shadow impact on our commercial executions as when customers from the morning to the evening listen to messages saying that the two committees are going to merge, I mean most likely it reduce a bit the appetite to come to Sprint stores. But that's very, very difficult to explain exactly, let's say the amount of traffic or whatever which is impacted by that, so that's why for me the major, major pieces are the ones that I have highlighted before.

John C. Hodulik
Analyst, UBS Securities LLC

Q

Got it. Thanks, Michel.

Operator: Next question is from Philip Cusick from JPMorgan Securities Incorporated. Your line is open.

Philip A. Cusick
Analyst, JPMorgan Securities LLC

Q

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Hi. Thank you. I like the formality. Can you talk about customers coming off those aggressive promotions? Churn was up, but maybe not as much as we'd feared. How should we think about the pace of those rolling off from here? And how many are left?

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

Well, Phil, [ph] just numbers on the (31:18) introductory prices planned such as 50% off for Unlimited Freedom, [indiscernible] (31:24) continue to roll off these promotions, and they will continue over the next several quarters. As customers join Sprint, they get these promotions all the time, so I mean that's something which has impacted this quarter and which will continue to impact the quarters to come.

As you know, these promotions were structured to have lower introductory rates that would then step up at a later date, so very similar to what has been implemented in the cable industry. And so that's what is let's say happening right now. And while we have seen some incremental churn pressure, many customers do stay after the promotional periods end, so it has helped our wireless service revenue trends.

So it's fair to say that this will continue to impact our churn moving forward. We have implemented some other actions in order to mitigate this point of pressure. That's all the investments that we are making in network. In customer experience, we've digital in removing some of the irritants that we had within the days for our customers, but that takes time, so that's why one side will be short-term pressure and on the mid-term, we have those structural moves that we are doing.

And all that, of course, is impacted also by the competitive environment in which we are, so that's why we see this continued pressure. That's why we are still higher than the rest of the industry, but slightly better than what was expected, and just remaining cautious as I know that it will continue to be [ph] tested (33:00) until it goes better thanks to the structural moves that we are implementing right now. And so depending on the competitive market in the quarters to come, it can be – we can have slightly more pressure or slightly less pressure. It will depend on what our major competitors will do.

Philip A. Cusick
Analyst, JPMorgan Securities LLC

Q

Thank you. And just to clarify, the slower or declining revenue is a function of subscribers, correct? Not any hedging on the ARPU tailwind? Can we expect ARPU to continue there?

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So I guess that from an ARPU point of view, we are more or less flat year-over-year and sequentially. So the postpaid phone ARPU was relatively flat, essentially flat year-over-year as base customers rolling off promotions and increasing their monthly spend with us along with other pricing actions offset the impact of other promotional discounts.

So we – as you have seen, we have posted for the first time in five years growth in postpaid wireless service revenue, which is driven by this stabilization of the ARPU and the increase in our base that we have had in the past few quarters.

As we see a slowdown in our base growth, I mean, you can expect that moving forward if the environment was to remain so competitive, we might have also some pressure on our revenue perspective, but in 2019, not in 2018.

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Philip A. Cusick
Analyst, JPMorgan Securities LLC

Q

Thank you.

Operator: Next question is from Brett Feldman from Goldman Sachs & Co. Incorporated. Your line is open.

Brett Feldman
Analyst, Goldman Sachs & Co. LLC

Q

Thanks for taking the question. You mentioned in your prepared remarks that you're now 75% through the process of upgrading your macro sites with 2.5 gigahertz. I just wanted to get an update on when you think you'll have that deployed across your full footprint of macro sites?

And then just thinking beyond that, you had a lot of projects not just to point at 2.5 GHz, focusing on small cells, some of the LTE Advanced features. What's the timeline for kind of completing some of this renewed investment in the network, and how do you think about what happens to your CapEx once you start to move past that? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

Okay. Maybe I will ask John to update you on our network plan.

John C. B. Saw
Chief Technology Officer, Sprint Corp.

A

Sure. Hey, Brett. We expect to be substantially done with adding 2.5 GHz to where we needed it in another quarter, towards spring this year. And like we have said, we have made significant progress. A year ago, we were only at 50% of our sites having 2.5 gigahertz.

Small cells, again, a lot of momentum recently, 27,000 small cells. A year ago, we only had 3,000. So the permits are starting to come in. Some of our infrastructure that we are leveraging, especially with the cable companies is making it easier for us to deploy small cells faster.

LTE Advanced has rolled out in more than 270 cities, and this is why we're starting to make an impression even in the big markets where our customer experience speeds have improved significantly because of LTE Advanced.

We expect the LTE Advanced upgrades to complete around spring this year as well. Small cells will continue to be a focus for us, because we need to continue to densify our networks even with 5G. [ph] A network is never done (36:44), Brett, so we are also rapidly transitioning to focusing on 5G as well. As you know, a lot of our radios that we're deploying today with Massive MIMO allows us to simultaneously support LTE and 5G, and that is going to be the main focus for the rest of this year for 5G.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

Just on the question that you raised as well in terms of CapEx, I guess that what we had said is that you can – we were expecting, sorry, an increase of our CapEx for 2018, 2019 and 2020 in between $5 billion and $6 billion per year in order to catch up and to deliver this plan, and then coming back to benchmarks compared to the other operators based on the number of customers that were in the base.

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Brett Feldman
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thank you.

Operator: Next question is from Michael Rollins from Citigroup Investment Research U.S. Your line is open.

Michael I. Rollins
Analyst, Citigroup Global Markets, Inc.

Q

Hi. Thanks for taking the questions. Two, if I could. First, when you look at the device leasing in the marketplace, does Sprint see that as a differentiator to get gross adds? Or is it really just a preference for how Sprint wants to finance the devices for the customers?

And then secondly and separate from device leasing, can you talk about what's happening with the credit profile for your customers? And are you taking a different look at how to measure credit for customers in an environment where devices are unbundled and some customers even bring their own devices? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So let Andrew, take the second question on credit profile and I will come back on device leading.

Andrew Mark Davies
Chief Financial Officer, Sprint Corp.

A

Yeah, so thanks for the question, Mike. So our credit profiling and the categorization if you will of our customer base by the different types of credit classes or tiers is relatively stable over time, actually. We don't see any material changes.

In terms of how we assess credit risk, we continue to monitor that on a regular basis. I'm talking daily and weekly and not just monthly. And when we see the need to make refinements to our methodologies, we do so. But they are really when we make refinements, it is purely peripheral stuff. We haven't made any material changes to how we profile assess customer credit risk for quite some time. And I see that – I don't see that changing any time in the near future.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

On your first question concerning device leasing, I guess it's fair that it's an economically-driven decision that we felt was appropriate for Sprint in the context in which Sprint was. We are always assessing the pros and cons of this scheme as we know that it delivers financial benefits.

But on the other side as we have seen in some of the previous questions, it has impact on churn and on the customer experience. So we assess that on a permanent basis and figuring out whether we should stick to leasing or whether at some stage we might open some other ways of device financing. Having in mind that all that is also looked at in the context of what's happening in the marketplace where the lifecycle of devices is extending, so maybe leasing might be less [indiscernible] (40:41) in the long run from a financial point of view.

Michael I. Rollins
Analyst, Citigroup Global Markets, Inc.

Q

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Thank you.

Operator: Next question is from Michael Niknam (sic) [Matt Niknam] (40:50) from Deutsche Bank. Your line is open.

Matthew Niknam
Analyst, Deutsche Bank Securities, Inc.
Q

Hey, guys. It's Matt Niknam from DB. So two questions. One, on the other postpaid devices so non-phone, what do you think is driving the strength here? Is it just a healthier consumer? Is it Sprint maybe promoting these a little more actively? But broadly trying to get a sense of what's driving some of the strength there? And whether you're seeing the benefits in terms of stickier accounts? And then secondly, as you sort of get closer to your Mobile 5G launch first half of this year, any color you can shed on the pricing and go-to-market strategy? Is this a incremental revenue opportunity? Or is this a little bit more of a churn-reducing retention tool? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.
A

On your first question, to be fair, I guess it's purely sales execution and sales focus, meaning that at the end of the day, we have shifted a little bit of focus of our retail, meaning that – and that's part of our strategy, which is let's make sure that we bring additional line on the existing accounts. And there was an opportunity that we had not captured in the past. And even tell you that we are less promotional than we used to be in that field a few years ago. And despite the fact that we are less promotional, we are much more efficient, because all the execution is focused on that.

And on top of that, as you know, we have introduced a new product, which is Sprint Drive. So now we have a portfolio of products from tablets, to watches, to Sprint Drive. So I think that we see there an opportunity. And when I benchmark us with other operators or other competitors, it's clear that we were not at par with our competitors in this area. So that's something which is good. And on top of that it has a similar [ph] ARPU as – ABPU as a phone add a line (42:58) with device cost which is lower, so which means that it has good profitability for Sprint. So from a strategic point of view, it's good profitability, it helps to reduce the churn, and on top of that there is a strong opportunity ahead of us that we have decided to capture. So that's the way I see it.

For 5G, as you can expect, that's commercially sensitive, so I will not unveil any commercial secret there, but [ph] it's subject that (43:31) for us 5G is a way to change the network perception of Sprint, which has been one of our weaknesses in the past. So being in the lead seat to launch 5G will help to change the network perception.

On top of that, of course, it will deliver better experience to the customers, so it might [indiscernible] (43:54) move up our customers to our high-end plans, you know that we have now several levels of plans, and so we expect that we'll be able to push our customers to the high-end plans. And of course, on top of that, I expect that with a better experience, we'll reduce churn as well for our customers. So that's a mix of all of that that we intend to grab from a benefit point of view.

Matthew Niknam
Analyst, Deutsche Bank Securities, Inc.
Q

Thank you.

Operator: The next question is from Simon Flannery from Morgan Stanley. Your line is open.

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Simon Flannery
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you very much. Just coming back to the network, I wonder, Dr. Saw, could you just talk about Massive MIMO and what's the plan for 2019? Is this something that you're going to start putting on thousands of cell sites? Or is it sort of targeted? And then, Michel, any impact from the government shutdown on the timing for the merger decision? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

Dr. Saw first.

John C. B. Saw
Chief Technology Officer, Sprint Corp.

A

Simon, I can go on all day about Massive MIMO. But you are correct. We are very encouraged with the testing results we have seen with Massive MIMO, both with LTE and 5G. So the plan is to, like you say, roll out thousands of Massive MIMO sites. That is our bridge to 5G from LTE.

With the spectrum that we have in the top 100 markets, we are able to simultaneously, over the same Massive MIMO radio, support both LTE and 5G, so it's a very efficient way for us to enhance our LTE coverage experience and add Massive MIMO to the same site, and also offer the same level of coverage, both for LTE and 5G, at the same time.

So with the results we're seeing so far, the plan is to continue moving ahead. We're deploying Massive MIMO, and as we look ahead at the merger scenario, if it's approved, I believe it's also going to be a technology that will be also very helpful for the new company as well.

Simon Flannery
Analyst, Morgan Stanley & Co. LLC

Q

Thank you.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

On your second question, we don't expect the impact of the government shutdown on the timeline. We continue to work through the regulatory process and continue to expect the deal to close in the first half of 2019, as we have always said. The FCC transaction clock resumed on January 29, the day after government reopened, and we look forward to picking up where we left off before the shutdown, so no major impact to be expected.

Simon Flannery
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thank you.

Operator: And your next question is from Amy Yong from Macquarie. Your line is open.

Amy Yong
Analyst, Macquarie Capital (USA), Inc.

Q

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Thanks, and good morning. Maybe two questions if I could squeeze it in. First on prepaid, it seems like there's been a greater focus from your competitors on this market. Can you talk about some of the churn trends this quarter and how you're positioning Boost and Virgin? And then my second question is on your relationship with your cable partners, any meaningful updates? Obviously, you're leveraging that partnership with Altice is pretty well. Do you anticipate any competition from them as they prepare to launch their MVNO? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So on prepaid, we continue to see a strength in Boost offset by losses in other brands that has been deemphasized. So if I look really at Boost which is our major brand in this area, we delivered our eighth consecutive quarter of Boost net adds before migrations.

And Boost gross adds grew year-over-year for the sixth consecutive quarter, so which means that our offers remain appealing and we continue to have a quite, so let's say, a nice [ph] churn rate (47:56) there. Fair to say that we have had some pressure from the competitive environment, which means that the churn as let's say slightly increased year-over-year as the market was extremely competitive. But that's what I can report on prepaid.

Prepaid service revenue grew year-over-year for the fifth consecutive quarter, and excluding new revenue standard, prepaid ARPU remained stable both sequentially and year-over-year. So that's for prepaid.

For your second question, I think that we're continuing to have a good relation with Altice and Cox, as it was reported by Dr. Saw earlier on, that's part of our deployment strategy, and so we have increasing the number of strand mounts sales that has been delivered, and so we have let's say – we are very happy with the agreements that we have with those two cable operators.

Amy Yong
Analyst, Macquarie Capital (USA), Inc.

Q

Great. Thank you.

Operator: Your next question is from David Barden from Bank of America. Your line is open.

Joshua M. Frantz
Analyst, Bank of America Merrill Lynch

Q

Hi, guys. It's Josh Frantz in for Dave. Thanks for taking the question. First, on the migrations, how do you guys qualify the customers? Is it more proactive or is it more of a savings tool? Any more on the process there would be helpful. And then second, quickly on tax season, do you have any plans that we should be thinking about, and do you think the government shutdown is going to really stretch this out more than expected? Thanks.

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

A

So on the migration service program was introduced to reward prepaid customers with access to postpaid financing offers into their respective brands, so that's a specific program which is often for customers which have been with us for more than a year and which have been good payers with Sprint, so which have a profile of a postpaid customer, if I can say so. And so we are offering or we are giving them access to postpaid financing under their brand, so that they can benefit from this type of financing.

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Prepaid to non-Sprint branded postpaid migrations were slightly above 100,000 in fiscal Q3, and we expect migrations to be relatively similar to this quarter going forward. We are of course monitoring the churn of those customers which is very similar to the churn of our postpaid customers.

On your second question, we don't currently expect any delay in tax reform this year.

Joshua M. Frantz
Analyst, Bank of America Merrill Lynch

Q

Got it. Great. Thanks for taking the question.

Jud Henry
Vice President, Corporate Strategy & Head of Investor Relations, Sprint Corp.

And, Bernard, that's all the time we have for questions, everyone. But before we end the call, I'd like to turn the call back to Michel for some closing comments. If you have any additional questions following the call, please contact the Sprint Investor Relations team.

Michel?

Michel Combes
Chief Executive Officer, President & Director, Sprint Corp.

Thanks, Jud. So I want to thank everyone for joining us today and for supporting Sprint. Our third quarter results demonstrate continued execution of our plan to balance customer growth and profitability while improving network performance. We continued to deliver retail net adds for the sixth consecutive quarter. We improved profitability, delivering operating income for 12 consecutive quarters, with our highest third quarter adjusted EBITDA in 12 years.

In addition, we are aggressively executing our Next-Gen Network deployment to deliver a Network Built for Unlimited with building the foundation for our Mobile 5G network that will launch commercially in the coming months. We continue to enhance our value proposition and continue to transform our cost structure and customer experience with digital, artificial intelligence, advanced analytics and automation.

Thank you, and have all a very great day.

Operator: Ladies and gentlemen, this concludes today's conference call. You may now disconnect. Thank you.

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