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PRESENTATION

Brett Feldman - *Deutsche Bank - Analyst*

I would like to welcome everybody to Deutsche Bank's 20th annual media and telecom conference. For those of you who haven't met me, I'm Brett Feldman. I'm the firm's US telecom services analyst. My co-hosts this week are Doug Mitchelson, he's our cable satellite and media analyst; and Matt Chesler, who follows advertising agencies and measurement companies here for Deutsche Bank.

So on behalf of Deutsche Bank's media and telecom equity research and banking teams, we'd like to welcome all of our clients, the presenting companies and everyone here who is on the webcast.

We're very excited this morning to open up our session with Verizon Communications and to welcome back to the conference Fran Shammo who is the Chief Financial Officer of the Company. So, Fran, you've been a big supporter of the conference. We're happy to have you back this year.

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Thanks, Brett, thanks for having me. Good morning, everyone.

Brett Feldman - *Deutsche Bank - Analyst*

This is going to be essentially a fireside chat/Q&A format. It's going to be the way we'll be doing most of the sessions. Some of you may have also downloaded an application when you checked in called the Yorn. I have an iPad up here. If you actually downloaded that, you'll be able to send questions directly to me during the session and I'll be keeping an eye on that.

I'm going to start off with a series of questions here for Fran, and then we're going to go to an open Q&A session towards the tail end. So, Fran, just to get things started a little bit here, I want to go back to something you talked about on the conference call. You alluded to the fact that the last 10 years had really been an investment period for Verizon.

Could you maybe just recap for everyone here in the room what it was you were investing in, the platform that you put in place, and then more importantly what your investors should expect out of the Company going forward in light of the investments you've made?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. So, I think if you put it into perspective, the last 10 years we repositioned the portfolio, divesting some of the access lines, bringing in some of the other platforms that we have. So let's first start with wireless. Obviously we've invested heavily into our wireless asset. We now announced the purchase of our spectrum from SpectrumCo, which we plan to get approved by midsummer.

That will bring in the spectrum that we need to really be the foundation of the 4G LTE network, which we really have built our future around with wireless, and we can talk more about that.



Then from a wireline perspective, obviously we've invested very heavily in the last five years into FiOS. That investment is starting to trim back. I think we're in a very good position with that platform as we continue to penetrate the market.

We think that we have a premier product with all-fiber that quite honestly we don't think anyone can match at this point. And so we're taking market share there.

And then when you look at the platforms of cloud, security, and then you think about mobility and how that comes together, we bought the Terremark asset and now we're executing on that cloud strategy.

And then if you just take it one step further and you think about the convergence of cloud and mobility and you bring all those platforms together, the one that we've been developing for the last 18 months is our Verizon digital media services platform, which is really a content delivery platform with our backbone, and we've invested in that.

So I think right now, I would say that we have our four key platforms that we'll continue to maintain, but these will be the growth engines of the future. So you won't see us really launching into some new venture at this point, investing another \$23 billion into a FiOS platform.

So when I said last 10 years have been a repositioning of the portfolio, very heavy investment, I think we are now to a point where we need to take these assets, put them together and execute on what we have. And that is the position we're in right now.

Brett Feldman - Deutsche Bank - Analyst

Great. So let's talk about one of those areas you're going to be focusing on, and very important for the Company is wireless. And the topic that everyone wants to talk about is margins. We obviously saw your margins take a step backwards in the fourth quarter as most of the carriers and industry did with the launch of the iPhone.

Could you maybe just sort of sketch out for us what the Company's strategy is for growing margins going forward, even in a period where you're still ramping your smartphone sales?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes. So I think if we go back to January of 2011 when we first launched the iPhone into our portfolio, I stood up and I said that wireless would end the year in the mid-40% margins, and that during the year we would be up and down depending upon when the launch of a new phone came. And I think we delivered on that. We delivered -- we ended the year at around 44.7% margins for the year. So we were right where we expected to be.

Now in the third quarter if you look at it, even with an iPhone we generated a record 47.8% margin for the quarter. And I think the resounding piece here is as we go into this year, you should expect us to get back to that level of profitability because in the last two years we've cut about \$3 billion worth of expense from the wireless side of the house. We have another \$2 billion on the table this year as a stretch target for them to deliver again.

There is a lot of efficiency that we can build into our wireless asset to offset some of these other subsidy issues, upgrade issues. So I think it's a balance, and I think that Verizon wireless has shown that they can grow and be profitable at the same time. And I think we showed that in the third quarter. So now coming into this year, you should expect that to be a more consistent type margin improvement.



Brett Feldman - *Deutsche Bank - Analyst*

I think it's pretty easy to see the way you guys have taken cost out of the business is something that we haven't necessarily seen at other carriers. Are there other things that you're going to try to achieve over the course of the year, whether its mix of handsets maybe balancing the iPhone versus LTE devices, potentially changes in pricing for services, changes in upgrade policies?

Are there other tools that you guys have that are going to be essential to kind of getting your margins up as you're trying to do and, therefore, get to maybe the upper end of your earnings guidance?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Well, a couple of things. Back in 2010, we did actually change our upgrade policy. We stopped early upgrades. We did away with the new every two that we had out there for a long time, which was every two years when you upgraded you got a \$100 credit. That went away in 2010. Now as we worked through the base in 2011, people were grandfathered onto that. So as they upgraded, we honored that, but now they will not get it again.

So as we go into the future, that in itself is several hundred million dollars worth of savings as we go. So we've put very strict rules in for upgrade policy.

The second thing is as we launched LTE, and if you think about we only did this back in the fourth quarter of 2010. And as we build out, now we cover almost 200 million POPs, we have now 20 devices on that ecosystem. So there were a lot of naysayers back when we launched this that said, oh, people are not going to develop the devices that go on that network. And here we sit today, we have over 20.

And I think as you saw us through the third quarter and into the fourth quarter, the percentage of our mix started to shift more to 4G LTE devices and you should expect to see that going forward. Now you've seen us do some things around 4G LTE where we did promos on Double Your Data, and we just announced that again for the first quarter because the results we saw in the fourth quarter actually did what we wanted.

We also have done some things around handset pricing on 4G LTE to entice people to take a harder look at that handset and move. And I think you'll see some of that trend continue here as we go throughout the year. So it's a balancing act in the portfolio, and again the Apple phone is one phone within our portfolio. It's an important part of our portfolio, but it's not the only thing that we have.

And now we have this big ecosystem of 4G LTE, which is quite honestly very important to us from a cost efficiency as well. So the more people we put on that, the better for us and quite honestly better for the consumer, because it's a faster network and there's a lot more innovation coming on that network.

Brett Feldman - *Deutsche Bank - Analyst*

And are your subsidies on the LTE devices on average lower than what you're incurring on the iPhone, for example? Is it a meaningful help if you can get your customers to shift over to those devices?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

When we look at -- when we do an analysis on a handset, we take each individual handset on its own basis and do an NPV on a customer value. So every handset is different, but generally because of the efficiency of the LTE network, we want to put more people on that network.



Brett Feldman - *Deutsche Bank - Analyst*

And as handset prices come down, what are you going to do about that in terms of pricing your product? Will you just lower the entry price of the handset itself? In other words, will you pass savings through to customers or is a reduction in handset prices on your end going to be a tool for expanding margins?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Well, I think it's both. I mean, look, this industry grew up from the very start in subsidizing handsets, and we've done that for the past 15 years. So this is not something new for us. And as the cost of handsets come down, then obviously the profitability of that handset gets better for us because all of that subsidy is not absorbed to the consumer.

So I think you have to look at each handset individually. And over time as smartphone handsets come down, which they will, the profitability of the industry will grow.

Brett Feldman - *Deutsche Bank - Analyst*

Let's talk a little bit about pricing. You alluded to the promotion that you're running on LTE. You've historically priced at a premium, and your baseline pricing for data is still at a premium. It's just you have this sort of temporary promotional period where actually you are the best deal in town for data.

How long do you intend to run these promotions for? And is it still your long-term strategy to be the premium price point in the market for wireless broadband services?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. Well, I think we built our brand on having the most reliable, best network in the world, and there's no difference for us for 4G. I mean we're way ahead of our competitors in 4G. We think that we can continue to have that premium based on our reliability and our speeds of the 4G LTE network.

We instituted the tiers because as we looked at future, albeit we believe that as people get onto the 4G network the usage will go up and, therefore, then they will buy up in tiers. And we've already seen that with our Jetpacks, which is the new brand name for our air cards or our dongles, if you will. But with Jetpacks we see people buying up into the higher tiers because with the speed that they can get over the Internet, their consumption is more.

So we're starting to see a little bit of that, but I think that's going to be another two to three years before you really start to see the accretion come through from the usage on 4G LTE.

Brett Feldman - *Deutsche Bank - Analyst*

But I guess the logic behind the Double Your Data promotion is that you didn't want to put any more pressure on your 3G network, because the iPhone was sort of the premier 3G device that you were selling. And the LTE network because it's so new has a lot of spare capacity in it, so it's a good time to go and do that.

I guess the idea is for how long can you continue to price so attractively before maybe your 4G network starts getting a little bit congested, and you have to go back more to baseline pricing?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes. Well, the 4G network has a ton of capacity. Obviously, we only have 5% of our customers on it right now. So it's a promotion to get people to move over to that 4G network. Like you said, Brett, it is very critical for us and we're playing a very delicate balancing act here that I don't want to spend any more money on my 3G network.

So we built the 3G network out to handle the iPhone launch, which we did very successfully, but now we really do want to keep that investment to a very, very minimum. Because based on my projections for every dollar I invest in that now, I will never get that dollar in return. So it's very important for us to move over.

And as far as maintaining these promotional periods, this promotion is only running for I think two months and then we'll come off of that promotion. There will be more 4G LTE phones out there, so you're going to see us -- we will do promotions here and there, but it's more critical for us from a cost benefit perspective, spectrum utilization perspective, to move more people to 4G from 3G.

Brett Feldman - Deutsche Bank - Analyst

Because if I think about it, why not continue to run these promos for an extended period of time? I mean, if you don't have a network congestion problem and it gives you a clear price advantage in the market, I mean you can really sort of just jab at your competitors who are trying a more gradual transition to LTE by just constantly undercutting them on price and still delivering higher-quality.

I mean to me it sounds like you can maybe stick with this promotion on and off for an extended period of time and have an advantage, or am I hearing that incorrectly?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Are you my marketing person now? So, look, we came out of the fourth quarter; it was a very successful promotion. There were some pricing changes in the markets and we felt we needed to address that, so we put the promotion back in. So it depends what the competition does where we'll insert the promo, where we won't insert the promo. But look, I mean we've got the promo now. We'll see what the marketing folks do in the future.

Brett Feldman - Deutsche Bank - Analyst

Okay. One of the things I think that was sort of brought up on the call and I think it's an interesting idea is sort of the seasonality of the iPhone. And is it purely a seasonal device or are you starting to see there is a longer tail to the demand cycle? You know, you had such a strong reception to the iPhone launch in the fourth quarter. There's been a lot of questioning whether that has extended well into the first quarter.

Can you give us any color as to how investors should think about the trends we should anticipate out of your business in the first quarter just from an overall success standpoint and maybe if even from a mix standpoint, we can think about margins?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes. So again, I think that from a mix standpoint you should envision that our mix of 4G LTE will continue to increase. I think it's also important to note than on the iPhone, 20% of these customers that bought an iPhone were new to Verizon, and 40% of them were new to that category. So as we continue to sell that device, we're bumping people up in revenue category from a basic phone to smartphone. So that all attributes to revenue accretion.

So I think if you looked at the third quarter to the fourth quarter where you started to see our revenue starting to accrete the way that everybody predicted that it would, and there's no reason to doubt that that won't continue into the first, second and third quarter of this year.



I think we are in a very good trend. We ended the year at 2.4% ARPU growth and 4% in phone ARPU growth, and you should see that continue to trend upward in the first quarter.

Now from an overall growth perspective, I think we've got to keep in mind we just came off a very strong fourth quarter with a new iPhone being launched. And if you look at the year ago, it was the first quarter where I launched an iPhone. So I think from a growth perspective, you should probably envision that growth won't be as strong as a year ago because of the iPhone launch.

Brett Feldman - *Deutsche Bank - Analyst*

Net adds you're saying?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

So -- net adds as far as a year ago. So I think you've got to reposition what does the industry look like going forward without a new iconic device hitting the marketplace. So from a wireless perspective, you should count on us improving the margin back to where a third-quarter margin would have been.

Brett Feldman - *Deutsche Bank - Analyst*

Got it. So we've got a strong margin quarter, a reset on the net adds, and it sounds like continued acceleration in ARPU as you started the year.

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Correct.

Brett Feldman - *Deutsche Bank - Analyst*

Is it going to be phone ARPU and total ARPU; they're both moving up at the same trend line?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes, an acceleration of all, including service revenue growth.

Brett Feldman - *Deutsche Bank - Analyst*

Okay. Sticking around the idea of pricing, one of the things that you have alluded to is the possibility of doing family or share plans for data. This is something you obviously did with great success with voice several years ago. Could you give us an update on where you are in that process?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. So we've been studying this for about a year now, and this is very important to us and it's also very important to our customers. Because as you think about data sharing, you have enterprise customers; you have family who have a number of devices in their portfolio where they would just want to pay a price and share the data instead of buying an individual data plan for each phone.

So as we go through this -- I'm not going to disclose exactly what we're looking at, but this is a very complex equation because we have to make sure that it's good for Verizon and it's also good for our customer.

Now it's also important to realize that the day we launch this account billing, everybody won't be migrating to the account billing day one. This is going to be a long-term migration into where we want to get data plan sharing, but this will be more of a 4G play for us and I think it will be critical for us. And you'll see something launched -- even Lowell alluded to it -- you'll see something launched midyear this year from us.

Brett Feldman - *Deutsche Bank - Analyst*

So what is the ultimate objective of having a share plan? With voice it was really about driving higher penetration of wireless services, getting the extra family member, the kid, the mother-in-law who is living with the family who didn't have the device. A lot of people have the devices now. So what are you ultimately trying to create by creating a share platform for data?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Well, if you think about -- okay, so let's just take a household. So you have a family; they have tablets; they have notebooks; they have their smartphones. Then you have to start thinking about then you have a washer and dryer, you have a refrigerator, and people are going to want to start to communicate with all of those devices.

So when you think about connecting the devices to the network, it's more than just a smartphone and a tablet. It's more around everything that happens in our daily lives. So when you talk about data sharing, you talk about having the ability to connect more devices without having to in essence pay more for a bundle.

Brett Feldman - *Deutsche Bank - Analyst*

Because what we saw with voice was that the movement to family share really reaccelerated the net adds. But we had to moderate our assumptions on ARPU because the incremental device came in \$15, \$20, in some cases \$10. Is that going to be the same dynamic we should expect with data, or is it a different approach to what you're trying to do here?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

I would say it is a very different approach and, of course, the thing that we have been analyzing so much recently is the fact that when we do this, we don't want to see any dilution in our portfolio. So what we are looking at is the way you should think about it is this will be over time accretive to us. And again, it won't be a mass conversion into this. It's going to take some time to convert people over.

But the fact is is that we need to give the consumers the ability to add devices as innovation continues on 4G LTE. So if you think about everything that has happened since this platform has been launched, and just within the medical industry and the energy and transportation, there are more and more devices coming on the market that will ride on this network.

So we need to give the people ability to connect as many as they want. So it's not going to be all about a net add. It's more about revenue growth from the devices that are put onto the network.

Brett Feldman - *Deutsche Bank - Analyst*

I was going to sort of switch gears here and we'll talk a bit more about those data devices. And I think you actually did your last conference call from your innovation center which we did a tour of over the summer. You are starting to see some more traction here with data-only devices being



a meaningful contributor to your net adds. Can you talk a little bit more about what your strategy is here for getting more of those devices on the network?

And also maybe talk a bit about the economic model. You know, when you sell a smartphone you have to incur very high acquisition costs. Are you looking at a different structure around data devices where maybe there is no acquisition cost and a different revenue profile? Something to help us understand how you're going to drive revenue and margins off of your data network.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Well, I mean without giving too much disclosure to my competition as to what we're going to do from a pricing perspective. I think the way we look at this is, look, I mean if we could drive the industry to a no subsidy perspective, that would be great. I think we've shown we can do that with tablets. We don't subsidize tablets unless you buy a two-year contract and there's a slight subsidy, but nothing near compared to where we were with smartphones. And certain tablets we don't subsidize at all. So I think we start there.

And then if you look at the Jetpack, what you should anticipate is that is another area where I don't think we need to subsidize those devices. And then when you get into machine to machine, obviously there should be no subsidy on those devices. So I think as you bring in some of these other technologies, the carriers will move away from that subsidy model on these other things.

Brett Feldman - Deutsche Bank - Analyst

Are we getting closer to a point where this could become the large majority of your customer growth going forward?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Well, sure. I think that as I said, I think tablets; I don't think we've seen yet how that's going to dynamically change the way people work. If you think about enterprise, you think about college students and how they carry that around. I think we're at the beginning stages of how a transition, if you will, from like a mainframe to a PC and now you're going from a PC to a tablet, I think you're going to see that carry through the marketplace with very strong growth in the future for the industry.

And then I think that the whole machine-to-machine perspective and all these devices that are coming to market, especially across the industry around like I said healthcare and home monitoring systems. So there is so much growth opportunity in this industry from an innovation perspective. That's where you're going to see the growth from.

Brett Feldman - Deutsche Bank - Analyst

It's a lot of fun to talk about the type of growth you're going to achieve from these new data plans, and I think a lot of people realize that your network, your LTE network, is a great platform for that. The reality is right now, a lot of your data profitability comes from pretty old stuff like SMS.

And we've been getting questions increasingly from investors, how much should we worry about the inevitable decline of the SMS business, particularly as people move to messaging applications? Should we just assume that SMS inevitably does go away sort of like long distance did? And if it does, what is your strategy for managing that and ultimately replacing it over time?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Well, I think -- the way I think of this is you'll see bundles. So instead of just looking at SMS on an individual basis, voice on an individual basis, data on an individual basis, you're going to see more bundles across the horizon here. And look, SMS, we still continue to have growth. 90% plus of our customers still take a bundle today of SMS.



So this is not a huge issue for the US carriers at this point. It's more of an issue for the European carriers. But look, we're watching it very closely; it's coming. But I think the way you should think about this is really the way that we thought about long distance, which is you create bundles and you price in the price of that bundle. And you're going to maintain your ARPU from a bundle, not necessarily individual components.

Brett Feldman - Deutsche Bank - Analyst

Okay. I'm going to shift back to something you were talking about early about investing in the Company, and you mentioned the SpectrumCo deal. Could you give us an update on where you are in terms of getting the SpectrumCo and the Cox transactions through the FCC, the expected timelines for getting approvals, for example?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes, I think it's important to note these are two very separate distinct agreements. One is the purchase of the spectrum. That is sitting in front of the FCC now; it's on a 180-day clock. We see no issue with them closing this out by midsummer. And it's exactly where we expect it to be. We knew who was going to oppose it, no surprise there. So we're exactly where we thought we would be and we're expecting this to come to closure by midsummer.

On the commercial agreements, we're cooperating with the Department of Justice and taking them through the agreements. There is angst around the competitive nature of those agreements, but as I continue to say we will compete in the FiOS footprint vigorously. I have a superior product. and the real advantage of this agreement is to bring the innovation to the marketplace that we could not do on an individual basis.

And that innovation will be given to FiOS, will be given to the cable competitors, and we'll compete with that innovation. But let's not stop the innovation to the consumer based on this out of footprint issue. We will continue to compete. So we're exactly where we thought we would be and we'll see where we end up there.

Brett Feldman - Deutsche Bank - Analyst

Are any of these deals tied together? I know they're separate transactions, but can you be flexible in terms of dealing with the regulators, that they have different levels of reservations about the spectrum deal versus say the joint marketing agreement?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

These are two very distinct separate agreements. One is not tied to the other.

Brett Feldman - Deutsche Bank - Analyst

So you could still move ahead with the spectrum deal even if you modified the joint marketing agreements.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

That's correct.



Brett Feldman - *Deutsche Bank - Analyst*

Okay, good. Speaking about other joint ventures, you recently entered into one with Redbox. And you alluded to the content delivery platform, the video delivery platform you've been investing in. Could you maybe give us a better feel here for what the Company's content strategy is? Because it seems like it's starting to take a little bit more form with this joint venture.

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. So, as I said, about 18 months ago we started an internal development project which was the Verizon Digital Media Services, which was really constructing an efficient platform that could take content in from large content providers, redigitalize that, reformat that, to be able to be delivered to ultimately anywhere in the world on any device.

And I think that we have successfully done that. We've launched a commercial launch here in the fourth quarter. We actually started to generate a little bit of a revenue from our charter customers on them processing content through that platform. By doing that, though, we've created a very efficient model for us to be able to deliver that content.

So it was just a natural step then to go into the, if you will, over-the-top model. And we looked at a number of different partners and we felt that Coinstar and Redbox fit naturally within what we wanted. They brought something to the table that we didn't have and we brought something to the table that they didn't have.

So they have 30 million customers. They have something like 35,000 customers a day that visit their Redbox terminals in stores, so they have a very strong following. And now this is a way for us to really utilize our strength in the FiOS content that we have, bring something to the table in a bundle with Redbox, and then give that as an over-the-top play to their consumer.

So we think this is very strong for us. This is going to be, we believe, a very good growth engine for us, the wireline business in the future, and it should be a very good partnership. So we'll see where that goes and we'll commercially launch that in August.

But this is a fundamental way for us to enter the market and as I've said, this is really an offensive play but maybe also a defensive play at the same time.

Brett Feldman - *Deutsche Bank - Analyst*

Can you maybe just expand a bit more around like a bigger picture how you're thinking about content in light of the fact that you have this -- you have residential broadband content delivery platform in FiOS. You have what's almost -- is going to eventually be a nationwide content delivery platform on the wireless side through LTE.

Are you trying to create a more unified approach to buying and distributing content across all of the Verizon platforms? And is this Redbox JV sort of the first step in that direction? I guess I'm trying to understand the extent to which your various business units can create some synergy in the way they're interacting with content.

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. Well, of course, I mean obviously when we first entered into the FiOS arena and we were last to market, obviously the content providers made us pay a premium price for that. And as now as we have built FiOS up to exceed some other carriers -- we're now I think number 5 in the nation on number of subs as far as a linear TV goes -- then you bring in the 100 million eyeballs from wireless.

Now you bring in over-the-top play from Redbox. We are starting to see some major discussions with content providers on cost synergy. So exactly to your point, Brett, we're looking at this as a content play for all of our platforms, not just for one.



Brett Feldman - Deutsche Bank - Analyst

And are you going to be able to leverage what you're doing with Redbox into Verizon Wireless? Is that part of the original agreement or is that something you could expand upon over time?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

No, Redbox is just a joint venture with the wireline unit. Wireless is not involved.

Brett Feldman - Deutsche Bank - Analyst

And that's going to be reported within your consumer segment, I assume?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

That's correct.

Brett Feldman - Deutsche Bank - Analyst

Okay. Speaking about wireline, there's a lot of focus on wireline margins as well. Could you maybe sort of walk us through what the key levers are that you guys can work with here to grow the margins in the wireline business?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Well, I think you heard me talk about this a little bit on the fourth-quarter call. But we have a very renewed strategic strategy here that says that we need to take our copper chronic problem customers and move them over to FiOS. And this is going to be a very strategic initiative for us, but it's probably going to be -- there's going to be a little lumpiness in the wireline margins as we do this.

So my effort right now is to go as fast as we can in the beginning of the year because the payback is six months. So if you think about a chronic customer, if I have to do a truck roll to that chronic customer two times in six months, it costs me on average about \$900 in cash all-in to service that customer. If I just go and connect up to FiOS, which is now around \$700, I immediately get a payback within six months.

So we are going to significantly shift chronic copper problems onto the FiOS network. And by doing that, we get an immediate cash benefit but we also get a cost reduction, because the maintenance of our FiOS network is much different than the maintenance on the copper network. So by doing this, we believe that over the next two to three years you will really start to see some cost synergy benefit in the wireline unit.

Brett Feldman - Deutsche Bank - Analyst

And do you think we can see -- this year you said in your call you're very confident you're going to be able to expand your wireline margins this year.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes, and when I say that I mean when you look at it an annual year over an annual year, we will accrete our margins.



Brett Feldman - *Deutsche Bank - Analyst*

But probably in the front end of the year they could compress a little. I mean, seasonality alone usually starts you off a little bit lower. You're going to be ramping up this project. Is that kind of the right way to think about margins over the course of the year?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Correct, that is absolutely correct.

Brett Feldman - *Deutsche Bank - Analyst*

How about on the top line for wireline? We ask you this question every year about the economy. Are you getting help from the economy? How do we think about the impact the economy is having on your business right now?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Well, I think you have to split it. If you look at the consumer segment, I would say absolutely no impact at all. I mean FiOS is growing; it's now 61% of the portfolio. Our access line loss is decreasing because we're doing a much better job in converting those copper access lines over to FiOS access lines. So I think that portfolio itself is good. It's growing at 1% plus year over year. So I think we're in good shape there.

When you get down into the small business, I think this an area where quite honestly we have not executed as well as we could. And we have felt a lot of pressure from the economic condition and some other issues that we have in that small business unit where we have felt more pain in that area than probably most, and we need to improve that. I think you saw a little bit of improvement in the fourth quarter, but we have a long way to go here.

And then when you think about enterprise, I would say it is stable. I wouldn't say that it is causing a problem in a downward pressure wise, but I don't see us having any type of a lift from the economic improvement either. So I think right now, we're stable.

And with our Terremark asset and security asset, you saw it in the fourth quarter. We posted \$111 million from that asset. It's growing at almost 30% year over year now, so I think we're doing all the right things for that asset to be the acceleration of our enterprise business.

Brett Feldman - *Deutsche Bank - Analyst*

So it sounds like absent a change in the economic environment, it's very modest growth, I guess, is sort of what you're looking at here; return to growth in the wireline business. So no real inflection, kind of steady as she goes in the top line; is that the right takeaway?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

I would say that if you take apart the wireline unit, I think what you'll see is you'll see growth in all items except for wholesale. And wholesale will continue to be at a decrease of 7% to 8% year over year.

Brett Feldman - *Deutsche Bank - Analyst*

And this is partly because of the price and the adjustments you've made in that segment, right?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Pricing adjustments and just the mere fact that the core voice is going away. People are flipping over to more data. And as we do that conversion, there is not yet enough to offset one from the other.

Brett Feldman - Deutsche Bank - Analyst

So within that type of top-line trend, it sounds like the real margin mover to get back to your previous point is continuing to groom the residential network, pulling copper out, moving over to fiber and getting the efficiencies associated with that. Is that the right way to think about this?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

That's correct, Brett.

Brett Feldman - Deutsche Bank - Analyst

And then where are you with the unions right now? It seems like that's another opportunity to maybe kind of right size the cost structure of the business. What should we expect with these discussions?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Well, I think we've been pretty clear on this one. We need cost restructure with the contract. Benefits and pension are the big issues on the table. We continue to negotiate, and there's really nothing more to report at this point in time. We continue to negotiate and when we're done, I'll let you know.

Brett Feldman - Deutsche Bank - Analyst

Any targeted timeline here?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

I have no targeted timeline.

Brett Feldman - Deutsche Bank - Analyst

Okay. We have about 10 minutes left. I think what I'll do is I'll pause. If anybody has a question, we can bring microphones around. So you can go ahead and raise your hand and they can bring it over to you, or we can just continue up here.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Nobody is using your app.

Brett Feldman - Deutsche Bank - Analyst

We haven't gotten a Yorn question yet. If you have the Yorn app, you can also send a question up here and I'll be able to read it anonymously.



Okay, well, I'll move on then. Let's talk a little bit about capital spending. It sounded like you expect capital intensity to be a bit lower this year; essentially sort of a flat overall capital spend for the Company. Revenues are growing and so the intensity is decreasing.

Could you just walk us through a little bit about wireless versus wireline this year, and then we'll come back with a couple follow-ups on that?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes. So I think if you look at wireless, obviously last year we spent a little bit more because of the 3G buildout. So I would anticipate that they will be flat to downish, to be honest, from a 3G perspective. So we'll save a little bit of money not investing as much in 3G capacity.

Brett Feldman - Deutsche Bank - Analyst

So overall, wireless CapEx will be flat or down, you're saying?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Flat to slightly down. And then everything else will be pretty much flat, so flat overall for the corporation. And look, I mean, we are extremely disciplined this year on where we are investing our capital. And obviously it's more focused, as I said, around the platforms. So that's really where we're concentrating on. So I would think flat, but I would say that by doing that, our CapEx to revenue ratio will continue to improve quarter over quarter.

Brett Feldman - Deutsche Bank - Analyst

It's not usual to see Verizon Wireless's CapEx go down. And if you think about it, if it's flat or down this year, as you move into next year and you're even further into the LTE upgrade, are we going to see absolute declines in wireless CapEx going forward?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Now you're trying to get me to give guidance. I'm not going to give guidance. I'll say flat, how's that?

Brett Feldman - Deutsche Bank - Analyst

Flat. So the intensity level should continue to compress and we'll just sort of say flat for the capital spend right now.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

There you go.

Brett Feldman - Deutsche Bank - Analyst

Okay, what about on the wireline side? I mean, you have essentially got FiOS most places you want it. You're going to be going through this grooming process pulling out the copper. Are we going to get to a point in the next couple years where wireline capital intensity could actually take another step down?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes, I think that the right way to look at this is we have a commitment to fulfill LFAs. We said that we would pass 18 million homes. Now 18 million homes in the original estimate, the way you count houses and households, it could actually end up being 20 million, but it's the same amount of money as 18 million. So we've committed to pass that, and it will take us another two years to complete that build and then you should see a stepdown function. That's the way I look at it.

Brett Feldman - Deutsche Bank - Analyst

And I guess at that point, the only thing that might drive capital higher would be if the economy comes back and you start making more investments in the business side; is that probably the right way to think about it?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes. I think the other thing that you have to look at is that there is an awful lot of demand out there for more Ethernet. So the -- and this is from an enterprise perspective but also from a backbone perspective. And do we invest more within the next two to three years more on the Ethernet because of the capacity that people want.

And especially when you think about the 100G, and we were the first ones to launch 100G over in Europe and we tested that, we will be launching that throughout the United States over the next two years. But again, overall flat capital, but there may be different pockets where you see us invest more than others and that's how we'll approach it.

Brett Feldman - Deutsche Bank - Analyst

Okay, so going back to the wireless side if we think about what you said, you've got continued growth in your wireless business. You have a plan in place to start growing margins again, and capital intensity is declining. That all says that cash flow is going to continue to inflate.

You just paid your dividends out of wireless to the parent companies. I'll probably kick off the annual process of pestering you here about the wireless dividend, but let me frame it a little differently. You've said in the past that one of the key reasons you like to keep cash in the business is the potential to buy spectrum.

You have a major spectrum deal pending right now. You have a lot of confidence that's going to close by the summer. We could go into next year where conceivably, you wouldn't have an opportunity to buy spectrum for years. Your cash flow is growing. Is that a good time to start rethinking at a board level around how you manage the cash that's coming out of Verizon Wireless?

And I guess the question would be, how would you think about it at that point in time? Is that the time to start sending more of it back up to the parent? And if you did, what would you do with it?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Yes, I couldn't get away from this conference without answering a question on Verizon Wireless dividends. But okay. Look, I think Lowell and I have always said we will be prudent with the cash. I am not going to let cash buildup in wireless for the sake of having it build up. So let's go through this year and see where we're at.

I mean we've got a spectrum deal coming up. We've got some debt repayments that are due on the wireless side. As I said before, I'm going to continue to pay down that debt when it matures. There is no reason to have debt on the Verizon Wireless books. So we'll continue there and we'll see where we end up this year, and we'll see what happens.



Brett Feldman - *Deutsche Bank - Analyst*

I'm going to try to bring us back a little bit to what we started off with, talking about what your shareholders should be expecting from the Company going forward. If you are generating all of this cash and you are through your peak investment period, you know, you already have a very high dividend.

So has the board begun to give some preliminary thoughts around how you might augment capital returns to shareholders with any excess cash the Company generates? For example, would you actually accelerate the rate that you would start raising the dividends, or might you start revisiting share repurchases? I think conceptually, how do you think about the most logical use of free cash when you get to the point where you have it?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Yes. So I think there's a couple levers here. One is obviously our dividend policy is very important to us. Share repurchase, we have talked about it. It's probably not going to happen this year. We may bring that to the table in 2013 or 2014, but probably not in 2012. We still have some delevering that we would like to do within our portfolio.

So there's a lot of different angles here from a cash perspective. But obviously, the dividend policy is extremely important and share repurchase is not off the table, probably a year to two out.

Brett Feldman - *Deutsche Bank - Analyst*

And thinking about Vodafone and the relationship you have with them, what is the status? You know, we always heard year after year that it was the Company's desire if able to buy out Vodafone. Is that still technically what you would like, to take 100% ownership of the wireless business? Do you have any visibility around being able to do that? And in the meantime, what is your relationship with Vodafone like?

Fran Shammo - *Verizon Communications Inc. - EVP & CFO*

Well, I mean, look, I mean we've made a lot of strides. Lowell has a very good relationship with Vittorio. I mean we've made a lots of strides in the strategic side of the partnership in working through the enterprise space and doing some purchasing activity; coordination on handset purchases and working with vendors, especially around the consistency of our LTE technology. They just launched Germany.

So there's a lot of cooperation going on. I think all the other discussion is just discussion at this point. Look, at the end of the day I think we've been very clear; we would love to own 100% of our wireless asset. If that happens, it happens. If it doesn't, we are fine continuing to execute the way we are.

Brett Feldman - *Deutsche Bank - Analyst*

I'll do one last chance if anybody in the audience here has a question. All right. Well, I'll ask a final one here thinking about strategy. We have constant headlines these days around potential deals that might be happening, particularly in the wireless space. You guys have fortunately stayed away from a lot of those headlines. You've talked about the last decade and the investments you've made building up the Company to what you want it to be.

How do we think about your M&A strategy right now? Is there an asset hole that you guys are still looking to fill? And if you did see a major transaction in the space, maybe something between AT&T and DISH, which has been reported about, does that change your view on what type of assets you need to own?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

No, it really doesn't. I mean as I said back from the very beginning of starting this discussion, I think we have the asset portfolio and one of the best in the world, and all we need to do is bring that together. I mean if you think about our wireless asset, the cloud, the security, our FiOS asset, I think we have the assets we need to execute on and grow the Company. And that's really what we're focused on is executing on what we have and generating growth from the portfolio, and I think we will do that.

I mean, we said that from January of 2011. I think we proved that in 2011 that we could do that. And I think 2012 will actually be a higher growth year for us than 2011 was. So I think we're executing well. Now, look, I mean we're always looking at things.

And as I said, is there certain little things that we would like to have? Probably. And if they're the right asset at the right price, we might buy it. But these are assets that are \$20 million, \$30 million buys. These are not \$1 billion buys. So at this point, focus on what we have and execute.

Brett Feldman - Deutsche Bank - Analyst

And just to follow up here. Just because it's been reported so much about AT&T and maybe having an interest in DISH, the theory there is that they would want DISH's spectrum. But if they did that transaction, they would end up with a DBS asset. If AT&T got into the DBS business, does that change your view as to whether Verizon should be in that business?

Fran Shammo - Verizon Communications Inc. - EVP & CFO

No, I don't think it does at all. I think I would lean towards that's what SpectrumCo and the commercial agreements were all about. So I think we're in a great position right now.

Brett Feldman - Deutsche Bank - Analyst

Great. Well, I think we've just run out of our time. Fran, thank you very much for joining us.

Fran Shammo - Verizon Communications Inc. - EVP & CFO

Brett, thank you so much. Thank you, everyone.

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