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# EDITED TRANSCRIPT

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## CORPORATE PARTICIPANTS

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

## CONFERENCE CALL PARTICIPANTS

**Mike McCormack** *Nomura Securities - Analyst*

## PRESENTATION

**Mike McCormack** - *Nomura Securities - Analyst*

Thanks, everyone. We are going to get started. This morning, we are very happy to have Fran Shammo, Executive Vice President and Chief Financial Officer of Verizon with us. We are going to do the standard format. There are also probably some cards floating around the room, so if you want to write down questions instead of use the mic, we can pass those forward. And I can ask those questions at the end of my question period. There also will be a roaming mic at some point, sort of roughly a half hour into the discussion and just raise your hand and we can get that mic over to you. So Fran, thanks for joining us.

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

Yes, good morning, everyone. Thanks, Mike.

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**Mike McCormack** - *Nomura Securities - Analyst*

I think we will just start with the obvious question that people have been talking about and frankly over the past week or so, it has been less talked about, but thinking about the Vodafone relationship and maybe we will change the discussion a little bit and put it in your court to say how important is it to resolve this? So obviously we have all written notes about the accretive benefits of it at certain valuation levels, but does it really matter to you?

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

That is an interesting question. That was very well formatted, Mike. Look, I think it is pretty evident that we have been pretty clear that we want to own the 45%. So for us to say that, I think that means that it is pretty important for us to have that happen, but obviously right now there is really nothing else to talk about and this has been going on for 12 years. So we will ultimately see where it ends up, but we continue to run the business and we control the enterprise and we will continue to operate the venture.

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**Mike McCormack** - *Nomura Securities - Analyst*

So thinking about -- you discussed a lean year for Verizon Wireless dividend distributions. Should we be thinking about this along the lines of wireline generates a certain amount of cash flow. There is a certain amount of cash that is required on the balance sheet to run the business and the balance, what is required to pay the corporate dividend, will be sort of the usual distribution?

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

Well, I think you have to look at it this way. The two really are independent of one another. So from Verizon Wireless's perspective, what Lowell and I have continued to say is we would be good stewards of cash. So we are not going to accumulate cash from wireless just to have wireless sit on cash. That doesn't really earn anything from an investment return perspective. So when we get to a point where we say, okay, we have more than enough cash to operate the business and we think we are in a good place, we do a distribution, which is what we just announced that we will do one here come June 27 for $7 billion because, based on projections, we really don't need that $7 billion sitting at wireless.

Now, once we do that distribution and we look forward over the next 18 months or so, we say, okay, there are some events coming up that we are going to need to start to accumulate cash and deal with these events. The one event is -- there is $5 billion worth of debt maturing, about $1.5 billion here in the fourth quarter of this year and then $3.5 billion in the first quarter of next year. So that is $5 billion that we will have to use for that. We are still looking at the FCC and what they are commenting on that they are going to try to conduct the auction in 2014. So we will participate in that auction, so we will need cash at Verizon Wireless to deal with that.

And then finally, just recently, there is another $5 billion worth of debt on the Verizon Wireless books that has very long maturity, very high coupon rate and that just became callable at this point in time. So we will have to take a hard look at that in 2014 to determine whether that is viable or not viable. I am not saying we are calling the public debt at this point, but given the high rate of interest, given the financials around that, that is something else that we will have to consider in 2014.

So as we go out, there are some uses of cash at Verizon Wireless that we will need over the next 12 to 18 months and as far as the corporate dividend goes, I have gotten this question as well. We have many uses -- many ways to raise cash and do other things with cash in order to fund the dividend. So that is not an issue and the two are really independent of one another.

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**Mike McCormack** - *Nomura Securities - Analyst*

I think you have talked publicly over the past few months just regarding the possibility of share repurchase at some point. Is that also on your radar screen later this year or maybe next year?

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

Yes, that was coming out in the fourth quarter and at that point in time, coming out of the fourth quarter after Sandy, I wanted to signal to the Street that I thought that the stock price at that point was undervalued. So at that point in plan, if it meant that I would buy back shares then I would buy back shares. We bought some back, but the stock has performed quite well, so it really didn't make any sense to continue to buy those shares back.

But if -- I always look at this as -- it's an opportunity. There is a right way to buy shares and there is a wrong way to buy shares and when your stock is performing well, it is not necessarily the right time to buy your shares back. So we monitor this. As I said, we did buy some shares back, but, at this point, we are kind of holding where we are and really paying attention more to the cash flow of the operations, reinvestment and the dividend policy.

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**Mike McCormack** - *Nomura Securities - Analyst*

We won't delve too much into it, but what is your confidence level on the government auction spectrums being sort of in that 2014/2015 timeframe? It seems like a lot of people think that might be a pretty aggressive expectation.

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

Yes, well, we think it is aggressive, but, at this point, the timeframe that they have been communicating is they are hoping to accomplish it in 2014. We hope that they can. We will be ready for that. If it passes to 2015, we will be ready.

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**Mike McCormack** - *Nomura Securities - Analyst*

Let's shift gears to operations and thinking about wireless and the competitive environment. One of the things that we hear consistently is that there is big concern about AT&T and Verizon being impacted by a resurgent Sprint or a resurgent T-Mobile. T-Mobile just got the iPhone recently, launching their Simple Choice plans. Sprint presumably will have a partner of some kind over the next four to six months or so. How does that change in your mind the competitive landscape?

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

Well, look, I think if you go back here, the wireless business has been extremely competitive since the day it was born. I mean this is a very, very competitive environment from a wireless perspective. And as I said, from an industry perspective, I have continued to say that a stronger Sprint and a stronger T-Mobile actually help the entire industry. And I think that is what you are going to see. I don't think that it is someone takes or loses share. I think what happens is, and what you are seeing right now with everybody talking about the second quarter, is the pie is growing and if you look at net adds, the pie of net adds will continue to grow because it is not just a business of a smartphone add anymore. The mix of smart -- the mix of the net adds is going to continue to expand over time.

When you think about the Internet devices and connected devices like the car and camera, which we launched in the fourth quarter and some of these other things, the pie is going to grow. So of course, everyone is going to grow with that. So coming out of the first quarter, I said that net adds would accelerate through the rest of the year similar to what happened the last year. So I would expect that the entire industry would increase in the second quarter and that is what you are kind of hearing. So I think that this competition is good for innovation bringing new products to the marketplace. So I think it just expands the market. I am not worried about it. We watch our competitors every day and we will compete fiercely, but we continue to march on our strategic initiatives.

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**Mike McCormack** - *Nomura Securities - Analyst*

One of the things that I thought was the focus this quarter was this handset addition commentary and Verizon Wireless performs remarkably well against the competitors on that front. How important is that versus what you are talking about now, which is sort of a more connected device growth opportunity? And then if you could just layer on a comment regarding the iDEN shutdown and how much of a beneficiary you have been from a handset perspective from that process?

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

Well, look, obviously, as part of our growth strategy, adding more smartphones to our network is important and we still have a pretty substantial base of basic phones in our network. We still have 70% of our customers on the 3G network that we would like to move to 4G because we know that when we move these customers to 4G, their usage patterns increase with the speed and the volume of 4G. So there is still a lot of -- we think there is still a lot of runway here for net phone growth in Verizon Wireless.

But beyond that, I mean if you look at the tablet growth and the Internet device growth, I mean these are strong areas of growth for us and it is a different model because you have to remember you are subsidizing that smartphone pretty substantially, but on these Internet devices and tablets and cameras and all these other things that are coming, there really is no subsidy model. So when you think about the actual revenue per unit, yes, it is less, but the profitability is there because you are not subsidizing it upfront.

So all of the connections are important to us from a service revenue growth and I think what you are going to see is over time and some have written this, I think you have even written about this, is that the industry model is going to shift more to watching service revenue growth and less focus on actually what the net adds are because net adds are going to continue to change. So that is -- I think our runway is still a very strong runway for smartphone growth.

As far as the competitors and who takes who and where does it come from, I mean obviously we have benefited from the iDEN shutdown, but I think that as far as the continued growth, that has significantly decreased over time. So that is really not a part of our growth anymore. So I am not really counting on any iDEN coming over at this point. I think that is all done.

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**Mike McCormack** - *Nomura Securities - Analyst*

So commenting on your comment a second go just regarding ARPAU, ARPU, measurement techniques and how service revenue growth is probably the most important metric. It seems like, in speaking with some of your competitors, they say, well, we are putting it out there because you guys want some metric, but it doesn't really mean anything. Do you subscribe to that same thought process?

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

Well, I think that is why we have moved away from ARPU because ARPU is going to be a meaningless metric. And the reason we went to ARPAU is because what is going to matter in the future is what is the revenue per account. And as you have seen what we have done with our shared pricing and the way we have built our data plans, what is important is that people connect more devices and drive usage up. And that is really what is going to drive the service revenue equation from just an account perspective because if you start to track ARPUs and let's say, like the fourth quarter, you add a camera, okay, to add that camera was $5. Okay, is that really what matters from a revenue per unit perspective? No, what matters is is that customers are willing to connect more of these devices into that shared plan and by having all these devices in that share plan is going to drive that usage up, which then they are going to buy up in tiers. That is really what drives service revenue growth in the future. So that is -- moving to that ARPAU metric we felt was more realistic of what the future holds for us.

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**Mike McCormack** - *Nomura Securities - Analyst*

So shifting away from the revenue side of the story on these shared plans into usage and what your experience has been sort of early on in the process with people moving up the stack, and I don't know what your household looks like, but I have got a 14-year-old daughter that has driven my usage from roughly 2 gig to now I am subscribing to 10 gig and it only took about four months.

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

Yes, well, in another four, you will be to 20. This is exactly why we said we needed to bundle data to be shared among these devices because you can't continue to manage device by device and your usage is going to fluctuate between users. And what we are seeing obviously, Mike, is what you are experiencing. As people move over to that LTE network and they start to drive their usage through that and it is very -- it is shaped by demographics. I mean the younger population does not have linear TV. They watch most of their content through the Internet. They do most of their stuff through the mobile. I have a 19-year-old. He drives probably 90% of my usage in my home because he does everything off of his mobile handset.

So there is a different usage pattern by age groups. So that is important to have that shared plan. And what we see is with LTE and some have actually projected out what data usage is going to be over the next 5 to 10 years and that charge is pretty close to what we are projecting the usage will be. So from an industry perspective, this usage of data is just going to continue to compound and grow.

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**Mike McCormack** - *Nomura Securities - Analyst*

Apparently there is a lot of Kim Kardashian following on these video apps on your phone that drives tremendous usage. So that is my struggle at home. So shifting to the subsidy situation, we have written extensively about what we call i-Pain and smartpain and we watch these sine waves of margin that creeps up in the first quarter, second quarter, third quarter, great and then we slam back down in the fourth quarter. You guys have been more immune to it than your competitors, but where is the solution? You have moved to 24 months for the upgrade cycle, which I think is a pretty good stake in the ground. It seems like nobody is willing to follow you in that, but are there other levers you can pull and with smartphone penetration for you so low, there is a lot of runway left I think from an ARPU perspective.

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

Well, look, I mean subsidy is just one of those -- one line item in the P&L to drive the profitability of the business. And this model has been here for 12 years now. We have seen some come in with installment plans. I mean we did an installment plan back with the tablet in the fourth quarter. So I think you're going to see some of these different ideas come to market to try to reduce the amount of pain that there is in that subsidy model. But the fact of the matter is is that these smartphones are extremely profitable customers. So taking the subsidy upfront, albeit, yes, it has a one-time hit to you, but the adoption rate, the stickiness of this, especially when you look at now the share plan and these customers coming into shared and the stickiness and the lower churn, the model still makes sense.

But in order to protect the profitability from this yoyo effect of when a new device comes to market, you have to make sure that you manage the rest of your cost portfolio. And I think Verizon Wireless has done a pretty decent job of this and we continue to challenge them and you have heard me say that it is a big entity, but I still say it is an inefficient entity and they have to drive more cost out of the business and I think you are seeing that with some of the things that we talk about in driving some of this $2 billion cost reduction out of the business this year through call centers and logistics systems and a bunch of other things that we are working on. So it is more than just about subsidy; it is managing the entire P&L of the business.

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**Mike McCormack** - *Nomura Securities - Analyst*

Thinking about the direction that T-Mobile has taken, I think it can be viewed by some as a sort of risky strategy. If you evaluate your business, does it make sense -- you are doing a little bit now, but does it make sense to have a more wholesale -- sort of this is the direction the whole industry should take and it is good for Verizon?

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

Yes, I think what is important to consumers is you have to give them choices and let them decide what is best for them at that point in time. And I think we saw that with the tablet when we installed the installment sale. Most of the installment sales were still bought outright and put on postpaid price plans. We had a number of customers who felt that they wanted to do an installment sale. So it comes down to choices and what is buyable for that consumer. And I think that what T-Mobile has done with the installment sale is interesting. But I would tell you if we go in that direction, it is not going to impact the service pricing. Our shared service pricing is our shared service pricing. So what we did with the tablet in the fourth quarter when we did installment sale, the service pricing didn't change. It was just a matter of you could elect to pay for the tablet over a period of time than paying for that tablet all upfront. So I think the consumer choice here is how you buy the device. But from a service pricing perspective, our service pricing won't change.

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**Mike McCormack** - *Nomura Securities - Analyst*

So thinking about, and this might be a bit of a loaded question, but to the extent that your competitors are losing phone additions and you guys are gaining and that is part of the reason they are losing phone additions, but is there something to be said that the lower end subscriber in the base is finally making the decision to go to a prepaid product that might be cheaper and we are seeing sort of a bleed out of those lower end customers? And then thinking about that customer, how valuable are they, because I think the argument might be, well, they are low ARPU, they don't really generate that much for us? But the reality I think is that they have got older phones that use few network resources, little spectrum needs and probably have big cash flow attached on a per sub basis. So in your view, are you seeing that move secondarily? Is that a cash flow stream that is very important to maintain?

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

Yes, so we have taken really a dual strategy here with network. So if you look at our 4G LTE network, that is strictly a postpaid retail network at this point. And that is the way it is going to stay at this point. If you look at our 3G network and what you have seen us do is we have come a little bit more aggressive around 3G from a wholesale perspective and from a prepaid retail perspective. So our view of it is what is key for us is we have stopped investing in that 3G network last year and we are only investing right now to keep the network up and running.

So from a contribution margin standpoint, Mike, getting back to your point, you want to try to keep that as full as possible because it really is mostly a fixed cost at this point network. So if you can keep that network full, the contribution margin is there. So these prepaid customers, and even on a wholesale basis, and you see us play with these two things from a lower end standpoint, if you will, or prepaid, both of those customers are very profitable customers on that 3G network. The key for us though is is we have to make sure that we can balance the 3G and continue to move smartphone customers to 4G because what we don't want is to overbuild that 3G network at this point.

So it is kind of a delicate situation that we have, but you can see us, we are executing -- coming out of the first quarter, we had a very successful reseller side of the house. We continue to grow our prepaid and you just probably saw us launch some new prepaid pricing recently. So you will see us play with this 3G network and get aggressive where we think we can, but obviously the point that we always hold is we can't get so aggressive that the prepaid market looks better than the postpaid market.

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**Mike McCormack** - *Nomura Securities - Analyst*

In thinking about -- you touched on this a second ago -- the cost savings opportunity and one of the things we have always been surprised about with Verizon is you have got one of the better or best growth profiles in the industry from a wireless perspective and yet costs continue to come out, which is sort of a disconnect I think and you are driving some of these initiatives from the top. Maybe you can just talk about some of the things you are doing there. You talked about $2.5 billion of incremental savings this year and then there is a lot of thought about where wireless margins can go over a period of time. You are already outperforming the industry in a big way.

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

Well, from a cost perspective, look, I think if you look at this, and the example I will give from last year, so we added 5 million net new customers, devices, whatever you want to call it, to the network and we closed three call centers. So if you look at the shared pricing plan, what we are seeing is, by giving unlimited voice and unlimited text, it has reduced the call volume from a shared pricing plan customer because they are no longer exceeding their bundle in minutes or exceeding their text messages. So that took all that complexity off the table, which drove a lot of cost out of the system and I guess it was a byproduct of the share price plan.

So as we look at this and we look at more customers are willing to self-serve online through their mobile handset or their tablet or the Internet, that cost structure, and if you think about the number of call centers we have and the number of employees that we have related to call centers, that is a pretty big cost structure there. But, again, it is a delicate balance because you have to make sure -- I mean we won JD Power's for the fourth year in a row for customer service and that is very important for us because that goes to -- it is not just pricing. It is around the network quality, it's around customer service of how you retain customers. So again, it is a delicate balance of how you service your customers, but what we are seeing is, as more customers move to that self-serve, it takes a lot of cost out of the business.

When you think about the logistic system and the number of devices that move through that and you think about the forward logistics, as we say, for new phones going out, but all the returned phones coming back, that is an enormous cost structure of the business. So even a penny, if you think about every penny you can take out of that logistics system times the number of volume of phones, which are millions and millions of phones, those dollars start to add up. So it is all these little things that we manage and obviously we just launched our Verizon lean Six Sigma as well, which is really getting down to the nitty-gritty of the process reengineering and wireless is doing that and we are also doing it now on wireline. So we do believe that there is still a very long road for us to be a much more efficient corporation.

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**Mike McCormack** - *Nomura Securities - Analyst*

In thinking about the handset ecosystem, one of the things that we have written about in the past is the poison apple, if you will and to the extent that you infiltrate your subscriber base with very low priced iPhones, whether it is the old version or two old versions ago, it seems to have a situation where the next iPhone release comes out and everybody has to get the next one and then you create this cycle. I think it is much more pervasive than the Droid devices or Window device. How much of that do you sort of view internally as let's not try to seed this space with too many iPhones, let's really distribute them on all the different providers?

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

Well, look, I think that we have shown we have a very balanced portfolio of devices in our lineup and I think we have done a pretty decent job in keeping that balance, but, at the end of the day, what is really important for us and what is important for our front line is that when the customer leaves that store, whatever device they leave with, they are satisfied with the device and they don't return the device. Because the worst thing that can happen to us financially under our Worry Free Guarantee is you force a device in their hand, they leave the store, they are not satisfied, they come back and say I don't like this one, give me another one. Okay, now you have subsidized two smartphones.

So it is more important for us to have that customer leave that store or online or wherever it is that they are satisfied with the device, that they are going to keep that device for the period of time. That is what matters. But, again, I think we have done a good job in balancing. I think that, as I have said before, having more competition in this ecosystem is good. Having Windows come into the lineup, having BlackBerry come back into the lineup, I think this is all good and gives our consumers more choice.

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**Mike McCormack** - *Nomura Securities - Analyst*

So thinking about the LTE network, you have identified how efficient it is versus 3G. As we look forward in the amount of usage we are talking about, and we talked earlier about explosive data demands, how do you sort of balance -- is there a real margin benefit as you look at moving to 4G LTE or is this going to be offset by just explosive traffic growth?

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

Well, the LTE network is 5 times more efficient than the 3G network. So the answer to your question is I think our margins speak for ourselves. So we do want people to move to the 4G network and obviously, the reason we want that is because we see what the usage is. But we also see what the ARPAU is. So yes, it does drive usage up, but it also drives the revenue as well. So the profitability metrics works for us.

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**Mike McCormack** - *Nomura Securities - Analyst*

And thinking again on spectrum, we talked about broadcast. You recently threw out a bid for some Clearwater spectrum as well. What was the rationale for that and is there other -- are there other opportunities out there, whether it is Dish spectrum or others that you might be interested in?

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

Well, look, I have always said that, from a spectrum perspective, you have to be very opportunistic in this marketplace because spectrum only comes up to the market once in a while and if it fits within your portfolio, you have to take a run at that market. And what we looked at was that the Clearwater spectrum would fit within our frequency portfolio. We could use it for LTE capacity, so we said, well, it's an opportunistic play. We will make a bid for it and we will see where we go.

Again, we are okay strategically with spectrum for the next four to five years. It is not an urgency for us, but you have to be opportunistic. And that is why I continue to say we will play in the next auction because that will have to be for future use for us. So you have to plan -- I mean I think we have done a pretty good job. You really have to plan five to seven years ahead of when you really need that spectrum in order not to cut yourself short here.

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**Mike McCormack** - *Nomura Securities - Analyst*

And then just thinking about capital intensity in the business, we were off-site I guess with Lowell two months ago and he was talking about -- well, don't get excited about capital intensity coming down because 4G turns into 5G turns into 6G. I assume you hold a similar viewpoint on that, that mid-teens is probably the right level to be thinking about longer term for wireless?

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

Yes, I think that with this one, we will have to watch this, but, obviously, we have done a lot of work in building out a brand-new network. We now have to go back in and fill in the capacity of this network. So a lot of people have asked me, well, Fran, since you have built it out, does that mean your CapEx comes down? The answer is no because now we will have to redeploy that CapEx to fill in the capacity and the gaps that we have. So I think, Mike, you are right. I think the way I look at this is we are really going to manage this on a CapEx to revenue ratio. And what we feel is that we can continue to improve that ratio, but obviously as revenue goes up, the actual dollars may stay flat or slightly increase, but the ratio will continue to decline.

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**Mike McCormack** - *Nomura Securities - Analyst*

Okay. So shifting gears to wireline, you guys had a goal, I believe, of hitting 5% revenue growth as you exited last year. Hurricane Sandy threw a wrench in that for you, but as you look out over 2013, how do we reaccelerate that? FiOS is obviously a key trigger there, but is there also a legacy piece that says we can see less line loss and we used to measure this pretty systematically back in the day, nobody cares about axis lines anymore, but is that also part of the features, sort of less legacy loss?

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

Yes, it's a combination of both. I mean we came out of the first quarter at 4.3%. So I will say that that 4.3% is better than what we have done mainly in the past. So it is still a pretty good growth rate for the wireline business. I know I had a target of 5% and I missed that. I will still target that 5%, but I am real comfortable with the progress that we are making here between FiOS. There is less line loss, but really what is the difference here is that if you look at our small business piece, which is still negative year-over-year, we are making improvements there. But if we can continue to improve on that small business piece then I get back to that 5% because right now that is still a drag of about negative 2% a quarter. So last year, it was negative 4%. So we have improved it by 50%. I need to get it to zero. Then I need to start growing again. So I think small business continues to be an opportunity for us to improve our growth profile on the wireline side.

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**Mike McCormack** - *Nomura Securities - Analyst*

And thinking about FiOS specifically and what we have heard consistently from the cable companies and telco to some extent as well is this post-promotion churn. And I actually -- I am a Verizon FiOS customer. I called them and I tried to negotiate my way to a lower price and I live in Manhattan, and Time Warner Cable is the alternative and they basically told me that I should continue on what I am doing or switch to Time Warner Cable. So I didn't get my discount. But my point to you is is there a lot of that going on? Is this horse-trading back and forth, I will get a lower price triple play from these guys, then I will switch in the next year or two and how does the industry sort of evolve to stop that process?

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

Yes, well, I mean, again, the cable industry has been extremely competitive since we have come to market and we have always had a hard time with this one and it reminds me of the long-distance business of ages ago where you had people pay $100 for somebody to switch to you and then three months later, they would go back and get $100 from the other player.

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**Mike McCormack** - *Nomura Securities - Analyst*

It's the best [pile-up] scam ever.

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

Yes, and it is a really bad, bad financial model to get into. And really what we are trying to do is really follow the wireless model, which is, if you build a quality product and you charge a fair price and you have good customer service, then that is really how you maintain a customer. You can't get in this battle of this postpaid, after you connect, let me see what the best deal is because we do believe that FiOS is a superior product to the cable business. I mean if you put it side-by-side, you can see that and we think that with our FiOS Quantum offer and the speeds that we are offering, we think we deliver an extremely good value there and we are seeing a lot of customers now starting to buy up in those tiers that we have.

So I think what you experienced was something that we really became disciplined in as we can't get caught in this -- well, if I go over there, I get it $20 cheaper. So if you give it to me for $20 cheaper, I will stay with you. And our answer is our price is our price. So I think that as you can see what we are doing is we are targeting the 600,000 net add growth for this year. I think we are right on target to meet that growth. We will continue to gain share in the marketplace and we just have to really concentrate on delivering excellent customer service of people -- that our customers don't have that tendency to say, well, price is everything and I will leave for the cheapest price.

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**Mike McCormack** - *Nomura Securities - Analyst*

I had a good conversation a couple weeks ago with Bob [Motz] regarding video conception in the home and what is he is seeing out there with people moving up into the tiers of FiOS. But we've spent a lot of time focusing on the sort of Wi-Fi. Offload tablets are exploding and all these handsets. Your son is a good example, I am sure, as well. It turns into a Wi-Fi device in the home and it sucks a tremendous amount of bandwidth. So maybe just a quick comment on what you are seeing from a usage pattern standpoint and how that positions Verizon, which, in our opinion, when you look across the sphere of competitors, is best positioned I think from a technology standpoint to deal with this problem.

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

Yes, so what we are seeing is -- what we are seeing is the amount of devices that are running in the house, and why we are seeing people buy up to the 50 and now the 75 and then to the 100 megabit price plans is because, as you load on more devices, if you don't have the input into your home, those devices are not going to perform if you get five or six devices running off of that router. So you need the throughput in order to keep the speed of those devices on the Wi-Fi network running.

What you are going to see is you are going to see more technology come out as well with the routers to be able to provide even more speed within the house through Wi-Fi via that throughput from the fiber. So there is a lot of technology that is going to come for us to be able to boost up that Wi-Fi network in the home to produce the speeds that you would expect. But also that is what is also producing the benefit of the FiOS Quantum right now because as people add four or five devices on that network in the home, they are needing to buy up for the speed in order to get that throughput to get those devices to run more efficiently over the Wi-Fi network.

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**Mike McCormack** - *Nomura Securities - Analyst*

It was not only Kim Kardashian, but six other devices in my home that moved me from 50 meg FiOS to 75 meg FiOS in the home, so my data consumption might be an anomaly, but maybe something to come down the road for many more people. When you think about FiOS on a going-forward basis and trying to take share, and this is -- Cablevision will be here later today. It's a market where you guys have blanketed pretty aggressively. The MDU market seems a little more ripe. So when you look at that, it is probably I would imagine a lower cost to connect in an MDU as well. What would be sort of the key target demographics to increase penetration for FiOS in a cost-effective manner?

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

Well, I mean obviously small business and MDU is really the gap between what we have passed and what we have opened and some of these are difficult because of challenges in getting inside the building and building out the building with the landlords and so forth. And we have made a lot of progress over the last four or five years to do that. But, obviously, what we are really concentrating on right now is selling to what we have open. We still have -- we have 18 million homes passed at this point. We have about 5 million plus customers, so we still have quite a bit that we can sell to. So it really isn't about opening more for sale; it is about penetrating what we have open for sale.

Our concentration on passing is we will continue to fulfill the LFA obligations we have. We are looking at a little bit right now that if we were to extend the build beyond what our commitment is, especially around small business, there may be an opportunity there for us and we are talking about $100 million incremental capital. So it is not a lot of capital, but it could be a lot of benefit. But we are toying with that right now. So we are really looking at this really honestly Mike from an ROIC perspective at this point. But I think I owe it to the investors to say I need to return the investment that we have already sunk into FiOS. So our concentration right now is sell what is open and get more penetration with what is open.

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**Mike McCormack** - *Nomura Securities - Analyst*

And just thinking about, without pegging you to a certain dollar amount, but the cost to connect an MDU versus a single-family unit I imagine is reasonably lower?

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

Yes, well, the initial cost to light up an MDU obviously is significantly higher because you have to enter the building, you have to go up all the risers, you have to get to each apartment, but then once you are in the building, obviously, it is a lot less expensive to connect that one individual unit than it would be for a single-family home.

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**Mike McCormack** - *Nomura Securities - Analyst*

There is a significant focus among many in the room regarding the media side of the world and content costs. One of the things we have seen for the cable industry or pay-TV industry is difficulty in taking price without seeing a negative impact on subscribers. How do you sort of combat the content costs and what are you seeing as sort of pushback? And you can bleed into an over-the-top discussion as well on whether or not that changes the content negotiations.

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

Well, I think that we have done a little bit of both recently. So you saw us launch a new package without regional sports in it, so we are trying to give our, again, customers many choices in order to have them to be able to pick and choose what they want to pay for. So that is one piece of it. We have rebundled much of our content to take it out of the lower content cost and move it up into the more premium channels in order to make the model work for us. Also, as you know, we have entered into the Redbox Instant joint venture, which is more an over-the-top play. So that is just another venture that we are doing.

But the indirect benefit of that is not only trying to attack the over-the-top market with some differentiated movie content and so forth and really hedging the 35 million customers that Redbox has, it also gives us the ability to negotiate content on a more broad basis, not just within the FiOS base. So we can use the Redbox subscribers to really benefit the FiOS content as well. So as we add more customers, we get more breadth, we get bigger, we get better content cost.

So it is a combination of all these, but unfortunately the model right now is is that content costs are going to go up every year and we think that, at least for the FiOS piece, it is probably 3% to 4% per year, which is what we have seen and in order to maintain the profitability of the product, we have to increase price every year and that is the model that cable has been following for years. So I don't see short term how that model changes until you get a real different ecosystem around content.

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**Mike McCormack** - *Nomura Securities - Analyst*

We have heard from other providers sort of saying we have got enough data to go back to some of the programmers and say my customers don't care enough about your content. Are you guys able to push back on some of the stuff whether it is regional sports or other content that is just simply not watched?

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

Yes, I mean, obviously, if you have seen what we did, we have taken some content off of our channels and you have to deal with the customer dissatisfaction because even if it is maybe 1,000 customers who watch that program, you still have dissatisfaction with 1,000 of your customers because -- so you have to deal with those types of situations. But, look, it doesn't make sense to pay a content cost on a 5 million base if you only have a couple hundred customers watching that content. So you have to make those hard decisions, but that is something that our content guys do every day.

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**Mike McCormack** - *Nomura Securities - Analyst*

Can you just touch on the copper to fiber migration or fiber -- copper to fiber migration? One of the things that we have been surprised by is just the number of homes out there that are making that move. I have always thought that going out and putting an OMT on the side of a house that is not paying you a lot of money doesn't have a great return, but there is obviously things back in the network that you are getting paid for or just cost savings on.

Can you just talk about that and where -- maybe broader discussion on where wireline margins can go? We have heard for a decade the struggle of we are going to get better, we are going to get better and we all hope for that, but it just seems to be stagnant. So is there a lever -- obviously, economy, enterprise, all that stuff, but from a consumer standpoint, what is the lever there to try to get margins higher?

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**Mike McCormack** - *Nomura Securities - Analyst*

All right, so let's talk about copper to fiber migration right now. So obviously, what we have looked at is as we have built out these 18 million homes passed and we have a number of copper properties still in those 18 million homes, what doesn't make sense is for us to continue to maintain these two networks. So we have gone out and we have attacked the high troubled areas first and have gone in and have moved those customers to copper or to move those customers to fiber. And the benefit we get there is, as we do this, it really cuts down on the amount of repair that we have to do. The side benefit of doing it though is what we are seeing is once we put that OMT on the side of the house and give you voice and give you the basic speed of FiOS, after a couple months, they are choosing to buy up in the speeds because now they are realizing this unbelievable fiber product that they have on the side of their home. So they are buying up into those tiers and we see that most people are buying up to the 50 megabit plan.

Then what happens is, six to eight months after that, you then start to market to them because what we found is you can't do it too soon because then they think they are being gamed somehow. So six to eight months later, you start to approach them on, hey, by the way, we think we can save you money on your cable bill by taking FiOS TV. What we are seeing is about a 35% to 36% take rate now on those copper customers who just had voice and DSL. Once they come over, within a year, they become a triple play on FiOS.

So there is a lot of benefit to doing this. It is benefit to the customer, but then it is also a backroom benefit to us that we can start to take up this copper network that is really deteriorating. You really can't -- there is no financial way to keep this thing running, so we have to get away from this copper network. And obviously, with the unfortunate event of Sandy, it really accelerated lower Manhattan into that fiber conversion. So from that perspective, it is a strategy that we are really pushing hard on and you can see coming out of the first quarter, we really accelerated the number that we did and we are going to continue that through the year.

Now as far as wireline margin, given the events of this year, I have said that we will probably be flat, but based on what I see right now, the margin will start to increase in 2014. And a lot of that is around -- it is the macroeconomics around enterprise, but it is also around the pressure that we are seeing from some of these startup things that we are doing, Redbox, VDMS, Hughes Telematics. So some of these things that we have invested in are actually negative to wireline right now. They will turn positive in 2014, so they will start to contribute.

I also see that as we get -- we went through the union contract negotiation. We said that there would be about a $500 million benefit over the life of this contract. But some of this benefit is taking time to get to. So an example of that is we got call sharing for the first time. But in order to do call sharing among all of our call centers, you have to take the reps offline and train them on all the different states that they get calls from. Whereas before, a rep only was trained in their state and only had to deal with their state.

So in essence, the cost structure actually increases in the short term because you have to take people off line to train them, but what we see is the efficiency of that will start to come later this year into next year. So there is a lot of things that we are gaining momentum on that I feel pretty good and I know you are a little bit pessimistic on me right now, Mike, about the wireline margin improvement, but I feel pretty good, but I think we will start to see signs of 2014 increasing margins.

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**Mike McCormack** - *Nomura Securities - Analyst*

And then you and I talked about this a month or so ago, but in the non-FiOS markets, what is the strategy there? It seems like -- I don't want to call it a slow death, but is there an outcome there that can be more stable than a real negative scenario?

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

Yes, this is a difficult one because where we don't have FiOS -- I mean obviously the copper is, in some areas, is performing okay; in other areas, it is not and obviously, this is ripe for cable to take share, which they are. But what we have come out with is we are coming out with some different products. Obviously, if you look at the situation just recently out on Fire Island where the entire network got destroyed, it doesn't make sense for us to rebuild the copper network. It doesn't make financial sense to invest fiber to the island. So what we are doing is we are coming in with a solution that says we will give you voice over LTE in order to replace that technology and we're working with the regulators and so forth to make that happen. And that is really where we have to go here because there is a different solution rather than building infrastructures in some of these what I would call more rural areas. And it is really with using the LTE technology, the fusion technology from a broadband perspective and we still have some work to do with regulators, but we are making headway here and I think that is the route that we will take.

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**Mike McCormack** - *Nomura Securities - Analyst*

So thinking about AT&T's Project VIP and rolling out IP DSLAM to a more broader audience, is that a solution that you would consider or is it just not a great return for you guys?

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

No, I think that we made our bed on fiber to the home and we have done that and outside the FiOS footprint at this point I think we are going to concentrate mainly on giving them a solution for voice and data and no, we are not going to take that strategy.

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**Mike McCormack** - *Nomura Securities - Analyst*

I have one or two more, but I want to see if the audience has any questions. There is a roving mic if anybody has a question, just raise your hand. There is one over there.

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## QUESTIONS AND ANSWERS

**Unidentified Audience Member**

Hi, good morning, thank you. Two sort of smaller issues, but is there any 2 or 2.5 G spectrum that is out there that you can bring back in? I guess when you were talking about 3 and 4, I just started thinking about that. And then using the voice over LTE, is the issue with that backup generators? Is that what the deal --?

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

Yes, so I think your question on the first one was more or less taking the 3G spectrum and moving it to 4G?

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**Unidentified Audience Member**

No, the 2 or 2.5, is there any of that --?

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**Mike McCormack** - *Nomura Securities - Analyst*

Just inventory in the marketplace of --.

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

I don't know the answer to that. I am not that familiar with it. I mean I know what we have. I don't really pay too much attention with what is the market. Verizon Wireless deals with that every day. Okay? So from a VoLTE perspective, on voice over LTE, as I said, we will be in a position where we are building that out. We have been testing it for over a year. We have actually been testing this with Vodafone as well so that when their LTE markets get up and running, we can have a seamless handoff between the two networks so that it almost looks like you haven't left either network and your features would all be the same.

So we have been testing that for over a year, but as far as launching VoLTE, the key for us is is that it is not backwards-compatible with CDMA. So the key for us is to make sure the footprint and the quality of that call will be the same as our 3G network so that our customers don't see a difference when they move to VoLTE from what they were used to on 3G. And that is why we are taking our time with this one.

But to answer your question on the launch of it, we will probably open it up in the fourth quarter of this year. We will really go commercial with it first half of next year and then we will have our LTE-only handset probably in the fourth quarter of 2014. But we will take this slow because we need to make sure that the quality of that voice call is no different than a 3G call.

**Unidentified Audience Member**

When looking at European markets, can see that convergence and the movement towards quad plays is gaining speed in a number of markets. You see that also in Canada. In the US, it really hasn't started yet. I am wondering what is the reason and what could be the trigger for that to change? Is possibly a successful Dish acquisition of Sprint that trigger?

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

Well, I mean, think. First, you have to step back. We have been doing quad play since we launched FiOS within the 13 states that we have FiOS. And I think what you are going to see is the market will mature over time. As the content converges between inside the home and outside the home, then a quad play makes more sense as you join up, which is why we entered into the cable ventures almost a year ago now because we saw that, as the ecosystem changes, it will become more important. So I think that here in the US, it is just a very different marketplace than it is in Europe. But I think that the quad play will become more important over time, but obviously cable companies and ourselves have been doing quad play for quite some time. So whoever wants it, it is there. But right now, consumers don't really shop that way. It is important for some, but not for others. But as we see this convergence coming together inside the home and outside the home, I think then it is going to start to come more important for customers.

**Mike McCormack** - *Nomura Securities - Analyst*

We have got time for just one more if there is one out there.

**Unidentified Audience Member**

A two-part question. Firstly, do you see -- they are both on the FiOS side. Do you see FiOS moving to any kind of usage-based high-speed data plan anytime in the near future? And then part two is around Google and their new fiber initiative. Obviously just in a few markets now, but how are you guys thinking about that?

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

Okay, good question. So first on the FiOS piece of it, we have not capped FiOS as others have in the cable industry and quite honestly, we have no plans to cap FiOS. There is really no reason to. I have dedicated fiber to the home and it is there and we can provision that up to the speed that you want. We now offer 300 megabits per second, so we have customers who buy that and it really is not a big deal for us to deliver that because we have already invested in that fiber to the home. So that view to us is a competitive advantage right now.

As far as Google Fiber goes, they are a great marketing machine and they have got a lot of spin around delivering 1 gig to the home. We did that almost three years ago in New York City to a home here. So yes, it is great. We can do it. Fiber can do that. So from my perspective, what Google is doing is -- their model is they want folks to use broadband because that is how they monetize their search engines and so forth. So by doing what they are doing, they are forcing everybody to say they have to step up their game, they have to provide more throughput to the home in order to generate that. FiOS already does that. So it is interesting to watch what they are doing, but we already do that and we compete vigorously on the FiOS footprint. I would highly doubt that Google will build anything in the fiber FiOS area.

**Mike McCormack** - *Nomura Securities - Analyst*

Well, thanks very much, Fran, for joining us. I appreciate it.

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

Thank you, everyone.