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# Sprint Corp. (S)

Q2 2018 Earnings Call

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# MANAGEMENT DISCUSSION SECTION

**Operator**: Good morning and thank you for standing by. Welcome to the Sprint Fiscal Second Quarter 2018 Conference Call. During today's conference call all participants will be in a listen-only mode. Following the opening remarks, the conference will be open for questions. I would now like to turn the conference over to Mr. Jud Henry Vice President of Investor Relations. Please go ahead, sir.

## Jud Henry

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

Good morning and welcome to Sprint's Second Quarter Fiscal 2018 Conference Call. Joining me on the call today are Sprint's President and CEO, Michel Combes; our CFO, Andrew Davies; and our CTO, Dr. John Saw. Before we get underway, let me remind you that our release, Quarterly Investor Update, and presentation slides that accompany this call are all available on the Sprint Investor Relations website at www.sprint.com/investors.

Slide 2 is our Cautionary Statement. I want to point out that in our remarks this morning, we will be discussing forward-looking information which involves a number of risks and uncertainties that may cause actual results to differ materially from our forward-looking statements. We provide a comprehensive list of risk factors in our SEC filings, which I encourage you to review.

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

Lastly, like last quarter, we have included reconciliations and qualitative disclosures to the tables that accompany our release and Investor Update to provide additional clarity regarding the adoption of the new revenue recognition standard on our quarterly results. For the remainder of this call, we will discuss results excluding the impact of the accounting change to provide clear comparability with prior periods, unless otherwise noted. I will now turn the call over to Michel to provide you an update on our results.

## Michel Combes

*Chief Executive Officer & Director, Sprint Corp.*

Thank you, Jud, and good morning, everyone. I am pleased to share with you our fiscal second quarter results on slide 4 which demonstrates our focus on improving the profitability of the company. First, we reached a major milestone by delivering year-over-year growth in wireless service revenue for the first time in nearly five years and earlier than our commitment to reach this milestone by the end of the fiscal year. We generated the highest adjusted EBITDA for a second quarter in 12 years as we continued to execute on our cost reduction initiatives.

Meanwhile, we delivered net income for the fourth consecutive quarter and operating income for the 11th consecutive quarter. Furthermore, we delivered positive adjusted free cash flow for the sixth time in the last seven quarters. We reached new milestone in our digital transformation and continued to lead the industry in several key metrics around digital sales and the implementation of artificial intelligence. In addition, we nearly doubled our network CapEx year-over-year and our network continued to improve as demonstrated by Ookla Speedtest data which shows Sprint's network was the most improved of any national carrier in terms of average download speeds.

Turning to slide 5. We delivered retail net additions for the fifth consecutive quarter. Let me take you a step back and share with you how we think about our commercial strategy to balance growth and profitability for the company. First, given the increasing saturation of postpaid phones as well as new competitors in the market, we are driving a renewed focus on growing revenue per account from non-phone devices. Our postpaid net additions were 109,000 in the second quarter as our focus on growing revenue from other devices such as tablets, watches were partially offset by slight losses in phones. We delivered positive tablet net adds for the first time in nearly three years and continue to build momentum in other devices such as wearables with more device options to come.

Looking back over the last few years, Sprint has suffered from poor network perception following the complete rebuild of the network with Network Vision. This is compounded by the fact that we cannot afford to spend big dollars on advertising like the other big carriers in the industry. As a result, we have utilized several promotions to encourage customers to give the new network a try. These promotions were structured to have a lower introductory rate that would then step up at a later date, very similar to what you see in the cable industry. We knew going in that this approach would put some incremental churn pressure on future periods as not all customers would stay upon the expiration of their promotional period, and this has been the primary driver of the year-over-year increase in churn. We expect the churn trend to continue through year end with seasonal sequential increase in the third quarter, likely around 15 basis points before improving seasonally in the fourth quarter.

As we work towards parity in LTE, preparing for 5G and embarking on a multiyear capital program on our Next-Gen Network, we have introduced new service plans to drive profitable revenue. At the beginning of the second quarter, we introduced new unlimited plans that were less promotional, relative to our previous rack rate pricing, providing multiple service tiers under the umbrella of Unlimited for All. These plans allow different features and services into a variety of [ph] bundles (06:27) and options for customers which creates buy-up opportunities versus the single rate plan offered previously.

While the combination of these actions and the competitive environment contributed to a year-over-year reduction in phone gross adds, we also saw an increase in the quality of our gross adds with our prime mix of postpaid phone gross adds up over 300 basis period points versus last year. Most importantly, we saw a 28% lift in monthly recurring charges on new account gross adds coming to Sprint compared to last year. So, resulting ARPU stabilization from both base customers and new gross adds led to year-over-year growth in wireless service revenue two quarters earlier that we originally guided.

Optimizing the balance of gross adds, churn and ARPU is expected to deliver a superior financial outcome over the long term and this quarter's results are early signs that the strategy is working. For new accounts coming in, our consumer phone gross adds value added or GAVA, which is a product of CLV times gross adds, was up compared to the second quarter last year, as the increase in customer CLV from the new plans more than offsets the volume impact that we saw. In addition, our business segment continues to have strong momentum with phone gross adds up year-over-year for the tenth consecutive quarter delivering postpaid phone net adds from business for eight consecutive quarters.

Now, let's discuss prepaid where we were relatively breakeven in net additions for the quarter. However, it's important to understand the underlying trends. Boost continued to have strong momentum with nearly 200,000 net adds before migration to postpaid, driven by year-over-year growth in the gross additions for the fifth consecutive quarter and continued year-over-year improvement in churn. This strength in Boost was offset by losses from other prepaid brands.

Turning to slide 6. We continued to make good progress in our Next-Gen Network deployment to provide customers a Network Built for Unlimited. As I have said previously, we remain full steam ahead on our Next-Gen Network deployments during the merger review process and we continue to build momentum in the second quarter with our efficient increase in capital spending.

First, we upgraded thousands of our existing macro sites to [ph] add (09:18) LTE on 800 MHz, 1.9 GHz, 2.5 GHz to sites that lacked those bands previously as we work to deploy all three of our spectrum bands to provide improved coverage and capacity across our footprint. We now have 2.5 GHz deployed on roughly 70% of our macro sites, compared to about 50% a year ago, and expect to complete the majority of our tri-band upgrades by the end of fiscal 2018.

In addition, we have deployed thousands of outdoor small cells in the quarter and now have 21,000 small cells on air, compared to only 2,000 at this time last year. This ramp in small cells includes more than tripling the number of mini macro sites on air year-over-year and the very successful roll-out of strand mounts which are delivering significant improvement in coverage, capacity, and time on LTE to improve the customer experience.

These network initiatives are delivering performance improvements as seen in the Ookla Speedtest Intelligence data which showed that Sprint had the largest percentage increase year-over-year of any national carrier in national average download speed and is number one for fastest average download speed in 123 cities, and the most city wins in Sprint history.

While expanding our 2.5 GHz footprint is delivering strong results, we have recently rolled-out LTE Advanced features nationwide which will further turbocharge the customer experience. The Advanced capabilities include 4X4 MIMO and 256 QAM to complement our 3x carrier aggregation roll-out for enhanced download speed as well as running out Uplink Carrier Aggregation for improved upload speeds. These enhancements are expected to deliver up to two times faster average speeds on capable devices to deliver an even better customer experience.

Our Massive MIMO deployment is delivering the significant improvement in LTE performance, as expected, and provides the building block for our mobile 5G network. We now have Massive MIMO sites commercially on air in a few markets where we are seeing very promising results including four times improvement in download speeds, double the upload speed, and a seven-time increase in capacity, the key benefit of this technology. We are also preparing to launch our mobile 5G network in the first half of 2019. Our Massive MIMO radios are software upgradable to [ph] 5G and up (12:10), as you know, allowing us to fully utilize our spectrum for both LTE and 5G simultaneously while we enhance capacity even further with 5G and begin to support new 5G use cases. The other carriers are not standing still but our significant network investments, spectrum resources, and cutting edge technologies will help us continue to improve our network.

Furthermore, on slide 7, we continue to play to our strength which is the capacity of our network to deliver the best unlimited plans in the industry and we recently made our unlimited plans even better to provide customers a Network Built for Unlimited at the best price.

In July, we launched new plans that give customers more choice to find the unlimited plan that fits them. Unlimited Basic is perfect for customers who may not need additional features but who still want unlimited talk, text and data at a great value. Meanwhile, Unlimited Plus is a feature-rich plan that includes unlimited data, talk and text, with more mobile hotspot data and bundled music and video services. Then, at the end of August, we expanded our portfolio of unlimited plans to include Unlimited Premium, a VIP wireless plan for the customer who wants it all with the combination of top notch features and services that customers won't find anywhere else in wireless. As I mentioned earlier, these new plans have delivered a year-over-year increase in monthly recurring charges for new account gross adds which should help [ph] secure (14:00) revenue trends.

Turning to slide 8, we're driving digital transformation of our company. Because we lack the scale of the other wireless carriers in the industry, we must be more innovative by leveraging digital capabilities and employ advanced analytics and artificial intelligence in our operations to further optimize our cost structure.

[ph] So, world (14:25) is in digital. As a company with a rich history of innovation, we want to make sure Sprint not only evolves in this new world, but we want to emerge as a digital telco leader. To become a digital telco, we created a new way of working called The Hive, the digital organization within Sprint that brings together innovators from across the organization to collaborate and solve problems for the business.

At The Hive, we lead with a data-first mindset and it includes [ph] a common center (14:57), AI-powered [ph] care (15:00), digital channel operations, and important initiatives such as same-day delivery and buy online, pick-up in-store. So Hive, helps us operate better, faster, and more collaboratively, for example, we have our top customer care employees working side-by-side with our engineers to make sure that our AI chatbots are best-in-class to meet our customers' needs.

We use data gathered in The Hive to build, test, and deliver unique digital experience for our customers. Our digital transformation is based upon three main pillars: increase digital revenue through improvement in gross adds and the upgrades through digital channels; provide intelligent customer experience by leveraging AI analytics and data-driven decisions; and improve digital engagements with our in-house digital marketing agency, [ph] and enhance our functions (15:56).

Third-party benchmarks would suggest that Sprint is leading the U.S. telco industry in many of these categories and I see tremendous opportunity to scale these initiatives based on what I have seen in other markets that are much more digital than in the U.S. Some countries have carriers with over 40% of gross adds for digital channels. From a digital sales perspective, benchmark shows that we are the leading U.S. carrier in terms of both the mix of sales for digital and the conversion of traffic.

Postpaid gross adds for digital were up nearly 60% year-over-year in the second quarter. This is driven by best-in-class traffic conversion for complete redesign of the end-to-end digital customer experience. This allows Sprint to have as many gross adds for digital as any other carrier, despite having by far the least amount of website traffic among the national carriers.

In addition, we exited the second quarter with over 20% of upgrades coming from digital. This is supported by our innovative Priority Status program, a recently launched exclusive program via the My Sprint app which gives upgrade-eligible customers the flexibility to reserve their spot in line and confirm their order for new iconic devices like the new iPhones. Likewise, we are ramping our roll-out of a cutting-edge intelligent customer experience, leveraging AI and analytics. AI agents can be available anytime and can provide a faster engagements with customers compared to live agents.

Third-party surveys suggest that 76% of telecommunications customers are satisfied with a fully-digital customer service experience. We are seeing growth in digital customer engagements through chats and on top of that, we have ramped to over 25% of chats being handled by virtual agents, and the experience continues to show improving SPS or customer satisfaction.

We have even enabled an artificial intelligence program so customers can easily and quickly complete a device upgrade via a chat function. We added [ph] additional carousels (18:26) and product selections to create a simple and seamless experience from start to finish. This is complementary to our overall customer experience as the automation of simple customer request allows our live agents to spend more time helping customers resolve their more complex issues.

Lastly, our in-house digital marketing agency is delivering solid early results compared to our previously outsourced model with Web conversions up year-over-year while online media spend and cost per click are down significantly. This digital transformation and data-driven [ph] structure (19:10) is expected to contribute to the next wave of cost reductions for the future.

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

## Andrew Mark Davies

*Chief Financial Officer, Sprint Corp.*

Thank you, Michel. And as Jud mentioned in his opening remarks, for better comparability, I'm going to discuss results based on prior revenue recognition standards beginning with revenue on slide 9.

Consolidated net operating revenues were $8.3 billion for the quarter, an increase of $345 million year-over-year. As Michel has already mentioned, wireless service revenue of $5.7 billion in the quarter increased year-over-year for the first time in nearly five years, mostly due to growth in our retail customer base and stabilizing ARPU trends. Postpaid ARPU of $44.99 was down 2% year-over-year, but has grown sequentially for the last two quarters due to base customers rolling off promotions and increasing their monthly spend with us along with other pricing actions. Prepaid service revenue of $1 billion grew year-over-year for the fourth consecutive quarter, mostly due to continued customer growth within our Boost brand.

Now, let's turn to costs and profitability on slide 10. We've we continued to execute on our cost transformation in the quarter as we realized about $100 million in net reductions year-over-year in combined operating expenses across cost and services and SG&A costs when adjusted for $56 million of merger related costs that were included in SG&A.

Cost of services of $1.7 billion in the quarter were up marginally by $16 million year-over-year mostly due to some incremental expenses associated with our increased network investments. SG&A costs were $2 billion in the quarter and when adjusting for the merger costs which are not included in adjusted EBITDA, SG&A was down $150 million year-over-year mostly due to more efficient marketing spend.

Excluding the impact of the new revenue recognition standard and merger costs, we have delivered over $500 billion (sic) [$500 million] (21:28) of combined year-over-year gross reductions in cost of services and SG&A in the first half of fiscal 2018 and approximately $200 million of net reductions year-to-date. For the full fiscal year, we continued to expect to deliver gross reductions of more than $1 billion for the fifth consecutive year with net reductions of slightly less than $500 million after reinvestments in our Next-Gen Network, digital capabilities, and other initiatives. Adjusted EBITDA of $3 billion for the quarter was the highest fiscal second quarter result in 12 years, and improved by approximately $300 million year-over-year.

Turning to slide 11, operating income was $553 million in the quarter, marking the 11th consecutive quarter of positive operating income. The current quarter had several non-recurring items including: $68 million related to a loss on asset dispositions, $36 million related to merger costs, $25 million of severance and lease exit costs, and a $32 million net benefit from hurricane-related reimbursements. Adjusting for these non-recurring items, and approximately $34 million of hurricane-related charges in the year ago period, operating income would have been up year-over-year. Net income of $18 million was the fourth consecutive quarter of positive net income and compares to a net loss of $48 million in the year ago quarter.

We'll now turn to slide 12 on CapEx and free cash flow. Network cash capital expenditures of $1.3 billion nearly doubled year-over-year and were up $134 million sequentially as we ramped-up our Next-Gen Network initiatives.

Net cash provided by operating activities of $2.9 billion improved by $125 million year-over-year while adjusted free cash flow, which had been positive for six of the last seven quarters, was $525 million in the quarter and improved by over $100 million year-on-year even with the significant increase in network cash CapEx.

We continued to have strong liquidity with over $11 billion of [ph] general purpose availability (23:55) including nearly $9 billion of cash, cash equivalents and short-term investments as we've pre-funded a significant portion of our capital investments and debt maturities for this fiscal year. However, we will continue to be opportunistic in looking at the capital markets and maintaining flexibility while we're in the merger process.

Let's now move to our latest outlook for fiscal 2018 on slide 13. Due to the strong year-to-date performance, we are raising guidance for adjusted EBITDA to a range of $12.4 billion to $12.7 billion, above the previous expectations of $12 billion to $12.5 billion. Similarly and excluding the impact of the new revenue recognition standard, we are raising our guidance for adjusted EBITDA to a range of $11.7 billion to $12 billion compared to the prior expectation of $11.3 billion to $11.8 billion.

Regarding network cash capital expenditures, we continue to expect spending to increase significantly year-over-year as we ramp-up our Next-Gen Network initiatives and prepare for the launch of 5G the first half of 2019. As we are now halfway through the year, we are narrowing our previous expectation of $5 billion to $6 billion to a range of $5 billion to $5.5 billion.

Additionally, we are increasing our adjusted free cash flow expectations from around negative $1 billion for the full year to a range of between negative $1 billion to negative $500 million on a full year basis. And with that, I'll now turn the call back to Jud to begin the Q&A. Thank you.

## Jud Henry

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

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

# QUESTION AND ANSWER SECTION

**Operator**: Yes, sir. [Operator Instructions] And your first question comes from Philip Cusick.

Philip A. Cusick
*Analyst, JPMorgan*

Q

Hi, guys. Thanks. I wonder if you can start talking more about the strategy of increasing revenue per account rather than going after, it sounds like new accounts. How does that play into your data device and tablet efforts? Tablet gross adds, are those picking up with the stability or is it just the churn is down? Because we've seen this before. It doesn't seem like a repeat of the tablet wave a few years ago, but I want to hear what you're thinking about? Thanks.

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

A

Good morning, Phil. So, first, on your questions related to the non-smartphone handsets, I guess, that [ph] it's fair (26:53) that given the increasing saturation of postpaid phone as well as new competitors in the market, we are driving a renewed focus on growing revenue per account from non-phone devices. Our competitors did that last year. I guess that we are putting a lot more effort this year. It brings additional ARPU. On top of that, it should reduce churn at the end of the day because that means more devices per account. As reported, we delivered positive tablet net additions for the first time in nearly three years and continue to build momentum in that space as well as [ph] doubling (27:31) momentum in other devices such as wearables with more device options to come.

And to your precise question around gross adds and churn, I mean, we see an uplift in terms of gross adds concerning the tablet, so an appetite for – from our customers to get those additional devices. Then, on your question on – so, of course, that has an impact on the postpaid ARPU and that has helped us to stabilize our ARPU and – or even to deliver growth sequentially in between Q1 and Q2 of 1%.

Philip A. Cusick
*Analyst, JPMorgan*

Q

Can you expand on that? Are you subsidizing the new devices like tablets and watches or are you just highlighting them more in stores and in advertising, how should we think about that?

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

A

Both, I would say. We have been a little bit more aggressive in terms of tablet promotions, as well as watches, but the most important is that we have highlighted those devices more in our stores. We have also changed the compensation of our retail reps in order to be more incentivized to drive those handset – those non-handset sales and that's the result that we have seen, and I expect that it will continue to grow.

Obviously, our priority remains to continue to sell smartphones and that's the first piece that a rep is due to do, but on top of that, we wanted to drive the right behaviors from our reps in order to make sure they sell as well tablets and watches. So, that's what we have been able to achieve, that was part of the strategy.

Our strategy on the one side was to rebalance in between smartphones and non-smartphones, and within smartphones, to drive an uplift in terms of MRC by bringing those new pricing plans that we have implemented, which gives us some ability to step-up in plans. And as you have seen, we have also been able to drive this improving MRC thanks a to good [ph] loading (29:41) of our Unlimited Plus versus Basic. So, which means that, all in all, our gross adds story is working and is delivering exactly in the way we were expecting it to deliver and that has translated in a GAVA which is higher this quarter compared to Q2 last year.

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Philip A. Cusick
*Analyst, JPMorgan*

Q

Thanks, Michel.

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**Operator**: Your next question comes from the line of Brett Feldman.

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Brett Feldman
*Analyst, Goldman Sachs & Co. LLC*

Q

Thanks. Few questions about your deployment of 2.5 gigahertz spectrum. The first is, once that is complete, how should we think about the CapEx profile of the company? Do you think your CapEx will start to moderate or go lower or do you think you will just redeploy that into some of your 5G initiatives? And then second, how you think about your go-to-market strategy once you've completed that deployment of spectrum? It seems like at that point, you would be very capacity rich. Would that be a good moment to maybe pivot back towards driving subscriber growth as opposed to being just mostly focused on ARPU growth? Thanks.

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

A

Well, on the second piece of your question, which is when that will be done, it's obvious that one of the real competitive advantage of Sprint will be capacity. So, meaning that's what we want to play as a strength vis-à-vis our competitors, which we already do by the way with the offers that we have implemented in the markets with, for example, the amount of data that we give for hotspot and all that stuff, which probably drives very differentiated offers for Sprint compared to its competitors. But it's obvious that we'll put more emphasis on that and I expect that it will drive gross adds in the future.

But when I look at it, I would say that, from a gross adds perspective, our share of gross adds is still 50% higher than our market share. So, which is quite significant, even which is quite good to be fair. The point is more that we have an higher churn than our competitors, as you all know, and one of the piece which is driving churn was we have [ph] a power (31:51) network. So, with these 2.5 GHz deployments, what I expect the most is that it will help us to close the gap from a churn point of view and then our net adds profile should be much better. And so, which means that it will be the right way to move forward in terms of related net adds profile moving forward.

In between, I guess that what we had said in this presentation earlier on is that thanks to all the investments that we have done, we are able to announce LTE Advanced on a national basis. Ando so, that's exactly placed to the question that you were asking which is – that by highlighting LTE Advanced, we are going to re-emphasize the quality of our network, this capacity benefit that we have, and this ability to drive more gross adds, but more importantly to reduce churn. From a...

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Brett Feldman
*Analyst, Goldman Sachs & Co. LLC*

Q

And then, on CapEx?

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

A

From a CapEx point of view, I guess that what we have always said is that we have two to three years of increased CapEx in order to cope with the deployment of 2.5 GHz and to cope with the deployment [indiscernible] (33:08) to the implementation of the network that we are seeing right now. And then, you should expect a slowdown of our CapEx investments within one to two years.

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Brett Feldman
*Analyst, Goldman Sachs & Co. LLC*

Q

Thank you.

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**Operator**: Your next question comes from the line of Jennifer Fritzsche.

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Jennifer M. Fritzsche
*Analyst, Wells Fargo Securities LLC*

Q

Thank you for taking the question. I just wanted to ask what you're seeing in the prepaid environments or competitive landscape? Both you and T-Mobile seem to come in [ph] lighter (33:35) than we would have thought on the prepaid side. And I know Cricket through AT&T has been more aggressive, but just can you comment on a little of the trends you're seeing there?

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

A

I guess, we see a market which is quite competitive. And so, you have seen the reports of our other competitors. Nevertheless, we continue to experience a very strong momentum in Boost, which is offset by losses in our other brands that we have de-emphasized. But as far as Boost is concerned, Boost net adds were nearly 200,000 before migrations and Boost gross adds grew year-over-year for the fifth consecutive quarter.

On top of that, our total prepaid churn has improved year-over-year for the ninth consecutive quarter. So, I really believe that the strategy that Sprint has implemented since seven quarters now, which is about expansion of our distribution, being more aggressive from [indiscernible] (34:35) point of view, driving family offers in order to reduce churn, is really paying off. And so, despite the aggressiveness that we see in the marketplace from a pricing point of view, from a device subsidy point of view, we have been able to drive quite well the growth of Boost.

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Jennifer M. Fritzsche
*Analyst, Wells Fargo Securities LLC*

Q

And [indiscernible] (34:56) should we expect fourth quarter trends then to show improvement sequentially or any [ph] kind of images (35:03) on the prepaid category?

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

A

We expect strong momentum in Boost to continue as we have experienced in the past few quarters, but we expect Boost – prepaid, sorry, to remain slightly negative for total – for fiscal Q3 2018 due to the impact of the other brands, as we have seen in Q2 before returning for total prepaid to growth in fiscal Q4 2018.

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Jennifer M. Fritzsche
*Analyst, Wells Fargo Securities LLC*

Q

Great, thank you.

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**Operator**: Your next question comes from the line of John Hodulik.

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John C. Hodulik
*Analyst, UBS Securities LLC*

Q

Great, thanks. Maybe a clarification and then a broader, more broader question. First, on the postpaid phone subs. Michel, there's the commentary or the answer to the first question or what the prepared remarks suggest that you're going to lose post – you expect to lose postpaid phone subscribers for the next year or so, or just sort of how you had losses this quarter after really strong momentum a year ago. Just how do you expect that to play out? And then, maybe just give – if you could give us some more detail on the 5G roll-out for first half of 2019? What spectrum are you going to building that mobile 5G on and how extensive of a build-out are we talking maybe by the end of the year? Thanks.

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

A

John, you want to take the second question first?

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

A

Sure. Hey, John. With regards to the 5G plans, we are very well on track. The tool that we're going to use to build our 5G network is [ph] using (36:38) Massive MIMO and the 5G spectrum that we're going to be leveraging is our 2.5 gigahertz spectrum.

So, we have already started building our Massive MIMO sites. We are very encouraged with the results we have seen so far. And we're seeing about seven times improvement in capacity, at least four times improvement in speeds, that bodes well – that bids well for when we add 5G. So, 5G for us, once we have this Massive MIMO sites built, will be a software and line card upgrade only, so no tower climbs needed. And we expect to launch in nine markets next year, and we have also announced recently our first 5G smartphone with LG. So, have good momentum. Results from Massive MIMO [ph] trials (37:39) looks very encouraging. In a couple of months, we will add the 5G software, we will be able to enable both LTE and 5G simultaneously on the same sites.

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

A

So, just to emphasize what John has just said on a – from a network point of view, I guess that – coming back also to previous questions, I guess, that we are in a right momentum moving from where we were to LTE Advanced today, which allows us really to unlock the benefit of our network and 5G kicking in H1 2019. So, that should help us to really reposition the network in a proper manner and take the benefit of that in order to add some impact on churn moving forward.

Of course, as we all know, there is always a lag in between what is delivered from a network point of view and perception received by the customers. But we expect that to improve in the next coming months and quarters. And you might expect from us to take some marketing initiatives in that field.

Coming back to your first question, in terms of postpaid phone net adds, I guess that even if we don't give quarterly guidance, it's probably safe to say that fiscal – you should expect, sorry, likely similar results in fiscal Q3 2018 as we do expect some additional seasonal churn pressure of 15 basis points sequentially, partially offset by a seasonal lift in gross adds. But as I have already said on different occasions, we continue to expect to be positive for the full fiscal year.

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John C. Hodulik
*Analyst, UBS Securities LLC*

Q

Okay. Thanks, Michel.

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**Operator**: Your next question comes from the line of Matthew Niknam.

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Matthew Niknam
*Analyst, Deutsche Bank Securities, Inc.*

Q

Hey, guys. Thanks for taking the question. How should we think about the magnitude or volumes of customers who are rolling off these promo discounts next quarter relative to this past one and when do you expect this to peak? And then, as we just think about this in terms of retention rates, any early data that you can share for customers – seeing that those reset – how many of these customers are you actually able to hold on to? Thanks.

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

A

So, as you can expect, we don't give precise figures on these type of [indiscernible] (40:02) tell you that the customers on introductory price plans, such as our 50% off and Unlimited Freedom with free line continued to roll off of these promotions over the next several quarters. So, it was something which was spread during the [ph] past few months or (40:22) past coming quarters as customers joined Sprint via these promotion over time. So, there is not a real peak, it – this is spread over different quarters.

These promotions, as you remember, were structured to have a low introductory rate that would then step up at a later date, very similar to what does exist in the cable industry. And while we have seen some incremental churn pressure, that I have reported – addressed earlier which is one of the reason of the increase in churn in between last year and this year, many customers do stay up to the promotional period and so it has [indiscernible] (41:02) revenue trend. So, on one side, it's a kind of self-inflicted churn which explains part of the gap that we have with our competitors, but not all the gap. There are some structural things that we have to solve. On the other side, it clearly has had a positive effect on our wireless service revenue and that explain why we have been able to be wireless service revenue positive starting this quarter.

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Matthew Niknam
*Analyst, Deutsche Bank Securities, Inc.*

Q

Got it. Thank you.

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**Operator**: Your next question comes from the line of Ric Prentiss.

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Ric H. Prentiss
*Analyst, Raymond James & Associates, Inc.*

Q

Yes, hi. Thanks for taking my question. Michel, I wanted to go back to what you were talking about. Obviously, churn is the big item. Network quality is the point you're trying to make. I think you mentioned that 50% of your sites had 2.5 gigahertz deployed a year ago. Can you help us understand, have you seen better churn in those areas where you have the 2.5 GHz already deployed or where you have the tri-band already deployed?

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

A

Yeah, [ph] that's a yes (42:07). And as you know, we have early indicators that we are looking at for analytics which is what, I guess, we have presented to you at different occasions, which is network QoE that we measure on a – at the customer level. And it's obvious that in the regions and places where we have been able to roll-out a 2.5 GHz, we have a better network QoE, which is a pretty good proxy for impact on churn moving forward.

So, the answer is definitively yes. That's why we are accelerating our investment in network where we have 50% one year ago, we have 70% now. We expect, by the end of the year, to be close to completion. So, which means that then all our customers will really get the benefit of it. Of course, during this year, as we made all those improvements, that has had some impact on the quality of our network, but that will be over in the next coming months as well. So, I truly expect that it will add a [ph] significative (43:12) impact on our churn.

When you look at the churn, I mean, it's all about network experience and these investments. Second is around customer experience, and all the investment that we are doing in the digital area in order to really be able to step change the customer experience that we deliver to our customers, and then to have the right offers in place which is the case because we continue to have the most aggressive offers in terms of unlimited offers in the marketplace.

So, I guess that we have the right setup moving forward. We are in this transition. What is positive is that we start to see early signs that our strategy that work. When I look at the mix of customers that we are attracting, more prime. When I look at the MRC that we can capture, [ph] high-yield (44:01) MRC compared to what we were doing in the – in previous years. So, meaning, more GAVA. Now, we need to fix churn. We still have a churn which is twice higher than most of our competitors. And so, that's what we need to focus on in order that in the mid – long run, this growth profile remains healthy and sustainable.

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Ric H. Prentiss
*Analyst, Raymond James & Associates, Inc.*

Q

And the other question I have, with the weakness possibly in the economy, have you looked at your customer base to see how sensitive – you mentioned, they're becoming more prime – but have you looked at to see how sensitive is your customer base to general economic trends or rising interest rates?

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

A

Well, I don't – so, of course, let's say, the economy went through different cycle in the past years. I don't really see major risk there or major weakness compared to any other carrier. The only piece that probably we see today is more early signs of impact of the merge discussions, so – which is not related to the economy. But, of course, let's say, [ph] we've traced articles every day (45:09) on the merge discussions, that's put a little bit of pressure on our base as well as on new customers who have so many [indiscernible] (45:20) pending merger is impacting stock traffic due to consumer confusion. So, that's more of this piece rather than any impact of the economy slowdown on our customer base.

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Ric H. Prentiss
*Analyst, Raymond James & Associates, Inc.*

Q

Very good. Thank you.

**Operator**: Our next question comes from the line of Simon Flannery.

Simon Flannery
*Analyst, Morgan Stanley & Co. LLC*

Q

Great thanks a lot. Good morning. Andrew, I was wondering if you could just talk about you said more efficient marketing spend. Can you just elaborate on what exactly you're able to do and just how should that trend into the December quarter given the holiday season?

And then, Michel, there's been a lot of focus on the wireless business, of course, but we haven't talked much about Wireline. Could you give us some perspective on what steps you're taking there to improve the growth and profitably profile? Thanks.

Andrew Mark Davies
*Chief Financial Officer, Sprint Corp.*

A

Hey, thanks there for the question, Simon. So, on marketing spend, this is another feature of our use of digital and analytics within the business. So, basically, we're able to do much more of a, if you will, econometric analysis of our marketing spend and ensure that we're getting the right band for the buck. And while, as you alluded to, if you will see a slight increase in absolute marketing dollars as we go through this upcoming holiday period, I think we're still broadly confident that the year-on-year improvements that we're see in marketing spend through the first half of this year will continue right through into the second half of the year as well.

Simon Flannery
*Analyst, Morgan Stanley & Co. LLC*

Q

So, is that by more digital, less TV, or what's the kind of big features of it?

Andrew Mark Davies
*Chief Financial Officer, Sprint Corp.*

A

No, it's – yeah, there's an element which is more digital and less TV, but it's just better placement of our marketing spend. So, just targeting the marketing spend where we can get a much better band for the buck.

Simon Flannery
*Analyst, Morgan Stanley & Co. LLC*

Q

Okay. Thanks.

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

A

And then – so, on your second question, Wireline. Wireline business helps the wireless business compete on the multi-element proposals in the business space, as you know. Our Wireline adjusted EBITDA of minus $20 million improved $22 million sequentially and $9 million year-over-year. Our – you know quite well, our strategy which is all around [ph] shrink (47:55) to grow meaning shutting down the legacy voice and TDM-based IP business. Voice are down complete but TDM [ph] to a Ethernet (48:05) IP migration is still in progress, should be completed in the next coming quarters. And then, putting all the emphasis on the strategic IP/MPLS which are actually growing. So, we are just in this transition which has been highlighted in the previous quarters and which will continue for the next coming quarters. But I guess that it's a great and critical asset for Sprint moving forward in order to compete in the business space.

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Simon Flannery
*Analyst, Morgan Stanley & Co. LLC*

Q

Great, thank you.

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**Operator**: Our next question comes from the line of Michael Rollins.

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Michael I. Rollins
*Analyst, Citigroup Investment Research*

Q

Hi. Good morning. I was wondering if you could talk a bit about your VoLTE migration. What's happening in terms of steps you're taking? What's required to optimize the performance for the customer? And is there a deadline that you see in the future that you have to hit relative to your expectation for device availability, and that includes the current CDMA features? Thanks.

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

A

Hey, Michael, John here. We have already launched a soft launch VoLTE in 35 markets out of the Sprint's 99 markets. And in a couple of weeks, we will soft launch more. The strategy is to have it commercially available in 2019. We're trying to transition our voice services from CDMA to VoLTE carefully. We do have a pretty good CDMA voice network today and, as you know, we have ample capacity. So, there is really no rush to [ph] refarm Spectrum (49:50) for VoLTE.

But at the same time, though, with Voice over LTE, with the most advanced [ph] codecs (49:58) that we're using, voice quality is much improved as well as our customers are able to simultaneously use voice with data at the same time. So, there are pluses with it. So, in the next few months, we will continue to soft launch the markets. What that means is that customers with phone set have a VoLTE capability will be able to choose on their own their voice service they want to use, whether it's CDMA voice or Voice over LTE. And then, at a certain point, probably in 2019, we will announce commercial availability and then make Voice over LTE our primary voice service. Our phones in the foreseeable future will continue to support CDMA and CDMA as voice network will continue to exist until we make a smooth and seamless transition.

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Michael I. Rollins
*Analyst, Citigroup Investment Research*

Q

Thanks very much.

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**Operator**: Our next question comes from the line of Jonathan Atkin. Jonathan Atkin, your line is open.

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Jonathan Atkin
*Analyst, RBC Capital Markets LLC*

Q

Sorry about that. So, I had a question about the network upgrade, and you talked about selling out 2.5 GHz spectrum. Do you feel like you have adequate macro density, macro cell density, or do you need to be adding more macro sites to get to the quality standards that you're hoping to get? And I wonder if you can maybe talk a little bit about small cell deployments and milestones, use of strand mounts, things of that nature? Thank you.

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

Sure. For in footprint coverage, we are – the reason why we're doing this upgrades, Jon, is to make sure that we fortify and densify the capabilities and capacities of our in footprint coverage. That includes adding a lot more 2.5 GHz spectrum to our existing towers. To supplement that and complement that in places where we have capacity hotspots or coverage [ph] holes (52:17), we are using small cells and strand mounds. And I think, like what Michel said earlier, we have made more progress with small cell build out in the last six months than we have two years ago. So, we have plowed this area a lot and invested and so we're starting to see good momentum. We had 21,000 small cells on air including great progress we're making with [ph] Altis and Cox (52:41) for strand mounts. So, they will continue to fortify the in footprint coverage.

As of out of footprint coverage, we are looking at adding new towers to expand our coverage into neighborhoods that have outgrown our legacy coverage. In the meantime, we are also benefiting from the roaming agreement we signed with T-Mobile that actually they have a slightly bigger out of footprint coverage and so we're able to leverage that as well as we are looking at building more towers to expand our own footprint organically.

Jonathan Atkin
*Analyst, RBC Capital Markets LLC*
Q

Thank you. And then, you talked about Massive MIMO. And I wonder if you could maybe be a bit more specific in terms of like where we are, is this 4T4R, 8T8R, or how many channels are we aggregating when you use that term in the context of 5G?

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

Sure. Massive MIMO that we're deploying is 64T64R. And in the context of 5G and LTE, what we're doing with 128 antenna elements is to physically and logically separate the antenna elements into two halves; half of it for LTE, and another half for 5G. You can get away with this for Sprint because we have enough spectrum to actually power up both halves of the Massive MIMO antenna and this is how we're able to use the same radio hardware to enable both LTE and 5G simultaneously using the same Massive MIMO antenna. So, lots of antenna elements that allows us to run this in split mode to support both LTE and 5G. And so far, like I said earlier, the results have been extremely encouraging. The form factor is actually smaller than what we have deployed today with 8T8R because it's a one box unit that has the radio and antenna all in one box.

Jonathan Atkin
*Analyst, RBC Capital Markets LLC*
Q

Thank you very much.

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

Yes.

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

Thanks, Jon. That's all the time we have for questions. But before we end the call, I'd like to turn it back to Michel for some closing comments. If you have any additional questions, please reach out to Sprint Investor Relations team. Michel?

## Michel Combes

*Chief Executive Officer & Director, Sprint Corp.*

Thanks, Jud. I want to thank everyone for joining us today and for supporting Sprint. Our second quarter results demonstrate continued execution of our plan to balance customer growth and profitability while improving network performance. We continued to deliver retail net adds for the fifth consecutive quarter. We improved profitability, delivering net income for the fourth consecutive quarter, and operating income for 11 consecutive quarters with our highest second quarter adjusted EBITDA in 12 years.

In addition, we are aggressively executing our Next-Gen Network deployments to deliver a Network Built for Unlimited while building the foundation for our mobile 5G network by deploying game-changing 5G technologies this year such as Massive MIMO. We continue to enhance our value proposition and continue to transform our cost structure and customer experience with digital and advanced analytics. Our postpaid gross adds share remains well above our market share and we are confident that we can improve churn over time with our LTE Advanced and our soon-to-come 5G network as well as customer experience improvements.

Thank you and have a very great day.

**Operator**: Thank you. This concludes today's conference call. You may now disconnect.