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EDITED TRANSCRIPT
VZ - Verizon Communications Inc at Goldman Sachs Communacopia Conference

EVENT DATE/TIME: SEPTEMBER 17, 2015 / 12:50PM GMT
So we are going to go ahead and get started here with our discussion with Lowell McAdam, the Chairman and CEO of Verizon Communications. Lowell, welcome back to Communacopia.

Let’s jump right into it. There has obviously been continued focus from investors on what appears to be an ongoing competitive environment in the Wireless space. It seems like you see new offers. It feels like it may be more of a balanced four-player market than we’ve seen in a while. Sitting on top of the industry, what is your view on the health of the Wireless market right now?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

So as I was saying, good morning. As I listened to the conference and read some of the notes from yesterday, the sense of optimism I thought was significant between last year and this year and we see that as well. If you look at the industry overall, the telecom industry overall and then we can talk more about Wireless obviously, but see usage going up significantly and Wireless as an example is up 20 times in the last five years.

If you look at investment levels, people are continuing to invest. We’ve invested $17 billion to $18 billion over the last decade and we are going to continue to do that now. You see players offering innovative things like Apple with just their leasing program, with Google with Fi. With some of the other WiFi based products that are out there. You see the cable companies now getting engaged here. And all of that is bringing innovation to customers.

As I look forward in things like Internet of Things, I’m sure we will talk about video. There’s a lot of disruption going on and a lot of new products being brought to market, products like Go90. So I think those are all highlights of a healthy market. And just last night, I’m sure we will chat about that with Altice buying Cablevision. They don’t -- people don’t typically jump into markets that are sick and in trouble. They jump into markets where there is still a lot of opportunity.

So I feel good about the industry. So now let’s take your question from the Verizon perspective, if you look at us through our second quarter, we’ve seen great growth rates, over 1 million net adds. We’ve see 800,000 smartphones. We’ve seen over 300,000 net phone additions. A lot of tablets are coming into the marketplace. I’m very excited about our video strategy. The skinny bundles was one part of it, the Go90, Mobile First, over-the-top video I think is going to be an important product. And as a look forward we announced last week at CTIA our 5G initiative. And when you see the things that 5G will bring to the marketplace, open up an entirely new wave of innovation, I’d say those are all signs of a pretty healthy industry and Verizon remains at the top of it, I think, on the US side.

Brett Feldman - Goldman Sachs - Analyst

You’ve historically done very well targeting the more profitable end of the market. Is there anything about your go to market strategy that’s changing or evolving as you look at some of the offers your competitors have out there?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, let’s start with the brand. We just launched a week ago a new Better Matters campaign and there’s two major aspects to that. One is simplicity and one is reinforcing the network. So we are going through, John Stratton and his team and Marni, as she brings out new products, are being very focused on simplicity and transparency with customers because if I am critical of the industry and I think one of the players has capitalized on that, is we got a little bit too complicated and a little bit too cute. So simplifying that is part of the Better Matters.

The other thing that we are going to go back and remind customers and if you recall we talked about this on the stage, that people talk about networks being better and catching Verizon, but as we transitioned from voice to data and now to video, every time you do that transition Verizon comes out on top.

If you look at the latest RootMetrics study, I think there is in the ballpark 250 markets that they measure. We won approximately 230 markets. The next company won well less than 100 markets and the next company won around 30. And the number four carrier won zero. So the differentiation of the quality of networks as you send more and more video over those networks is becoming very clear again. So that campaign about Better Matters I think resonates with customers and we see it, Brett, in our churn metrics.

The churn for second quarter, I think if you look at the 15 years we’ve been in business, 60 quarters, it was in the top seven. So the loyalty of our customer base is very strong. So while there’s a lot of innovation, while there is a lot of different offers in the marketplace, the bottom line do you measure our customers happy with us as a carrier? I think they are. We are showing could growth and we are showing good profitability. So you’ve got to cut through a lot of the smoke and get to the bottom line.

Brett Feldman - Goldman Sachs - Analyst

So it sounds like metrics like churn and margins probably are paramount over say raw net add numbers for the business?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, we try to pay attention to the profitability of a customer. It’s easy to measure it by saying well how many smartphone customers do you have? Well you have a flip phone customer that’s paying you $50 a month and not using your network a lot, that’s a good customer. So we don’t poo-poo that sort of lower end of the market. But there’s a lot of legs and ways you can extend the profitability of a smartphone customer with a tablet and with other offerings like Go90.

So we need to make sure that we take care of both ends of the market but we are not going to chase net adds just for the sake of chasing net adds.

Brett Feldman - Goldman Sachs - Analyst

All right. You mentioned video and I would agree, I think the video market is undergoing some pretty interesting changes. From where you sit, what does Verizon see as the most significant transitions happening in the video market now and then we can talk about some of the things you are doing to position for that.

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes. Well, there’s clearly a pent-up demand to get away from 300 channel bundles and there’s two ways I think you can do that. One is through the skinny bundles, the custom TV that we launched. Right now about 30% to 40% of our adds are coming in on the skinny bundle, so that shows you customers want that kind of service. And it allows for a little bit better profitability for us and it allows the customer to right-size their budget. So that’s clear.
The second one is the shift away from linear to over-the-top. Now we see that in two ways. When I first became the CEO about five years ago now, we were selling roughly equal amounts of broadband and FiOS TV. Now we are in the mode where it’s 2 to 1 and growing. It has diverged significantly. So customers are saying if I have to take 300 channels I’m going to go over-the-top. I’m going to do the Netflix and the Hulu and the other things that you can do.

The other phenomenon, Brett, is, and Marni talks a lot about this, is 40% of millennials do not and have never had a TV in their home. And another 20% have said they’ve got it but they don’t use it that much and they are considering cutting it. But what you see and you see it in the volumes of our networks, that’s that 20 times growth, is they are watching it over mobile and they are watching digital media versus broadcast kind of media.

So that’s why we use the term inside the business that we are skating toward where the puck is going when we launched this Go90 service, which is a mobile first service because we think that is going to play to were the market is going with the millennials in particular.

Brett Feldman - Goldman Sachs - Analyst

So you talked about some of the embedded aspects of the industry that are being disrupted. You are a top-five pay-TV provider meaning that FiOS TV is being disrupted by these trends. You seem to be trying to get in front of it. Can you talk to me about what your realistic expectation is for that business and how some of your new initiatives like custom TV fit into that strategy and then we can move on to Go90.

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, okay being top-five you can view it as a good thing or a not so good thing and our view is that if you don’t disrupt yourself somebody else is going to come in and disrupt you. So that’s why we bought OnCue to begin with, which was really an over-the-top broadband into the home.

We are really embracing -- we sell a lot of FiOS every year but we are embracing the broadband service because that’s where the market seems to be going. So we are offering higher speeds. We are selling a lots of 50 Mbps. We can easily do up to 500 Mbps. We can easily do all the way up to a gig if we need to. We are selling more 150 Mbps packages every day to our customers today. So we are going to embrace the broadband.

We will continue to support the linear TV as those customers want it but it’s very clear to us the market is moving more toward broadband, skinnier bundles and over-the-top.

Brett Feldman - Goldman Sachs - Analyst

How does custom TV fit into what you are dealing with that (multiple speakers) market?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

That’s the skinny bundle offering for us and we are working with the content companies now to try to break some of these big offerings where you have to take 10 and 12 channels; when you buy one you have to get all these others. I think the market wants us to do that and so we are going to continue to push for that.

Brett Feldman - Goldman Sachs - Analyst

ESPN is suing you over custom TV. Any update on how that process is unfolding?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I guess I would just say there’s always a lot of dialogue. If you’ve noticed ESPN is part of our Go90 offering. We sell a lot of Disney, sell a lot of services to Disney and we do a lot of advertising with Disney, so we are hopeful that we will be able to work through this. I won’t comment on the specific aspects of the lawsuit but the partnership is still there and I think there’s a win-win to be found.

Brett Feldman - Goldman Sachs - Analyst

Do you see the FiOS video subscriber base as being something you would expect to continue growing or are you really focused on driving profitability to the broadband product?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I think we need to do both. I think we can continue to grow FiOS. It is such a positive product. We’ve got some great markets. By selling the three satellite properties that we sold we can concentrate our firepower in the Washington to Boston corridor. There’s some good markets there that we can expand into under the right circumstances. So I do believe that FiOS profitability will continue but I also believe the trend to more broadband and less linear TV is probably likely.

Brett Feldman - Goldman Sachs - Analyst

Are right. I want to get onto Go90 now, which you described as a mobile first video service. So I guess the first question would be, what do you mean by a mobile first video service versus the video services we are accustomed to seeing?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, so it is not based on streaming your big 4 channels and 300 channel bundle. It is very specifically directed toward millennials and what their offerings are. So as I think about it, there will be some sports, which will be streamed using our multicast technology, so the network will be able to support it. The poster child for that is our relationship with the NFL. We’ve already announced some college sports. There will be more coming as we approach the commercial launch later in September.

There will be hour long shows and half hour-long shows that you can time shift and watch whenever you want, similar to Netflix, Hulu sort of offerings. But the real driver here is millennial content that frankly a lot of us in the room are not familiar with. So when we bought AOL we got Huffington Post. The Huffington Post Snackable content will be on there. VICE News will be on there. We’ve announced a partnership with DreamWorks and AwesomenessTV. Jeffrey Katzenberg and Marni are working to bring some exclusive content to Verizon. We’ve literally contracted for hundreds of hours of exclusive content -- they are very episodic -- that will bring people back to the service more and more.

So it is not your typical big 4 news at six o’clock sort of streaming what you get in your home onto your mobile device. It is very targeted to the millennial.

Brett Feldman - Goldman Sachs - Analyst

It sounds like what your saying is you view this as a distinct market. In other words, it’s not an extension of fixed video. You think that the way people interact with video on mobile devices is entirely different. Is that a fair conclusion?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, it is. And the thing that we have tried to do with Go90, which I think is going to be very exciting to people, is we've merged the aspects of social networking that people like with the video watching techniques. So the best example is if you are watching a sporting event or a particular show, you can actually go in and clip and share that with others. So if I see something that I think is awesome I can send it to you and you can send it to others.

The sports networks love that because they think they will be able to reach more people that aren't having the time to sit and watch an entire game. The millennials, they do that instinctively through Facebook and Twitter. They will now be able to do that on the video side through Go90.

Brett Feldman - Goldman Sachs - Analyst

There's obviously a lot of ways you can already watch video on a mobile device so listening to what you are saying it seems like premium content is a big part of what you are doing. Is that a fair way to describe how you are differentiating? How else do you think you can make this a go to location for people who want to watch video on a mobile device?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, one of the other aspects of the service which I think is interesting is if you and I are friends and I know you are great at finding comedy or a particular genre, I can set Brett up as one of my people to follow and when you set up your profile and you line up your shows, I get to see that. And there will be what they're calling crews on this where I can easily share with people that I interact with a lot and get content from them.

So it's not only the type of content, it is how you interact with the content that I think is going to be a hit with this generation.

Brett Feldman - Goldman Sachs - Analyst

Can we talk a little bit about the revenue models that you expect from Go90? I think the initial launch of it is free, so that would imply advertising?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, so there's a number of ways that we will see monetization within Verizon and then we really sat this up as a separate business so the business itself will have a different set of parameters. So within Verizon obviously the more people watch, the bigger the bundles they buy and that's what we are in business for, so data packages should go up, ARPAs should go up.

Within the business itself, they will be selling subscriptions to some of these services. For example, these large -- there's large concert venues that we will offer for a couple of dollars as an example. You can tune into the One Republic concert that happens to be in Miami and here in New York and with the capabilities of the devices these days, you will actually have a pretty good experience.

Now through AOL we've got a great capability around ad insertion and if you look just last week AOL bought Millennial Media, which is good at inserting apps -- inserting ads -- within the application. So we will know who the customer is, what their viewing habits have been and then we can almost back to this nirvana of N=1 marketing. Instead of doing broadbrush marketing we can go in and specifically target the individual with the ad.

So if Tim were here, if Marni was up here they would tell you that the advertising agencies are very intrigued at the capabilities that Go90 will bring to better target that millennial segment.
Brett Feldman - Goldman Sachs - Analyst

So just to sort of summarize what you are launching here, this is a distinct service. That was your point. This is not a Verizon Wireless exclusive offer. It’s something anybody with a mobile device can take advantage of and it does seem that advertising revenues at the outset you would expect to be the principal source of revenue generation and then to the extent your own customers are consuming on your network, they pay you for data like they would any other video consumption.

When are you going to be launching this? I think you have a soft lunch going on now?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, we have about 25,000 customers on it now. We’ve grown the beta testing over time. We’ve gone out with invitations to about five million of the Verizon Wireless customers and we will be adding them onto the platform this month and we expect to go live with it at the end of September.

Brett Feldman - Goldman Sachs - Analyst

Great. So can we talk about some of the other emerging opportunities you see in your wireless business? I think you mentioned Internet of Things. What’s the right framework for the investor to think that the size of that opportunity to Verizon?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, well when I talk about Internet of Things, I’m talking about things like intelligent cities, healthcare, transportation systems, the electrical grid, just to be clear. Obviously the connected car is a big thing.

I think investors should expect to see the connections on the network go up dramatically and you can do a lot of these connections even with 2G or 3G but when you get to 5G, that opens up even more because the latency and the throughput there is so high in 5G. That gives you the ability to do things like autonomous cars and to do healthcare where you are doing remote surgeries and that sort of thing so that the latency of the network is not at all a factor.

This year so far the first half of the year we’ve done I think around $320 million of revenue, so on the scale of Verizon it’s not a big deal. But we are generating by far the largest amount of revenue from Internet of Things of any company in the US. And if you look at some of the projections from Cisco and others on this topic, you see huge contributions to the economy and pretty significant volumes for us.

So I think it will be a meaningful line item on the budgets and our results for investors to look at in 2017.

Brett Feldman - Goldman Sachs - Analyst

If we think about what you were just talking about which is video over the mobile network, if that really turns into the principal long-term driver of usage, the long-term driver of revenue growth, that is a very capacity intensive way for someone to interact with the mobile network.

Can we talk about what you are doing to make sure that your network infrastructure is evolving to stay in front of that?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, so when we did the AWS auction, we were pretty clear about where we wanted to buy spectrum and where we felt we could increase capacity of the network by densifying, deploying small cell technology. I would tell you in the six months or whatever it’s been since the auction we actually
feel even more strongly about the viability of small cells. We’ve deployed them in every major urban market, Chicago, San Francisco, many, many places in New York City and the capacity advantage that we have gotten has been better than advertised.

Now as you go forward, we are already at 60% of the traffic is video -- capacity is video today and I think that will move more towards the 90% as we move forward. We will always need more spectrum, so I get asked the question a lot, are you going to participate in the 600 auction which is coming up sometime next year? I think it is likely. There’s still a number of rules that need to be defined and as those rules are clarified we will be able to clarify our position, but if there is a good price per megahertz POP for us to purchase, I can see us playing in that in order to support the capacity needs of video going forward.

Brett Feldman - Goldman Sachs - Analyst

We typically think of that spectrum as being more helpful in creating coverage than capacity. You don’t have a coverage problem. That would imply that dollar for dollar it may not be as valuable to you as the licenses you most recently purchased?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, I think that’s right. The 700 gives us what we need. Those of you that have heard me talk before I liken good spectrum management to building a wedding cake and when you’ve got that strong base of 700, you are really well set. Having a second base isn’t as valuable as building the tiers in the higher spectrum. So that AWS is clearly more interesting to us but depending on the price per megahertz POP, you may take something that’s not quite as ideal and you may use it. So it just really depends on how the auction goes.

Brett Feldman - Goldman Sachs - Analyst

So I’ve got to ask the question, there is some unused AWS out there. It’s mostly owned by Dish.

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Is there? I hadn’t heard that?

Brett Feldman - Goldman Sachs - Analyst

It’s a real secret. You’ve been asked the question in the past, is Dish a viable partner for you from a spectrum standpoint?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, I think you have to bifurcate their business. I think they’ve got a very good satellite business. Charlie has built a great business there. But it’s not consistent with the strategy that we just laid out of where we see the market going on more of a mobile and a digital service versus linear. So it can be a great business but it doesn’t need to be part of Verizon.

The spectrum that he has, we’ve had discussions about how we can provide him megabytes and he can pay for it with spectrum. Those sorts of options are still open to us. But to get the spectrum by buying the entire company isn’t something that we are interested in.

Brett Feldman - Goldman Sachs - Analyst

So if you could come up with commercial terms on the spectrum, that’s the discussion you would be happy to have?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Sure.

Brett Feldman - Goldman Sachs - Analyst

Okay. How do we think about other opportunities to bring more spectrum into your network because I think we all accept that densifying the network is a completely viable way to add capacity but the history has shown that as traffic grows it is usually helpful to identify unused spectrum you can bring in. What else do you see on the roadmap over the next several years if not decade including your discussions with the FCC about how you get spectrum that fits the way you are designing your network going forward?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, I think Tom Wheeler was out at CTIA last week and he outlined several blocks of spectrum that the government has today that he would like to see more clearly identified and moved into commercial markets and I salute him for that. I think we are all supportive of that. It takes a while to do it so you are going to have to move on that sooner rather than later. Typically it takes about 10 years from the time it’s identified until it gets through the process and gets into the carrier’s hands. So I think the more quickly we move on that the better.

There are lots of spectrum sharing techniques out there. As you know there’s a lot of spectrum tied up in the military satellites that are flying overhead that they pass overhead once or twice a day and there’s lots of opportunity to do spectrum sharing in the meantime. I think we need to explore that. I think there’s a lot of good compression techniques that are being explored and will continue to be explored, which will allow us to carry more capacity.

The 5G standard that we are working through literally increases throughputs by about a factor of 10 over where we are today, so all of those things together, Brett, I think give us a pretty optimistic view of capacity management and spectrum going forward.

Brett Feldman - Goldman Sachs - Analyst

But in the near term it would seem like small cells are going to be a big thrust of where you are deploying capital?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, that’s our -- we feel very good about that and it’s been a mix. We’ve got a lot of good spectrum. We’ve bought recently another $10 billion of very good spectrum and so it’s a mix but we think that the small cell technology really takes a lot of pressure off.

Brett Feldman - Goldman Sachs - Analyst

So we’ve been talking very high-level about where you are taking the business but obviously we have day-to-day considerations. So first if we just think about the immediate priorities in the wireless business, you are out there. You have about 16% penetration of installment plan phones. As you talk to your operating teams on a daily basis, what are they focused on? Is it getting people into the right devices? Is it upgrading customers who have not yet upgraded to a 4G device? How are you trying to make sure you hit the near-term objectives you’ve established for the business?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I think the first one and I have alluded to ready it already is simplification of the experience for the customer. And that’s part of the reason, Brett, we moved from a subsidy model and an equipment installment plan to more equipment installment because the experience for the customer and the difficulty for our reps in the stores to manage that was just too difficult. So I think simplification is number one.

The second thing is the more folks we move into the smartphone category, the more I think they enjoy all of the services that a wireless company can offer them and therefore they do remain more sticky. As I said, it doesn’t mean we don’t like the basic phone customer but moving them up and then giving them the other services like tablets and exposing them to things like Go90.

So it’s basically make sure they had a good experience then get them into the best device match for them and then give them the exposure to the services that we think will make them more loyal to Verizon.

Brett Feldman - Goldman Sachs - Analyst

And what do you think about Apple’s decision to get into the installment plan business?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, I think it makes perfect sense for them. They would love to have people stay on iPhones forever. And if I look at it from our perspective, from a cash flow perspective it is relatively positive, marginally positive, I guess, so it’s not a threat.

It’s similar -- I think about it the way I think about bring your own device, which we’ve been doing for quite a while. Apple today is a very small piece of our distribution, so it’s not going to shift the way we do business in any way. Right now it doesn’t look like a threat to us. Now we have to pay attention over time and see how that evolves. But I would say right now it’s a positive if anything.

Brett Feldman - Goldman Sachs - Analyst

I think AT&T indicated that they have something like 10 times as many stores as Apple, suggesting that maybe Apple was only 10% of distribution. Is that a comparable number for Verizon?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, they are single digits for us.

Brett Feldman - Goldman Sachs - Analyst

Are you at all worried that they are selling unlocked phones?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

No I'm not actually because every time there’s been a level playing field, and I would point you back to local number portability, everybody was, wow, you are big. You're the target. Shouldn’t you be worried about people being able to port their number? Hey, that's competition.

So I think the churn numbers, our RootMetrics numbers and as you look at the experience as you drive more and more toward video, the things that are going to drive the network are not things like whether Apple is selling a device on a leasing program or not. It’s going to be how well does your network perform when you need it.
Brett Feldman - Goldman Sachs - Analyst

Some of your competitors are actually leasing versus installment plans. Does Verizon have a view on whether one of those models is better for the Company or not?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I think for us -- I really can't comment on whether it's good for others or not. But I think for us it complicates the sale and I think that's the big thing for us is simplicity at the point-of-sale. So even if you go into other stores that lease, they do the sale and then they hand you off to somebody else who does the leasing. And that's kind of a cumbersome process and I think from an internal perspective leasing can complicate the balance sheet a little bit.

So I guess I would say we'll have to see were the market goes. I don't know why the market would like leasing payments versus equipment installment payments. A payment is a payment. But we will watch it. But I think we are not good to push in that direction because of the complexities.

Brett Feldman - Goldman Sachs - Analyst

So you can do it if you ultimately decide it's the right thing for your customers -- (multiple speakers)

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

If you wanted to sure you could do it but --

Brett Feldman - Goldman Sachs - Analyst

So we sort of think about some of the areas of focus you just talked about, you are still working to get the right devices, upgraded devices into your customers' hands and we know that can impact the way financials are presented for wireless carriers, particularly when you are moving into installment plans meaning sometimes the ARPUs will come down, the installment billings go up.

You are also very focused on building out some new businesses that have a lot of long-term potential but aren't necessarily contributing to the business today. And so as we sit here and we think about maybe the near-term trajectory of the business through the balance of this year and through next year, what's the right framework for thinking about the growth of Verizon during that period of time?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Yes, so there's a couple of things going on in the model that I think you talk about and then sort of the trajectory sort of falls out.

So equipment installment plans is a big shift from service revenue to total revenue. We will be securitizing some of that debt. The banks have been very supportive of it but it changes the profile of your cash flows. If you look at the three properties that we sold, California, Texas and Florida, very profitable properties for us and they will do well with Frontier. But we felt we needed to move those into someone else's hands so that we could focus on that Northeast corridor.

You mentioned Go90 and AOL. We are funding those heavily and investing more in things like Millennial Media so the framework of our business as you go from 2014 and 2015 to 2016 and 2017 is changing. We are in one of those transitional periods.
So as I look at our overall profitability and earnings per share, I see comparables between 2015 and 2016 are going to be very different. The models are different. So I see a plateauing, if you will, between 2015 and 2016 and then I see 2017 we move back into the growth trajectory.

So it's a little bit -- in chatting with the team -- it's a little bit of our FiOS moment, if you think about it. When Ivan said you know we've got to shift the framework of this business off of copper and onto fiber, we are shifting the framework of this business more onto digital media than our traditional services, so that's why the frameworks change and the comps are going to be a little difficult for us in 2016.

**Brett Feldman - Goldman Sachs - Analyst**

So we will get clearer guidance later but you are basically saying because of all those factors the run rate of earnings we see in 2015 is approximately the right ZIP Code for 2016 and then you are off to the races after that?

**Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO**

Yes, that's our belief.

**Brett Feldman - Goldman Sachs - Analyst**

Within that you had talked about a focus on reducing costs sort of as a follow-on to the Frontier transaction. Can you give us an update on where you are with regard to that cost-cutting initiative and maybe just a bigger picture view on underlying operating margins in the business outside of some of the transitional stuff you cited?

**Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO**

Yes, that’s one of the main focus areas for John Stratton is to not only reduce the overhead after the three properties go but just generally retool and reorganize the Wireline side of the business and we gave him the wireless side of the business here roughly a little less than a year ago at this point and he is on the same path there.

So we completely restructured our network and service provisioning organization and really created a factory that you think about where it’s Bobby Mudge’s job to establish the network, maintain the network and then do the provisioning when services come through. We've seen dramatic cost reductions as a result of that.

Changing spans of leadership -- our mean time to prepare is coming down, our time to install is coming down, so we've been able to take some significant costs out of the Wireline side of the network. He’s looking at the same sort of process improvement and the simplification that I mentioned on the wireless side, so I see lots of opportunity to improve the bottom-line margins on both the Wireline side and the wireless side of the business. But again that will all be part of that transition as you begin to invest in things like cell densification and things like that.

**Brett Feldman - Goldman Sachs - Analyst**

Let’s go back to something we were talking about earlier which is when we were discussing the FiOS business. Once you complete these transactions with Frontier you are going to be left with what you described as sort of the Washington to Boston Corridor. That will be the hub of your Wireline footprint. It is a substantially fiber optic FiOS footprint. And you have a new competitor coming into the New York market in the form of Altice taking out Cablevision.

How do you think about the strategic significance of that piece of your Wireline business to your strategy as you go forward?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, we've talked a lot already about broadband being so important to customers as they go forward and I think the ability for a customer to seamlessly move content back and forth between wireless and Wireline is important. No one has come up with the killer application, the quad play application. Quad has really been more of the bottom-of-the-bill discount and I know Vittorio was on the stage here before I came up and we had breakfast this morning and I think whether you are in Europe or Asia or the US, we are still searching for that silver bullet that really ties it all together.

But if you think of our core business being wireless, having access to those fiber nodes that connect all the cell sites and all the switching together is an important aspect of it. I think there's still lots of room within that Washington to Boston corridor to further penetrate where we already cover and if you can get the right relationships between what the local governments are looking for, what we are looking for, we need some cooperation from our unions, I wouldn't rule out some further expansion of FiOS. But you've got to figure out the right formula to get it.

But in the meantime it's a good asset returning good returns for us and it fits with the overall portfolio. So when people ask me and I know there's speculation that we might be interested in selling the Wireline properties, I don't see it at -- you never say never but I don't see it in the near term.

Brett Feldman - Goldman Sachs - Analyst

So we just talked about whether there will be assets you could sell and you answered that. As you look at the way the industry is evolving and what your competitors are buying, do you have a sense that maybe there's an asset class you need to have greater ownership of whether it's content or something else?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I think you always want to continue to enhance the portfolio and things like Millennial Media at $200 million is not a huge purchase for us. I don't expect to see us go out and buy cable companies and expanding the footprint. I think the footprint we have is right. What I want to do is build those digital media capabilities. That doesn't necessarily mean content. Relationships like we have with DreamWorks, you can deliver the kind of content you need in a commercial relationship, maybe a little bit closer but I don't see us going out and buying a network TV or that sort of thing.

The digital media which is the direction that we are headed with Mobile First, are much more smaller companies and wouldn't frankly register in a big way for investors when we purchase them.

Brett Feldman - Goldman Sachs - Analyst

So you will continue investing around that strategy but the size of those investments would not necessarily qualify as transformative for Verizon?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

No, I don't think at least at the initial purchase. Now I would tell you the plans and the hopes that we have for AOL is that it will be transformative for us in the digital video space. But is $4.4 billion viewed as a transformative deal from an investor perspective? Probably not.

Brett Feldman - Goldman Sachs - Analyst

So I got to ask you about regulation. It was a big year for the regulators. They determined that they would reclassify broadband as a common carrier service under Title II and obviously there's some dispute over that. But as they've structured this decision if it were to hold, how does that affect your business if at all?
Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

What that's been the issue for us, Brett. I think the original Tom Wheeler concept of treating the broadband services that are fixed line one way and wireless another way made a lot of sense to us. What they have put in place in and of itself the way they are talking about implementing it today doesn't have much impact on us. But what we have objected to is them giving themselves a potentially broad range of oversight, including wireless that we don't think is justified or authorized by Congress and that's why we are challenging that.

So to answer your question, today, none. But if they started using some of the tools that they gave themselves it could going forward and that's why we are challenging it in court.

Brett Feldman - Goldman Sachs - Analyst

Beyond the challenge, what would be the preferred final solution you would hope to see?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

I think much closer to what Tom was talking about, maintain a light touch on wireless. And then more of the Title II type regulation on the Wireline. And the reason I say that is, to single out the carriers in an environment where you could argue that Facebook, Google, Apple, Microsoft, you name it has as much impact on the customers' experience as the person that provides the airwave connection to the phone, they have as much to say about that as we do, so to single us out for regulation just makes no sense.

Brett Feldman - Goldman Sachs - Analyst

All right. So this is going to be my last question. When we are sitting here again next year and we are thinking about how Verizon is positioned into 2017, what are we going to be talking about? What will have been the big things you will expect to have accomplished by then and what are you going to be optimistic about as you look into the following year?

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Well, I hope we are sitting here talking about how wildly successful our mobile video product has been and how we've added additional facets to that product that make it even more interesting. I hope that we will also be doing something similar with over-the-top broadband into the home at that point.

I think that we will be -- I am fairly confident -- we will have significant revenues coming from the Internet of Things and I think we will be up here talking about applications in areas of healthcare and transportation and energy management that people are going wow, that's really cool.

And then I fully expect there will be a third area that we have no idea what it is today that we will come up and we will say, wow, this is the big idea that will propel us into 2017 and 2018. And I think 5G will be part of that and I think we will be reporting out on some of the early returns on that and I think we are probably going to be pretty optimistic about what it will do for the industry.

Brett Feldman - Goldman Sachs - Analyst

Well, I look forward to that. Thanks for being here.

Lowell McAdam - Verizon Communications, Inc. - Chairman and CEO

Okay. Thank you, Brett.