Seeking Alpha α

Transcripts | **Technology**

CenturyLink, Inc. (CTL) CEO Jeff Storey on Q3 2019 Results - Earnings Call Transcript

Nov. 6, 2019 7:01 PM ET14 comments | 8 Likes
by: SA Transcripts

Q3: 11-06-19 Earnings Summary

Press Release SEC *10-Q* *Slides*

EPS of $0.31 misses by $-0.01 | Revenue of $5.61B (-3.64% Y/Y) beats by $71.66M

Earning Call Audio

Subscribers Only

00:00 -45:51

CenturyLink, Inc. (NYSE:CTL) Q3 2019 Earnings Conference Call November 6, 2019 5:00 PM ET

Company Participants

Valerie Finberg - Vice President of Investor Relations

Jeff Storey - President, Chief Executive Officer & Director

Neel Dev - Executive Vice President & Chief Financial Officer

Conference Call Participants

Timothy Horan - Oppenheimer & Co.

Simon Flannery - Morgan Stanley

Frank Louthan - Raymond James

David Barden - Bank of America

Mike McCormack - Guggenheim Partners

Batya Levi - UBS

Nick Del Deo - MoffettNathanson

Reed Kern - JPMorgan

Operator

Greetings and welcome to CenturyLink's Third Quarter 2019 Earnings Call. During the presentation, all participants will be in a listen-only mode. Afterwards, we will conduct a question-and-answer session [Operator Instructions] And as a reminder, this conference is being recorded today, Wednesday, November 6, 2019.

It is now my pleasure to turn our conference over to Valerie Finberg, Vice President of Investor Relations. Please go ahead.

Valerie Finberg

Thank you, Jen. Good afternoon, everyone, and thank you for joining us for the CenturyLink third quarter 2019 earnings call. With us on the call today are Jeff Storey, President and Chief Executive Officer; and Neel Dev, Executive Vice President and Chief Financial Officer.

Before we get started, I need to call your attention to our safe harbor statement on Slide 2 of our 3Q 2019 presentation, which notes that this conference call may include forward-looking statements subject to certain risks and uncertainties. In addition, we will refer to certain non-GAAP financial measures, which are reconciled to the most comparable GAAP measures. Those reconciliations can be found in our earnings press release or our supplemental schedules. Additionally, please note that certain metrics discussed on the call today exclude transformation costs and other special items as noted in our earnings materials.

With that, I'll turn the call over to Jeff.

Jeff Storey

Thanks, Valerie, and thank you to everyone for joining us. On today's call, I'll give you an update on the state of the business. Neel will provide an overview of the quarter's financial results, and then we'll go into your questions.

During the quarter, we continued executing on our strategy around four key areas: investing in growth through product and network expansions; delivering an enhanced customer experience across our business; transforming the operations of our company to improve efficiency and employee experience; and delevering to further strengthen our balance sheet.

Our expanding adjusted EBITDA margin and year-over-year revenue growth in IGAM, Enterprise and consumer broadband demonstrate these efforts are making a difference. Our focus on providing innovative networking solutions continues to resonate with our large business customers for both IGAM and Enterprise. In addition to the year-over-year revenue growth, we followed strong sales in the second quarter with higher sales this quarter.

Included within the Enterprise segment results is our federal sector. We're seeing early wins under the federal EIS contract. We believe we are well positioned to grow our federal relationship under this new contract vehicle.

We're seeing mixed results in our SMB segment. The biggest challenge is offsetting pressures from legacy services such as TDM voice. But by tailoring product capabilities, specifically for this customer segment, products like Unified Communications as a Service, network security, and SD-WAN, we're bringing much-needed solutions to the market for SMB customers.

We believe we operate one of the world's most extensive and capable fiber networks for business and wholesale customers. We continue to focus investments on improving that advantage by expanding our network reach to new buildings.

During the quarter, we added approximately 4,900 new fiber-fed buildings, bringing the year-to-date total to roughly 14,500. These investments are particularly relevant to the SMB customers located in those buildings. Our sales team is focused on leveraging these investments both within and beyond our legacy LEC footprint. Utilizing the entire

CenturyLink fiber footprint, our team is intent on becoming a major provider to SMB customers throughout the U.S. I'm excited about the opportunities for SMB and expect improved performance in the future.

Our Wholesale results met our expectations. While revenue can be lumpy in any given quarter, the market is large and CenturyLink is a key player. We do, however, continue to expect this segment to decline over time, offset to some extent by our expanding on-net footprint and Ethernet capabilities. We're obviously focused on leveraging the power of our fiber network to drive growth in all of our business segments.

I'd also like to highlight some of the ways we are enhancing the products and the capabilities we deliver across our platform. We continue to enable our Dynamic Connections product, which provides our customers real-time and self-serve access to secure multi-cloud connectivity across thousands of global endpoints.

Last month, we announced that we added Google Cloud to our ecosystem. Shortly after that announcement, we had customers logging in to our Dynamic Connections platform to connect workloads to the Google Cloud without having to call us or establish new physical connections.

On our second quarter earnings call, we announced plans for our edge computing solutions, which combines our edge computing infrastructure with our incredible fiber network, Dynamic Connections offerings, cloud application management tools, and managed services portfolio. We've already begun closing sales of this newly enabled offering with recently closed a deal to support a global edge computing solution for an IT-intensive securities trading customer.

Our edge computing capabilities enable the customer to move trading system workloads closer to the digital interactions with other trading platforms all over the world. Our solution provides the customer fully managed compute, storage, network, managed security, and market connectivity, monitor 24/7 by a managed services team aligned to financial services industry best practices.

We're enriching our CDN platform, both organically by expanding our capabilities, capacity, and footprint and inorganically through the acquisition of technology companies like the Streamroot acquisition we announced in September. I won't go too far into the details. The Streamroot gives us disruptive technology that enables connected devices to deliver content through secure and privately meshed networks.

We continue to expand our overbuild of the nationwide ultra-low loss fiber infrastructure discussed on the second quarter call. By leveraging our significant conduit infrastructure, we are deploying this next-generation fiber network at what we believe are significantly lower cost and a much faster time to market.

Investments in these capabilities are leading customers to select CenturyLink to support their complex networking and technology needs. As an example, I'll briefly discuss our relationship with Chick-fil-A. Before I get into the details, I have to say that personally I'm an avid fan of Chick-fil-A. It certainly starts with liking the food, but I also appreciate the way they've integrated technology into providing a superior customer experience.

To even further enhance that customer experience, Chick-fil-A required increased bandwidth capabilities at their restaurants, which we supported with fiber investments to hundreds of locations nationwide. Fiber connectivity is a foundational component of the Chick-fil-A digital strategy and is enabling many of their smart restaurant initiatives. We continue to work with this customer to support their future digital requirements.

Turning to our Consumer segment, over the past couple of years, we've made strides in our efforts to transform our Consumer business. We have simplified our go-to-market approach, focusing on an easy-to-understand, non-promotional offering known as Price for Life. This simplified product has significantly improved the customer and employee experience, reduced marketing and customer care costs, lowered churn and driven higher ARPU. Coupled with our transformation initiatives, we focused on driving higher levels of digital interaction and customer self-service. You heard me say a number of times, we will grow where we invest, and we continue to invest in deploying consumer fiber where it is economical to do so.

In 2018, we shifted to a consumer investment strategy that was heavily weighted to fiber-to-the-home solutions rather than investments in copper-based technologies like bonding and vectoring. We're seeing good success with this strategy. Micro-targeting our fiber builds down to the neighborhood level and digitally targeting sales efforts down to the individual households.

As I said, these efforts are paying off. Through our Price for Life offer, higher levels of fiber deployment and improved customer experience initiatives, we've seen year-over-year growth in consumer broadband revenue each and every quarter since the beginning of last year. We're very focused on accelerating that growth and while we certainly have more to do, I'm pleased with our ability to operate the Consumer business to grow where we invest and to generate significant free cash flow.

I'd like to touch briefly on our ongoing strategic review of the Consumer business. We continue to make good progress with the review. However, as I've previously said, these are complex assets and this is an extensive process. We believe there are good opportunities in the Consumer business, and we are dedicated to identifying the best path forward for our shareholders. We remain open to the various potential outcomes, but we won't give specific details until we complete the review and decide upon a definitive course of action.

Moving back to our overall strategy. The entire thesis of our business is that we will build and leverage our extensive fiber network to deliver the capabilities our customers require for their own digital transformations. As we look at our company going forward we have several strong beliefs that form the basis of our strategy.

First of all, the reliance of enterprises on networking solutions is growing not diminishing. Customers need our products and services for artificial intelligence and big data, augmented reality, multi-cloud environments and the exponential growth of IoT devices, complex networking services are the key enablers for these applications.

Of course, we have to keep pace with technology advancements and adapt our products, adapt our services and the delivery mechanisms to match. But that's the true opportunity for us to execute well in the market and we are intensely focused on it.

Secondly, whether compared to copper, hybrid fiber-coax, wireless or even 5G, we believe fiber is the long-term technology winner. We all spend a lot of time talking about wireless and it certainly has its place in the last few hundred feet. But there is no scalable communications technology where fiber is not the true underlying infrastructure. Wi-Fi, private LTE, 4G all go back to fiber as quickly as possible. In fact, the key enabling technology for 5G will be the continual densification of our own fiber infrastructure.

Third, for Wholesale and Enterprise customers, direct fiber-based services are a clear favor to wireless or copper solutions. The scalability, the reliability and affordability of fiber is unmatched by wireless, free space optics, microwave, HFC or any other transport technology you can name. We will continue to invest in being the preferred provider of direct fiber-based solutions.

Lastly, investments in our digital transformation and expanding our fiber reach, our investments in long-life assets that generate sustainable free cash flow into the future and are key to our growth and improving profitable revenue.

From a transformation perspective, we believe simplification and automation will drive a better employee experience, a better customer experience, lower churn, improved sales and increased margins. We've made steady progress toward transforming our company during 2019 and have a milestone-based set of initiatives over the next few years to drive those outcomes.

In summary, we continue to invest in the growth of our business through product enhancement and network expansion. We remain focused on providing a superior customer experience by transforming the efficiency and effectiveness of our operating capabilities and we are committed to meeting our deleveraging objectives, while driving long-term sustainable free cash flow per share.

With that, I'll now turn the call over to Neel to provide an update on our detailed financial results for the quarter. Neel?

Neel Dev

Thank you, Jeff, and good afternoon, everyone. I'll start with our financial summary on slide four. For the third quarter of 2019, we generated adjusted EBITDA of $2.261 billion. Year-over-year, adjusted EBITDA margin expanded to 40.3% from 29.3% from the year ago quarter. From a cost transformation perspective, we achieved approximately $360 million of annualized run rate adjusted EBITDA savings which compares to $290 million reported in the second quarter.

We are pleased with the improved revenue performance this quarter, specifically for IGAM and Enterprise. Based on our year-to-date performance, we are reiterating all full year 2019 financial outlook measures. While revenue declined, year-to-date adjusted EBITDA grew compared to the same period in 2018.

This growth was driven by improved revenue trajectory in our Enterprise business, our continued focus on profitable revenue. Management of legacy product declines, along with the benefits from our cost transformation initiatives.

Turning to revenue on slide five. Total revenue in the third quarter declined 3.6% to $5.606 billion. This compares to declines of 5.5% in the second quarter and 5% in the first quarter. Before moving to revenue by segment, I want to point out that we saw a substantial increase in USF or Universal Service Fund rates this quarter.

Relative to the first couple of quarters this year, USF revenue is up approximately $40 million this quarter. Keep in mind; this is pass-through revenue we collect for the FCC. Sequentially, excluding the step-up in USF that I just mentioned, total revenue decreased 0.2% compared to the 1.2% sequential decline we saw in the second quarter and a 2.3% decline in the first quarter.

Within our IGAM segment, revenue grew 0.8% year-over-year. We saw currency pressures, both year-over-year and sequentially. On a constant currency basis, revenue grew 1.9% year-over-year compared to 1.6% growth in the second quarter. Sequentially, revenue was roughly flat. As a reminder, last quarter benefited from strength in non-recurring revenue of approximately $15 million.

Moving to our Enterprise segment. Revenue grew 3% both year-over-year and sequentially. Adjusting for the step-up in the USF, revenue grew 1.5% year-over-year and sequentially. This compares to a decline of 1.2% both year-over-year and sequentially in the second quarter of 2019.

Revenue growth was driven by installs from sales earlier in the year as well as strength in the federal government channel. Overall, we're pleased with the progress towards our objective of growing both IGAM and Enterprise revenue in the second half of 2019 compared to the first half of 2019.

SMB revenue decreased 6.4% year-over-year compared to a decline of 10% in the second quarter of 2019. Sequentially, revenue declined 0.3% compared to a decline of 2.5% last quarter. We continue to invest in our product capabilities and continue to feel good about our ability to sell into our on-net building footprint with a large addressable market opportunity.

Wholesale revenue decreased 6.6% year-over-year. Sequentially, we saw an increase of 0.7% compared to a decline of 1.8% last quarter. I'd like to point out that specific to the third quarter of 2019, we did see a benefit from a carrier settlement of approximately $15 million.

Turning to Consumer on Slide 6. Third quarter 2019 revenue declined 9.2% year-over-year. In the third quarter of 2018 revenue was stronger due to a benefit of roughly $40 million from a revenue recognition-related adjustment completed during that quarter.

As a reminder, we adopted the new revenue recognition standard in 2018. Excluding the benefit of that adjustment in third quarter 2018, revenue would have declined 6.7% year-over-year. This compares to an 8% decline last quarter. Sequentially, revenue declined 1.3%, which compares to declines of 1.7% in the second quarter and 1.8% in the first quarter.

Broadband revenue for the third quarter 2019 grew 2.3% year-over-year, which compares to growth of 1.8% last quarter. Broadband performance last year was largely driven by our Price for Life initiative. This quarter and going forward, our performance will be a function of our fiber-to-the-home investments and improving the penetration of our competitive assets.

In the third quarter, we saw a net loss of 36,000 total broadband subs. In speeds of 100 meg and above, we added 54 000 subs. I'd like to point out that for the third quarter of 2019 versus the third quarter of 2018, we have roughly doubled our greater than 100 meg sub additions. We also saw similar year-over-year growth in the first and second quarter of this year.

Turning to adjusted EBITDA on Slide 7. For the third quarter 2019 adjusted EBITDA was $2.261 billion compared to $2.287 billion in the third quarter 2018. As you think about EBITDA performance on a year-over-year basis, keep in mind, the revenue recognition adjustment that I just mentioned benefited third quarter 2018 adjusted EBITDA. On a sequential basis, we saw the typical increase in utility costs in our network facilities. Adjusted EBITDA margin was 40.3% for the third quarter 2019, compared to 39.3% in the year ago quarter and 35.5% at the close of the Level 3 transaction.

As of the end of the third quarter, we've achieved approximately $360 million of annualized run rate adjusted EBITDA transformation savings. Integration and transformation costs and special items incurred in the third quarter 2019 impacted adjusted EBITDA by $38 million and free cash flow by $32 million.

Moving to slide eight. For the third quarter 2019, capital expenditures were $957 million. We continue to invest in expanding our fiber footprint, adding buildings to our network and the initiatives that Jeff mentioned earlier. In the third quarter 2019, the company generated free cash flow of $983 million.

Turning to slide nine. We exited the quarter with our net debt to adjusted EBITDA ratio at 3.7 times which compares to 4.3 times at the close of the Level 3 transaction. During the quarter, we retired approximately $700 million of debt and through the third quarter we have addressed roughly $1.5 billion through a combination of actions.

After quarter end, in October, we paid out maturity to approximately $150 million in debt. Including this fourth quarter transaction, we paid down approximately $1.7 billion in debt obligations this year. In addition, we completed a transaction to refinance $1 billion of debt, which lowers interest costs and extends maturities.

As we indicated at the time, these proceeds will be used in the fourth quarter for redemptions. We paid down $ 400 million of debt in October and will pay down $600 million in early December. Overall, we remain highly focused on getting to our 2.75 to 3.25 net debt to adjusted EBITDA leverage target.

Turning to the business outlook on slide 10. We continue to feel good with our progress this year and are reiterating all of our full year 2019 financial outlook measures. In summary, we continue to remain focused on execution, specifically on improving revenue trajectory, maximizing profitability and staying disciplined on cost transformation and deleveraging.

Jeff Storey

Thank you, Neel. Operator, would you explain the process for questions?

Question-and-Answer Session

Operator

Certainly. [Operator Instructions] And our first question comes from the line of Timothy Horan with Oppenheimer & Co. Please go ahead.

Timothy Horan

Thanks a lot, guys. Can you discuss the booking trends on how they've kind of continued in the third quarter and maybe so far this quarter?

Jeff Storey

I didn't hear the first part.

Neel Dev

Booking trends.

Jeff Storey

Booking trends. Go ahead.

Neel Dev

So I think, Tim, for both IGAM and Enterprise, we had strong sales or bookings in the second quarter, and sequentially it was up in third quarter relative to what we saw in second quarter for both IGAM and Enterprise.

Timothy Horan

And any more color on what's driving the strength in bookings?

Jeff Storey

I think it's our products and services and the way we deliver on them, and we have confidence in the market and the types of things that we sell our customers need, the types of products and services we have, they're going to need in the future. And I think it's just best doing a good job in the market and expect to continue. I hope to continue.

Timothy Horan

Thank you. Thanks a lot.

Operator

And our next question comes from the line of Simon Flannery with Morgan Stanley. Please go ahead.

Simon Flannery

Great. Good afternoon. Jeff, you talked about the customer experience and trying to improve the efficiency of the network. Can you just give us a little bit more anecdotal of what you're seeing on the ground and how that's transforming itself into the bookings that Tim was asking about? And maybe Neel just following up, again the visibility you have into moving past the 360 and continuing to move towards the full program opportunity in over the next few quarters? Thanks.

Jeff Storey

Sure. On the customer experience, I mean there's some thing that are just basic blocking and tackling, doing a good job in service delivery, doing it -- having a reliable network and doing a great job in service assurance. Those are things that we focus on every single day.

Part of it has to do with evolving our products. If you look at Dynamic Connections and you think about a customer experience where they can all of a sudden reroute traffic from one cloud location to another, and it can be their own private data center to another private data center, but when they can reroute capacity, scale capacity up and down, move it around, however they like, without having to pick up a phone, without having to call through us, without having to wait for service delivery, that's a much better customer experience.

And so, we're making enhancements in our products and services. We're making enhancements continuing to move things on-net. More you're on-net, the better reliability, the better experience our customers have. So, we're continuing to focus on a whole array of initiatives to drive the customer experience there.

Simon Flannery

And are you -- like Net Promoter Scores, is there any -- are you seeing any kind of metrics or things that is going to help you kind of get more tangible about how your -- how the customers are really feeling?

Jeff Storey

Sure. And especially, if you look at our Consumer business in the -- our fiber product, our Net Promoter Scores have, have improved dramatically and are pretty good. We're pretty pleased with the Net Promoter Scores there. And so, yes, we look at a lot of internal metrics to know that what we're doing is actually affecting our customers and the performance that they're receiving is improving their experience overall.

Neel Dev

Simon, on your question on visibility. I think if we look at IGAM and Enterprise, our 90-day funnel is very healthy. And more importantly, the conversations that we're having with the customers are very, very positive in terms of what they're trying to do with their business. The two examples that Jeff gave in his prepared remarks, we're seeing a lot of those were the conversations have been with the CIOs in terms of how they are trying to transform their business. So, it's a very different discussion where we can bring to bear our whole assets and capabilities, and we're leaning in there and we are adding fiber into customers' locations to enable a lot of that transformation.

Simon Flannery

Great. And on the EIS, that's good to see. I mean, is that something that will be -- you'll see much in 2020? Or is that -- it's going to take a while to get that through?

Jeff Storey

And I don't want to predict specific timing on contracts, but we're seeing early success already. We were the first company to be certified or whatever the word was to receive bids through that contract and we're seeing that early success.

It's a long-term contract, extends for years and years. And I expect that the traffic will be moving and services will be moving to that contract over a long period of time.

Simon Flannery

Great. Thank you.

Jeff Storey

But, of course, if we're seeing results already, I expect results in 2020 as well.

Simon Flannery

Yeah. Thank you.

Jeff Storey

Sure.

Operator

And our next question is from the line of Frank Louthan with Raymond James. Please go ahead.

Frank Louthan

Great. Thank you. Looking out to the Rural Digital Opportunity Fund auction, how are you thinking about the change there from the current CAF II funding that you're getting, and what's sort of the point where you might walk away from some of that? Auction 903 came in well below the cost model and spread, likely this one probably would come in as well.

Is there a point where maybe you would walk away from that? And then, with that, where are you on the thoughts on the asset sales for Consumer? Are you closer to the end of that process and what completions did come to you? Thanks.

Jeff Storey

Sure. So I'll answer about CAF II and the Digital Opportunity Fund, make sure I'm clear, I'll answer them separately. We have no intention of walking away from CAF II. We're doing a great job. We've got -- we're very far along the way of building that out. And so, there's nothing I'm about to say changes any of that.

With respect to the Digital Opportunity Fund, when would we walk away from it? When it's not advantageous our company. If it doesn't make sense for us to do, we won't do it. And that's not a big problem for us.

We only are going to do things that make sense. So we will be involved in the process. We will make sure that we fully evaluate what it means for CenturyLink. And if we can do something economically that benefits our shareholders, we'll do it. And if we don't, we'll walk away.

Neel Dev

Yeah. Just to add to that, I think, for all the things keep in mind is, that there's an opportunity cost for us to participate. So we -- if you think about the -- our consumer management team and our planning teams, et cetera, if we're going to participate, we want to make sure it's economical, it's a long-term asset that we can drive good penetration on.

And so, that's what we'll evaluate versus just participating for the -- the subsidy is good, but there's also an offset on the capital side. So we're going to look at the overall economics.

Jeff Storey

Frank, I think you had a second --

Neel Dev

Consumer asset sales.

Jeff Storey

Consumer assets. Are we closer to the end of that process? Yes. But we're not there yet and we really won't talk about the details of it. What we are focused on in the Consumer business, is making sure we run the best Consumer business possible, making sure that where we invest we grow and we're introducing products and services and the customer experience that resonate with our customers and we're doing that. And then we'll evaluate that and all of the other strategic options and we are evaluating that and all the other strategic options that are out there. And I expect we're closer, obviously, to the end of it.

Frank Louthan

Okay. Any other asset sales that you might consider real estate or other things that you're not getting a lot of credit for on the balance sheet that could help delevering?

Jeff Storey

Yes. We look at everything. We try to be diligent and disciplined about all of our assets and look at things periodically to make sure and I think there are some things that we're not getting the full appreciation for the value of these assets. And so, if there's something that we can divest, if there's something that we can acquire, where we think we can drive better free cash flow per share for our customers or excuse me, for our shareholders then we'll do that. And we're pretty open and agnostic about – there's nothing that's off the table. It's not quite – but I think you get the point.

Frank Louthan

Great. All right. Thank you very much.

Operator

And our next question is from the line of David Barden from Bank of America. Please go ahead.

David Barden

Hey, guys, thanks for taking my question. I guess to follow up on that. Specifically, there's been reports out there Jeff that, essentially it has been shopping the Latin American fiber assets. And it seems somewhat counterintuitive to me, if that is in fact going on just because you've become focused on developing these enterprise services and assets on a global basis.

If you could kind of comment on whether that's a real thing or not it would be helpful. And then I guess just second on the – this is the impressive pivot in some of the kind of fundamental IGAM and Enterprise business lift. And I guess the question I have is just in terms of the kind of the composition of that lift. Is it – are we talking about kind of hundreds of smaller contracts that kind of are just going through the machine and getting installed and kind of run rating? Or are these kind of chunkier, big contracts like the federal contracts that are kind of driving the business at the moment? Thanks.

Jeff Storey

Sure. I'll try and answer the question on LatAm and all of our asset sales -- potential assets sales more eloquently than I did on Frank's question. Look we value our LatAm business. We value our EMEA business. We value the North America business. We think we have great strengths and great capabilities.

We don't comment on speculation and rumors that are out there but we do look at all aspects of our company. And while I won't specifically comment on LatAm or any other thing specific other than the consumer process that we've announced, we are focused on creating long-term value for our shareholders and we'll look into the various opportunities within the context of that.

Neel Dev

On your second question David, I think for Enterprise, it really is installs from second quarter sales. So I think we mentioned second quarter was a good sales quarter. Also for federal, keep in mind we have the federal shutdown in fourth quarter and impacted in January and February of this year, but we had strong federal sales in March of this year. And so a lot of installs on the Fed side as well. So performance on the Fed channel and overall installs related to sells in the Enterprise business.

For IGAM, it's just strength from our large customers. Again, second quarter sales was good from those customers. And we also -- our international business performed well as well. So those are the drivers.

David Barden

Got it. Thanks, guys.

Operator

And our next question is from the line of Mike McCormack with Guggenheim Partners. Please go…

Mike McCormack

Hi, guys. Thanks. Maybe just two quick ones. Neel, on the equipment revenue for the quarter, I think what should be thinking about there? And then also, I guess, looking into Q4 as well? And then, secondly, a lot of the peers are concerned about pricing in the business marketplace around Enterprise. What are you guys seeing out there as far as spot pricing goes? Thanks.

Neel Dev

So, I'll take the pricing one first and then Jeff may want to add to that. I think, we're seeing pricing dynamic as very rational and we're not really seeing anything that would concern us. Now, on the transactional side, like if you think about long-haul waves, there are certain pockets.

If it's competitive, then we step away at price points that we don't like. But generally, most of what we see are solutions that we're having discussions with customers where price is part of the discussion, but it's not starting with price. They're more focused on the overall solution, specific to some of the examples that Jeff shared. A lot of those are solutions that we're deploying for the customers that our products and services wrapped with professional services and other capabilities.

Jeff Storey

I think that's right. I mean, prices is an important point for customers, but we think pricing in the market is rational and we think that we can win at the prices that are out there.

Neel Dev

And from an equipment perspective, I think, we've deemphasized, like we've said before, low-margin equipment sales, but we do have equipment every quarter, which is more wrapped around solutions that we're deploying. And the margins there are relatively healthy and there's network attached to that. And we see that every quarter, then there's nothing out of the ordinary there.

In terms of fourth quarter, the only thing I would highlight is, keep in mind that fourth quarter of last year was fairly strong. We had roughly $40 million of non-recurring revenues that we highlighted. But as we say here today, we don't see anything like that in the fourth quarter of this year.

Mike McCormack

Great. Thank you, guys.

Operator

And our next question is from the line of Batya Levi from UBS. Please go ahead.

Batya Levi

Great. Thank you. You had prior guidance that you expect Enterprise and IGAM revenues to be up sequentially in the fourth quarter. Do you still expect that? Is there another USF contribution that we need to think about? And also, on the expense side, can you quantify maybe the seasonal expenses that you saw in the quarter? Going forward, can we expect cost-cutting to continue at the pace of the top line decline?

Neel Dev

So for IGAM and Enterprise, I think, as I said in my prepared remarks, we have seen improvement excluding USF and we expect the same going into fourth quarter. So, overall, we do expect IGAM and Enterprise to do better in the second half of this year relative to the first half of this year. The only thing to keep in mind is, currency has been a headwind.

In terms of your question on seasonality -- cost seasonality. We did see the typical increase in utilities in the third quarter, roughly $20 million. And in terms of the cost savings over the long term, we still feel good about the $800 million to $1 billion. And we have good line of sight there and our execution has been good. So we feel good about that.

Batya Levi

Okay. Thank you.

Neel Dev

Thank you.

Operator

And our next question is from the line of Nick Del Deo with MoffettNathanson. Please go ahead.

Nicholas Del Deo

Hi. Thanks for taking my question. You had a pretty substantial sequential decline in SG&A this quarter. I know there's some noise in that number based on integration costs when they're booked. Is there anything worth calling out behind that decline? And should we think of that as a good jumping off point for Q4 and beyond?

Neel Dev

Yes. No there's nothing specific to call out. Now these things are never linear, so we're very milestone-based. And so nothing specific to call out. There might be some noise like you mentioned with the integration costs. So there might have been some integration costs last year in that -- last quarter I mean in that category. But nothing specific to call out.

Nicholas Del Deo

Okay. That's helpful. And you guys have talked about an opportunity to drive SMB revenue by targeting on-net buildings. Can you help us understand how you're sizing that opportunity and when we might start to see an impact?

Jeff Storey

Well, we don't really talk about how we size it but we look at the various buildings that are out there. We look at the customers in them and we target our network expansions with multiple factors in mind.

We look at off-net expense. If we have off-net expense, we know how much we get to save by moving that building on-net. And so it's a guaranteed returns for us. We look at existing customers and then we look – and we transition those customers into our on-net footprint and we can provide better service to them.

And then we look at potential customers and we have a pretty sophisticated targeting capability to look digitally at these customers to understand where they are, how we're going to serve them and really position our products for them. And so we'll continue to do that inside the legacy ILEC footprint but we have a lot of opportunity outside the legacy ILEC footprint as well.

Neel Dev

And opportunity outside the ILEC footprint that Jeff just mentioned, the addressable opportunity is large. It really is about improving our execution and that's where we're spending a lot of time in terms of fine-tuning how we go-to-market and how do we drive better penetration there. So that's just a function of execution. We're not constrained by the market opportunity there.

Nicholas Del Deo

Okay. Great. And maybe one quick one for Neel. The $40 million sequential increase in USF how is that split between consumer and business?

Neel Dev

Consumer is very small. It's mostly business.

Nicholas Del Deo

Mostly business. Okay. Great. Thank you.

Operator

And our next question comes from the line of Philip Cusick with JPMorgan. Please go ahead.

Reed Kern

Hi. This is Reed for Philip. Two follow-ups if I can. First you talked about equipment. How far through the exit from unprofitable revenue is CenturyLink today? And what's the composition of that remaining revenue? Is it all video? And second I think it goes to Frank and Dave's question, can you expand on CenturyLink's strategy for moving closer to the edge and how that strategy influences your thinking about potentially monetizing non-core assets on the map?

Neel Dev

So on the unprofitable revenue I think the best way to think about it is going forward it's fairly clean. Is there a little things around the edges yes primarily Prism. So we still have call it that $30 million of Prism revenues that will continue to straight way going forward. But as you think about sequential performance relatively clean.

Jeff Storey

With respect to going closer to the edge, fiber is the edge. That's how we pick up customers, how we bring them into the network. So the fiber is the edge of the network. But we -- when we talk about edge computing, that means taking customers' computing resources and moving them closer to that fiber connected edge to the -- closer to the place that that traffic is originated or that traffic needs to be terminated.

CDN is the same way. We continue to move CDN resources that we have closer and closer to our customer, making them closer to the edge where we directly connect to the customers with the fiber infrastructure that we have. I hope that answers the question.

Reed Kern

Thank you.

Jeff Storey

Okay. Operator, I think, that's the last question we have. So I'd like to wrap up, before we conclude the call, to summarize a few key points. As we said and as demonstrated in our third quarter results, we expect revenue performance will be better for IGAM and Enterprise, comparing the second half of 2019 to the first half.

We operate what we believe to be the world's best fiber network and we will continue to focus our capital deployment on expanding our fiber footprint and providing innovative solutions over that network. We are executing on our transformation initiatives, which improve the customer experience and increase efficiency throughout the organization.

We delivered another quarter of solid progress on our deleveraging objectives and expect to be within our leverage target in our three-year time frame. And all of these initiatives and accomplishments are aligned to our overall guiding principle, which is to grow free cash flow per share.

Thank you for joining today's call and for your continued support of CenturyLink. Operator that concludes the call.

Operator

Thank you, Jeff. We would like to thank everyone for your participation and for using CenturyLink conferencing service today. This does conclude the conference call. We ask that you please disconnect your lines and have a great day, everyone.