Operator

Ladies and gentlemen thank you standing by. And welcome to the AT&T Fourth Quarter 2014 Earnings Conference Call. At this time all participants are in a listen-only mode and then later we will conduct a question-and-answer session, instructions will be given at that time (Operator Instructions).And I would now like to turn the conference call over to our host, Senior Vice President of Investor Relations for AT&T Mr. Michael Viola. Please go ahead sir.

Michael Viola

Thank you, Lorry and good afternoon everyone. Welcome to our fourth quarter conference call. It's great to have you with us today. As Lorry said I'm Mike Viola, Head of Investor Relations for AT&T. Joining me on the call today is Randall Stephenson, AT&T's Chairman and Chief Executive Officer and John Stephens, Chief Financial Officer. Randall will provide some opening comments then close with 2015 guidance, John will cover our results and then we'll follow that with a Q&A.

Let me remind you our earnings material is available on the Investor Relations page of the AT&T website. Please call your attention to our Safe Harbor statement before we begin which says that some of our comments today maybe forward-looking. As such they are subject to risks and uncertainties, actual results may differ materially. And additional information is available on our Forms 8-K, other SEC filings and on the investor relations page of AT&T's website. I also want to remind you that we are still in the quite period for FCC Spectrum Auction 97 or the AWS-3 Auction so we cannot address any questions about Spectrum today. So with that overview, I will now turn the call over to AT&Ts Chairman and Chief Executive Officer, Randall Stephenson. Randall?

Randall Stephenson

Hey Mike. Thanks and good afternoon. Fighting cold around here Lorry may end up having to handle this call for us. But before John takes you through the results I want to take just take a couple of minutes and frame where we are. 2012 to 2014 was a really period of unprecedented investment for AT&T and for the industry for that matter. And during this period we built our LTE network to cover more than 300 million people, we expanded our U-verse broadband footprint to 57 million customer locations and we deployed fiber to 725,000 business locations. And at the same time we reengineered our mobile network and we now deliver the strongest LTE signal in the U.S.

Now at the same time we've been aggressively repositioning our wireless customer base. We're giving our customers now a choice of moving away from heavy handset subsidies in exchange for lower monthly prices. And as a result our customer satisfaction continues to climb and defections continue to fall and you can see that by our record low annual postpaid churn rate. And we also delivered our best ever full year adjusted EBITDA service margins. We've also made a significant investment to migrate our wireline customer bases to the new platforms. At the end of 2014 76% of our broadband customers were on our fastest IP based platforms and our strategic IP based business services now represent a $10 billion annualized revenue stream and it's growing 14% when you adjust it for the Kinetica sale.

And that brings us to 2015, because with these foundational investments largely behind us and several strategic investments announced to-date the ground work's now being laid for 2015 and beyond. And today our customers are expecting us to deliver video across all of our platforms whether it's traditional linear video or over the top on U-verse broadband or video to the mobile device. So we've been assembling the pieces that we need to do exactly that. DIRECTV quickly and significantly shores up the economics of our U-verse video product and it brings us the best content relationships in the industry.

Our fixed broadband footprint will quickly begin expanding to 70 million customer locations in the U.S. when we complete the DIRECTV transaction. And in the Cricket acquisition it’s proven to be a cost effective way to strengthen our spectrum portfolio which is a prerequisite for in the mobile video delivery business. We also laid the ground word for expanding these capabilities outside the U.S. We've always believed the demand for the mobile internet and economic benefit experienced in the U.S. would be repeated throughout the world. And so with that we have been looking for opportunities to gain a wireless foothold in key market for the regulatory in the investment climate is right.

And used cell and net cell international’s Mexico give us this opportunity. The changes in the Mexican legal and regulatory framework make it attractive for a new entrant to invest and we close on use of sale and then once we complete Next sale we will have a very deep spectrum portfolio and this is the first element needed for a robust mobile internet offering.

We will now have the ability to expand our U.S. network directly into Mexico building one seamless network that's spanning 400 million people. And whether it’s cross border businesses, Latino customers and either Cricket or AT&T or Mexican consumers we will be the only company with mobile internet capabilities spanning both counties. And don’t forget DIRECTV brings the premier video business in Latin America.

So the bi-product of this is represented on Slide 5, you go 12 months now AT&T's revenue is going to look very different. It will be much more diversified. The way we integrate our products and services will be different. And when in 2015 post DIRECTV our revenues will come from four areas, our largest will be business solutions, that includes both fixed and wireless services and is growing nicely in fact in the fourth quarter that area is growing nearly 6%. The next area will be our consumer TV and broadband business, then third will be our consumer mobility business, then obviously our Latin American businesses where satellite TV and then the Mexican mobility businesses will be our fastest growing area. And we like this mix a lot, and by the end of the year we are going to be uniquely positioned in a world of high-speed connectivity dominated by video and is going to be a very different business.

So, with that I am going to turn it over to you John to go through 2014.

John Stephens

Thank you Ran and hello everyone. Let me start with our consolidated financial summary which is on Slide 6. We finished the year strong with solid revenue and EPS growth in the fourth quarter. Consolidated revenues grew to more than $34 billion up 4.5% when you adjust for the sale of our sale of our Connecticut properties. This was driven by strong wireless growth as we continue to reposition our business model and adjusted revenue growth in wireline, thanks to gains in the Strategic Business Services and U-verse.

For the full year we saw adjusted consolidated revenue grow by more than 3%. This helped drive strong EPS growth. Reported EPS for the quarter was a loss of $0.77 however when you exclude the significant items we disclosed in the last weeks, earnings per share was $0.55. That's up nearly 4% from a year-ago. And if you consider that last year included about $0.02 of equity income from our divested America Movil interest, that percentage would be closer to 8%. Adjusted EPS was up slightly for the year even after a $0.06 impact from the sale of our America Movil investment.

These adjustments include $0.94 of non-cash pressure from the year-end mark-to-market charge for our benefit plans. This was almost a reverse of last year when we had a strong mark-to-market gain. The actuarial loss was largely driven by a decrease in the discount rate but was partially offset by strong performance of our benefit plan investments. We also had a $0.25 non-cash pressure from the write-off of certain network assets which we told you about earlier this month. And we had $0.13 of cost associated with wireless integration, DIRECTV transaction cost and the loss on the sale of the Connecticut properties.

Now let's turn to our operational highlights starting with wireless on Slide 7. Before I get to the quarter, it's important to take a look back at the full year and see how far we've come with repositioning our wireless business. It's been almost a year since we first introduced our Mobile Share Value plans and began to accelerate the move of our smartphone base off the subsidy model to AT&T Next.

Since that time the results have been dramatic. First, we've had nearly 3.3 million postpaid net adds, thanks to strong growth of phones and tablets. That's our best full year gain in five years. And this includes more than 700,000 postpaid phone net adds during the year. These postpaid gains along with an end of year surge of connected device subscribers, thanks mainly to the connected car, helped to drive 5.6 million total net adds. Our strongest growth in three years. Just as impressive, we added nearly 5 million new smartphone subscribers during the year. These high value high quality customers have an ARPU of about twice that of non-smartphone subscribers.

At the same time, we had our best ever full year postpaid churn. That's a remarkable achievement anytime, but even more so when you consider the intense competitive environment we face during the year.

We also had our best ever full year adjusted EBITDA service margins. We achieved that even with record full year smartphone sales. This is the impact of AT&T Next. Already more than a quarter of our postpaid smartphone base are on equipment installment plans and more than half of our smartphone base has moved off the subsidy model pricing. These are the long-term results we have talked with you about throughout 2014. A repositioning of the smartphone base is working with nearly 70% of our postpaid base now on mobile share plans.

Now let's look at fourth quarter results starting on Slide 8. Let's begin with net adds where we had another strong quarter. We added nearly 2 million total subscribers led by postpaid and connected devices. We added more than 850,000 postpaid subscribers thanks to strong growth of tablets. These tablet gains more than offset a slight decline of feature phone subscribers, but we also grew high quality postpaid smartphone base by another million in the quarter. This includes upgrades and migrations which we don't include in our net add number. Connected devices also continued their strong growth as the Internet things begins to evolve. Nearly 1.3 million connected devices were added in the quarter including 800,000 connected cars.

Prepaid showed a loss in the fourth quarter however the Cricket brand is showing momentum with positive net adds after losing customers in the pre-acquisition a year-ago fourth quarter. The Cricket integration is going strong, distribution's been expanded, churn is improving and now nearly three quarters of the customer base has transitioned to the AT&T network. Our fourth quarter's is traditionally a strong sales quarter and you see that in our results. We had record smartphone postpaid gross adds and upgrades, with more than 10 million smartphones sold in the quarter. That includes record total upgrades, those customers choosing to stay with AT&T and commit to new device plans. Our upgrade rate exceeded 11% in the quarter. Smartphones were 94% of all postpaid phone sales, another record for us in the quarter.

As expected, postpaid churn was up in the quarter. The fourth quarter traditionally sees increased levels of churn for all carriers. And when you add in the intense competitive activity in the quarter, it's no surprise to see churn at these levels. But even with all this noise in the market, postpaid churn levels were comparable to two years ago, the last time a fully refreshed iPhone hit the market. And this was the first time that all major carriers were able to sell that phone during the busy fourth quarter.

Now let's look at revenue gains on Slide 9. Total wireless revenues grew nearly 8% as the revenue mix shift we have seen throughout the year continue to play out in the fourth quarter. Equipment revenue growth tapped 70% with strong AT&T Next sales. Service revenues were pressured as customers continue to sign up for Mobile Share Value plans and move away from the traditional subsidy model.

We now have more than 18 million smart Mobile Share accounts covering nearly 70% of our postpaid subscribers and about 58% of our postpaid smartphone base is on no subsidy pricing. Mobile Share customers continue to buy up to larger buckets of data. Half of our accounts are on the plans of 10 gigabytes or larger. That compares to 27% a year ago. And we're seeing a move to even bigger larger data plans, nearly 20% are on plans of 15 gigs or more. That's three times more than a year ago. This helped drive an 18% increase in data billings.

The take rate for AT&T Next increased to 58% in the fourth quarter or about 5.9 million new Next customers. This impacted cash flows, but we consider this an investment in a great customer base that we are more than willing to make. We also had about 400,000 customers who bring their own devices onto our network.

The next take rate was a step-up from prior quarters, while we continue to see strong customer response at our company owned stores and agents with a Next take rate of about 90% of upgrades, the take rate for Next to our other retailers was much less. The strong holiday sales played a role here. We typically have a higher percentage of our sales with other retailers in the fourth quarter. These stores are still becoming familiar with Next plans and our sales show that, plus with a rush of the holiday season, sales personnel with these retailers don't always have the time to take the steps necessary to close the Next transaction. We will continue to work with these stores and expect the take rate at those locations to pick up in the future.

As expected the strong Next take rate helped drive the second consecutive quarter of sequential ARPU growth when you factor in Next billings. When you add in Next billings you get a more accurate idea of what an average customer pays us every month. Our average monthly Next billings were up about $28 per month even with the introduction of the Next 24-month plan. As the Next pace grows so does the impact of billings nearly 27% of our smartphone base is now on AT&T Next.

Now let`s move to our wireline operations on slide 10. The transformation of our wireline networks IP technology has helped drive year-over-year wireline revenue growth. We say it again has helped drive year-over-year wireline revenue growth when you adjust for the sale of our Kinetica operations. We're really seeing the overall revenue impact of the strategic business services and the U-verse.

Total adjusted U-verse revenues increased by more than 20% and are now about two-thirds of consumer revenues. And strategic business service revenues grew by more than 14% and are now 30% of total wireline business revenues. Growth looks even stronger when you adjust out the impact of foreign exchange. Overall adjusted wireline consumer revenue increased 2.4%, adjusted wireline business revenues were down 1.8%. However if you adjust for the effect of discontinued Global Hubbing businesses and foreign exchange that decline would have been just about a 0.5%.

We're still dealing with the impacts of an uneven economy. But enterprise revenues were up slightly. However the lack of new business formations continue to pressure small businesses. Wholesale also saw pressure in the quarter in part due to our focus on profitable sales. These results helped drive a sequential improvement in wireline margins which were up 120 basis points over the third quarter of 2014. That's a reversal of trends in recent years when we had seen sequential declines between the third and fourth quarter.

U-verse subscribers also grew in the quarter. We added more than 400,000 high speed broadband subscribers and now added 2.1 million for the full year. We finished the year with 12.2 million high speed broadband subscribers or more than three quarters of our broadband base. The transformation to IP broadband is a remarkable accomplishment for entire wireline team. U-verse CD subscriber net adds came in at 73,000. Net adds were impacted by a strategic move to improve the profitability of our wireline consumer business. With our high content costs we targeted profitable, long-term value subscribers with lower churn rates while still taking market share.

Now let's take a look at margins on slide 11. We will start with our wireless margins. Wireless margins were pressured by strong smartphone gross adds and upgrades, investment related expenses and wireless integration costs. We mentioned earlier that we had our best ever full year adjusted service margins even with record sales thanks to AT&T Next. We also see the impact of Next on our quarterly results. Our wireless EBITDA service margin was down slightly when compared to a year ago. The fourth quarter of 2014 saw 2.6 million more smartphone sales than in the previous year. And if you compare the results to two years ago when smartphone sales were comparable service margins improved over 700 basis points.

Wireline margins improved from a year ago. Wireline margins usually are flat or down between the third and fourth quarter but that trend changed last quarter. There was pressure from investment expenses and content cost but this was offset by growth in wireline revenues and solid execution on cost initiatives. For the quarter our adjusted consolidated margins were 14.2% compared to 15.5% a year ago quarter and just under 13% two years ago. Strong smartphone sales also pressured consolidated margins but our continued efforts for cost efficiency helped offset some of that pressure.

Now let's move to cash flow [indiscernible] on slide 12. For 2014 cash from operations totaled $31.3 billion and $5.7 billion for the quarter. Capital expenditures were $21.4 billion and $4.4 billion for the quarter and free cash flow before dividends was $9.9 billion and $1.3 billion for the quarter. Free cash flow was impacted by the nearly 6 million AT&T Next sales in the fourth quarter. We pay upfront for those devices while our customers pay us back overtime. The record upgrades and strong iPhone sales with a higher sales price mix made an impact as well.

This speaks to our willingness to invest in our premium smartphone customer base. We aren't going to turn away good business to manage to a cash flow number. We have the financial strength to finance devices for our best customers, we have the lowest churn and higher ARPU and that is our focus.

At the same time our Next receivables significantly increased while our bad debt ratios stayed at traditionally low levels. These are high quality receivables we did monetize 1.2 billion of the Next receivables in the quarter as there continues to be great interest for financial institutions and we do expect future sales of those receivables.

Also in the fourth quarter we sold our Connecticut wireline operations to Frontier for $2 billion. Our asset sales strengthened our balance sheet and cash position. In fact we had more than $10 billion in cash and short-term investments on hand at the end of 2014. We had more than 3 billion in combined free cash flow and asset sales during the fourth quarter with $18 billion for the full year.

In terms of usage of cash dividends sold of 9.6 billion for the year and we continue to have one of the strongest yields around. We also announced the dividend increase last month. This is the 31st consecutive year that we have increased the dividend that puts us on a small and select group of companies. That should give you a good idea of how we look at our dividend, saying that dividend is important to us is another statement we consider the very important aspect of our shareholder return and are committed to it.

At the same time we maintain the best credit ratings in the industry. Net debt to adjusted-EBITDA was at 1.75. And as we told you at the end of the last year the company will continue to focus on maintaining a strong balance sheet, but I suspect that with pending investments in the near-term we may go over our 1.8 times net debt to EBITDA target. Also as we told you earlier, after we closed the DIRECTV transaction our focus with free cash flow after dividends will be on paying down debt. That's a look of fourth quarter end of 2014 I would now like to turn it back to Randall to talk about our 2015 outlook.

Randall Stephenson

Okay, thanks John. We are going to provide more definitive 2015 guidance after we closed the DIRECTV transaction and we do expect that to happen in the first half of this year. Let me frame for you what you can expect from us this year, and I am going to start by talking about AT&T on a standalone basis, that is before our Mexico and DIRECTV acquisitions. What we expect to deliver is continued consolidated revenue growth, our adjusted-EPS growth will be in the low single-digit range. We will have expanding margins, consolidated wireless and wireline margins. We will also have improving free cash flow and improving dividend coverage.

I think capital expenditures will be in the $18 billion range, the same as we got earlier and that's thanks for the completion of a lot of the Project VIP initiatives. Now if we include Mexico and DIRECTV, the first thing I would want to note is that, we now expect to achieve ever higher multiyear synergies than we had communicated and anticipated we announced the DIRECTV deal. And so when you add Mexico and DIRECTV we anticipate no delusion to our adjusted-EPS, meaning our adjusted-EPS growth including Mexico and DIRECTV will be in the low single-digit range. We would like to 2015 a very different company. We'll be a company with the ability to deliver video to any device. We'll have a unique capability to integrate solutions across the diversified base of customers, geographies and technology platforms that are mobile, fast and highly secure and we will have a path to profitable TV growth. And we'll have a nice set of growing Latin American businesses positioned well in video and the mobile internet.

So that’s where we are focused for 2015 and beyond. We are very excited about the opportunities that are ahead here for us. And so with that Lorrie I think we are ready to take questions.

Question-and-Answer Session

Operator

[Operator Instructions]. Our first question from John Hodulik with UBS. Please go ahead.

John Hodulik

Couple of strategic questions for Randall if I could. First Randall you’ve been able to put together a Mexican strategy at a very reasonable cost. Is that how we should expect in terms of Mexico given the expectation that AMX is going to spitting off a large piece of their business over the next year or so. And then if you could expand that you also have a large footprint now in South America, especially Brazil, what are your thoughts on that market? And then maybe the same for Canada, you talked in a recent release about a North American calling market. If you could comment on your view on the attractiveness of those markets, that would be great.

Randall Stephenson

Sure John, thanks. I will start with your question on Mexico. And the American Movil asset sale has been one of those things floating out there, nobody really yet knows what that’s going to look like. And for us if we wanted to move into Mexico there were a couple of really unique opportunities in front of us. And just to try to flush out what was going to be required by American Movil to sell their assets seemed like an uncertain process. So we pursued use to sell and then with the Nextel Mexico assets what we have here is a set of assets, a spectrum portfolio that is really a robust spectrum portfolio, a nice cell site grid that will be a very nice place to start in a nice customer base. And so we have the makings for what we need for a very viable and strong Mexico strategy, where our America Movil sales assets are not and so that's what we try to do is chart a path that that would get us into Mexico and get us a platform that would sustain itself. And we like these assets. We think these assets are more than sufficient to compete in Mexico and to go and compete aggressively and take share, so feel good about the assets we've got.

On South America and Brazil, it's too early to say John. What we have down there is the best pay-TV business in Latin America and it's a business that continues to grow. It's got a great brand name down there. DIRECTV has done a very nice job of assembling some nice spectrum in various Latin American markets where they're doing a fixed wireless type solution for broadband, so there are number of markets where they have line of sight and the ability to bundle broadband with the TV product and their brand is strong enough that where they do that they have really-really good success. And so we're actually anxious to get the transaction closed and leverage those assets in Latin America and it is, it's a really good product, a really good footprint, a really good brand. So we're excited about getting it.

On Canada, I think right now we have about as much as we as a company can handle, we're not prepared to start talking about going north of the border right now. We've got a lot to execute on the DIRECTV, get the deal approved and then we've got some serious integration efforts that we need to get busy on and then obviously building out Mexico is going to be a full core press for the next couple of years. So we've got more than we can chew. We've bitten off more than we can chew right now and you'll see us focused on what we've consummated to-date.

Operator

We got to Mike McCormack with Jefferies. Please go ahead.

Mike McCormack

Randall, I guess just following on, you started off the conversation with the discussion around revenue diversification. What is your thought, just as you look at the US wireless landscape into 2015, with respect to how bad can it get from here, with respect to pricing and promotion. From AT&T's standpoint, is share loss okay? Are you willing to accept sort of lower-end share loss? And then maybe one for John, just thinking about free cash flow into 2015, if we ex-out DTV and the acquisitions, just if you could frame out the moving parts there to give us a little more comfort on the dividend payout. And also maybe just a comment on whether or not you have talked to ratings agencies about the appetite for how high leverage could go?

Randall Stephenson

Yes Mike. In terms of the wireless business, when you look at 2014 there's some aggressive pricing in the marketplace, but John I thought did a nice job of giving a good basis of compare to 2012. And so fourth quarter 2012, there were three competitors with an iPhone in the marketplace that was the last time there was a major iPhone launch. And our churn rate this quarter was very comparable to what it was in 2012 and this quarter there were everybody in the market had an iPhone and so the churn rates in the fourth quarter relative to what we've seen in the past were fairly consistent. When you look at the churn rates for the year in light of what I think was a very robust pricing environment we had our lowest churn rates ever.

Now as we move forward what we're really going to be focused on is the smartphone base. You're going to see us continue to penetrate our customer base with smartphones. We added a million in the fourth quarter by itself. And you're going to really see us focused more and more intently on the business side of the equation. And you're seeing how we're laying out what our segmentation -- of what our business segments will look like as we move into 2015. And we've had a lot of success really focusing on the business segment with our wireless products and bundling that with VPN solutions or security solutions. And as I mentioned in the opening, that when you put those two areas together, we'll not put the two together, but when you look at our enterprise business segment both fix line and wireless combined, it's growing 5.8% in the fourth quarter. That business segment -- that segment of customers churns lower than any other segment in the marketplace. It is price competitive, but it's interesting when you bundle it with VPN and other product sets, if you have a very-very nice business that grows very nicely and as John showed we're expanding margins as well. So we're really focused on the high end customer base.

The area where we're seeing a lot more pressure in the market is in the feature phones. We churn feature phones much higher than our traditional smartphone base and so that's what Cricket serves the purpose to do is to help us address that into the market with a very robust and aggressive prepaid product and as John pointed out in his comments Cricket we're getting to the transition and it is now growing our prepaid base is growing that customer base is obviously a very nice complement to what we're doing in Mexico, we're looking forward to taking advantage of the Mexico footprint to with Cricket and as you noticed in the last week we've announced that pre-unlimited calling from the U.S to Mexico and you will see more and more of those offers materialize going the other way as we build out the Mexican footprint and the Mexican network.

John Stephens

So, Mike this is John and with regard to free cash flow let me frame it up this way. As you know we've announced -- we're committed to do about an $18 billion range for CapEx that's about a $3.5 billion reduction in the CapEx or improvement in free cash flow, that's step one.

Step two is with all our free cash flow -- with all our CapEx spending and investment there comes some trailing expense. With a reduction in our CapEx we'll see a reduction to that trailing expense that will not only help us with margins but will also help us with free cash flow. So those are two major steps.

The third one is we have invested significantly in our customer base with regard to Next. High quality receivables, the banks continue to be interested in them but we have a portfolio of those that we will be able securitize this year and we will see some turnaround and payback of cash for those that we haven't securitized, so we're optimistic about that.

That will be pressured, those things will be pressured by the continued success of Next, so we may reinvest some of those Next dollars that we [indiscernible] this year, we may reinvest in our customer base, we will make those judgments as we go. And then we will see some increase in taxes but not significant but we will likely see some increases in taxes. With all of that being said we're very comfortable about the increasing free cash flow and improving dividend coverage guidance that Randall mentioned.

We carefully talked to the credit rating agencies, work with them on our plans and try to be transparent with what we have going on. I would expect we will see some -- they have made some announcements on their own and I am sure they will make their decisions as we kind of go through the rest of this year and the final VTV integration plans that we have they will come out and make their viewpoint shown. But those -- and I would tell you those conversations have been productive and constructive but they are well understanding our strategies and our approach.

Mike McCormack

John, I guess without the crystal ball, but thinking about the phone on the ARPU level, is there a level of penetration of the value plans inside your base where we should start to see that more stable? I know in the past, you talked about maybe stability as we get into 2015 on various moving parts. But I guess just isolating phone-only ARPU, getting a sense for when that might be more stable?

John Stephens

Yes, so Mike as you know on the phone-only ARPU when I think about that I think a phone-only ARPU plus our Next billings and if you look at that then sequentially they grew. And the difference between the historical service ARPUs and the service ARPUs plus Next billings that gap has been closing. You guys can figure out the math but quite correctly when you sell almost 6 million phones in the fourth quarter on Next and you start billing those for the entire first quarter and throughout next year on a $28 or $30 a month basis you can understand our optimism about improving ARPU's as we define those and remember we are fine that way because that's what the customer is paying in cash every month.

So we feel real good about where we're going and the where the process is, we're not predicting or giving a guidance with regard to when ARPU plus Next billings will be greater than they were in the prior year quarter. But we look forward to getting through this year and continuing the progress especially after having a fourth quarter where the sales team did an outstanding job of adding almost 6 million customers to the Next program.

Operator

Next we will go to Phil Cusick with JPMorgan. Please go ahead.

Phil Cusick

I guess the couple of things I want to hit -- one, if you could just clarify guidance. Is guidance to revenue and EPS growth, really just if we pull Connecticut out 2014, and, if so, what are the base revenue and EPS numbers?

John Stephens

Yes. Maybe -- we'll pull out Connecticut as you said we're not giving detailed analysis of the product line or sub products but your assumption Phil that it is without Connecticut is correct that is the base line.

Phil Cusick

Okay. Thanks, John. And then second, if you could talk about Next, 58% in the fourth quarter. What's going on in distribution? Are you going to expand that further? And do you expect a working capital drag in 2015 to be larger or smaller than 2014?

John Stephens

Yes. So the Next sales go like this, in our company owned stores, in authorizations great performance more than 80% nearly 90% as we mentioned, great take rate in a busy fourth quarter. Quite frankly on the large national retailers and the manufacturer owns retail stores the take rates were smaller but in the fourth quarter they had a lot of activity for us, they sell a lot of our phones, a higher proportion of fourth quarter because of the holiday season than any other quarter. And so we're optimistic about Next take rates increasing overall through the year and we're also optimistic about working with the national retailers and the other retailers to provide them additional support on how to sell Next and how it works.

So we're still real positive about Next and believe that we will get the number of customers on the non-subsidy plans in line with the number of customers on Next plus bring our own device. So we are really moving directly out of the subsidy business, that's a good thing long-term and short-term. With regard to the -- if free cash flow impacts will have the flexibility to monetize, we expect to have the flexibility to continue to monetize large blocks in these securitizations, it's worked very well. The banks continue to have very much interest. And as we stated before we want to continue a regular pattern of doing this so that we build the history for this out the -- that will keep us with flexibility and financing going forward. I would suggest you that the activities we have going on now are not intended to be looked at to generate cash flow in out of them in, in out of the sales to pump up cash flow in any way shape or form, it's really more of just a prudent management process throughout the year, we'll have flexibility to push forward or pull back to depending upon continued interest rates, continued attractiveness from the banks, and so forth, but so far the process has gone extremely well. We have been very pleased with not only the demand but also the financial terms.

Randall Stephenson

We'll continue to be confident this Next take rate [indiscernible] as John said in our retail channel we are now hitting 90% it's a learning curve. People learning how to sell this and the mechanics and the process for doing a handset financing program. We then moved it into our agent channel which is a very extensive agent channel. In the beginning it was not very impressive and the agent channel is now beginning to perform at levels that look like our retail channel. And so then you move into the big box retailers, it will follow a similar curve. And we come to the holiday season and John mentioned it then they are pushing volumes and this takes a little bit more time to sell a handset that's financed rather just one in a box. And so it's just going to be a learning curve, and we are going to stay patient but we actually feel very good that the numbers continue to move in the positive direction.

Operator

Thanks we go to Simon Flannery with Morgan Stanley. Please go ahead.

Simon Flannery

Randall, you talked a little bit about DIRECTV. Could you just give us a little bit more insight into the deal process? The 180-day clock expires in March. I think you referred to a first-half close, so how that's going? And any updates on the synergies? I think you talked about higher numbers. Is that content synergies? Is that more bundling synergies? Is that something that's going to come in early on, versus later? And I think you also talked about video to any device. I know Verizon has talked about an over-the-top rollout in mid-year. So is this something that you are going to have a similar type offering this year? And is that contingent on the DIRECTV close? Thanks.

Randall Stephenson

First of all deal process, you nailed when the 180 day clock is running again, but obviously there is a legal challenge going on between the content providers and the FCC and that’s kind of the big unknown in our process right now. We are hopeful that the two parties the FCC and content folks can get that deal settled in short order. I believe there is court proceeding let’s do here soon that will help to determine the pace in which that progresses. But even with that Simon, we are still fairly confident this thing gets done first half of the year. And so I can’t get any more refined that because of this issue. And so this issue would be the only issue that will cause a delay of the 180 day clock to our knowledge right now.

As it relates to the synergies, it's a fairly predictable formula with us and we do these large scale deals and when we are doing the deals we tend to be fairly conservative. And we have obviously have begun with the DIRECTV management team some forward discussions and getting to a level of detail that’s appropriate within the confines of the DOJ review and so forth. And so we are starting to see details on the channels and then channel costs and so forth. And as a result as you start drilling down through it, it's fairly much across the board we are seeing better opportunities and what we baked into the original deal economics. And so that’s why we are feeling pretty confident that we will exceed the merger synergies that we announced at the time that we did the deal.

And across the board there are looking good. There are even revenue synergies, when you have 20 million DIRECTV customers that are very, very high-end customers and see what the wireless penetration rate that we have in that customer base it looks really good. The opportunity to be able to sell mobility into those channels and so forth. So across the Board cost synergies, a few revenue synergies, it’s all looking better to what we had anticipated when we announced the deal.

And then in terms of video to any device, this is one of the key opportunities that we were pursuing. When we did this deal our customers are demanding video to be delivered across any device. And so one of the primary objectives we will have coming out of the close of the deal is taking advantage of the [content] [ph] relationships that DIRECTV has and our wireless customer base, we envision customers being able to walk out of our stores with content available to them on devices that they have purchased in our store. You are familiar with the order deal that we have done with the Chernin Group, where we are developing over the top content with them and taking advantage of ways of delivering that to our customers as well, so it's going to be a multi-faceted approach in terms of how we bring video to our customers, but we’re looking at multiple channels and channel line-ups that we’d be able to accommodate into our wireless customers both tablet as well as handsets as well as our broadband customer base 16 million broadband customers. And so stay tuned, there’ll be more to come, but this is a high priority for us is getting the content delivered to the mobile handsets and tablets.

Operator

We go to Joe Mastrogiovanni with Credit Suisse. Please go ahead.

Joe Mastrogiovanni

A couple follow-on questions, if I could. John, if there was an attractive opportunity in Latin America, maybe something sizable like America Movil is expected to be, given your funding requirements over the next few years, do you think a transaction like that -- you could do a transaction like that and stay within a comfortable leverage range? Or should we expect some equity component for a sizable transaction? And then, Randall, part of the strategy of allowing the base to move to new pricing, with the help on the churn side, and while we saw the benefits of that over the prior two quarters, we did see churn return to a level similar to two years ago, as you pointed out. Are you comfortable with the current pricing strategy in place right now? And do you think this fourth quarter was more of a one-time-ish in nature, or should we expect churn to remain at elevated levels as we move throughout 2015?

Randall Stephenson

I’ll answer John’s question on Latin America. The America Movil thing is just too uncertain even answer your question on and I will say it again, we’ve got all we can handle right now in Mexico. And we’re going to be focused on getting Nextel International closed, integrating that network, integrating those customer channels, integrating the distribution channels and getting ourselves scaled in Mexico, so anything else is just kind of speculation and then probably isn’t worth conversation at this point.

In terms of churn, I would tell you I’m comfortable with the performance we had in the fourth quarter as it relates to churn. And I’ll say it again, when we compare it to two years ago which was the last major iPhone launch and only three national carriers carrying the iPhone to have a comparable level of churn, with the kind of pricing moves we’re seeing in the marketplace versus two years ago, I think that’s pretty good performance. And this performance for the quarter, we’re comfortable with. We are as I mentioned before, really focused on that area of our customer base that tends to have the lower churn and that is our business customer base and the high-end consumer customer base where we’re experiencing the churn.

As John said in the feature phone side of the house and we will address that with our Cricket platform. And so right now who can call where pricing goes in this industry? I haven't the slightest idea. It moves, it’s very volatile, but right now we’d like the value equation we have in the marketplace. We have a customer base that demands reliability, that demands speed and that demands quality. They demand a very sophisticated consumer channel and business channel, we have probably the most sophisticated business channel in the industry for B2B. And we think it’s very important and we think also that that B2B customer segment is more and more demanding security solutions integrated all the way through the cloud with our net bond strategy and that’s proving to be a very powerful combination in the marketplace. So that’s where you’ll see us focused and like I said I can’t predict where pricing will go.

Operator

And we’ll go to David Barden with Bank of America Merrill Lynch. Please go ahead.

David Barden

Maybe first one, just Randall, obviously your views have been expressed on this Title II as a way to get to the net neutrality issue. But I guess from the investment community standpoint, are you of the view that there is going to be really anything different about the business, in terms of the business you do, or how you do it? Or are the investments you are making kind of on a middle- to long-term basis? If you could kind of talk us through the investment side of that equation. And then, John, just a question on the write-down of the copper plant. Could you talk a little bit about what that was, where it was, and what kind of expectations we have for that going forward? Thanks.

John Donovan

Sure Dave let me give Randall a break and I'll take the copper question first. We went through a study and in our business there is active payers that are copper payers that are connected to customers and serving customers. There's spare payers in that network that are available that are in great working condition and available to be used if needed. And then there are what we would consider dead payers or payers that need significant repair work that are not connected to any customers, they need significant repair work and investment to make functional.

We did a detailed study across our network by our network engineers in conjunction with that, identified marked and made the decision to abandon those ineffective payers or what we would -- what the [indiscernible] dead payers. We have plenty of capacity to serve our customers with our active payers and spare payers, so we don't expect any limitations on that. That's how we went through the process it was a very extensive process that was a very unusual process to go through. We don't expect any further write-offs like this we're not aware of any and we just felt it was appropriate to recognize this fact anybody has found our business has seen the change in our access line customer base over the last five or six years could understand that we would have peers that would be inactive and in this case ones that were not economical to activate not to mention the fact there is not demand for us to make that [indiscernible]. So that's the background on just across our traditional wireline footprint.

Randall Stephenson

A favorite topic title 2.

David Barden

Sorry Randall.

Randall Stephenson

Look I will address it from a couple of perspectives. First net neutrality, what this debate started out as to be pursuing was how do we protect net neutrality, a neutral internet. And I would tell you I am not -- I don't know if anybody in the industry who really argues that we shouldn't have net neutrality and indeed the President laid out four principals for what that meant. And we look at those four principals and said we're okay with those.

Those four principals is what resulted from all of this was the FCC were given authority to enforce those four principals, it has no bearing or impact on our investment decisions none whatsoever. What causes us pause is if the way you effect those four principals is by categorizing the internet and wireless services as title 2 communication services that's a different deal, alright and that's something we have to say what does that mean and whether the implications of categorizing these services as title 2 services to our industry.

And the example I give is we're right now trying to obsolete our old legacy telephone services moving to IP or to all wireless and there is a very specific process one has to go through to obsolete those services and replace them with the new advanced services. And we're working through that with the FCC, it's a very collaborative process it works but it takes a lot of time to make that happen. And we think that we might be able to get to a point where we can obsolete these services or begin replacing them with the new services by 2020 that's an aggressive time line.

The idea of beginning to put our wireless services and our broadband products under those categories and subjecting ourselves to that kind of regulatory oversight is what causes us pause and when we say we are pausing investment till we understand where this is going, that's what we're referring to.

Now Chairman Wheeler can find some creative solution, categorizing these as title 2 but doesn't cause the industry to slowdown, doesn't cause investment cycles to slowdown, does not cause innovation cycles to slowdown. It will give us some confidence and relief to continue investing at the same pace we have. But till we have kind of have clarity we're saying we're just on any new investments we're in a bit of a pause mode but it's really up in the air right now.

There are a lot of ways of getting what the President has articulated he wanted to accomplish. One of them is the Congress is working on it and that is that the Congress would pass legislation that would give the SEC the authority to enforce the four principals that the President articulated were important. That works to us, that puts us very similar to where we are today and probably doesn't change our investment thesis for anything we're trying to do.

But these really strident heavy handed regulations on wireless and broadband if we go down that path that's what causes everybody some apprehension and uncertainty and begins to change investment thesis and so forth. So it's up in the air, right now we're just anxious to see when the SEC comes out, so we now begin to formulate our plans.

Operator

And we will go to Amir Rozwadowski with Barclays. Please go ahead.

Amir Rozwadowski

I was wondering if we could chat briefly about your commentary that post the completion of some of your pending acquisitions, and some other initiatives that seem to be on the table, your debt coverage ratio may go over that sort of 1.8 times level. Could you perhaps give us a sense on where that could go? And, perhaps, what is your priority maintaining your near-term credit rating? It sounds like discussions with credit rating agencies have been constructive. But I was hoping to get some clarification, if possible.

John Stephens

I will take that if you look at the Direct TV transaction based on some of the most recent published financials you will know that there is a cash fees in that transaction that would approximate about 15 billion and I think if you go back to the last financial statement their gross debt level could be at $18 billion to $20 billion level that would be the debt we would be adding on as well as any impacts from closing Nextel and [indiscernible] as compared to our first quarter.

And then we've got some other -- as we mentioned we can't talk about the special options and so we won't do that, but will have other impacts from matters ongoing that will impact our debt range.

With regard to that it is very conceivable that our net debt to EBITDA ratio would go above two, I think that's assumed and possibly in somewhere in between the 2 to 2.5 range, I know that’s a great wide range but that’s where we feel comfort right now stating in. Those are the kinds of levels of debt that we would expect that could occur once we close all the transactions. What we would then focus on doing is because we will have accretive free cash flow after the DTV transaction as we said before we would take the excess cash flows after dividend and use that to commit that to paying down debt as quickly as possible.

We suggested over the course of the three year cycle that ought to get us back to what is more traditional levels, for us that’s a 1.8 times net-debt-to-EBITDA. And if you look at our current cost of borrowings, some of our recent transactions but quite frankly our entire portfolio today, we have after tax cost of debt well below 3%, so its producing interest expense at a very acceptable level at 1.8, where just a few years ago our expense rates were higher.

You might have gotten a comparable answer with the 1.5 or 1.6 net-debt-to-EBITDA. So that's where we are at. We will let the debt rating agencies deal with it as they see fit, but we are comfortable with where we are going and we understand the implications.

The last thing I would tell you here is as we announced last week we set up a facility with a collection of banks in 18 month, three year, five year terms for over $11 billion, the net after tax cost of that debt averages less than 1%. And we have been very transparent with our plans and activities, such that reasonable people at the banks are in this process are still very interested in providing a significant funding at very attractive rates within ability for us to prepay without penalty and ability just to live the if you will facility open until such time as we needed.

So we feel really good about where we stand in the crowded market. We will continue to work on it but we will continue to feel good about where we are at.

Amir Rozwadowski

Thank you very much, John. And just one additional follow-up, if I may. In addition to your significant acquisition activity, you folks have also been successful at monetizing some non-core assets over the last 12 to 24 months. I was wondering if we should consider this element of your strategy, and how it may fit into your priorities for 2015.

John Stephens

Yes Amir, it's a great question. I am not going to comment on the specific items. I think we started talking about monetization assets back three years-ago. I think that was the first major transaction we had done was a Yellow Pages transaction. So if you think back from that timeframe to today, you understand that -- I mean you clearly understand the multibillion, tens of billions of dollars we generate, I will say this we have a $300 billion of assets on our balance sheet and we have a history of being Fortune 100 type publically traded companies, we are done yet. We have an opportunity to do more. We will continue to evaluate and as management we have an obligation to maximize returns on our assets. So getting to high utilization and high results that's part of our responsibility, we will continue to focus on it. Though the balance sheet as large as ours it would be inappropriate to collecting the things are complete. There is always opportunities.

Operator

And that is from Brett Feldman with Goldman Sachs. Please go ahead.

Brett Feldman

So, earlier, Randall was talking about lessons learned as you move up the curve with Next. One of your competitors, T-Mobile, has learned that they can change the way they provide credit to their customers. They are placing a higher priority now on payment history than some of the traditional credit metrics. Have you learned the same thing? And is there any change in the way you are extending credit to your customers as they adopt Next? Thanks.

Randall Stephenson

I don't think there are lessons learned, I think all of us over the years in this industry know that you know your customers better than anybody else does. And customers that have been with you for a period of time regardless of what their credit scores are you tend to treat differently. And we have for many years done that whether it be on the fixed line side or broadband, U-Verse customers who pay us well that may have lower credit scores, we have actually gone ahead and extended them services like U-verse which requires significant upfront investments and so forth. You are doing on the business side of the house too, you know your customers well. And so you are willing to invest in your customers that you know who may have credit scores that are weaker than what a new customer you will be willing to do with the new customer coming with a low credit score.

So there are not any new games in this business, we have all been playing this credit scoring game for a long time. It's a fairly predictable process, we know our customers well, we know when we tweak credit policy, what to expect and within what timeframe to expect that reactions. And it's actually gotten fairly mechanical and arithmetic to be quite honest with you. So I don't think there is any new science out here on this.

Brett Feldman

And are you finding that the banks that you are working with are recognizing those lessons that you have learned in the way they finance your receivables?

John Stephens

Absolutely. We have gotten very high, that's one of the reasons why we have high demand in a securitization process and we are able to get the pricing levels that we are able to get. So they recognized that and quite frankly all of you know, most of you go to our financial statements and our provision for bad debts and understand with a company that has over $130 billion worth of revenues, you can clearly see just how effective we are at managing -- particularly in a difficult economy how effective we are in managing our receivables. The team has done a very good job across the board business consumer through processes just like Randall described.

Randall Stephenson

You bet. Thank you Brett. Thank everybody for joining us and taking the time to listen in on the call. As we articulated at the beginning, we feel very good about where we're going in 2015. As we get to the end of 2015, we're going to be talking about a very different business and a very different company and we're excited about it and look forward to working with you over the course of this year. So thanks again for joining us.

John Stephens

Thank you all very much. Take care.