Operator

Ladies and gentlemen, thank you for standing by and welcome to the AT&T's First Quarter Earnings Release 2014. At this time, all lines are in a listen-only mode. Later, there will be an opportunity for your questions and instructions will be given at that time. (Operator Instructions) And as a reminder, this conference is being recorded.

I will now turn the conference over to Susan Johnson, Senior Vice President, Investor Relations. Please go ahead.

Susan Johnson

Thank you, Cathy. Good afternoon, everyone, and welcome. It's great to have you with us today. I am Susan Johnson, Head of Investor Relations for AT&T. Joining me on the call today is John Stephens, AT&T's Chief Financial Officer. John will provide an overview with perspective on the quarter. Then we will follow up with questions and answers.

Let me remind you, our earnings material is available on the Investor Relations page of the AT&T website, that's www.att.com/investor.relations.

Now, before I turn the call over to John let me quickly cover our consolidated financial summary, which is on Slide 3. We had our best consolidated revenue growth in more than two years up 3.6% driven by strong wireless growth, our best consumer wireline growth since the introduction of U-verse in 2006 and rapid growth in strategic business services.

EPS for the quarter was $0.71 when adjusting for some transactional expense associated with the Leap acquisition. When compared on an adjusted basis that's up nearly 11% over last year's first quarter. Consolidated margins were up year-over-year due to wireless expansion margin expansion offsetting wireline pressure.

Cash flow started the year strong. In fact cash from operating activities for the quarter was the highest it's been since 2007 $8.8 billion. Our solid cash flow allowed us to make significant investments in Project VIP and the growth drivers of our business. Capital spending was $5.8 billion and that gave us free cash flow of $3.0 billion for the quarter. We also continued to be opportunistic in buying back shares as part of our repurchase program. In the first quarter, we bought back about 37 million shares for $1.2 billion.

Now with that overview I'll turn the call over to AT&T's Chief Financial Officer, John Stephens. John?

John J. Stephens

Thanks, Susan and hello everyone, and thanks for joining us today and for your interest in AT&T. Before I get to our operational highlights, let me take a moment and give you a broader view of our business strategy beginning with slide 3. As you know, we have been working very deliberately on multi-year plan to transform our business.

In the first quarter, we really began to see the benefits of this transformation effort. You've seen us transform our networks from the legacy services to an all IP platform and a best in class network. Project VIP is accelerating that transformation through our LTE deployment, U-verse expansion and fiber build to businesses. We also reached a significant milestone in the quarter with our domain 2.0 initiative. We named two leading companies, Amdocs and Juniper Networks, as primary vendors that will help us achieve our vision of a user-defined network cloud of modern cloud-based architecture.

We also make significant strides in transforming the wireless customer value proposition. This transformation began with the move from feature phones to smartphones. These smartphones soon became the remote control of our lives and drove significant data usage. In recent years we began the transition to usage based pricing and away from device subsidies.

In the first quarter, we accelerated that transformation, thanks to the transparency and simplicity of our Mobile Share and Next plans. At the same time, we transformed our wireline business from legacy services, such as DSL to IP networks and IP services. In the first quarter this transformation helped drive our strongest consumer wireline growth in years. And in business our strategic business services continued its steady growth. And our transformation is not slowing down.

Yesterday, you saw us announced plans that strategically target 21 new markets to expand our ultra-fast fiber networks to deliver U-verse with GigaPower. Moves such as this are one more indicator of our ongoing transformation. Behind all this is the strength of our balance sheet, our strong cash from operations allows us to return substantial value to shareholders through dividends and share buybacks, while still having the ability to invest in our future.

Now let's get to our highlights for the quarter which begin on Slide five. We had an impressive start to the year. Let me begin with a quick overview of the quarter. We made major moves in wireless that are reshaping the way we do business. We completed our Leap transaction and have begun the integration process. This will accelerate our prepaid initiative as we launched a new Cricket brand in the second quarter. And we have reached a critical point in our wireline business where we can clearly see that our Project VIP plans are working and transforming the business. These efforts results in our strongest consolidated revenue growth in more than two years while also driving double-digit adjusted EPS gains. And we did this while still dealing with a very weak economy.

To start wireless execution was superb in the quarter. We had our best postpaid net adds first-quarter in five years and revenue growth was strong. We also made massive strides in changing the subsidy model giving customers greater choice and a more transparent way of choosing their wireless equipment and service plan.

AT&T Next take rates were strong as more and more customers chose the installment plan method of purchasing handsets. And the shift to Mobile Share plans was nothing short of incredible. The number of new Mobile Share counts and connections tripled year-over-year with nearly half of our accounts now on 10 gigabyte or larger plans.

At the same time, U-verse continued its steady march of transforming our wireline business. In fact we had our best consumer wireline revenue growth since the introduction of U-verse about eight years ago. And the outlook for U-verse continues to be solid, as we expand the U-verse footprint and look to increase penetration.

Transformation also continues in business wireline, strategic business services revenues were up more than 16% in the quarter. So, a very solid start with excellent momentum. Now let me provide more details starting with our business our wireline, our wireless business on slide 6. Perhaps the biggest story in the quarter was the strong growth in total and postpaid subscribers, we added more than 600,000 postpaid subscribers in the quarter with smartphones and tablets leading the way, that’s more than twice as many as the year ago and the best first quarter in five years.

Overall, we had more than a million net ads in the quarter, as we showed year-over-year improvement in every customer category. In prepaid, we continue to make progress in adding smartphone subscribers. In the first quarter alone we added 255,000 prepaid smartphone subscribers to our network, this help drive year-over-year prepaid revenue growth. Also during the quarter, we took a major step in transforming prepaid with the close of our lead transaction, adding 4.5 million prepaid customers of which nearly 70% are using smartphones. We are really excited about this new opportunity. Churn continues to be a solid story for us. Total churn was stable for the quarter with postpaid churn down sequentially and up slightly year-over-year. That is a great achievement and what is definitely a noisy competitive environment.

We believe Mobile Share will have a positive long-term impact on churn. In fact, postpaid churn got progressively better throughout the quarter. As the transition of our customer base to usage-based plans accelerates, so does the shipping of our handset sales to AT&T Next. Those details as well as revenue breakouts are on Slide 7.

The transformation of our customer base can be clearly seen in this quarter. The combination of AT&T Next to Mobile Share value plans has annual level of transparency in the smartphone buying model that customers haven't seen before. This new model lets customers choose, what plan best suites their need, and many customers have been choosing to move after subsidy model for simpler pricing and for a large number of our customers that means AT&T Next. More than 40% of smartphone gross add and upgrade to the quarter were on AT&T Next, that's up from 15% in the fourth quarter. We shipped away from the subsidy of subsidy model as major implications.

First, when we shift two equipment and service as customer signed up for the next contracts you. You see that in our strong equipment growth to the quarter with slower service revenue growth. Second, AT&T Next accelerates the move to LTE capable devices. About 57% of smartphones on our network are LTE capable providing a superior customer experience on a best-in-class network that also means the honorable sufficient network? And third we see this as an investment in our high quality customer base and in customer choice.

It peels back the layers of the subsidy model and allows customers to make clear choices. It also helps build a stronger bond with our postpaid base in a noisy competitive environment. And we believe we are well positioned to use working capital in this way. With our strong balance sheet, we believe we can do this prudently and effectively.

Another important aspect of Next, is that these are highest credit quality customers, that's Next was designed for and that's who is selecting Next. I talked earlier about our transformation, it leads us to a different set of metrics, than what we have used in the past. Next in a shift to equipment revenue changes the way we look at ARPU. Phone-only ARPU a metric we have shared for sometime and which includes only service revenue increased by 0.4% in the quarter.

However, phone-only ARPU plus Next monthly billings increased by 2% year-over-year. This move to Mobile Share plans in the quarter was incredible, more details is on slide 8. During the quarter, we introduced several new Mobile Share value pricing plans for both families and individuals to help customers move out to subsidy model. First, we introduced new attractive pricing for the 10 gig or larger plans for customers who purchase a phone with AT&T Next or bring their own device.

Second, we rolled out similar value pricing for one and two gigabyte plans. At the same time, we made it easier for subscribers to move off the traditional subsidy model by allowing them to take advantage of these attractive new Mobile Share value pricing options in advance of upgrading to Next. We see this as another investment in our customer base. The cumulative impact of these changes was significant.

First, the number of Mobile Share accounts and connections rose sharply in the quarter, increasing by more than 50% since year-end and tripling year-over-year. Second, there was a major migration of subscribers to Mobile Share plans up 10 gigs or higher. Customers bought up more than two-thirds of Mobile Share account activity with the gigabytes or higher plans in the quarter driving overall penetration to almost 50%, that's up from just 27% in the fourth quarter of 2013.

And third, these new offerings prompted about 1 million postpaid subscribers who were on unlimited plans to elect to shift to Mobile Share pricing. This helped drive the overall number of smartphones subscribers on tiered data pricing to 81% that's a full six percent point increase in just one quarter. At the same time, we added more than $1 million new postpaid smartphone customers that includes customers who are staying with us and upgrading from feature phones. Our postpaid smartphone sales continue to run in the 90% plus range and our total postpaid smartphone base is at 78%.

Now let's look at margins on Slide 9. In the first quarter, wireless EBITDA service margins were 45.4% that's a 220 basis point increase from year ago levels. Even though we had a significant increase in postpaid gross add year-over-year. The margin expansion was driven by several factors, such as the move to the 24 months upgrade, network efficiencies, and operational improvements. Next also had a positive impact on margins.

All these activities more than offset the pressures we saw in the quarter. Cause of strong net adds both postpaid and total customer growth, additional promotional activity relating to our transformation, additional customer care costs related to Mobile Share and Next, and increased start-up investment in prepaid and digital life.

Our actions to improve margins also help to ease the pressure from about 1.1 million accelerated smartphone upgrades that occurred in the quarter. These are customers who took advantage of new pricing and move to Mobile

Share plans and upgraded early. Without this boost, Next take rate would have been closer to 35%. In total, we had 2.9 million AT&T Next sales in the quarter. And now more than a quarter of our postpaid smartphone base is on a Mobile Share value non-subsidy pricing, and is no longer tied to the subsidy model.

Another margin comparison to total wireless EBITDA margin that was stable year-over-year even with all the growth in investment activities we had underway in the quarter. There is a lot of moving pieces in our wireless business last quarter. The huge shift to Mobile Share plans, the tremendous popularity of AT&T Next, the increase in total and postpaid net adds, and the transitional way for the subsidy model. But it all comes down to customer choice. We are making the buying process as open and transparent as possible and then letting customers manage the process. We believe this is not only best for our customers, but best for our share holders.

Now, let me turn to our wireline story starting on slide 10. The wireline story continues to be one of the transformation. That transformation began first in consumer when we introduced U-verse, since that time we have flipped the revenue model. But once with the declining revenue stream at a 4.3% growth in the first quarter accelerating from 2% a year ago.

Total U-verse revenues are now at nearly $14 billion annualized revenue stream and still growing at almost 30%. And U-verse now represents almost 60% of consumer revenues. We also see the transformation in our broadband results. More than two-thirds of our total broadband base are about a 11 million subscribers are now on U-verse broadband, highest speed and highest quality product. These gains drove total positive broadband net adds in the quarter. And we are positioned to continue that growth as our U-verse footprint expense and penetration improves.

It also helps drive total broadband ARPU which was up 9% in the quarter. U-verse TV continues to be popular as we added more than 200,000 subscribers churn continues to be low as penetration is growing. And U-verse voice, our voice-over-IP product just passed 4 million customers. We also announced that important initiative in the over the top space with the churn in group.

We are excited about the new venture and believe the combination of our two skill sets can create something truly impressive. We hope to start rolling out an offering later this year. Now let's move to business wireline which is on slide 11. While wireline consumer was the first out of the gates with this move to IP, wireline business started the process a little later, but you can still see the transformation going on there as well.

The clearest way to see it is in the steady consisting growth of strategic business services. These are services such as VPN, Ethernet, hosting and other advanced IP services. Those services now make up more than 26% of total business wireline revenue and growth is up more than 16% year-over-year.

Overall revenues were down year-over-year inline with the slow economy and recent trend, but there are positive signs. In enterprise, our global business services we actually showed slight service revenue growth year-over-year, given recent headwinds that seemed as very positive. The biggest drag on the quarter was wholesale. It was challenged by network grooming, as wireless carriers aggressively decommissioned the legacy circuit.

However, if you look at our retail business by itself, enterprise, and small and medium size businesses total revenue was down only slightly in the quarter. And when you look at what business customers' pay us for their total AT&T bill, both wireline and wireless total retail revenue actually grew year-over-year. We expect our transformational IP will continue to make headway in the business space. At the same time we continue to look for the signs that the economy will improve and provide us with additional lift.

Now, let's look at consolidated wireline margins on Slide 12. You see the impacts from our transformation on these consolidated margins. For the quarter our consolidated margin was 19.3% up 40 basis points year-over-year. Wireless margin improvement help to offset wireline pressure from the trailing expenses tied to Project VIP. Wireline margins were down from a year ago, but essentially flat with fourth quarter. Declines in legacy services, and content, and retransmission price increases pressured our results.

And this pressure was partially offset by relative consumer revenues and gains and strategic business services. At the same time Project Agile is gaining steam. Project Agile's are new initiatives that is improving efficiency and how the company organizes and operates to deliver best-in-class customer experience as in all IP, all mobile and all cloud services company. We are taking our initial cost savings from Agile and reinvesting in the Project. We expect one rate savings in the $3 billion range by 2017.

Now let's move to cash flows our summary is on Slide 13. Our ability to generate cash continues to be strong, in the first quarter cash from operations totaled $8.8 billion or about $1.70 a share, that's the highest cash from ops in seven years and almost four times our quarterly dividend commitment.

Capital expenditures were $5.8 billion as we took the strong cash flows and invested in Project VIP. And free cash flow before dividends was $3 billion on track with our full year guidance even as AT&T Next changes the subsidy model.

In terms of uses of cash, dividend payments for the quarter totaled about $2.4 billion and we repurchased about $37 million shares for another $1.2 billion. Our board of directors has also approved a $308 million share buyback as we continue to be opportunistic in buying back shares. Since we begin buying back shares about two years ago, we have bought back about 13% of the outstanding shares of the company and save more than a billion dollars in cash from eased divided requirements.

We also continue to look for opportunities to monetize some of our assets. This included more than $400 million in sales of América Móvil shares and real estate in the first quarter. We continue to move forward on our brands to sell our Connecticut wireline properties to Frontier for $2 billion and we expect that transaction to close by the end of the year.

During the first quarter we also closed our Leap acquisition. A high level look at that strategy and integration of Leap assets is on Slide 14. First and foremost the acquisition of Leap has clear and immediate benefits and value creation. The value of the spectrum what we see was significant about $3 billion in value. At the same time we will be able to get significant value from Leap's $3 billion tax net operating loss and turn that into real cash for shareholders. And finally, we immediately refinance about 90% of Leap's debt which will save us $500 million in interest expense or just the remaining term of that debt.

When you add these synergies together, the value of just these items was greater than the total purchase price of Leap. From a strategic perspective, the acquisition of the Cricket brand accelerates our move into the prepaid space. We planned to launch the new Cricket brand in the second quarter combining with AT&T's existing prepaid operations to create the new cricket with the national presence and more than 3,000 distribution points across the country. The focus will be on simple plans with affordable devices helping customers take advantage of this thing, of the smart new choice in no contract wireless and all this is not a best-in-class network.

We are also integrating Leap customers and its networks. The customer transition is expected to take about 18 months as we move customers off of the outdated CDMA network on to AT&T's GSM network. We will start deploying unutilized spectrum immediately, continuing our efforts into 2015. Integration costs are expected to be about $1.2 billion over a two year period with about half of that expected in 2014.

CapEx will be in a $1 billion range, but significantly offset by efficiencies with other wireless bill plans and with the majority of the spend targeted in 2015. Leap operational pressure will drive $0.05 of dilution in EPS this year with most of it in the second half of 2014.

We are very excited about this new growth opportunity and expected to really kick start our new prepaid strategy. We are also updating our outlook for the full year after Leap acquisition. Those details are on slide 15. We now expect consolidated revenue growth of 4% or greater for the year as we hold in Leap and see continued strength in wireless and wireline consumer. We continue to expect stable consolidated margins, which includes Leap operational pressure. So we expect EPS growth in the mid single-digit even with the dilution from the Leap operations and continue to investment in growth initiatives.

We still expect capital spending to be in the $21 billion range that we gave you in January with most of Leap's integration impact in 2015. We also expect free cash flow in $11 billion range at even with expected strong Next sales and Leap cost. And you can expect us to continue to invest in our business transformation and growth opportunities.

And now I will turn it back to Susan for quick summary of the quarter and then we can get to your questions.

Susan Johnson

Thank you, John. Our recap of a very solid quarter is on slide 16, we definitely saw the impact of our business transformation in the first quarter. Revenue growth was strong that includes the best consolidated revenue growth in more than two years and the strongest consumer revenue growth since we launched U-verse. That help drive double-digit adjusted EPS growth for the quarter, wireless was led by the best first quarter postpaid growth we've seen in five years and AT&T Next and Mobile Share are transforming the customer value proposition, and put a large dent in this subsidy model while accelerating the growth of larger tiered data plan.

In wireline we are seeing the impact of our investments in IP. U-verse continues its robust growth and business continues to transform with growth and strategic business services. I will now close out the call with a quick review of our Safe Harbor statement and then we are going to open it up for question-and-answers.

Our Safe Harbor statement is shown on slide 2. This presentation and the comments we are going through make contain forward-looking statements that are subject to risks. Results may differ materially, details on our SEC filings and on AT&T's website.

And now Cathy let's go ahead and we will open up the call to take your questions.

Question-and-Answer Session

Operator

Thank you. (Operator Instructions) We will take our first question from Simon Flannery with Morgan Stanley. Go ahead please.

Simon Flannery – Morgan Stanley & Co. LLC

Thank you, very much. Good afternoon, John, if we could start with the guidance revision, and in particular, the Next impact. Can you just talk about the context of where you are in the middle of April versus where you were in January, when you set the original guidance? It sounds like Next is gaining more momentum than you expected. So if you could give color around this 35%, 40% - are you expecting that to be 50% next quarter or 60% in the second half? Some color around what you expect, what we should think about there, and how that has changed over three months. You gave the monthly take rates last quarter; you didn't do that this quarter. And then if you could just touch briefly on Europe. Any update to the commentary around, perhaps, the window being closing there? Thank you.

John J. Stephens

Thanks, Simon. Thanks for your question. First and foremost with regard to Europe, we stand by what we said before for all the same reason we said before the window is closing by the day, but I will say this as you can see from these results and as Randall and I and others have said before we are focused here on this market and you can see why from the success that we've had in this first quarter, see why we have that focus here in the United States and remains there.

With regard to the Next impact from an adoption standpoint, what we wanted to make sure everyone was aware of that, we made a decision in February to allow customers to early adopt or early upgrade under Next and that drove about 1.1 million early adoptions that drove the margin pressure quite frankly in the first quarter, we were able to overcome it, but those early adoptions to drive some pressure, so the real normal kind of a run rate for the group of customers that were qualified under a normal 24-month process ended up being about $1.8 million, and that's about 35%.

So we did grow from that December 20% or the fourth quarter overall 15% up to 35%, and we will see how it goes forward. I wouldn't expect that same acceleration from the 15% to more than 40% because of that early adoption, and quite frankly because of the early adoption we may have some impact on the customer during the last three quarters of the year because they move their adoptions up and causes that margin pressure in the first quarter. But I do – we're very pleased with the take rates, customers seem to like it and we're going to expand some of the channels we have the sales in. And so I do believe that the 35% is going to become a new standard, we may do better than that and we'll see how it goes as we move forward, we're not giving a specific prediction.

Simon Flannery – Morgan Stanley & Co. LLC

Okay. So there has been a little bit of a change in your expectations, I guess, versus when you set guidance originally, because I guess you are only changing revenues at this point. But I guess there are some puts and takes on the other lines.

John J. Stephens

Yes, I mean so what we do on our revenues is really off the strength of consumer wireline, what we saw there, and quite frankly off the strength of wireless as much as Next certainly we'll have an impact, but really it was much more about postpaid net adds and total net adds. And as we mentioned earlier what we've seen in churn and this improving churn picture that we've seen throughout the quarter giving us optimism about the full year and a ability to raise that guidance to 4% or greater. That's what's driving the change in guidance.

Simon Flannery – Morgan Stanley & Co. LLC

Good. Thanks a lot.

John J. Stephens

Thank you.

Operator

Thank you. Our next question is from Mike McCormack with Jefferies. Please go ahead.

Mike L. McCormack – Jefferies LLC

Hi, guys thanks. John, just thinking about the higher Next uptake, I think, than what was initially anticipated, and outpacing. The impact on the cash flow – obviously, you are not changing your guidance for that, but were there anticipated levers that you are thinking about pulling there? And is VIP factoring part of that thought process? And then thinking about wireline margins, what are we thinking about the puts and takes there as far as the ability to increase margin? Does Agile have a positive impact? And thinking about U-verse margins overall, are they starting to contribute in a more meaningful way?

John J. Stephens

Thanks for the questions, Mike; let's make sure I knock them all off here if you will, first and foremost with margins in wireline, [we feel we are at] [ph] in our VIP build process, we are going to continue to see some investments and the customers in the build through 2015.

So while we are working very, very hard to improve margins as we did sequentially in the first quarter as we did we expect real margin or larger margin improvements in 2016 and forward in wireline, so it’s the first point. Agile is definitely generating savings and we’re optimistic about its impact. But right now at this time we are choosing to reinvest the savings wherever we can in a prudent manner to accelerate the overall growth of the company.

Third with regard to free cash flow the real thought process on not changing guidance as a couple of different factors one we came down with the final Leap business plan, we are focused on getting the unutilized spectrum into service right away; we have some commitments on a 90 day and a 12 month process, quite frankly that’s – putting that spectrum to use, the team is really good at it. They are already well underway on it but it’s not a capital intensive, it’s adding it to already existing network, the big piece the capital the transformation and the CDMA network to our GSM network is going to really have a capital pressure in 2015. So that’s the first point.

Second point is our working capital is evidenced by our cash flow operations of $8.8 billion, our working capital was very strong. And we have efforts across the board receivables, payables, inventory management a number of items. The success the overall team showed is being able to achieve good cash management gives us the confidence to keep free cash flow guidance at the same level even with these increasing Next sales.

So really that’s where that’s going. With regard to your specific question on financing and VIP, we have a very active process in evaluating that. We have not done that. We haven’t committed to do that. It all comes down to costs, and whether we can do it in reasonable manner from a cost perspective. We are optimistic about the ability to do that and we have a - we are well down the road and talking to really qualified parties who’d be interested in participating with us; we haven’t made that decision yet.

Mike L. McCormack – Jefferies LLC

Great, thanks John.

John J. Stephens

Thank you, Mike.

Operator

Thank you and our next question is from John Hodulik with UBS. Go ahead please.

John C. Hodulik – UBS Securities LLC

Okay. Thanks. John, could you just give us a little more detail on the accelerated upgrades that you saw in the quarter? Is that going to continue into the second quarter? And if possible - I could probably figure it out - but if you could quantify the impact on margins. And then as it relates to service revenue growth, we saw a deceleration there, but then stronger customer adds than we thought. How should we expect that to trend through the year? I mean you know, it was a big decrease quarter-to-quarter. Is that going to continue, or is this a sort of a new level? How do those two variables work out? Thanks.

John J. Stephens

Well, let me make sure I get things knocked out here for you. John first of all the 1.1 million, let me give you this impression, or this explanation. First and foremost, with an average unit costing about $600, those that are sold on Next would cause us to recognize $600 of equipment expense. On a revenue side, we would start by measuring those receivables which will be $600 million and then basically taking two charges against those, one for an interest charge for the receivable being payable over 20 months to 26 months.

But secondly, for the forgiveness of the remaining receivables when the phone is traded in and we're not giving specific numbers, I will tell you, we have gone by model by model and evaluated the trade-in value, and we take into account all kinds of variables, whether we sold the model, the day it was launched whether we sold the model, six months or eight months after launch, so on and so forth. How other related models been selling in the used market, whether there is an overseas market, we take all this into account. Essentially though I can give you this kind of guidance, on the day we issue it, you could have a write-down on the revenues from the handset from anywhere from zero to 25% depending upon the different facts and circumstances.

I'll just give you that as the way to think about it, you can make – you could then take that differential, those discounts on interest and those discounts on the trade-in value, and compare how much of a loss that generates per unit, it will give you the idea of kind of the pressure we face in the first quarter from those accelerated units.

Secondly, I can't give you specific guidance on how that continued upgrade opportunity will impact this in the second, third and fourth quarter. The same program is out there, it's the available number of people that take advantage of it, had shrunk for two reasons. One because the 1.1 million customers already took it and two because we've expanded time and some of the people are recovered by, now would have qualified anyway. And so it will work itself down, I would suggest you though the strongest piece of it may have already occurred just because it was so successful on the first quarter.

We forgot the customer adds. John, we are not giving specific guidance on that. I will tell you, we were very pleased with the strength of the customer adds improved throughout the quarter. And the churn improved throughout the quarter. So we believe that this combination of Mobile Share, Next are quite frankly transparency and pricing and if you will, upfront honestly with customers is working. And we believe that's going position us well in this, what I call noisy competitive environment. So we're optimistic about going forward with it, but we are not giving any specific guidance.

John C. Hodulik – UBS Securities LLC

Okay, thanks John.

John J. Stephens

Thank you.

Operator

Thank you. We have a question from Joseph Mastrogiovanni with Credit Suisse. Go ahead please.

Joseph A. Mastrogiovanni – Credit Suisse Securities LLC

Hi, thanks for taking the question. John, given the growth you are seeing in data, now with a plan to sell prepaid more aggressively on the LTE network, how comfortable are you with your spectrum position? And you know, we have seen the comments about potentially reevaluating your participation in the broadcast auctions. How do you view your need for low band versus mid band spectrum?

John J. Stephens

Good question Joe. Let me first, be clear on something with regard to the broadcast spectrums. We would like to participate at the auction, we are and have been working with the commission to establish auction rules that will fairly promote a good result for AT&T, but we will also pull out successful result for the auction. So we are interested in participating. With that being said, I will tell you, I'm very pleased we got the Leap transaction done. And that we are able to work through with the SEC and the DOJ to get that completed.

The unutilized spectrum that we have available to us immediately in over 200 markets that our team is putting into service right now is actively getting that done is really helping us and will help us in quality service in dealing with the network demands. This acceleration through Next in these early upgrades to LTE devices is really helping us with our network, because our LTE network is our most efficient.

So we're moving a lot of customers on to that and that's another way we're dealing with our issues. If you will though, the first and foremost is we feel pretty good with our spectrum position right now we feel like we could position ourselves well with the transactions the spectrum deals we done over the last few years. And we're optimistic about it, but as with anybody we are always looking to continue to have that available. Last question again Joe, was on prepaid and quite frankly that's a great opportunity for us particularly with the new Cricket brand that if you will platform that distribution, that customer saying that we haven't necessarily focused on in the past.

Second, we believe the network differentiation will provide a real opportunity there. The third as we mentioned 70% of the cricket, new Cricket customers use smartphones. So over that 18 months when we have to transition them to GSM smartphones, it will be really – it could be very opportunistic for us if we're able to figure out away to take our next program trade-in and provide those kind of quality handsets to our prepaid customers, not only elevate the cost, but give them a real quality experience. So we're optimistic about all that, we'll have to do – have a lot of work ahead of us, but we're optimistic about it.

Joseph A. Mastrogiovanni – Credit Suisse Securities LLC

Great, thanks.

Operator

Thank you. We'll go next to Philip Cusick with JPMorgan. Please go ahead.

Philip A. Cusick – JPMorgan Securities LLC

Hey, guys thanks. I guess, first, a really quick follow-up. I wanted to make sure that I understood when you talk about the revenue guidance increase; does that include the acquisition of Leap? Is that in there?

John J. Stephens

Yes, it does.

Philip A. Cusick – JPMorgan Securities LLC

Okay. And that's about, call it, 100 basis points or a little more. Is that fair?

John J. Stephens

100 basis points? That's a fair number, yes.

Philip A. Cusick – JPMorgan Securities LLC

Okay. And then, I guess, second question: as you think about the Next plan and sort of making it transparent for customers on what the handsets cost, are you seeing a different sort of selection of handsets for Next customers versus subsidized customers, when they walk in and they see what handsets really go for?

John J. Stephens

So I think it's a little early for us to make any conclusions on that I won't – I say that in suggesting that I don't know that we've seen anything that is really substantially different, so we don't want to leave you with the impression that we have and we're not sharing it. It just hasn't happened yet. But it is early in the process. I'll say it's as much as anything; it's been a great process for us. When we started the trade-in program last year about the middle of last year and learned about how the trade-in process would work and how to utilize and then taking those skills for us, quite frankly in the first quarter we're continuing to learn and continuing to refine the process. But I can't tell you we've seen a dramatic change in purchasing activity.

Philip A. Cusick – JPMorgan Securities LLC

And just to follow up there, what is the sort of reverse logistics happening in that trade-in program? What are you doing with the phones now? And how do you expect to deal with them as the volumes, I would expect, ramp pretty aggressively in the next couple of years?

John J. Stephens

So it’s about expect from the next program itself we don’t have very many trade-ins yet, right, because we haven’t lapped the first year and that first 12 months cycle. But the expectations are couple one we are seeing great take rates on our insurance program, not only historically but specifically with Next. And so these trade-in phones we expect will be used in our insurance fulfillment that’s one. Two we are working hard to figure out a way to make them cost efficiently deployable in our prepaid market whether in specifically in the new Cricket brand.

Three we always have the opportunity to sell them on the wholesale market which is what we did mainly last year, with the quality of the handsets our customers use and without having the international standard for handset technology, we were satisfied or pleased with the demand for our handsets that we dealt with last year and feel optimistic, because the handsets we may be dealing with this year might be newer in their lifecycle than the once we had do with last year. So those are the, if you will, mechanisms to make sure we get value out of the process.

Philip A. Cusick – JPMorgan Securities LLC

Got it thanks John

Operator

Thank you. We now have a question from Tim Horan with Oppenheimer. Please go ahead.

Tim K. Horan – Oppenheimer & Co., Inc.

Good afternoon guys. Great quarter. John, I think you blew through – definitely our estimates, but I think the Street estimates, on subscriber adds. Can you maybe give a little more color? What's going on? Do you think the overall market is just expanding, or are you guys kind of gaining share? If so, maybe talk about who you are gaining it from? And then I guess we were concerned, and there's been some concern out there, about the early termination fees that some of your competitors are paying. Can you talk about how that process hit you throughout the quarter? Thanks.

John J. Stephens

Yes, sure Tim. Let me, first of all I would say that lot of the offers that came out right at the beginning of the quarter. I will say that they didn’t have the impact but I will say that the impacts and everything we did change throughout the quarter, and specifically the biggest impact was the decision to push Mobile Share, value plans in February and early adoption of Next.

And when we did those two things in connection, we saw significant take rates and we saw improvements in not only in customer growth customer additions. But we saw a churn come down. And we saw that improve throughout the quarter. So the more customers understood the better it got in the results. So, I guess, real simply, while it's a very noisy, competitive environment, we were able to do well across the board we don't give individual porting ratios, but we were certainly positive porting in total. And very strong results from all aspects of our business. We don't have any reason to believe, we should be able to continue with, we need to see how things play out, and how we continue to play in this competitive environment. But we are optimistic about what we can do going forward.

Tim K. Horan – Oppenheimer & Co., Inc.

And then just maybe a longer-term outlook on Next. Have you thought at all about maybe just phasing out the subsidy programs and moving everyone over to Next in the next couple of years? Because it seems like it would be substantially more profitable. I know you talked about going through some of the economics there, but your subsidies were in the $400 range before that. And maybe it's $100 upfront here on Next.

John J. Stephens

Yes. So Tim I mean, we certainly continue those things I guess the first thing – and this may sound simplistic, but the first thing is it starts with the customer. And so our customers still and some of our customer still choose the subsidy program even in the first quarter. So we want to make sure we stay focused on what they have and what they want and be responsive to them. So that's the first thing, so I wouldn't suggest that it would be eliminated as long as there is a significant amount of customers who enjoy and prefer it.

I'll tell you this, so as we see the next program grow, who are expecting to see some changes in pricing and some ability for the consumer to drive efficiency in the market, maybe the handset providers are the – the transport companies couldn't drive themselves. And that will give us an opportunity to not only to your customers a better deal – as they drive efficiency, they will get savings. But we believe as they drive efficiency and get savings for themselves to give us the opportunity to get savings under the subsidy model. And that's a long-term optimistic point for us, so that $400 to reference Tim, we would hope based on the success of Next and the customers purchasing activities in that would help us to give us an opportunity to make in roads into that $400.

Tim K. Horan – Oppenheimer & Co., Inc.

Thank you.

Operator

Thank you. Our next question is from Frank Louthan with Raymond James. Please go ahead.

Frank G. Louthan – Raymond James & Associates, Inc.

Great, thank you. I want to talk a little bit about the fiber builds that you have announced – they put them out yesterday. I just wanted to see what sort of the time frame and the commitment to those markets. And then talk just a little bit about the economics of deploying fiber – on the GigaPower product now versus what you saw a couple of years ago. It seems like the economics have improved for you. What are some of the drivers of that that are making that more of a feasible build than what you saw a few years ago?

John J. Stephens

Yes, so first and far most right now the four markets that we've announced in, specifically, Austin, where we made the most progress in – we are being able to view this within our scope of our VIP program and in our scope of U-verse, if you will able to direct dollars from that effort and move them into this fiber-focused effort of GigaPower.

What we're seeing there is take rates in Austin that surprised us that exceeded our expectations. We're seeing customers quality scores – very pleased. And what we're seeing is being able to sell much more online, in a much more efficient manner than necessarily we have done in the past. The key to the success there was that we're able to get kind of right way, and permitting and pull rights and other rights to build in the same manner as other companies which we haven't had historically.

And we're able to focus our build on the customers that drove demand as a oppose to the ubiquitous coverage. And so those two things really driving the success those two things drive the changes in the financial metrics when you can build where the demand is you can have much higher penetrations and get much higher returns to support that build.

We will start - in fact, I think there have been discussions today with many of the leaders of the market areas, the cities that we spelled out. We're very opportunistic, optimistic I should say about those markets and believe we're uniquely positioned in many of those markets because the existing backbone we have in many of those markets. So build off of and to provide that really high quality service.

Frank G. Louthan – Raymond James & Associates, Inc.

Okay, great thank you.

John J. Stephens

Thank you.

Susan Johnson

I think I am going to call for the last question as we are almost out of time.

Operator

Thank you, that will come from David Barden with Bank of America. Go ahead please.

David Barden – Bank of America Merrill Lynch

Hi guys, thanks for taking the question I appreciate it. So I guess I've got a couple of questions, if I could. So, John, thank you for your kind of walking through some of the accounting practices that go along with Next. I guess my math is that every Next customer is generating something around $500 of upfront equipment revenue relative to the traditional subscriber, who might be generating closer to $200. And that $300 delta times 2.9 million Next adds would be about $900 million of incremental equipment revenue relative to the old approach.

And that seems to foot with the year-over-year change in your accounts receivable working capital number. So I was wondering if we could kind of just go right to the nuts and bolts of it and see what was the Next impact on the quarter, specifically, from the differences in how you account now versus how you would have accounted if you just used the subsidy model? And then, I guess, the second question, if I could, was, it looks like you changed the definition of ARPU in the disclosures this quarter. I guess the old numbers look about $2 higher than or $2 lower than the new numbers. So I was wondering if you could kind of talk a little bit about that change as well? Thanks.

John J. Stephens

Sure. First of all Dave, we're not going to give specific details, but let me give you a couple of points about what you said that I think are maybe a little bit need some refinement. First and foremost on day under the old subsidy model, we got about $240. We also got a $200 copayment, but we usually had about somewhere between – about a $40 activation fee, so that's the first piece.

Second piece is if you think about an average phone cost about $600 and you would adjust that for an interest charge and you adjust it from anywhere from 0% to 25% contingency loss for the trade-in value reduction, you are going to get a much different numbers than $500. You are going to get a lower number than $500.

Second, if you think about what happened in the quarter, we had $1.1 million accelerated upgrade. So this next program generated those, that doesn't generate a benefit actually that generates pressure on the margins. So I think all of those items have to be taken into account. Specifically I'll tell you on the change in accounts receivable, yes, there is some accounts receivable change related to Next. Our total Next accounts receivables are going to be in the $2 billion range. I think we said at the end of last year was in the $900 million, but I want to be straight with everyone in a sense that the 12 months receivables, the billings for the next 12 months are in our accounts receivable line because they are short-term, the current assets. And those receivables that go up beyond 12 months are our long-term other assets. So it's not – the accounting rules don't allow us to be that – have that clarity with regard to it that's why we provided in our quarterly filings the total Next receivable.

With regard to ARPUs, you are right, we are changing it as we're shifting the model and having people pay for equipment, and choosing – they are electing to pay for equipment, and for in return, they are taking a discounted service price. Our new ARPU metric is service ARPU plus monthly Next billings and when you add those together which we've done in our presentation you can see our growth rates still strong 2% on the ARPU side, so you feel good about that. But if you will, a view towards what the customer is paying us, you know writing the check to us for on a monthly basis.

David Barden – Bank of America Merrill Lynch

So, John, just on that – so you are adding service ARPU plus a portion of the equipment revenue back into the service revenue number for the ARPU calculation?

John J. Stephens

Just a monthly billings.

David Barden – Bank of America Merrill Lynch

Okay. And then, just if I could clarify that…

John J. Stephens

And David, that won't tie to equipment revenue, because the equipment revenue is – you're right. Much when it's recognized upfront. This is how much we – this is the $30 a month we bill a customer who is on a 20 month Next plan for a phone that costs $600.

David Barden – Bank of America Merrill Lynch

Right. And for those advanced upgrade plans, the ones that kind of you allowed to upgrade early, did you book any revenue for those? Or did you just give them the phone?

John J. Stephens

No. They came in and signed up to pay us, effectively the $30 a month for 20 straight months. So, yes, we booked revenue in the same manner as we booked all the others.

David Barden – Bank of America Merrill Lynch

Okay. Great, thank you guys for helping.

John J. Stephens

Thank you. Folks with that let me take a moment to thank all of you for being on the call today. We have started off the year very strong and have made major strides in transforming our business. As a result we saw strong revenue and EPS growth, along with major gains in our growth drivers. We drove a strategic shift, subsidy model by changing the way customers buy their handsets. It's been an exciting quarter and an exciting start to the year. And we look forward to the opportunities that lie ahead. Thanks again for being on the call. And as always thank you for your interest in AT&T and have a good evening.