Operator

Ladies and gentlemen, thank you for standing by. Welcome to the AT&T Second Quarter 2018 Earnings Call. At this time, all of your participant phone lines are in a listen-only mode. Later, we will conduct a question-and-answer session. Instructions will be given at that time. [Operator Instructions]

I would now like to turn the conference over to our host, Michael Viola, Senior Vice President, Investor Relations. Please go ahead.

Michael Viola

Okay. Thanks, Lori, and good afternoon, everyone. Welcome to the second quarter conference call. As Lori said, I'm Mike Viola, Head of Investor Relations here at AT&T. This is our first call - first earnings call after we closed our acquisition of Time Warner, and we're broadcasting this call from WarnerMedia headquarters in New York.

As we told you earlier, we're going to use this call not only to discuss the quarter, but we're also going to provide more details on our strategy. And to do that, we've brought together the CEO, CFO and four business leaders of our business units.

Today's agenda is going to begin with John Stephens, who will cover AT&T and Time Warner's second quarter financial results as well as update our outlook and guidance. Randall will provide a strategic perspective of the business. And then each of the business unit leaders will take -- will talk about their second quarter results and give a perspective of their businesses going forward. After that, the entire team will be available to participate in the Q&A session.

I'd like to mention one save the date item. We plan host a sell-side meeting on the evening of November 29 and followed by a buy-side meeting that next morning on the 30th. Both would be here in New York, and all the folks on this call will join us for those meetings. So please mark your calendars, and more details to come.

Now before I turn the call over to John, I need to call your attention to our safe harbor statement. It says that some of the comments today will be forward looking and as such is subject to risks, uncertainties. Results may differ materially. In addition, information is available on the Investor Relations website.

I also need to remind you that we're in the quiet period from the FCC CAF-II auction, so we can't address any questions about that today. As always, our earnings materials are available on the Investor Relations page of the AT&T website. That includes the news release, 8-K, investor briefing, other associated schedules, and available on our website are materials on Warner Media's full second quarter. It includes trending schedule and other important documents.

And so now I'd like to turn the call over to AT&T's Chief Financial Officer, John Stephens.

John Stephens

Thanks, Mike, and hello, everyone, and thanks for being on the call today. Let me begin with our financial summary, which is on Slide 5.

I think most of you know the FASB has been very, very busy this past year implementing a number of accounting standards, five of which have direct impact on AT&T. Those include standards that deal with revenue recognition, pension reporting, impacts on cash flow reporting.

These changes impact our income statements and cash flow. At the same time, the company made a policy decision to record universal service fees net as an offset to our regulatory fees.

We're working hard to help you understand these changes. So in addition to the GAAP financial information, we're providing comparable historical results to help you better understand the impact on the financials from revenue recognition and the policy decisions, as well as Time Warner's second quarter results on a historical basis. We will be referring to these historical results in our comparisons during the call.

Now let's start with EPS. We continue to show strong adjusted EPS growth, up more than 15% for both the quarter and year-to-date. Tax reform continues to have a positive impact on EPS as does the adoption of revenue recognition.

We also had about $0.02 of help from the 16 days we own Time Warner, which we have renamed WarnerMedia. The WarnerMedia earnings contribution was slightly more than what you might expect for such a short period. But as you know, financial results can be uneven, and we saw that in the second quarter.

Consolidated revenue came in at $39 billion, down slightly from a year ago, but that includes about $900 million of pressure from how we are now accounting for USF fees on a net basis.

When you look on a comparable basis, revenues were up slightly, thanks mostly due to the two weeks of Time Warner revenue but also helped by gains in wireless and AdWorks.

We continue to use our tax reform savings to invest in and grow our customer base. As John Donovan will discuss, these investments help drive post-paid phone growth and significant year-over-year improvement in prepaid phone net adds, continued growth in consumer broadband customers even in a seasonally challenging quarter and solid subscriber growth in total video customers.

Adjusted consolidated operating margins in the quarter were up year-over-year on a reported basis but down on a comparable one. Solid smartphone sales drove some of the pressure to margins, but the biggest factor continues to be customer transition to over-the-top video.

Let's now look at free cash flow. It was a strong $5.1 billion for the quarter, up substantially both year-over-year and sequentially. Year-to-date, our cash from operations and free cash flow is up about $1.5 billion, which makes us very comfortable with our free cash flow guidance for the full year.

Our cash flows also reflect the timing differences between spending for FirstNet and the reimbursements we received from the organization. This usually trail spending by several months. Year-to-date, that comes to more than $100 million of free cash flow pressure. Capital spending for the quarter was $5.1 billion or $5.4 billion before the $300 million of FirstNet reimbursements we did receive in the quarter.

Let's now cover financial results from operations beginning on Slide 6. AT&T's domestic mobility operations are divided between the Business Solutions and consumer wireless segments. For comparison purposes, we're providing supplemental information for our total U.S. wireless operations.

Our wireless business turned in very good results. Year-over-year service revenue turned positive. Margins remained strong, and we had phone growth in both post-paid and pre-paid.

Total revenues were up year-over-year, thanks to gains in both service and equipment revenues. Also, service revenues were up almost 2% sequentially. Strong sales in BYOD supported that growth.

Our upgrade rate was down year-over-year, but our equipment revenues were up, reflecting customers' purchasing habits and their choice of more expensive devices. But even with these strong sales, margins were very good with service margins coming in over 50% on a comparable basis.

Looking ahead, we expect positive service revenue growth for the full year on a comparable basis.

Turning to our Entertainment Group. We continue to see the impact of the video transition in our revenues and our margins. This would take a while to work through, and we expect it to continue the rest of the year. But we are seeing some sequential stability in both revenues and margins.

We're making changes to drive revenues and effectively manage the transition. We're going to introduce some promotional pricing that impacted revenues in the past, and we now have new features on our next-generation platform that will drive additional revenue opportunities such as cloud DVR, a more robust VOD experience with new pay-per-view options and an additional stream capability. John Donovan is going to walk you through those plans in a few minutes.

Also helping is AdWorks, which continues to grow at a double-digit rate and has now an annualized revenue stream of over $1.8 billion.

Moving to our Business Solutions group. Revenues were down as gains in wireless and strategic business services helped offset declines in legacy services. Business wireless with strong growth, up more than 4%. This is driven by both equipment and service revenues.

Wireline revenues were down more than 4% year-over-year. We still expect tax reform to produce a lift in communication spend, but we just haven't seen it yet. Wireline EBITDA margins were up slightly on a comparable basis. Cost efficiencies continue to offset pressure from legacy products and our investments in FirstNet.

In our International business, solid customer performance helped to offset currency pressures. Revenues were stable year-over-year, while margins were pressured by World Cup expenses as well as foreign exchange.

Now let's look at Time Warner's second quarter financials on Slide 7. Time Warner had strong growth at all operating conditions on a comparable basis. This includes strong subscription revenue growth on both Turner and HBO. Turner also showed solid advertising revenue growth of 3%. Adjusted operating income was $1.8 billion, driven by increases at Warner and HBO.

Now for some housekeeping items. With recent FASB accounting rules, the Time Warner merger and purchase price accounting rules, there's going to be a lot of new information included in our results. We're going to do our best to make that easy for you to understand.

First, we'll file pro formas with the SEC in August. Second, we have posted the full second quarter results for Time Warner on our Investor Relations website. This includes the Time Warner historical results, trending schedules, all the information you're accustomed to seeing.

Finally, as you're updating your models, keep in mind the following: Results will continue to be reported at the divisional level, but there are certain things that will be eliminated in the Corporate and Other segment, including about $3 billion of annual inter-company content revenues and purchase accounting impacts on customer base and deferred production costs.

We're very excited that Time Warner is part of the AT&T family and the WarnerMedia as part of the AT&T family, and John Stankey is going to provide more insights and highlights in a few minutes.

Now let's look at our 2018 outlook with Time Warner included. We're raising adjusted earnings per share growth to the upper end of the $3.50 range with WarnerMedia included.

Year-to-date, we're already seeing 15% growth. Impact of tax reform, improving wireless service and advertising revenues as well as the addition of Time Warner support strong adjusted EPS growth even with the additional shares issued as part of the deal.

Looking at free cash flow. Our free cash flow guidance at the beginning of the year was standalone. We expect most of the benefit of the Time Warner free cash flow for the last half of the year, about $2 billion, will be absorbed by integration and deal costs, including severance costs, retention incentives, legal fees, bankers' costs and interest expense prior to close.

When you consider those items and slightly lower cash capital spending, we're raising expected free cash flow to the upper end of the $21 billion range with dividend coverage in the low 60% range, and that's even with the additional shares and dividend responsibility from the merger with Time Warner.

Now that we are halfway through the year, we also have a better view of CapEx. Capital investment is expected to be in the $25 billion range, but that will be $22 billion of CapEx on our cash flow statements after you net out our FirstNet reimbursements and some of the vendor financing opportunities that our team has pursued.

A primary focus for us this year and the next few years is deleveraging the business. We have a strong business that generates a ton of cash and EBITDA, and we are very confident in the deleveraging targets that we have given you. Let me recap them now.

Net debt to EBITDA is projected to be in the 2.9x range by the end of this year and a 2.5 range by the end of next year. To reach that target, we expect EBITDA growth. We'll use excess cash to pay down debt, and as always, we'll continue to look for ways to monetize non-strategic assets.

You've seen that recently with the data center deal and our pending sale of broadcast 600 spectrum. We expect to return to historic debt levels in the 1.8 times range by the end of 2022.

That's the financial summary. Now I'll turn it over to Randall. Randall?

Randall Stephenson

Okay. Thanks, John. And it was an exciting quarter. After 600 days of reviews and litigation, we did finally complete the acquisition of Time Warner. And then just a few days later, we announced our agreement to acquire AppNexus. And if you're not familiar with AppNexus, it's one of the top ad technology companies around.

And as John mentioned, we've renamed Time Warner to WarnerMedia, so we'll be referring to that as WarnerMedia from here forward. And as John Stankey will cover later, they had a really strong second quarter. We couldn't be pleased -- more pleased with the condition Jeff left the company with us.

We've now assembled the key elements of a modern media company, and it all begins with owning a wide array of premium content because we are absolutely convinced that there is nothing that drives customer engagement like high-quality premium content.

And whether it's Netflix, Amazon, Google, Disney or Comcast, everybody is now pursuing the same thing. How do you deliver great media and entertainment experiences to our customers? And I think the recent valuations of media companies is reinforcing this point.

But we couldn't be any happier with the range and quality of brands that we now own. For life programming, it doesn't get any better than CNN for news. And for sports, we have the NBA, March Madness, NFL SUNDAY TICKET, Major League Baseball and PGA. And for original premium subscription content, there is nobody better than HBO.

Our cable networks at Turner are among the best, and they're performing well. And for content creation, our production studio at Warner Bros. is the gold standard, and they possess one of the deepest IP libraries around.

And when you talk about digital content, we now own the cnn.com digital brands, and these are the most visited websites in the world. And add Bleacher Report and the Otter Media properties, and we have what we think are a terrific set of digital assets. Bottom line, we absolutely love this portfolio.

But just owning great content is no longer sufficient. The modern media company must develop extensive direct-to-consumer relationships, and we think pure wholesale business models for media companies will be really tough to sustain over time. And when you look across our wireless, pay TV and our broadband businesses, we now have more than 170 million direct-to-consumer relationships.

And these relationships are critical as we begin developing new media experiences for all kinds of different audiences. And then the 170 million relationships provide invaluable insights for new advertising models, and that's exactly what's behind our investment in ad technology.

Today, we use our data insights. We deliver ads on DIRECTV. And when we do this, our advertising yields improve by 3 to 5x. As you're going to hear from Brian Lesser shortly, that business grew 16% in the second quarter.

Now Turner has an ad inventory that's 3 times the size of our DIRECTV inventory, and as we apply the same data to that inventory, we expect a significant lift. At AppNexus, that acquisition is all about improving our capabilities and reducing our time to market here.

So you take these three elements, premium content, 170 million direct-to-consumer relationships and great ad technology and then you combine those with our high-speed networks, and we think all of this is a game changer.

Bringing these four elements together has changed the way we think about our customer value proposition. We spend our time now thinking about how to combine these elements to create unique customer experiences. How do we combine the best content wherever you are and make it easy to find and consume?

What are the new products that combine content and connectivity? How do we create personalized content experiences, including personalized ads that you find useful? So hopefully, you begin to see why we're so excited about putting all of these capabilities together.

Now we knew the WarnerMedia deal was not going to be like any other we had done. It's a vertical bolt on with a media business. And the media business obviously has very distinct culture, talent and business models. So last fall, in anticipation of the merger, we reorganized the company into 4 separate businesses, and you can see those on the next slide.

What we've done is pushed the core staff functions and the decision-making out into the business units, and we left behind a very small staff at corporate. And this is all about increasing speed and efficiency at each of these businesses. But at the same time, we need to foster cross-platform coordination to generate the synergies that John Stankey will be touching on next.

Today, we're going to change the earnings call around a little bit as John Stephens pointed out. We're going to give you a chance to hear from each of these business unit leaders. And then when they finish, we're going to stay on the phone and answer any questions that you have. And then John Stankey is going to lead us off. John is the Head of WarnerMedia.

And then you're going to next hear from John Donovan, who heads up AT&T Communications; and then Brian Lesser, he's the Head of our Advertising & Analytics business. And he's going to walk you through his plans. And then finally, you'll hear from Lori Lee, who heads up our Latin American businesses.

And she's going to take you through an update on, really, the great market momentum that we're experiencing in Mexico and also talk about the latest on our Latin American TV business.

So with that, I'm now going to hand it over to John Stankey. John?

John Stankey

Thanks, Randall. Good afternoon to all of you. I've been on the job now a little bit more than a month, but during the time, I've had the opportunity to meet with various leadership teams at WarnerMedia. And I don't think it's a surprise to any of you what I found is what I believe to be an unmatched dedication to producing unique and engaging content across film, television, sports and journalism.

Looking forward to my continued work with this team, and I think we have the great opportunities in front of us to further harness the exceptional content and capabilities at WarnerMedia.

John gave you the financial highlights of WarnerMedia's second quarter, but let me dig in deeper, and you'll see those results on Slide 13. Time Warner's last quarter as a stand-alone company had strong revenue gains in Turner, HBO and Warner Bros.

Turner saw solid growth with gains in both subscription and advertising revenues. Subscription revenues benefited from higher domestic rates and growth at Turner's international networks.

Subscriber counts have been stable thanks to growth in virtual MVPDs with 3 of the top 5 ad-supported cable networks among adults 18 to 49 in primetime. The Turner Networks are proving popular in every video bundle as evidenced by their inclusion in every major live OTT provider. Turner Sports properties helped drive strong advertising revenue growth in the second quarter led by the NBA on TNT broadcast.

HBO also delivered solid revenue growth in the quarter. Subscriber revenues were up 13% due to strong U.S. subscriber growth and gains in international markets. Higher television revenues helped drive strong revenue growth at Warner Bros., Warner Bros. TV looks to build on that success with more than 75 TV series in production for the 2018, '19 season. That is the studio's largest number of TV series in production at one time ever.

Here's another good indicator of what kind of quarter and year WarnerMedia has had. WarnerMedia companies, HBO, Turner, Warner Bros. received 166 Emmy nominations, which include 22 nominations for HBO's Game of Thrones alone, followed by 21 nominations for Westworld, which is produced for HBO by Warner Bros., a real trooper for us.

These nominations speak to the caliber of the talent and dedication to quality across the company. My congratulations go to the entire WarnerMedia team for their exceptional creative achievements.

During the roughly six weeks since we closed the deal on June 14, we've been working strategically to integrate the two companies. That includes applying the data analytics from AT&T's distribution to the Turner ad inventory. As you know, this is one of the benefits of combining our two businesses.

You've seen the success of the AdWorks group using targeted advertising for DIRECTV and U-verse. Now we have 3x the ad inventory to work with. We believe we can get meaningful CPM improvement in what Turner sees today. Brian Lesser will explain in a few minutes. We expect this is only the beginning of our success.

We've also moved quickly to position WarnerMedia content on AT&T distribution platforms. We intend to push the WarnerMedia consumer brands even further across all platforms. We've been busy with the basic blocking and tackling that comes with any merger, integrating corporate and staff functions, getting our infrastructure systems to work together and aligning corporate management.

We'll look to achieve synergies with our advertising spend and other procurement areas by getting better rates from vendors and suppliers. For example, AT&T was not the primary telecom supplier for Time Warner. Now we begin that transition for WarnerMedia. These types of efforts will help us to deliver on the $2.5 billion in merger synergies we promised.

While all this has been going on, we've been very deliberate in shaping some long-term initiatives that we think will add even greater value. We developed thoughtful plans on where we want to go next with WarnerMedia and have several goals that we want to accomplish.

First, we want to increase our investment in premium content. HBO's name is synonymous with quality entertainment. The creative talent at HBO is the best in the industry. My goal is to give the HBO team the resources to greenlight additional projects already in the development funnel.

We want to invest more in original content while still retaining the high quality and unique brand position of HBO. This will further strengthen the HBO brand, enhance the customer experience, improve churn and drive more engagement with some of our most valued customers.

Second, we plan to further develop and nurture our direct-to-consumer distribution, including HBO NOW. That will include enhancing existing platforms as well as delivering premium content to the more than 170 million direct-to-consumer relationships across AT&T's video, mobile and broadband platforms in the United States and Latin America. We also plan to add even greater value to these relationships by focusing, aggregating and incorporating more WarnerMedia intellectual property.

And third, we also are looking at our international markets and explore ways to maximize our content globally to create greater value. We believe there's a lot of opportunity that remains in this area.

Obviously, we're very early in the game when it comes to implementing our plans, but we're off to a good start and look to quicken the pace as we move past close.

Now I'd like to turn it over to John Donovan for details on AT&T's Communications second quarter results. John?

John Donovan

Thanks, John. I'm really excited about WarnerMedia coming into our portfolio because it strengthens our ability to innovate across our businesses like content and content -- I'm sorry, connectivity.

So if we discuss AT&T Communications operating results, we'll start on Slide 16. Our wireless business turned in an impressive quarter. John Stephens told you about the service revenue growth and strong margins, but we also had strong subscriber gains and continued our low post-paid culture. For the quarter, we added 46,000 post-paid phones. That makes nine consecutive quarters of year-over-year improvement.

We had our best prepaid quarter in nine quarters with 453,000 prepaid net adds. This includes 356,000 phone net adds. We had a record connected device net add quarter as well, adding 3 million new devices.

Churn continues to run at near-record low levels. Post-paid phone churn was 0.82%, just three basis points higher than last year's all-time record, and we have a record low prepaid churn, thanks to our multi-line plan penetration and auto bill pay.

These customer gains and low churn are showing up in our service revenue, where we turned positive both sequentially and year-over-year on a comparative basis.

With the unlimited launch well behind us and targeted promotional activity, we saw service revenue improve each month in the quarter, and we're on track to grow service revenue for the full year on a comparable basis. And we maintained comparable service margins above 50% again this quarter.

Moving over to our Entertainment Group. We continue to see total video subscriber gains as we move through the transition of our video business. We had 80,000 total video net adds in the quarter with gains in DTV Now and U-verse more than offsetting losses in DIRECTV.

We also turned in solid broadband gains. Our Entertainment Group had 76,000 IP broadband net adds with 23,000 total broadband net adds. That's their seventh consecutive quarter of broadband growth.

About 95% of our consumer broadband base is now on our IP broadband as our transition from DSL is drawing to a close. Our fiber build continues at a fast clip, now passing more than 9 million customer locations, and we expect that this time next year to reach 14 million locations.

This gives us a long runway for broadband growth. We're doing very well in our fiber markets, including a 246,000 net increase in subs on our fiber network in the second quarter.

Now I'd like to update you on several key initiatives we have underway, so we'll turn to Slide 17. Evolving our video portfolio is top priority for us. We believe we're well positioned as our customers move toward a more personalized set of streaming products.

Our new platform was launched in May as the DIRECTV NOW user interface, and it's now live on all supported device operating systems and has been well received with strong engagement by customers.

It offers a new cloud-based DVR and more robust video-on-demand experience with new pay-per-view options. Over time, it will bring additional advertising and data insight opportunities.

This new video platform gives us flexibility to adapt to the market with new offerings and products. Late in the quarter, we added our third video offering called WatchTV, a small package of 30 live channels and 15,000 on-demand titles.

We include WatchTV in our unlimited, more wireless plans where you can purchase it for $15 a month, making it perfect for customers who want video but not at the cost of a large package.

This complements DIRECTV NOW where we continue to see success in attracting cord cutters and cord severs. And later this year, we will begin testing a premium product extension, which is a streaming product that will give the full DIRECTV experience over any broadband, ours or competitors'.

It will have additional benefits of an improved search and discovery feature and an enhanced user interface. We're excited that this will complement our top-end product for those who don't want or can't have a satellite dish.

Our open-video platform also dovetails nicely with our ongoing focus on driving the industry's leading cost structure. The new platform is low touch with lower acquisition costs as streaming services becomes a bigger part of our business.

Digital sales are a cost-efficient way of customer engagement, and we're seeing double-digit growth in our digital sales and service. We're also seeing operating expense savings from our move to a virtualized software-defined network.

More than 55% of our network functions were virtualized at the end of 2017, and we're well on our way to meet or exceed our goal of 75% virtualized by 2020. These and other cost management initiatives have helped drive 13 straight quarters of cost reductions in our technology and infrastructure group.

Finally, I'd like to give an update on our FirstNet build and other network investments. Our FirstNet network build is accelerating. We expect to have between 12,000 and 15,000 band 14 sites on air by the end of this year 2018, and we're ahead of our contractual commitment.

And don't forget, when we're putting in equipment for FirstNet, we're also deploying our AWS and WCS spectrum, utilizing the one touch, one tower approach. This approach allows all customers access to our improved network.

FirstNet also gives us an opportunity to sell to first responders. So far, more than 1,500 public safety agencies across 52 states and territories have joined FirstNet, nearly doubling the network's adoption since April.

In addition to our efforts with FirstNet, 5G and 5G Evolution work continues its development in several different areas that will pave the way to the next generation of higher speeds for our customers.

We now have 5G Evolution in more than 140 markets, covering nearly 100 million people with theoretical peak speeds of at least 400 megabits per second with plans to cover 400-plus markets by the end of this year.

Our millimeter wave mobile 5G trials are also going well, and we're on track to launch service in parts of 12 markets by the end of this year.

With that, I now turn it over to Brian Lesser to discuss our Advertising & Analytics business. Brian?

Brian Lesser

Thank you, John, and good afternoon, everyone. As Randall mentioned, a critical component of the modern media company is a dynamic advertising business, one that can deliver on the promise of making advertising relevant, engaging and actually matter to consumers and make it work harder for advertisers and make it more valuable and optimized for publishers.

I think about this simply. The course of the ad industry has been set by a series of defining moments. The rise of broadcast networks, the proliferation of cable networks and the pay TV bundle, digital advertising and its ability to target audiences, we sit here again today at yet another point that will define advertising for years to come. The pain points are obvious.

Traditional advertising doesn't satisfy what both consumers and brands are looking for. Brands are frustrated with lack of access to data, lack of competence in targeting and measurement and non-transparent ad tech costs. The industry talked about video convergence, but no tangible examples yet have emerged to deliver a unified buy-side and sell-side platform.

So while the timing for disrupting the ad industry is right, you must have the assets to execute, and there is no doubt that AT&T is uniquely positioned to lead this disruption.

In our view, successful ad marketplaces must have two key assets: number one, its premium content. Sports, news, original programming, we love our position with Turner content along with the scaled portfolio of ad inventory.

Number two is distribution. Customers dictate how and where they consume content. Likewise, a relevant ad marketplace must be able to reach customers where they are, whether it's a 50-foot screen in a theater or a 3-inch screen in your pocket.

Number three is data. AT&T has access to expansive datasets on customer behavior and preferences. 170 million direct-to-consumer relationships across its wireless video and broadband businesses, 40 million set-top boxes, 20 million connected cars, and that's just for starters. But data needs to be activated to have value. We're building targeting and measurement capabilities that will bring greater value to consumers, advertisers and publishers.

And number four is technology. Content distribution and data must be integrated on a best-in-class ad technology platform. That's the rationale for our recent announcement to acquire AppNexus.

This is a best-in-class independent advertising marketplace supported by the best talent in the industry. We cannot wait to combine our teams and partner to make advertising matter to consumers.

It is important to note we are not starting from a standstill. Both AT&T Advertising & Analytics and Turner have executed fabulously by using data and technology to fuel growth.

AT&T Advertising & Analytics is consistently delivering double-digit revenue growth, including 16% growth in the second quarter. We will employ the same momentum and scale to deliver on our vision.

So in closing, our plan is nothing short of leading the industry and creating a premium advertising marketplace across both TV and digital by quickly integrating AT&T assets, including AppNexus. It's this unique moment in time, coupled with this unique set of assets, that gives me confidence in our path forward.

With that, I will hand it over to Lori Lee to talk about our Latin American operation.

Lori Lee

Thank you, Brian. The advertising opportunities that Brian laid out apply to Latin America as well. We have more than 30 million direct-to-consumer relationships, and we plan to run the same play with the LatAm business that we will be using in the United States. It won't happen overnight, but the opportunity is definitely there.

Let me discuss our second quarter results. Those details are on Slide 21. Starting with our Mexico Wireless operations, we turned in another strong subscriber quarter with more than 750,000 net adds. That totaled more than 3 million new customers in the past 12 months, doubling our subscriber base to a 16.4 million since entering Mexico just 3 years ago.

During that time, we've built a world-class LTE network and developed a marketing presence reflecting the AT&T brand. Our network build is in the final stages as we close in on covering 100 million people.

We have rebranded 3,000 stores and have approximately 6,000 total retail locations, expanding our marketing presence and distribution. And we've upgraded and integrated our different billing systems. All this puts us in a great position to add customers and revenues at a lower cost.

We're also making a lot of progress in improving our financials. Operationally, we're pushing on all fronts to exit the year EBITDA positive. In our Vrio pay-TV business, currency devaluations have impacted our financial results, but the strength of our subscriber base and our profitability remains consistent.

That continued to be true in the second quarter. The World Cup drove strong subscriber growth of 140,000 with particularly strong gains in prepaid. We finished the quarter with 13.7 million pay-TV subscribers, a number that has held fairly steady since we acquired the business. The World Cup did drive higher expenses in the quarter, but we continue to drive profitability and positive free cash flow year-to-date.

Now I'll turn it back to Mike for Q&A.

Michael Viola

Okay. Thanks, Lori. Lori - operator Lori, we are ready to take questions.

Question-and-Answer Session

Operator

[Operator Instructions] And our first question from John Hodulik with UBS.

John Hodulik

Thanks. And I think I'm going to bounce around a little bit. But maybe first for John Donovan, the wireless business, it looks like EBITDA was down about 0.7%, I think, on like-for-like basis. But obviously, you returned to growth in subscribers and some margin improvement. Should we be expecting that segment still your biggest [ph] to return to EBITDA growth as we look forward?

And then maybe one for Brian and then for John Stankey. Brian, we've heard a lot about addressable advertising, 3% growth this quarter on the advertising line. What are some of the milestones that we should expect and maybe the timing of when this addressable advertising opportunity starts to take hold within these numbers?

And then lastly, John Stankey, the - you obviously got some press recently in terms of interview you did about the new WarnerMedia. Could you talk a little bit about the size of that HBO spend? I think the HBO spends about $2 billion. You're competing with companies that spend $8 billion a year, much bigger numbers. I mean, how should we think of that in terms of the overall financial profile of the company?

And maybe if you could elaborate on other D-to-C efforts you may have. We've heard about DC -- DC Universe and the HBO NOW but if there's any other sort of initiatives we should be looking for? Thanks.

John Donovan

Hey, John, it's John Donovan. I'll start the question on wireless and EBITDA. We've had now three quarters in a row where our year-over-year compares on subscriber growth was very good. We crossed over that all-important date, where we got a lot of the reseller stuff behind us.

We crossed over that date for the unlimited plans. And you've seen a lot of momentum in prepaid, which has really become a really nice business for us right now. We're in a really good rhythm there firing on all cylinders.

And so what we're seeing right now in this quarter, John mentioned in his opening remarks that we were stronger each month of the quarter within the quarter. We're starting to see us roll over some of those earlier events, and now we're beginning to get strength in them.

And so because we - in the - each month of this quarter strengthened from subscriber counts, we also have some pricing moves, calibration of pricing, if you will, that made us consistent with our value proposition in the marketplace. So we expect that we'll have growth for the year and the EBITDA margins to improve.

Brian Lesser

John, I'll take the next part of your question. This is Brian Lesser. So you asked about milestones in the advertising business. I think it's important to know that we have posted a $2 billion advertising business outside of what we just acquired in Turner, and that advertising business was growing 16% in the second quarter. So we're already showing the value of data and technology on our advertising business.

I think in terms of going forward, you should look for some things that we've already mentioned here in this call, number one, our ability to increase the yield on the inventory that we have now within Turner and WarnerMedia more broadly and also increase value to the firm but also value to publishers, advertisers and the consumers.

You'll see us continue to develop the ad platform. AppNexus, once we close that deal, is an important milestone for us, but you'll see us lean in and develop additional technologies around that platform.

And then third is our ability to partner with other media companies outside of AT&T. In some ways, our success will depend on our ability to attract additional sources of inventory to reach critical mass for advertisers.

John Stankey

So John, let me just amplify the last piece that Brian gave. Data that we have had within the AT&T company applying to AdWorks has already been moved over into the Turner team to begin applying into existing inventory that we have using the same techniques we piloted in selling the two minutes of advertising that the AT&T team has across the broader inventory of Turner.

So that's near term. That's not a milestone issue. That's, today, we're starting to look at those business cases and how we would do that. Teams have already come up with a variety of different initiatives around that, including - we found out that Brian had a great opportunity to do addressable advertising in the pharmaceutical space, and some of the pharmaceutical companies wanted 90-second avails. And he didn't have 90 seconds of inventory.

So we're bridging Turner inventory with what used to be AT&T inventory so that we can have new addressable products to bring in. So that's - there's benefit to that data that's occurring now even without the broad mechanization and intelligence and platform work that Brian brought to the table that's just discussed.

So on direct to consumer, what I will tell you is what we know about this space is it requires scale. And you mentioned that there's a number of different initiatives underway within the WarnerMedia companies, and they're all good within their own right. But they all generate what I would consider to be relatively small scale audiences, company our size. We want to be generating audience. It's in the tens of millions, not in the single-digits millions.

And so the way I would think about our direct-to-consumer efforts over time is it's better together. So a lot of very strong brands in the family that generate interest among groups of audiences and on a stand-alone basis, they're not as powerful as they are when they're brought together. And you can assemble the genre of content and bring them together on one platform and one experience that aggregates and gets scale.

So over time, what you should think about how we're going to approach the discrete brands that we have is ultimately unify them in a more consistent and more focused experience. It starts to bring some scale in.

Still very important properties, they still need to be developed. We've got to get the formula right for them, but over time, we want to strengthen them to come together. In terms of your reference to the new cycles on HBO, it wasn't an interview.

I think it was an internal discussion that was right to act, but I would tell you, I don't believe in it effectively characterizing what we are about. What we are about, as I said, is we have a tremendous amount of great projects already in the funnel that as the HBO team and Richard would describe it, they have not been in a position to say yes to because of constraints on certain resources.

What we're attempting to do is open up those constraints on very high, top-quality projects that we think will balance out the schedule so that we have a more engaging experience with HBO throughout the course of the year. That will improve the fact that we can see, especially on the digital platforms, you have customers jumping in and out based on scheduling. And if we can smooth that schedule, we can drive churn down or improve retention and power additional subscriber growth.

So I'm not going to give you the exact investment number, but the way I would think about it is we will make decisions to reinvest some of the efficiencies that we pick up from combining these companies together and running them at a little different fashion.

We may get back a margin point or so in the near term as we grow the subscriber base as we reinvest in it. But it's going to be a very responsible investment and great projects we've already scoped out, we already have rights for, we want to get into the development funnel. And the team feels very, very comfortable that we can flex up on our development in a way that we think rounds out the schedule very nicely.

Randall Stephenson

John, this is Randall. It - well, this merger is different in terms it's a vertical merger. There are certain aspects of the playbook that you just heard John describe that they're going to be exactly the same in that it generates synergies and then reinvest significant portion of those synergies back in to your capabilities and your products.

Direct to consumer and deeper HBO content, it's just part and parcel to that. That's no different to what we've done in the past, and you should probably expect it's going to happen here as well. Thanks for your question. Lori, we'll take the next question.

Operator

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

Simon Flannery

Great. Thank you very much. For John Stephens, John, in the past, you'd given some guidance with DIRECTV on the medium term on EPS. Can you give us any color about the benefits of Time Warner or WarnerMedia in a full year '19? How should we be thinking about that given the upside to guidance this year?

And then on the balance sheet, what are you assuming in terms of getting 2.5 around additional divestitures and about things like spectrum acquisitions? Or is that just run rate with what you have right now? Thanks.

John Stephens

A couple of things, Simon. Thanks for the questions. First of all, beginning to - on the 2.5x by the end of next year, that's driven mainly by run rate with regard to cash flows, taking the cash flows above the dividend and paying down debt.

Secondly, it is important to achieve the synergies, particularly the EBITDA boosting synergies and the growth that we're seeing and some of the growth that we're seeing in wireless and customer additions so that we get a higher EBITDA number.

Well, we have normally planned for asset sales and constantly look at underutilized assets for monetization, for example, the data centers, the broadcast spectrum 600, which is a couple of billion dollars right there, we have under contract and waiting for approvals today.

We'll continue to do that. If you want to give a scope to it, as of today, we have about $500 billion in total assets. And so finding a few more opportunities to monetize assets seems to be very reasonable on top of the things that we've kind of commonly done with regard to real estate and other underutilized business in spectrum. So that batch [ph], I'm not giving you any specific number on asset sales, but as we've proven this year, we're going to continue to do that.

And with regard to EPS guidance specifically around the acquisition, I'll say it this way. First and foremost, the point is, is that WarnerMedia -- Time Warner, WarnerMedia, immediately accretive. Revenues, free cash flow, EPS, we've seen it already. So that guidance that we've given, we'd expect we're standing by that and continue to expect that and have started to prove that out already.

Secondly, we're not going to give a specific guidance with regard to Time Warner's impacts, but I'd suggest it this way. If you think about $3.50 EPS range, for us, that means $3.40 to $3.60. And we just said that we expect to be in the high end of that range. So that'll give you an indication of using your own estimates, other's estimates, where we were, what we expected to be for the rest of the year.

I will point out that the $0.02 we've got in the second quarter for two weeks was, as I said, uneven, and specifically because the NBA contract for playoffs, all that content was extended before we merged.

The Golden State Warriors won the championship in June 8, so that content expense was recognized before we got the deal. So we have some higher profitability in those 16 days you might otherwise expect.

But I'd expect profitability to continue no matter what. We'll give specific EPS guidance for '19 in the coming months. I would just suggest that we continue to expect this transaction to be accretive, revenue, free cash flow and EPS.

Randall Stephenson

Lori, we'll take the next question

Operator

We go to Phil Cusick, JPMorgan. Please proceed.

Phil Cusick

Hi, guys. Seems like we're going around in the same questions. But one for Brian. Can you talk about - clearly, what has to be done here to realize the addressable ad vision? And what's the timing of this coming through to accelerate the numbers and start to be really material on the company?

Can this impact 2019 or are we really talking about 2020? And how do you see the potential to reduce the ad load while you raise CPMs? Thanks.

Brian Lesser

In terms of - thanks for the question, Phil. In terms of timing, as John Stankey outlined, there are some things that we can do immediately and start to add value to Turner ad inventory, and that's already in motion. And so we think there's short-term value there in 2018.

I would say in terms of the overall addressable opportunity, that's a little bit further out. We have work to do in terms of building the technology platform, but the good news there is because of the amount of inventory that exists within DIRECTV, also within WarnerMedia, we can prove out the value of AT&T data and the investments that we're making in technology plus the evolution of our direct-to-consumer relationship that John Donovan talked about.

So I think we still keep our losses [ph] to really start to extract value from inside AT&T using our inventory across DIRECTV and WarnerMedia in 2018. And then in 2019, we're going to start to partner very effectively across other sources of inventory to bring value.

John Stephens

Phil, John Stephens, if I could add to that. I mean, want to point out Brian's humble here in that sense that he started getting 16% revenue growth on those ads, DIRECTV, U-verse footprint, possibility, those ads watched by the same people as the ones who watch the Turner ads. So we've got proof then this works.

Secondly, when the AppNexus deal closes, we'll have the ability to take our internal activity and put it on that supply-side platform that will be within our control. So we are optimistic about the opportunities to get value out of the AppNexus platform.

We've got DOJ approved forward. We're going to need to get [indiscernible] approved and hope to close it before the next time we speak certainly. But I'm optimistic about that, too, so probably a lot of things going and heading in the right direction.

Phil Cusick

And in terms of the ad load? Thank you.

Brian Lesser

In terms of the ad load, so our objective, Phil, is not just to improve advertising as it exists today but to also improve the experience for consumers. We're in a unique position to do that because of our vertical integration because we have content and we have that direct-to-consumer relationship over a traditional television, over a mobile phone, over other mobile devices.

We can start to do things in terms of innovating the ad experience. As an example, you'll see us start to introduce products across the rest of this year and obviously, the next year, where the consumer watching television has a better experience that is less interruptive.

Imagine a DIRECTV customer watching the big screen on their living room wall and instead of seeing a traditional ad break, they see an icon on a car in a movie that they're interested in or in a show that they're interested in.

And then we have the ability to create a seamless ad experience on their mobile device, which is on the coffee table or in their pocket, pause real-time content to interact with a better ad experience and therefore, deliver more relevant content to our customer and to the consumer more broadly.

That has the ability, number one, to be a better experience for our customers and consumers, a better business for us because those ad units will generate a higher CPM and a higher yield and a better experience for advertisers and the media company representing the content. So that's really our objective, is to start to innovate because of our access to data technology and the direct-to-customer relationship.

John Stankey

I would -- Phil, I would just comment that this notion of more innovative ad formats is critical. It's not just a lighter ad load. Well, that's important, and we'd like to achieve it. I think what we all understand is that viewing habits are moving away, in many instances, from the linear fee, and so my a goal working with distributors such as my partner here at the table who is a large distributor of my product is just also start to take these better software-driven platforms that they have and lay out more on-demand content for them that allows for what used to be linear content to be available and stacked and other formats and then attach to that the right kind of advertising that isn't loading that on-demand content with the same commercial loads but is also highly targeted and customized to the particular experience that the individual is going through.

We saw how mobilizing and moving to TV Everywhere raised consumption of the traditional linear affair. I think we have another opportunity to take a fairly mature pay-TV product and extend the runway even further by being more aggressive in trying to incent the distributors to carry more depth in a library.

Randall Stephenson

Operator, we'll take the next question please.

Operator

We go to John Janedis with Jefferies.

John Janedis

Thank you. One for John Stankey. Maybe a follow-up on HBO. As you know, domestic subs have been in the 30 million to maybe 35 million or so range over the past few years.

And you talked about the content investment. But will there be a more aggressive direct-to-consumer push that perhaps would include maybe a Turner bundle or maybe a change to more wholesale deals with existing distributors?

And is there any consideration to reset the price, which has largely remained steady as many of your peers have been more promotional? Thank you.

John Stankey

So I would tell you that our wholesale distributors remain a really important part of our product, and we want to make the product better to improve its performance for their businesses as well as the HBO brand overall.

And as I indicated, we'd like to, for example, improve our term characteristics by getting a more complete annual schedule that has people fully incented to stay in the product and not jump in and out of it as various content comes and goes through the course of the year. We think we've got some good steps that we can take in that regard that will help our sub counts and continue to grow through our traditional distribution channel.

I do believe that as we invest in the platform itself, the direct-to-consumer platform and improve some of the technical capabilities associated with it that our features that can be brought to bear in a typical OTT SVOD environment, that we can also increase the distribution of the digital versions of the product that go direct on retail.

And so we want to run that play as well. I will tell you that I don't think that's a -- what I would call right now a step function change over the next couple of months, but we can incrementally get better on our current run rates by having some success in that regard.

In terms of what other content can be paired with HBO and maybe a more broad offer, I think we have a number of distributors out there that have some great ideas around how they might want to match HBO to their particular content offerings.

And as I said, I want to look at the depth of our WarnerMedia offerings that we have and get better together and understand how we can bring some of our WarnerMedia brands and our other curated options into a more focused direct-to-consumer strategy that I think, as we start to get our strategy together on that, move forward on it, you could see that step function increase in more retail oriented customers.

John Janedis

Thanks, John.

Randall Stephenson

Take the next question operator.

Operator

And we go to Brett Feldman with Goldman Sachs. Please go ahead.

Brett Feldman

Thanks. One of the stronger trends we saw in this quarter was a nice improvement in postpaid phone ARPU, and actually, some of your peers, we've seen something similar so far this quarter.

Also, if we look at the market and we look at some of the pricing moves you've made and others have made, there's an introduction of higher price points. It's not really price increases, but it's really just if you pay more, you'll get more.

So I was hoping maybe you could just expand in terms of what your customers are asking for, why you've identified a cohort that has shown a willingness to pay more for more. And how durable do you think this trend might be?

John Donovan

Yes. Brett, you've been obviously watching our commercials. That whole idea and more. And so what we're trying to do is differentiate the product in ways that don't have to do with speeds, megabytes or rack rate pricing. And so what we're really focused on is product engagement. The value of any customer will be based on the combination of the price and the value that they use for.

And that's why I would say, from a consumer perspective, our strength in consumer has been heavily in the bundling of video with wireless. So we see increased engagement. We're finding that people find a lot of value for it, and then we're kind of spreading the offers to fit budgets and engagement. And so you've seen that in wireless.

And I would point out to you that, that pattern may look familiar in video, and we're trying to find various price points, engagements and content combinations that fit everybody's budget so that everybody views that they're getting value. And they do that not just by focusing on megabytes and pricing.

So I think that it's not an accidental trend that we stumbled onto. It's actually a strategy that's centered in the DIRECTV merger that we were pushing in, and that fits very well with this next step with WarnerMedia. And our sister over there provides us a lot of flexibility.

So I do think it's a trend. I do think that if we succeed - when we succeed, others will be -- will follow and make some of the moves in their own. And I think that right now we see the most important thing, which was engagement and customer delight for the product improving.

And that, to us, translates to value, and we're going to price the value. And so I think the industry will continue, hopefully, to take - to look at that and we - rationalism result to that. So we're going to continue down this path, more of it rather than less of it and expected to be successful.

Brett Feldman

A quick follow-up if you don't mind. Obviously, the plans that include a lot of content tend to be the higher prices, and you clearly see that helps ARPU. Are you seeing that they are also helping churn?

John Donovan

Yes. If you look at the churn, this year was again 3 bps up over. But I think that compared to the industry, we did really well. Compared to seasonality, we did really well, and the number that we're comparing to last year was our all-time low. So I do think that it's a strategy that's working for consumers and therefore, working for us.

And that is the currency that we're after there because you could start to trade some things that customers value higher than the ARPU differential. So we are carefully managing this portfolio, same strategy in wireless and in video.

Brett Feldman

Thanks for taking the questions.

John Donovan

Sure.

Randall Stephenson

Lori, we’ll go to next question please.

Operator

We'll go to David Barden with Bank of America Merrill Lynch.

David Barden

Hi, guys thanks for taking the questions. Thanks for the expenses format on the call, I think it's super helpful. Randall, I guess, my first question would be the telco guy, the media industry is definitely not my wheelhouse yet. But if I'm watching what's happening out there, we've got Fox deciding that they're not big enough to be a competitor in the media industry, so they're selling.

And we've got two large competitors in Comcast and Disney who feel, in order to be competitive with the Netflixes and the Googles of the world, they need to get even bigger.

And so I guess, my question for you is kind of how do you - how comfortable, do you feel, with the scale that you have now in the content business. And are you on the cusp of having a global strategy that's going to kind of try to compete with those other larger content houses? That will be my first one if I could.

And then the second one, John, will be for you. We've been hearing a lot about the directionality of the deal about how we take the information from your side of the business, we bring it over to Brian and let him crunch through it and sell it into Turner.

But as you sit there and look at what WarnerMedia could mean to your business, the broadband business, the mobile business, even the business, business, kind of what do you see as the opportunities? And if you could give us some examples, that would be super helpful? Thanks.

Randall Stephenson

David, this is Randall. I'll go first, and I'll hand it over to John Donovan. You said John. That's just not just very descriptive. But I'll direct that to John Donovan when I finish. In terms of the - what you're seeing happen in the landscape, the media landscape, it's fascinating to us.

We expected some time back this is exactly what you would see happen, that you'd begin to see media companies consolidate and people would see the importance of scale and changing models, changing distribution models and so forth. And so it's hard to imagine.

But it was back in 2016 when we actually did this deal, and so it was early in 2016 where we were asking ourselves, if you believe that's going to happen, if you believe that your networks are going to be able to distribute seamlessly premium content, if you believe that your information and your distribution business is really valuable and can drive different advertising models, then you probably ought to move fast and own media.

And as we look at a scan of what opportunities are out there, Time Warner jumped out. It's just the obvious choice. It was the one scale player that had a great scaled distribution platform, a great scale in terms of advertising inventory and cable networks.

It had the scale position in terms of content creation with Warner Bros. And it was just the obvious partner for us, and everything else was a distant second. And so from the -- to answer your question directly, we feel really good about what we have. And then you add to it the digital properties and CNN being an off-the-charts, great digital property.

You put all the CNN digital properties together, they are the most accessed digital news sites in the world. And so putting all this capability, data, ad tech and so forth, together with the media company, we think is a really, really great combination, and we could not be happier that we moved first.

I think moving first, you rarely forget -- you rarely regret it when you see an industry trend happen. So we saw this would happen. We went first, and we think we got the best business that was on the -- that was actually in the media space. So we feel really good about it. JD, you want to talk about integration of content?

John Donovan

Sure. Thanks. So Dave, we had 600 days to think about this. And when you form your synergies, you deal with some of the straightforward things that John Stankey talked about. But we -- over the last year or so, as we started to put wireless and video together and saw the trend I talked about earlier start to manifest, we are learning as an integrated carrier.

So I circle back and say, when we bought DIRECTV, remember, we talked about bundling up and a lot of skepticism about the value of bundling up versus it being just a price discount.

And I got to tell you, you start to look at the economics of churn reduction and you start to learn how these currencies pass back and forth, you see the same opportunities here. You see -- because the killer app right now on broadband and on wireless is video.

So as you start to look at what customers place value on and you move from buying and reselling or see us being completely out of that market and you go to owner's economics, we really have always had a good sense as to what customers are using and doing on our network.

So to be able to value that into pricing and start to trade off these currencies that we learned over the last 3 years of how do you trade off an acquisition dollar for a dollar of content, how do you trade off a customer install cost versus a churn reduction, we've built some solid muscle now to know how those economics move around.

So we are really thrilled about what the content business can mean for us in simple ways. Store traffic, our -- one of our wireless strengths is that our close rates in stores are up. We want more traffic in the store. If we have a tent-pole release from the studio and we can find a way to integrate in the stores and drive traffic, we found a synergy.

So basic things that video does, like drive traffic and hours of consumption, become assets for us to acquire value in ARPU and retain customers, and we really are getting our strides to figure out how to move those currencies across franchises. So we're really thrilled about what this can do for broadband and for mobility.

John Stankey

David, let me suggest -- I would flip your first question around slightly. I don't worry about scale and content. I mentioned at the outset of this discussion, we're going to do 70 TV shows to the industry this year out of Warner Bros. Didn't even talk about what the incremental number of series will be coming out of HBO, which is very unique, high-valued, premium content that's targeted.

Our ability as a company to decide to produce content that scales, that matters is probably second to none in the industry, and that's at a rate that I'm not sure others operate at or are just coming close to that.

I think the race is on for scaling customer bases, not scale on media content. We're on a good shape on our ability to scale media content. We have -- and we start with 170 million customer relationships in that race to have a scaled customer base to sell to. So I don't worry about that dynamic.

Randall Stephenson

And add to Stankey's comments, the 170 million, add to it what John has over at WarnerMedia, when we talk about cnn.com being the most frequented news site in the world, you put cnn.com, the Otter Media, Bleacher Report together, there's another -- I think it was almost 200 million monthly users, unique monthly users on each of those sites.

And so this is already a big scale direct-to-consumer business. And so now what can you do with HBO and some of the Warner content in terms of taking it directly to the consumer as well that add owner's economics that John Donovan just spoke of and then the ability to have owner's economics going across these platforms, pretty exciting.

David Barden

Thanks for taking the question. Thank you.

Operator

And we go to Mike McCormack, Guggenheim Securities.

Mike McCormack

Hi, guys. Thanks. John Donovan, just maybe some questions regarding entertainment margin, some puts and takes as we think about second half. Obviously, you've got NFL costs that are going to uptick. But what should we be thinking about as sustainability in that sort of 24% type range?

And then secondly, I guess, a question, I guess, just for -- actually, maybe John Donovan and John Stankey. Just thinking about the WatchTV product. I guess, firstly, any sort of early takeaways from that product, how successful it is?

And then also, can you use that as a model for more integration with the Time Warner or WarnerMedia assets? And how far can you take that without risking legacy linear distribution revenue? Thanks.

John Donovan

Yes. Thanks, Mike, a lot of questions nested in there. I'll try to be brief and have you ask follow-ups if I missed anything. If you start with video margins, you see this at the beginning of the evolution of our products that we're trying to get them, as I mentioned earlier, into affordability slots where you get high engagement and therefore, high value for the money.

One of the things that is -- it's not well published as you think about these ad stream count differentials, so you fit in the different viewing patterns. So WatchTV has a single stream product; the DIRECTV NOW having two with a pay up to three, obviously, the linear TV products, the satellite delivered and what we are going to be coming out with here in beta next quarter in the early stages, which is a broadband delivered version of it.

Now all of a sudden, you'd have a whole series of price points. And so you saw the beginning of what we're doing to reshape DIRECTV NOW. DIRECTV NOW is a placeholder in the market until the deal was finished. A placeholder in the market, that product tried to do too much and too little. So we tried to stretch it down on price. We tried to stretch it up in value.

But over time, we think that there will need to be - hit various price points and get the right package bundled in there so customers find value for it. So you saw the first moves that we added, vertical capabilities on top of it, a third stream. And when we got cloud DVR and enhanced the product, we put the price into the market rate for that price.

So we've seen DIRECTV NOW. We just had a very strong quarter of DIRECTV NOW ads. So a highlight for you that when you net all of this drama out for a minute on sub counts, if we start there, we were 25 million subscribers when we bought DIRECTV. We're at 25 million subscribers now.

Customers we lost in cord nevers and cord cutters, we replaced with products that fit their affordability range. We watched cannibalization closely. Roughly 15% to 17% on every given - in any given month is the cannibalization rate, but 1/3 of those are listed in our linear TV product. It's very likely to churn because of their engagement and where the costs don't fit.

So we are watching that very closely. We're slotting these products into affordability and an engagement range where we get the value of it. And I'll point out to you how we procure content on WatchTV. And there's a variable nature to its cost. It is profitable and reasonably comparable to the traditional margins of the business on a percentage of revenue basis.

And so the real question that we're learning as we go, once we get out of linear TV and get into open video, which is software-based TV, how much does the category grow because we're getting cord nevers, cord cutters, but also we're getting redundant accounts where it's becoming a personal video product, where a team with a more personalized approach can build a playlist and stack their favorites in a way that it becomes a one stream product that is a playlist that behaves much like music.

So when you start to look at addressable markets, you look at the ARPU available, the margins and then you add the owner's economics, which is Brian Lesser getting higher CPMs and John Stankey having owner's economics on a portion of that video cost, now these margins start to blend up into much higher territory.

So we look very closely at the blended margin and the movement between these rungs, all while keeping an eye to make sure our subscriber counts keep us at that 25% to 30% share player in the marketplaces. So that's how we're thinking about the strategies in the margins.

And the last thing I'll point out is that on those lower-end products, on a revenue basis, I'll remind you that the acquisition cost is much lower because it's much more heavily a digitally acquired product and also, the stacked costs are lower. The cost to deploy, the cost to maintain is much lower. So over time, as we build those volumes up, those are products that will get scalable margins. I'll stop there and see if I missed anything.

John Stephens

This is John Stephens. JD, great job on that. I'll give it to you this way. First of all, Mike, we're not giving out specific guidance on margins on any of the specific businesses as I mentioned before, when I think Simon asked the question with regard to Time Warner's specific EPS impact.

What I will tell you is this. JD talked about the fact we'll be able to move DTV Now's deliverables, cloud DVR, streams, pay per view, future data insights and other opportunities, it's going to provide revenue opportunities.

Secondly, the fact that we've got the four products that are going to cut down on subscriber acquisition costs moving from a satellite -- the only truck that shows up now is now one of our trucks that hang a dish but maybe the UPS or the FedEx truck delivering that incline in the future.

All of those things give us the expectations that we can see the margins continue to improve. As our advertising team continues to learn more and get more effective, those advertising revenues will help out on that entertainment margins. So all of those things are giving us optimism as we go forward.

With that being said, we've got -- traditionally have tough compares with the NFL content so forth the rest of the year, so we're not giving specific guidance on margins for the third and fourth quarter. Well aware of the improvement in some of the stabilization of the operating contributions in the Entertainment Group, we're - we noticed that.

We're aware of it. The team's working hard to achieve that, but we'll keep this process going to see overall improvement on a year-over-year basis coming in 2019, and that's when we expect to see it.

Randall Stephenson

Okay. Thanks, Mike. Lori, we will take one more question.

Operator

Thank you. That's from Mike Rollins with Citi. Please go ahead.

Mike Rollins

Hi. Thanks for taking the questions. Two if I could. How do you view your sports rights between SUNDAY TICKET for DTV and the NBA for Turner as sustainable points of differentiation for your media strategy? And how important is it to take those content right and put them into your emerging, evolving direct-to-consumer strategy and platforms?

John Stankey

Well, let me all answer on behalf on the Turner side of things in sports and John can certainly address the NFL relationship on DIRECTV. The -- look, I view the right sports rights as being critical to our strategy over time. And I view the right sports rights with leads that want to participate in a manner that is reflective of how platforms are evolving and how technology is evolving and how consumers are changing their consumption patterns as being the right partners to work with.

And I feel pretty good about the partners that we have at Turner and their flexibility to sit down and look at new models, new approaches to how they put their content in front of consumers, how they think about the importance of digital and their product and the speed at which they're willing to move around those things.

Our advertising business is a healthier business with sports in the mix. I think you saw that in the second quarter numbers. Those were largely powered by the great performance of the NBA and a wonderful product that they have, and they're great partners.

And so I think it'll be very important for us to continue to manage that portfolio and have the right mix of sports and general entertainment in our portfolio that's attractive to customers in the linear format, and we'll continue to do that going forward. Now that mix may change a little bit.

Over time, different options may show up, but the asset test is going to be, I think, sports that are well received by customers, that are valued properly, that are flexible on how they work with distribution rights and technology and then working today's fast paced and dynamic society in terms of how they are consumed.

Randall Stephenson

I don't know -- this is Randall, Mike. I don't know if there's much to add as it relates to NFL. I think John Stankey just characterized what it is that we look for in terms of what's important when we think about sports programming.

And it's really critical when you think about our business, where everything is going, where John Stankey is going direct-to-consumer, where John Donovan is building platforms, better streaming platforms, where Brian Lesser's monetization opportunities for advertising are tied to streaming capabilities, those are probably our best opportunities. So finding sports programming that fits within those directions, where we as a company are going, are really, really important.

John Donovan

And I would also say, just as we get more targeted, just sort of one way to think about it is a sports lover in the future is not going to be the segmentation. It's going to be a Red Sox fan, a Yankee fan who spends winters in Tampa.

So these things had been acquisition tools over time. They're much more retention and engagement tools now that fit in that profile I mentioned earlier. And so we're going to really be trying to innovate on all of these things that are very segment specific, and I think you're going to see us really get creative in what we do going forward.

Randall Stephenson

Okay, very good. Listen, that wraps up what we wanted to cover with you this evening. I appreciate everybody joining us. What I would sum it up by saying is we've had a few months of distraction. And make no mistake about it. It's been a bit of a distraction for both businesses, the WarnerMedia as well as the AT&T side.

That is behind us, and we are executing. And I feel like we're executing very well on the communications business side, the momentum it's gaining as you're seeing service revenues are up. Subscriber metrics are improving, margins are improving. I feel really good about how that team is executing.

The WarnerMedia side, I couldn't be happier with the position that the company is in, the business is in, and it's going quite well. Our LatAm business, Mexico, it's going on all cylinders. It's been aggressive on pricing down there, but we are staying the course. We're competing aggressively.

We're gaining a lot of momentum. It has a strong path and a good line of sight to profitability. And stay tuned on advertising. I could not be more excited about the opportunity here for advertising, the ad tech acquisitions we've made. So thanks again for joining us and look forward to seeing and talking to everybody again.