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T - AT&T Inc at Barclays Global Technology, Media and Telecommunications Conference

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Kannan Venkateshwar *Barclays Bank PLC, Research Division - Director & Senior Research Analyst*

PRESENTATION

Kannan Venkateshwar - *Barclays Bank PLC, Research Division - Director & Senior Research Analyst*

All right. I guess we'll get started. So thanks for being here. I'm really happy to have with me Jeff McElfresh, who heads the wireless business at AT&T. Jeff, thanks for being here. Jeff has a lot of history in different parts of AT&T's businesses. And therefore to start off, Jeff, I guess what would help us a lot is, if you could just give us some perspective on where you came from that will inform a lot of what you say during the conversation. Can you give us a better context?

Jeffery Scott McElfresh - *AT&T Inc. - CEO of AT&T Communications LLC*

Yes. Great, Kannan. Thanks for having me. And before I get started, I've got to read a very quick safe harbor statement.

First, before we begin, I want to call to your attention our safe harbor statement which says, some of our comments may be forward-looking, subject to risks and uncertainties. Results may differ materially. And you can find further information on our website or in our SEC filings.

And so with that, Kannan, thanks for having me here today. Yes, I find myself today running a business more than wireless. Wireless is certainly a very large component of AT&T's communications company and clearly a critical component to our growth agenda over the next 3 years.

But it's fun for me to return back to a part of the business that I began my career about 24 years ago. I'm an engineer, and I started with the corporation deploying the very first digital network as we were converting analog to digital here in the U.S. And I've made my way through all the Gs: the 2G to 3G, 3G to 4G and now 5G, and I've done that over multiple continents. I've had the privilege of operating businesses in different parts of the world and different product sets, not only wireless, but also our pay TV video business in Latin America.

And so when the company asked me to return back to the States and take on a role to head up our technology organization, I found myself quite fortunate because the women and men of AT&T and the technology organization had been doing a banged-up job getting our wireless network into a very strong position. And so about 1.5 years ago when I took that role, it was on the precipice of a real launchpad of quality and speed and performance improvement in the wireless network.

And so now I find myself today gratefully being asked to lead the communications company division. And as you might imagine, we're going to lean heavy on our wireless portfolio for that.

QUESTIONS AND ANSWERS

Kannan Venkateshwar - *Barclays Bank PLC, Research Division - Director & Senior Research Analyst*

And so on the wireless side of the business, you have a revenue guidance of 1% to 2% growth over time and over the next 3 years. And when you think about the components of that, obviously, 5G is a big part of it. But if you could help us walk through the different components and the different levers that you have to drive growth over the coming years, that would be a good place to start.



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Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Well, as you've seen as we posted our third quarter results, we've experienced nice subscriber growth, we're experiencing service revenue growth, ARPU growth as well as margin expansion. It's really good momentum in our wireless business, and this is just the beginning. As our momentum is improving with the deployment of our FirstNet program and serving our public safety community in the U.S., we're seeing really nice subscriber gains, and we are projecting that to continue as we're just at the beginning of that program.

Our network quality is leading. As you know, our network is the best in the U.S. According to the nation's largest drive test, it's also the fastest. And so we've got network capacity and performance that our sales channels are excited to sell into. We've expanded our retail distribution in our wireless business aggressively this year as well. And as that productivity starts to ramp up, we're seeing increasing subscriber momentum.

And then as you think about the computation of our wireless base, about half of our subscribers are on unlimited plans, just half. And we most recently launched new unlimited rate plans right before the holiday and we're seeing some really nice momentum in adoption as our subscribers are upgrading into those unlimited rate plans.

Going into 2020, we're excited as we launch our HBO Max offering. That will be an integral component to the value proposition of our wireless offering. That will happen in May of 2020. And then towards the middle of the year, we will turn up our nationwide 5G sub-6 network. And our growth, we project will come from subscribers looking to upgrade to a 5G handset. And as they do, we're going to serve them up some nice entertainment with our HBO Max offering and our unlimited rate plans.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And one of the other components of revenue growth that you guys have talked about is, of course, wholesale. And you already have some of your competitors with wholesale deals with potentially cable companies and others. How are you thinking about that opportunity? Is this something that a stand-alone opportunity because of the network capacity that you guys have built up or is there also an opportunity to maybe partner with cable companies on things like strand mounts and increase the quality of your networks? How are you thinking about that?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Well, I think for the first time in a very long time, AT&T's network is in the strongest position it's ever been in. And that comes from the 60 megahertz of spectrum that we have installed across our network over the last 2 years. As a result of that, I think if you look at the compares, our reseller lines have been somewhat of a pressure to us on the year-over-year compares, but we now have got ample capacity to serve both retail and wholesale subscribers. And I would say it gives us optionality as we look at the different strategies to monetize that wireless network. So we're in a pretty good, pretty strong position to look at all options in that regard.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And when you think about some of the recent competitive dynamics, you have Verizon offering Disney+ and you mentioned HBO. So when you think about the kind of market structure we are moving to, it seems increasingly likely that there are other elements within the pricing plans that are becoming more important beyond just speed. So if you could just help us understand competitive trends near term, but more importantly longer term, how you're thinking about the kind of market structure in a 5G world and whatever components that competition will entail beyond just the core service?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Well, I think it first begins with the core network. I mean, subscribers, first and foremost, are going to purchase or make their purchase decision based on the quality and the speed of the network. And I'm proud to say that as the nation's best network and the fastest network, we continue



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to be in a leadership position, Kannan. In fact, in the 5G realm, there's been, I would say, kind of a lot of hype and a lot of snark that you've seen entering around the industry. And I'm here to tell you, I was on the ground with the technology team when we deployed the very first standards-based mobile 5G service here in the U.S. And as we deployed incremental millimeter wave, high-band 5G sites in venues and high-traffic locations, we've also been lifting up our 5G new radio assets on our towers through our One Touch program as we're deploying incremental spectrum in association with the FirstNet program. And so we're in a really good position to launch our sub-6 5G network in the middle of next year.

But the irony of all this is, over the last 2 years, as our engineers have been deploying the spectrum and upspeeding all the fiber and backhaul in the cell sites, our 5G Evolution network is actually the fastest network in the U.S. and remains the fastest network today regardless of any recent market launch. And we took some pretty healthy inbound and attacks from competitors like T-Mobile about our 5G Evolution, branding of the nation's best network. And I think tests here pretty soon will show just how fast and how solid our 5G Evolution network is relative to their most recent nationwide launch.

And so I would say, I just shared that to say, the fundamentals of the wireless network and the investments that AT&T has made has positioned our core product in a very strong position leading into the 2020 5G campaign.

In regards to entertainment, years ago, as the U.S. industry evolved from a kind of pay as you go or metered to an unlimited rate plan, the differentiation in how you compete in the market has shifted from maybe a rate plan structure on a per gig basis to other value and benefit. And so as a company that's got a superior spectrum position, and that spectrum has now been deployed, we have the opportunity to offer our customers differentiated service levels on our wireless network today. We don't have to wait for our 5G deployment in the future. And as part of our product design with our new unlimited rate plans, we have integrated our HBO Max offering when it comes available in May.

And on our highest tier, think about as our subscribers step up in the ARPU journey with us to the basic plan, to the mid-tier plan, to the high-tier plan, each step up gets them a faster access in a premium service tier on our existing network structure today.

And so our retail team, our marketing teams are really excited about the HBO Max offer and how that translates to our business in terms of economics. We've seen evidence in our base today of subscribers that subscribe to our wireless plans and our premium products and HBO. And they engage with HBO, the current legacy product, the churn profile of those subscribers is superior to those who do not. And HBO Max isn't HBO itself. HBO Max is a much broader demographic appealing product set. And so we're looking forward to offering that product to a wide breadth of new customers as we attract them to the AT&T network in May of 2020. And we think that helps translate into improved churn trends, improved share gain trends. So we're pretty excited about that.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

I guess another source of revenue growth that you guys have been optimistic about is penetration of broadband.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

That's right.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

Now what we've seen over the course of the last few years, I mean, you have built out a new fiber network post DIRECTV. But so far, the fiber has just been offsetting some of the declines in copper. And you've spoken about penetration rates going up to that 50% threshold that seems to be quite high.



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Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

That's right.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

So how are you thinking about this opportunity as you go into 2020? Should we see an acceleration in that path? And is this basically incremental to just the losses on the copper side? What's the kind of opportunity you are thinking there?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Well, the economic performance of our broadband business is very strong, setting aside subscriber losses in the lower speed DSL segment in the copper network.

In the fiber business and the fiber product line, where we have fiber, we win and we win handedly. As you mentioned, we've guided to driving penetration of our 14.5 million households to our fiber network to a 50% mark over the 3-year period. And we have proof of how we do this historically. As you look at the fiber that we built out in the ground in 2016, at the 3-year mark, we roughly approach about a 50% share gain in that territory. And so for 2020, with the bulk of our investments behind us in this fiber plan, our tactics are to drive penetration with the fiber that we've built.

As we roll through driving up incremental penetration of that investment that's already been made, we bring forth incremental products and services to that subscriber base, like our new AT&T TV product that we'll launch around the first quarter of next year for incremental value creation in that fiber product set.

I think John spoke earlier this week at another conference, as you described, some of the cost and optimization work that we have underway in the communications company is looking to create a little bit of headroom for us where we may find areas of reinvesting some savings and operational efficiencies in areas of the business, look for us to drive incremental found investment dollars back into our wireless business and into that fiber broadband business.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And fixed wireless is something that Verizon's talked a lot about, but you guys have some presence already in CAF-II markets.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. We do.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

But you haven't spoken as actively about it. How are you thinking about that opportunity going forward? Is that something over and above the fiber opportunity longer term?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. It could be. I think that's still a few cycles away. As we look at the economics of providing broadband to neighborhoods and households, still the economics prove that fiber to the home is the best play. But as technology evolves, we see an opportunity to serve all sorts of use cases with that 5G network. I've got to stress, though, it requires spectrum and it requires massive amounts of backhaul and capacity and fiber. And that takes



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quite some time to go deploy. And I like AT&T's position to date with the very large fiber footprint that we offer to enterprise and consumers, but also the underpinning fiber that we have deployed in our wireless network.

I'm not sure if we spoke about this last night or not, but I think about 2 weeks ago, we announced the first 400-gigabit data link with live traffic between Atlanta and Dallas, some of the work that's come out of our R&D and our Labs group to push the envelope on capacity that we can get over our backhaul fiber networks. And that advanced technology, we look to push that deeper into our network fabric.

And as we roll out 5G next year and the following years, I think the capacity will be available. I think the spectrum that we have put up on our wireless network will open up opportunities to serve home broadband as consumers today are generally using their smartphones or their iPads for broadband regardless of WiFi or the availability of something in the house anyway. So good spectrum position, good quality network with great coverage, with great backhaul puts AT&T in a great position to serve all markets.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And another headline more recently has been the partnership between AT&T and IBM and Microsoft on one side. And then, of course, Verizon's recently announced something with AWS. So when you think about some of the technology companies getting closer to the edge, I'm sure there's a cost component to it and there is also potentially a revenue opportunity to it. So how are you guys thinking about those tech partnerships and how that evolves over time?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. I think that's a really insightful question. So the relationship that we announced earlier this year with Microsoft and IBM both was a part of what we call our public cloud first policy. And this is a big move for AT&T. I mean, historically, we have always developed our own internal on-prem clouds and technology. And we made a decision earlier this year that to accelerate our cost curves faster than what we could ordinarily mine out of doing things faster, leaner, quicker, we're going to have to leverage the public cloud to migrate many of our workloads that serve our legacy telco and our wireless operations. And so those deals that we consummated were in one part designed to help us accelerate a migration of the AT&T Communications company back-office into the Microsoft cloud and the IBM cloud.

Now IBM is positioned with us on our enterprise space and they're very tight strategic partners with us in our enterprise business segment. And on the Microsoft side, we've been working on migrating more of our consumer base back-office applications over to the Azure cloud.

Having said that, as you walk through the motion and the technology that you have to integrate in order to lift and shift those applications to the public cloud, invariably, there are opportunities that you bump into of how you can extend the web-scale public cloud out closer to the edge with a network partner like an AT&T. And so look to see us to continue to drive innovation with multi-access edge compute and network edge compute with IBM and Microsoft as we roll out our 5G network in the middle part of next year.

I think also, Kannan, the cloud migration is an underpinning component of kind of the other half of our 3-year operating plan, and that is to drive margin expansion at an accelerated rate inside of the communications company. And historically, we've been really good at mining efficiency and cost in our technology operations. And now as we work with the help of Bill Morrow who has joined us. He's about 30, 45 days into the program. He's integrated with my leadership team on my floor back in Dallas. And as we are looking at opportunities to drive a portfolio and product rationalization inside of the communications company to drive some efficiencies for us to go look at areas of the business that might be subscale or may not be key growth components, we will attack those opportunities as we execute this 3-year plan and look to reinvest savings from that part of the program back into our top tier growth objectives.

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Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

I guess it makes sense to decompose that a little bit more in terms of the cost savings and how you're working with Bill. And yesterday, during the dinner, you mentioned how the network really hasn't caught up with some of the evolution of the underlying customer base over time and where the opportunity in cost comes from. So it would be useful to just decompose the cost opportunity.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Well, we're early into it. I mean I'm about 90 days into this job, and we've got new eyes on the portfolio. But invariably, as you look at a company as large as AT&T that's got such diversified revenue across so many different product lines, you arrive and you see that you've got areas of your copper network where the subscribers have already migrated to, let's say, maybe fiber or to wireless or to some other more advanced technology and your efficiency of that copper network might be underutilized. So we have maintained that network for many years.

And so we're working through looking at ways to optimize geographically areas of our network where we might be able to reclaim that. We do shrink our footprint, lower expenses, maybe have the opportunity to monetize some physical real estate in that part of our footprint would be some examples.

Other examples might be, as we call out some of these long tail products and services that aren't really value accretive to the broader AT&T, that helps us simplify our processes and our customer-facing customer service organizations and all the IT platforms that are in the back-office that support all those products and services.

And so simplification, focus are the elements of the program that Bill is helping me and my team using external benchmarks, challenging the status quo, if you will. And I can tell you, 90 days into this, I'm excited. There's plenty of opportunity. We're excited to get after it. And I think it'll result in AT&T being a leaner operation, a more focused operation on the high-growth areas of our portfolio. And our team is excited to get after that.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And in terms of time lines, I mean, when you think about this cost-saving opportunity, what are the kind of horizon you are looking at? I mean is this something that you're targeting over 2 years, 3 years or is there something that we might see even more near term?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. I think it's going to be feathered in. As the plans are developed and as we make our decisions and as we deploy these, you'll see some benefits occur earlier in the program. And some will take time to mine out and get the benefit towards the tail end. This is not a program that all the benefits arrive at the end of the 3-year plan. I don't want you to think that. We're looking to drive quarter-over-quarter improvement in our performance in the communications company. And many of these initiatives will be balanced across that 3-year period. Some may be accelerated, but it will be a fairly robust plan and well executed, well executed.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And when you think about the go-to-market strategy, you mentioned AT&T TV and you have HBO and so on.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

That's right.



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Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And as you go forward into next year, it does look like a lot of your competitors might replicate it, but more in partnership with others in terms of the way they go to market. So when you look at rolling out more 5G devices potentially next year and going to market with AT&T TV and HBO NOW and so on, is there any kind of a difference in the way organizationally you're approaching this instead of maybe in marketing each of these product set? Is there a bigger push potentially that we might see next year for a bundled product?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. I think success might look like, and you could judge our management team's performance on this. As we get into the depths of next year that you'll see a very clean market posture from our AT&T Communications company. You'll see lead product offers that are the best products that we can offer from wireless, fiber and AT&T TV and HBO Max in geographies where we offer the best infrastructure-based broadband. In parts of the territory where there is no broadband available, you'll see us lead with our satellite legacy pay TV product and wireless.

And some of the organizational changes John and I have made early in the cycle have set up dedicated teams mission-focused on each of these product segments such that we provide for, I think, a much cleaner, simpler face to the customer and face to the market. And that would result in tighter integrated plans between our HBO Max partners in the WarnerMedia side of the family and our wireless offerings and our 5,500 retail stores.

So I think you'll see us be very tightly integrated now under John's leadership. And we're looking to really run hard there in May as we watch HBO Max integrated in with our most premium products and offers across our portfolio.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

And on the video side of it, I think you guys have communicated broadly that this year might be the trough and then trends might improve going forward.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

That's right.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

From a dynamics perspective, I mean, how much of that is basically products like AT&T TV and their asset-light products with obviously a cost component with benefits, which are just the trend lines in legacy DIRECTV improving?

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. So 2019 will be the peak year of subscriber losses on the legacy television platform because we're actually in flight right now of architecting a market reorientation, getting ready for our AT&T TV nationwide launch in February of next year.

And as you think about how the subscriber volumes of our legacy business, we will improve the performance of that. But our growth agenda is on fiber and our entertainment group and on AT&T TV and the AT&T TV product that will be offered nationwide. I'm excited about this product because I think of it as a CapEx-light product. Acquisition costs are about half of what the legacy satellite product enabled. And the content and the programming lineup is every bit as good and the user experience is future leaning. It's the latest technology in virtual MVPD. And so we're excited to get that launched.



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And we'll grow with a better CapEx payback profile in our pay TV business with AT&T TV coupled with a focus on our fiber broadband footprint driving incremental penetration, and that's how we balance out our entertainment group's performance in 2020 and beyond.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

I think that's all we have time for.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. It shows 0, 0.

Kannan Venkateshwar - Barclays Bank PLC, Research Division - Director & Senior Research Analyst

That's right. Thank you, Jeff. Thanks a lot for coming here. Thanks for your insights.

Jeffery Scott McElfresh - AT&T Inc. - CEO of AT&T Communications LLC

Yes. Thanks, Kannan.

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