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# EDITED TRANSCRIPT

VZ - Verizon at JPMorgan Global Technology, Media and Telecom Conference

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## CORPORATE PARTICIPANTS

**Lowell McAdam** *Verizon Communications Inc. - Chairman & CEO*

## CONFERENCE CALL PARTICIPANTS

**Phil Cusick** *JPMorgan - Analyst*

## PRESENTATION

**Phil Cusick** - *JPMorgan - Analyst*

Hi, thanks for joining us. My name is Phil Cusick, I cover telecom and cable here at JPMorgan. And I want to welcome Lowell McAdam, Chairman and CEO of Verizon. For those who haven't met Lowell, he has been the CEO since August 2011 and the Chairman since January 2012. Lowell, thanks for joining us.

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**Lowell McAdam** - *Verizon Communications Inc. - Chairman & CEO*

Good morning, Phil, and good morning, everyone. I hand it to you, JPMorgan, you know how to time your conferences around the big announcements. So, congratulations.

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**Phil Cusick** - *JPMorgan - Analyst*

Right, it was very, very carefully timed.

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**Lowell McAdam** - *Verizon Communications Inc. - Chairman & CEO*

Yes.

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**Phil Cusick** - *JPMorgan - Analyst*

So congratulations on the Verizon Wireless deal. As you look at the next few years for Verizon can you talk to us about some of the continued growth drivers for wireless?

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**Lowell McAdam** - *Verizon Communications Inc. - Chairman & CEO*

Yes. So obviously the big deal for us in first quarter was getting the Vodafone purchase complete and we are really pleased with how that worked. There have been no surprises. We knew that asset very well and obviously this gives us a chance to tap into those cash flows.

If you look at our first quarter, Phil, I think we really were very, very pleased with the financials. If you look at our top-line revenue of 4.8%, up year over year, if you look at our earnings per share up 23% of the year. As we said we would, we expanded margins in both wireless and Wireline. So a very strong quarter for us.

And we have just come off of Mother's Day and momentum is continuing to build for us. So we feel very good about our momentum. As we look forward I see lots of opportunities here on both Wireline and wireless. FiOS, for example, we have seen tremendous adoption of our Quantum service which allows a customer to go up to 500 megs of throughput. We have seen 50% of the base already opt in for increased speeds.

On the wireless side we're continuing to convert our basic phone set. We have got about 22 million, roughly, basic phones in the base that we can convert. We've got roughly the same number of 3G phones that we can convert to 4G smartphones, which gives us the cost advantage of 4G.

So the basic business, which we are very focused on, has a lot of headroom for us. As we look forward -- we've talked about this, you have heard some of your other guests -- we think we're very well-positioned on video transport. We've made some investments in first quarter to augment what we call our Verizon digital media services platform.

We bought OnCue and upLynk and EdgeCast. All of those set us up very well for transporting and delivering video at insertion, those sorts of things. And OnCue gives us a great platform for IPTV as well as over-the-top video. So great opportunities on converged and independent, I'd call them, video services.

And then the machine-to-machine piece is beginning to take off for us. The Hughes asset that we bought is doing very well, expanding with Mercedes and Audi and VW and others. There is a couple of big -- we just won Hyundai in the last month. So there are a couple of big opportunities there. And we are seeing the healthcare piece and the transportation piece take off as well in machine to machine.

So, whereas a year ago I would say we were literally at the starting gate or maybe five steps behind the starting gate on machine to machine, now I think we are away and we're beginning to see some real pick up in volume.

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**Phil Cusick** - JPMorgan - Analyst

Okay, let's start with tablets, it seems like each quarter we are surprised with the momentum in that business. And is this still accelerating and do you anticipate a fairly decent penetration of the base over time from what right now is what, single-digit percent?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, I do. I mean, the last quarter was a record for us in tablet adoption. And you are seeing a nice array of SKUs out there now whereas you have got anything from the 7 inch all the way up to larger than the iPad from Samsung and LG. So people are able to get what they want.

And I think the advent of the tablets and the availability of more video are coming hand-in-hand and they are both driving adoption of the other. So I expect to see tablets significantly increase for us and it's a very small -- as you say, a very small part of the base at this point. But we are seeing more and more when people come in and buy a device they also pick up a tablet when they do that.

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**Phil Cusick** - JPMorgan - Analyst

And then talk about healthcare, which is something you have talked about a number of times in the past. Number one, where do you see really the opportunity and when does that come along? But also, what assets do you have that really give you an advantage to drive that business?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, about a year and a half ago we started a CEO Council on this, and Dr. Patrick Soon-Shiong out of LA, a very highly respected cancer researcher, asked Muhtar Kent from Coke and I to co-chair a committee with him. And we have 35 of the largest CEOs, we have Aetna, Blue Cross Blue Shield, we've got some of the big hospital chains, the Cleveland Clinic, the Mayo Clinic are represented, BofA is on there. We've got big companies represented.

And what we took on the task of is first to create a best practice set for businesses to keep their costs down and improve their outcomes. And then we took on the technologies to see what technologies would really be useful for an employer and an employee to drive lower costs and better health outcomes. And there are literally hundreds and hundreds of technical applications.

We took the team through our Waltham innovation center right here outside of Boston. And everything from medication monitoring, blood chemistry monitoring, the video consultation services, all of those involve mobile, they involve the cloud, which we have at least I think it is still the only HIPAA compliant cloud in the market at this point.

Security is a huge aspect in healthcare because of all the information that has passed around. So it really is the sweet spot for Verizon. We're fortunate to have Greg Wasson from Walgreens on our Board. And he is a terrific partner, Walgreens is very innovative and we're piloting a number of the possibilities with Walgreens. And I think this is going to really take off.

No matter how you feel about the Affordable Care Act, it has offered us that disruption that businesses are taking advantage of and we are one of the ones that is going to lead the charge here. So I expect healthcare to be a significant driver of our top- and bottom-line revenue here in the next two, three years.

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**Phil Cusick** - JPMorgan - Analyst

Okay. And so between healthcare, connected car and some other initiatives, two to three years is when we can start to see those as really impacting the top line?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, I think so. And another example, I was a guest at -- Rosabeth Moss Kanter had a symposium here at Harvard on the transportation system. And we had former transportation secretaries in the trucking industry, the railroad industry, aircraft -- every segment was talking about how they imbed the devices in the vehicles and the aircraft engines and the supply chain so that you can track the movement of goods. And the cost reduction associated with that is significant.

I mean I heard people quoting 20% reduction in their transportation cost if you can have an intelligent grid. And I mean, some of it is kind of fun and sort of on the drawing board, the autonomous car is one. But you are also into the very practical implementation of embedding chips, for example, in the paint that you use to outline parking spots in malls and sports stadiums.

There is actually an interesting study in Brooklyn that says 40% of the fuel burned in Brooklyn is by drivers driving around trying to find a parking spot. I mean even if it is 10% and you can make that more efficient by notifying the car where an empty parking spot is you see some significant savings here. So there is a lot of interest in that and I think that is another area of opportunity for us.

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**Phil Cusick** - JPMorgan - Analyst

And this isn't just connectivity, this is you providing services on top of the overall business?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Sure. Because all of that is -- you are storing it in the cloud, you are doing the data analytics especially in large transportation systems. LTE is absolutely crucial because of the latency. And if you get to the ultimate vision of communication between cars you are going to want to have that information available in nanoseconds to the other cars and to the transportation system. So it's a combination again of security, cloud and the connectivity space.

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**Phil Cusick** - JPMorgan - Analyst

Okay. And as you think about connectivity you have been in the wireless industry a long time, I feel like I have been in the wireless industry a long time.

**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

You look better than I do at this point.

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**Phil Cusick** - JPMorgan - Analyst

But when I started average minutes of use were 250 a month, something like that and then we ended up at 1,200. Today people with a 4G phone use what 1.5, 2 gigabytes a month?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Right.

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**Phil Cusick** - JPMorgan - Analyst

Do you anticipate a similar level of growth of data usage of the next five, 10 years as we have seen in voice?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, I think so. Machine to machine is a going to drive a lot of capacity gains but video does. And I would point to what we saw at the Super Bowl this year. We are one of the big sponsors of MetLife Stadium and we went in and really we put AWS in our sites, we put in additional cell sites. In one hour of this year's Super Bowl we carried more traffic than the entire game in New Orleans a year ago.

And at the halftime show -- I mean we've never seen that kind of volume on a network because everybody was shooting Bruno Mars and shooting the helicopters going over and uploading all of that data. And that just shows you what the potential could be as video becomes more and more dominant as the driver of the network traffic.

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**Phil Cusick** - JPMorgan - Analyst

And can all these pieces both connectivity and tablets, smart phones, new businesses coming on, can they keep Verizon's revenue growing in the sort of mid- to high-single-digits where we have been in wireless?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, you always do a very good job of getting me to provide guidance when I am not going to do that. But -- so look, we have seen -- out of wireless we have seen 8% last year. I think first quarter we announced that it was 7.5% top-line revenue growth. There is always pressure on the pricing in any -- if you look back over the 15 years of wireless, we went from a huge amount -- everything was voice and now voice is also a throwaway application.

So there will always be pressure. But I think there is so much innovation out there and the devices are becoming so much more embedded in people's lives that I do expect that we will see revenue growth here over the next five -- five years at least. So there is tremendous opportunity.

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**Phil Cusick** - JPMorgan - Analyst

Okay. Speaking of competition there have been a lot of headlines by competition in the last especially six months. Again, having been around for a little while and looking back over the last number of years, do you feel like competition today is higher, lower, in-line, with where we have been?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

As you mentioned, I've been around the industry for a while. And you get to a point where you think your life is a circle here. But if I look back at 1999 when we brought Verizon together there was tremendous competition, the names were different, MCI was a big reseller at that point, you had Airstream and others that have since been purchased. Sprint was the big innovator at that point and really was the company to beat. So I think there has always been tremendous competition.

Now I think there is a little bit of hype and there is a little bit of using the social networks to generate hype that can be good for the industry, it can also be hype. So -- but I think if you look at where we are, there have been some good innovations. I like to think we drove a lot of those.

I mean tablet installment sales we have had in the market for 18 months. Just in the last six month it has become a big deal for handsets. But that is fine, the customers enjoy it. It's at least neutral for the carrier. So that is fine.

Some of the entry-level pricing, I look back and I remember when we had \$25 entry-level plans for voice and they are a step up plan for people that want to really use their device.

So having a \$40, 250 meg plan is great, it is an entry-level plan. It is not really all that innovative, but if it generates some buzz and more people join the industry I think that is terrific.

I think the most important thing for me, Phil, is I look at the competitive environment and see is it destroying value for the carrier or for the customer. And I don't think we are at that point. If you look at a lot of the price changes that have gone on I would actually call those promotions, they are typically in for 30 days and out. And if you look at some of the promotions that have gone on recently right afterwards is a price take up.

So I don't see any empirical data that says that value is being destroyed here. We are expanding the market and if there is a little bit of excitement out there that is the great thing for the industry.

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**Phil Cusick** - JPMorgan - Analyst

Some people have been very concerned about the trade down potential on some of these new plans. You are not seeing that within the base?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, you always have that as a dynamic, right. You have people that are using the device that are moving up and you have people that see an opportunity to trade down and they trade down. It's imperative for us to come up with new applications like some of the ones we've talked about to get people to use the device more.

But if you compare our usage versus countries in Europe, our usage is -- I mean it is two, three, four times of the amount of usage. So people are getting good value, they are using the device, they are integral to their lives. I think that is an indication of a healthy industry. So the dynamic there on pricing moves up and down, doesn't bother me. At the end of the day I our revenue in wireless was up 7.5%, that sort of speaks for itself.

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**Phil Cusick** - JPMorgan - Analyst

Right. And there has been a lot of discussion about consolidation in wireless, whether it happens, does it not happen. Do you have any opinion on whether you are better off with three or four players in the industry and is the country better off -- consumer better off with three or four?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, to be honest I don't spend a lot of time worrying about whether there is consolidation. We can certainly compete in a four player market. If there becomes a third player market the economists would argue that we'd probably be better off. There will be a period of distraction during the approval process and then the integration process after that, typically three player markets are more stable than four player markets.

So I think we've shown we can compete pretty well in a four player market and whatever the regulators decide, they decide. That's sort of our view.

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**Phil Cusick** - JPMorgan - Analyst

And so, outside of wireless, as AT&T buys DirecTV and other video providers get bigger, do you feel like the game is changing and you need to follow along and do something different.

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, I think we did our big deal, right. I mean, people say well, don't you have to do a merger? Well, I just did a \$130 billion merger in my view. So we want to pay that off. I don't feel the need to do anything else at this point, Phil. You could debate the merits of a DirecTV/AT&T deal, but I think it made sense for both of those parties. So that's all we typically have to say on something like that.

I know there are reports out there that we're talking to DISH. I can tell you that that's somebody's fantasy. There have not been any discussions and there aren't any discussions going on with DISH.

Now, I think DISH has some interesting assets and there are things that a company like Verizon and DISH could do together, but I don't feel that owning a satellite company is something that I'm finding intriguing at this point. And we're much more interested in the video transport over-the-top mobile first sort of application versus a linear play and that's where we're focused.

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**Phil Cusick** - JPMorgan - Analyst

So there are two great ways to go there. I want to stick with spectrum for a minute. Two auctions probably coming in the next two years.

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Right.

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**Phil Cusick** - JPMorgan - Analyst

How do you think about Verizon's, one, need, and, two, desire to buy more spectrum balanced with the regulatory environment?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, when you see the volume increasing the way we see it across the various platforms that we have you are always going to look for spectrum. Spectrum needs to be a good match with a portfolio that you already have.

I am very encouraged and congratulate Chairman Wheeler for what he was able to orchestrate on the AWS auction later this year. I think it's a terrific set of spectrum, it will have availability. I think there will be enough for the major players to continue to feed the demand of consumers. And I think he did the right thing by having all of the spectrum in the numerator and denominator.

So AWS makes sense for us, you've seen us do some trades here recently with T-Mobile where we got AWS and we gave them some of the 700 A and B that we didn't feel fit with our portfolio quite so well. So I am expecting to participate fully in AWS.

The 600 because it is what I call a reverse auction, getting the broadcasters to contribute their spectrum and then a forward auction for others to buy, I think there is still a lot more information that needs to be gleaned from the process here.

So far it looks pretty positive, but there has to be enough interest from the broadcasters to create the pool before we get too committed one way or the other about whether we are going to participate and how much we need. So I would like to be able to join the 800 auction and be opportunistic, but we will have to see how things shake out.

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**Phil Cusick** - JPMorgan - Analyst

Okay. And there is a lot of -- I often hear Verizon is going to run out of spectrum or AT&T is going to run out of spectrum in year X. How do you think about other ways to create capacity? Last night we talked about unlicensed spectrum a little bit, can you go into that a little bit?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes. Well, I mean there are a couple of things. There are some pure technology plays like our multicast which we demonstrated at the Super Bowl. We got a tremendous amount of interest there. What that allows us to do is just put up one channel and we're able to take care of everybody in this room or everybody in the city on a cell site. So you get almost unlimited capacity for major events like that.

Certainly 3G to 4G gave us tremendously more efficiency. As you start looking at LTE Advanced there are some additional efficiencies associated with that. And then there are various compression techniques that are being explored by companies like Alcatel Lucent and Ericsson and others. I think there are some interesting technology advances that will help with that sort of capacity need as we go forward.

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**Phil Cusick** - JPMorgan - Analyst

Okay. Let's shift over to the Wireline side. You mentioned the video side a minute ago. What is the trajectory of the FiOS video group business? And is the profitability there something you can protect over time or is does it just erode as content costs go up?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, I think there are a couple of major things going on there. So we have been really encouraged by Quantum. As I said, we have set that up for up to 500 megs of throughput. We've got a new router going in place being deployed now.

We've got what we call a Verizon media server which allows us to get out of the coax game inside the house and we will be much more efficient in the installation process and the maintenance obviously will be more attractive that way, because you don't have as many things to break inside the house. Much less dependent on a set-top box as we know it today as we transition to IPTV.

So there is profitability opportunity there. The biggest growth markets for us right now are places like New York City. And the beauty of that is we've already got the fiber running down the avenues and the cross streets and we are just doing short extensions into these high-rise buildings. And within a very relatively short period of time we will have 35% penetration, we have got markets now where we are up to 45% and 50% penetration.



I think the other dynamic here, Phil, that is interesting is we used to sell a TV service and then an equal number of broadband services. And we are seeing the gap now increase significantly and you saw that in first quarter where you are seeing 20%, 30%, 40% more broadband sales than you are linear TV sales.

And I think that gets back a little bit to our philosophy on the MobileFirst and the broadband pipe and the over-the-top play is where we want to make sure we are well-positioned for versus continuation of linear TV. So because of the content costs going up so much I think a pure broadband play for us is at least as attractive, I would argue a bit more attractive for us and we are encouraged by that trend too.

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**Phil Cusick** - *JPMorgan - Analyst*

So first just a follow-up on the video side with 40%, 45% penetration in some markets it is a much better number than you expected when you built the FiOS business model, eight, nine years ago. Does that bring you to want to build out some more territories? You have got 5 million, 6 million more homes you could go to.

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**Lowell McAdam** - *Verizon Communications Inc. - Chairman & CEO*

Yes, probably not. I think the way we think about it is if you expand the borders of where you are and go deeper into the franchise area that we already have, that is going to be the general rule of thumb for us. So New York is, again, the best example of just pushing out a little farther into the neighborhoods than we have been.

That is a relatively cheap expansion for us versus coming into a greenfield market where you've already got probably one, or more likely two, competitors in place already. So I think it will be few and far between when we go into a new franchise area.

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**Phil Cusick** - *JPMorgan - Analyst*

And you mentioned over-the-top video. I want to make sure we are on the same page. Your OnCue acquisition creates an IP product for your own FiOS business and then you mentioned over-the-top as well. Can you talk about the differences between the two?

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**Lowell McAdam** - *Verizon Communications Inc. - Chairman & CEO*

Yes. Well, the OnCue user interface and a platform that they built it on is obviously all IP and we can transport that into our Verizon media server and make that system much easier to transform and use different IP-based applications as we go forward. So that is sort of the base case for purchasing that asset.

That group was built originally almost to create a linear TV offering as a pure over-the-top play. Now we don't think that model is particularly attractive because of the overall content cost. But if you look at a service, you know we use Redbox.

If you look at the video jukebox sort of services, the Hulu's the Netflix, the Kindle Fire and you create something like that that a customer can pull down from the cloud what they want when they want it and you have a much broader array of content -- the YouTube types of content and -- there are so many of these springing up out there these days with individual content. I think that is a very attractive model for us.

So we are not in the mode of having 80 channels bundled running over OnCue for Verizon, but we are in the mode of having an over-the-top play that customers can pull down what they want when they want it.

There may be some of the content that you see from the CBS's and the ABC's, we hope there is and we are having discussions with them. But it can't be the bundle 10 channels together and force them to take it over-the-top the way they have done in the current linear model.



**Phil Cusick** - JPMorgan - Analyst

And to wrap that back to what you talked about in wireless, the multicast product, is multicast wireless ever going to be five, 10 channels or is that really more of a specific event sort of a single, maybe a couple options at the same time?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

I think it could be. It is very interesting to see the use cases that are popping up that people that came through our Super Bowl event see. So we had all the major sport venues, I mean even Formula One you know are a big sponsor of the Indy races. MLB, NBA, the NCAA leagues. Those are the obvious ones.

But it has been interesting, many of the concert promoters have come in and they have said, gee, if we had the ability to take a concert make it up, it is in Miami and we want to be able to allow people to pay \$3 to watch whatever the hot act is no matter where they are in the country would you guys do that? Yes, I think we would.

And if you charged a nominal fee like that and if you look at the quality of the screens so that you could watch it and, let's take it a little farther. You talk to Twitter about integrating tweets during the session and you take our ability to insert ads and target the customer on the other end. And you take our ability to do something like our Isis mobile commerce play and you deliver coupons to the customer for things that are going on in the concert, there is an interesting business here.

Is it going to drive the bottom line of the business in the next couple years? Probably not. But there is a real use case here that people are getting some excitement about. So I think it could be more than single channel and single event.

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**Phil Cusick** - JPMorgan - Analyst

So you have talked about your own over-the-top associations and potential. What about the risk of over-the-top in the video side, one, putting a lot of traffic on the FiOS pipes and, two, cannibalizing what contribution margin you do make on FiOS video. How do you (multiple speakers) about that?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

FiOS broadband is more attractive for us then FiOS video is. So my view is if we convert over that is fine. We will have those broadband pipes and, if you think about it, the more traffic that goes into the home the better for us because we have got the technology that is future proof it is easy for us.

I kid around with Larry Page all the time. I say it is interesting you are building Kansas City. Please give me a few applications that require a gigabit of throughput and I will love you. Because we have got it, I mean it has been built for eight years. So I think we are in the best position to capitalize on high-volume traffic going into a home like that. And so I hope it comes.

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**Phil Cusick** - JPMorgan - Analyst

Yes, it is funny that Larry is not building over any of your markets.

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, we will see.



**Phil Cusick** - JPMorgan - Analyst

And that sort of brings us to the net neutrality conversation. There were some proposed rules from the FCC last week. Can you talk about your overall thoughts there?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, I think this is an example where emotion is trumping logic I am afraid for some people. Just the fact that people try to tie the Netflix agreement to net neutrality is very curious to put it nicely I guess. We have had peering arrangements forever in our industry and this is nothing different than an asymmetrical peering arrangement that both companies feel pretty good about the agreement that we have reached.

Net neutrality in general -- we have posted our position on our website, it is probably been up there for nine months at this point. If you think about it we make money by carrying Internet traffic more and more. And so, manipulating that traffic other than to protect the network security makes no sense for us. So we want to see a very strong Internet, we want to see a very open Internet and I think the FCC is understanding that position.

The push to Title II is absolutely the wrong way to go. And if you talk to the people in Silicon Valley, they agree. I mean they signed letters to the FCC calling for an open Internet, I'd sign that exact letter as well, no issue.

I think we have seen from other countries around the world the minute you start to heavily regulate the Internet, and especially in a forum like Title II, that will guarantee investment will dry up in the Internet. Then that web has to be cast to capture companies like -- that are really the main drivers of the Internet, the Google's, the Facebook's, the Twitters, etc., the Netflix.

And so, once you try to start regulating the Silicon Valley companies I think things move way too fast for a regulatory agency in Washington to keep up with that. So my guess is that cooler heads will prevail here. As I say Chairman Wheeler understands the business pretty well and he will certainly hear everybody's point of view. But I don't think Title II is a legitimate threat at this point.

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**Phil Cusick** - JPMorgan - Analyst

And even if we went to Title II, I mean wireless is regulated under Title II, do you think that there would be sort of a light touch and the FCC continue to encourage broadband investment?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, I mean they would like to for sure. I mean the Telecom Act of 1996 really encouraged the light touch to wireless in general and we had Commissioner Rosenworcel at our leadership meeting here last week and I think the FCC is in the envious position that people around the world are coming to them saying, wow, you guys got it right. What would you do to advise us?

And that is not the way it was. 10 years ago everybody was going to Europe that they got it right and we have seen at this point they haven't. So I think there is an understandable and appreciated view that we need to be careful what we do because you have not seen any country in the world see the investment in wireless and broadband networks that we have.

At least on the scale that we have. You can argue about Japan, but that is pretty small relative to the US. So, I think we've got a pretty good formula here and we need to be very purposeful about any regulation.

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**Phil Cusick** - JPMorgan - Analyst

And you mentioned Quantum, but people are paying up for better speeds and they desire it.



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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes.

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**Phil Cusick** - JPMorgan - Analyst

What sort of applications are driving the Quantum upgrade and what sort of level of acceptance do you have so far?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, well our head of our consumer and mass business group, Bobby Mudge, puts it very clearly. He said you think about you've got five members of your family, everybody wants to jump in the shower at the same time, you sort of run out of hot water pretty quickly. And with Quantum you can go in on your set-top box and one click you can increase the amount of hot water that you get in your house. So Bobby is a man of good examples.

Anyway, that is really the driver for us on Quantum is the number of devices showing up in the home is continuing to skyrocket and people want to use Wi-Fi to watch something while they are having their TV set on. So we have seen 50% adoption of Quantum in our base so far. So that is pretty amazing given that it has been out there six months or nine months at this point.

So I expect that will continue. And what I am hoping is that we can then raise to the next level of a gig and we will see people upsell to that. But we've got to come up with a few more applications beside just video, a number of devices I think to drive that.

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**Phil Cusick** - JPMorgan - Analyst

The cost side doesn't have a sexy name like Quantum, but I continue to be surprised with how much money you can pull out of your cost side, both wireless and Wireline. Remind us, one, how much are you pulling out this year that you have said. And two, the systems level in Wireline that just continues to be pulled down and how does that change the business over time?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Yes, I think the one thing we really did right in wireless when we brought it together is we invested in our IT resources to get ourselves down to a single billing system so that if we need to make a pivot in the marketplace we can do it very quickly.

And when I became the Chief Operating Officer we formalized the program that we had in wireless. And it is a Lean Six Sigma approach so we call it Verizon Lean Six Sigma or VLSS and we have now deployed that across the Company. And that is what we use to make sure we understand the customer and then we go and design a process that delivers what the customer wants and we streamline the process, take a lot of cost out in the process.

So last year two we took out \$5.7 billion. On the enterprise side alone we retired over 300 different systems. So our throughput is dramatically accelerated, the amount of rework is dramatically reduced. This year our target is over \$6 billion coming out.

And there is still lots of headroom on the wireless side. Last year roughly it was about \$2 billion out of Wireline and the balance out of wireless, so \$3.7 billion out of wireless. So there is still lots of opportunity for us in understanding the customer and then driving the kind of process improvement that supports their requirements.

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**Phil Cusick** - JPMorgan - Analyst

And to put those 300 systems in context, how many -- I think John said at one point last year there were 900 systems within Wireline that needed to be pared down. Where do you end up? And what is the level of OpEx savings as you go through that process over a five-year period?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, I am not sure I'm going to want to quantify a five-year target. But we see about \$5 billion to \$6 billion coming out over the next several years in our planning process. So if you look at even the Wireline side of the business, I occasionally will get a note from a customer that says, gee, I got a bill from you that said MCI on it. So I mean, that tells you some of the issues we have got to deal with here.

So, but we will -- in our consumer and mass business group we will be down to one billing system. By the way, it is the same billing system that we have on the wireless side. And on enterprise it is obviously a much more complicated process. But we will get down to one billing system there over the next couple of years.

And when you do that all the ancillary systems that have to support provisioning and maintenance process can be dramatically reduced. And you do a lot better job of understanding the inventory that is out there. I mean, we learned a tremendous amount during Hurricane Sandy of what our inventory, how accurate our inventory was.

And as we went in and cut out all of the copper cables in those three big central offices in Lower Manhattan and put them in fiber we were able to upgrade the system, bring them on to a new inventory system. So the provisioning, maintenance and testing processes are dramatically streamlined and much more efficient. So there is a lot of that left to do, Phil.

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**Phil Cusick** - JPMorgan - Analyst

Okay. Let's switch over quickly to the macro environment with the couple minutes that we have left. What are you seeing in terms of business environment overall, activity overall and split between enterprise and SMB?

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**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, consumer I think continues to be strong because we are able to bring out services like Quantum, new handsets. We just launched what we call XLTE on the wireless side, that will generate some excitement as we raise the capabilities of the network.

On the enterprise side, if you flip all the way to the other end, there's still a lot of overhang over are taxes going to change? What sort of investments are people willing to make? So there's still a lot of pressure to reduce costs.

But I will say over the last couple of months we are beginning to see some signs that may indicate that people have just gotten either numb to it or they believe that things like bonus depreciation may actually come. So we are seeing some cautious investment.

And then I hope to see that come down to the small business side. That has been more of a push for us in areas where we have FiOS as an example. We are pushing into the small business to provide them the fiber services, the cloud services that we typically have on the enterprise side.

And we have made some changes, as you have seen, in our small business pricing for wireless where we can -- you can now get 10 line bundles and 20 line bundles. And I am hopeful that that will over the second half of 2014 be a little bit stronger for us.

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**Phil Cusick** - JPMorgan - Analyst

Good, we are about out of time. Lowell, thank you very much for joining us.



**Lowell McAdam** - Verizon Communications Inc. - Chairman & CEO

Well, thank you, thank you all.

**Phil Cusick** - JPMorgan - Analyst

Nice to see you.

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