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T.N - Q1 2022 AT&T Inc Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to AT&T's First Quarter 2022 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would like to turn the conference over to our host, Amir Rozwadowski, Senior Vice President, Finance and Investor Relations. Please go ahead.

Amir Rozwadowski - *AT&T Inc. - Senior VP of Finance & IR*

Thank you, and good morning, everyone. Welcome to our first quarter call. I'm Amir Rozwadowski, Head of Investor Relations for AT&T. Joining me on the call today are John Stankey, our CEO; and Pascal Desroches, our CFO.

Before we begin, I need to call your attention to our safe harbor statement. It says that some of our comments today may be forward-looking. As such, they're subject to risks and uncertainties described in AT&T's SEC filings. Results may differ materially. Additional information is available on the Investor Relations website. And as always, our earnings materials are on our website.

With that, I'll turn the call over to John Stankey. John?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Thanks, Amir, and good morning to all of you. I appreciate you joining us this morning.

Two weeks ago, we reached a major milestone in the repositioning of our business with the completion of the WarnerMedia-Discovery transaction less than 11 months after announcing the deal. I'd like to thank everyone who played a role in getting this across the finish line in good time and with a little drama, just as we promised you.

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I'd also like to share how proud we are of the entire WarnerMedia team. David inherits an organization with one of the best global portfolios of beloved intellectual property, a team with unparalleled talent and one of the few truly global direct-to-consumer players, as evidenced by the continued growth in HBO Max and HBO subscribers which closed this quarter at nearly 77 million globally, up 3 million from last quarter and nearly 13 million year-over-year. We're excited about the potential for continued HBO Max growth as the service launches in more new territories.

Warner Bros. Discovery is well positioned to lead the transformation we're seeing unfold across the media and entertainment landscape. And like many of my fellow AT&T shareholders who own a stake in this new and promising enterprise, we're excited to continue to watch their success and the value they create as one of the leading global media companies.

So let me turn to AT&T and the new era and opportunities ahead of us. Our transaction marks a critical step in the repositioning of our business. We're now able to focus intensely on what we believe will be multiyear secular tailwinds in connectivity. We now have the right asset base and financial structure to devote our energy to becoming America's best broadband provider. Over a 5-year period, we expect a fivefold data increase on our networks and we plan to capitalize on the growing desire from consumers and businesses for ubiquitous access to best-in-class connectivity solutions.

The results we've achieved the past 7 quarters, all while undergoing a significant repositioning of our business, give me confidence that we can accomplish this goal.

Our first quarter financial results are consistent with our expectations and once again demonstrate that our teams are executing well against our consistent business priorities. We're seeing record levels of net additions in Mobility and consistently strong AT&T Fiber growth, thanks to our disciplined and consistent go-to-market strategy.

In Mobility, our strong network performance, simplified offers and improving customer experience brought in the most first quarter postpaid phone net adds in more than a decade, surpassing last year's then decade best first quarter total. And we're confident we can continue this momentum in a disciplined manner, given our subscriber success has come from diversified channels that span consumers and businesses.

In Fiber, we continue our great build velocity and now have the ability to serve 17 million customer locations. This expansion continues to allow our business to grow. And this quarter, we achieved overall broadband subscriber and revenue growth as our Fiber net adds more than offset legacy non-Fiber broadband losses.

I'm pleased with the improved fiber momentum we're seeing with our multi-gig plans launched early in the first quarter. It's also noteworthy that we're experiencing improved subscriber growth following the introduction of our straightforward pricing across the fiber portfolio, which does away with discounted introductory pricing. This improvement in share gains suggest that consumers are finding value and higher quality services when they're made available to them.

So taking a step back, let's review our progress over the last 7 quarters. During that time, we've added industry-best subscriber totals of more than 5.3 million in postpaid phones and nearly 2 million in AT&T Fiber, as our fast-growing fiber revenues now make up nearly half of our Consumer Wireline broadband revenues. This is real and sustainable momentum.

We also continue to emphasize effectiveness and efficiency across our operations. As we shared at our Analyst Day last month, we expect to achieve more than $4 billion of our $6 billion cost savings run rate target by the end of this year.

Our focus on driving efficiencies continues to show tangible results from our network build-out to customer experience. As we told you, we're initially reinvesting these savings to fuel growth in our core connectivity businesses. However, as we move to the back half of this year, we expect these savings to start to fall to the bottom line.

Our success over the past 7 quarters can also be attributed to our focus on better recognizing and delivering on what customers want. Our Mobility and Fiber Net Promoter Scores are up year-over-year and near historically low churn levels across all businesses demonstrate how our improvements to the customer experience are real and delivering a positive impact.

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Our Business Wireline unit continues its transformation. As we move through this year, we had planned to accelerate the pace at which we reposition the business as we focus our energy on growing repeatable core connectivity and transport solutions where we have owners economics. At the same time, we'll continue to rationalize reselling low-margin, third-party products and services. The expansion of our fiber footprint is enabling our business portfolio to target significant opportunities in the small and medium business market, allowing us to capture a greater portion of the opportunities in core transport and connectivity. In addition, as we open up relationships with more customers, we'll have incremental opportunities to continue our growth in business wireless.

We expect to take advantage of these near-term opportunities to help stabilize our Business Wireline unit as we simplify the portfolio and grow connectivity with small- to medium-sized businesses complementing our leading enterprise position.

As we thoughtfully fuel growth for services powered by our owned and operated connectivity assets, we're also being deliberate in how we allocate our capital. We've taken significant steps to improve our financial flexibility, and we're now in a much better place to grow our business as we significantly invest in the future of connectivity through 5G and fiber.

With the completion of the WarnerMedia-Discovery transaction, we've monetized more than $50 billion of assets since the beginning of 2021. And with this transaction, we reduced our net debt by approximately $40 billion in April. As we share, we feel as though we're really well suited to navigate this unique moment in time. This leaves us in a much better position to pay down debt. In fact, we've already addressed some of our near-term maturities and paid off over $10 billion in bank loans.

This improved financial posture gives us the flexibility to carefully and prudently use the balance of the WarnerMedia proceeds to reduce our outstanding debt by opportunistically using the evolving higher rate environment to redeem debt securities at lower prices while also working to reduce cash interest. In addition, our expectations for continued strong cash generation provide us with incremental capabilities to reduce leverage while still paying an attractive dividend yield near the top of the Fortune 500. This improved financial flexibility also allows us to pursue durable and sustainable growth opportunities that offer future upside for customers and shareholders.

If you couldn't tell, I'm proud of all the work the team has accomplished to reposition the business over the last 7 quarters and could not be more excited about this next chapter for AT&T. I know our teams are thrilled about the momentum we're generating with our deliberate and focused approach in attracting and retaining customers.

I'll now turn it over to Pascal to discuss the details of the quarter. Pascal?

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

Thank you, John, and good morning, everyone. Let's start by taking a look at our first quarter consolidated financial summary on Slide 5. It's important to note that our first quarter consolidated results include the contributions of WarnerMedia and that last year's first quarter included results of our U.S. Video business and Vrio. Accordingly, our reported results do not provide a clear reflection of our business on a forward-looking basis. So let me quickly cover a few key points before reviewing the financial results of our new stand-alone AT&T operations on the next slide.

On a consolidated basis, including a full quarter of WarnerMedia, our adjusted EPS for the quarter was $0.77 compared to $0.85 in the first quarter of 2021. In addition to merger amortization, adjustments for the quarter were made to exclude our proportionate share of DIRECTV intangible amortization and a gain in our benefit plans.

Year-over-year earnings declines were primarily driven by WarnerMedia and, to a lesser extent, certain onetime costs in the Communications segment. The declines in earnings at WarnerMedia reflect increased investments incurred in launching CNN+ and expanding new territories at HBO Max. HBO Max and HBO now reached an impressive global subscriber base of nearly 77 million. WarnerMedia's results were also impacted by the advertising sharing agreement entered into with DIRECTV upon its separation in last year's third quarter and the termination of HBO Max's wholesale agreement with Amazon late last year.

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When excluding revenues from our U.S. Video business and Vrio from the prior year quarter, AT&T consolidated revenues were $38.1 billion, up 1.6% or $600 million year-over-year.

Cash from operations came in at $5.7 billion for the quarter.

Overall spending was up with capital investments totaling $6.3 billion.

Free cash flow was $700 million for the quarter. WarnerMedia had declines of $2.6 billion in free cash flow year-over-year. This decline was driven by $1.2 billion in lower year-over-year securitization of receivables in advance of the transaction, $600 million in higher cash content spend, increased investments in HBO Max's global footprint and ramp-up for the CNN+ launch as well as NHL right payments and other working capital changes.

Now let's look at our financials for the new stand-alone AT&T on Slide 6. On a comparative like-for-like basis, our financial results for the quarter are in line with our expectations for how we expect the year to trend. However, our subscriber metrics came in better than we expected as market conditions remain strong. This gives us confidence in the annual guidance provided at our recent Analyst Day.

Revenues were $29.7 billion, up 2.5% or $700 million year-over-year, driven by wireless and broadband revenue growth, partially offset by declines in Business Wireline.

Adjusted EBITDA was flattish year-over-year as lower retained video costs were offset by peak impact from our 3G network shutdown, continued success-based investments in wireless and fiber and the launch of multi-gig fiber plans. We remain confident that Q1 will be the trough in our year-over-year adjusted EBITDA trajectory. We continue to expect the year-over-year trend line to progressively improve through the year.

On a comparative basis, adjusted EPS for the quarter was $0.63 versus $0.58 in the first quarter of 2021 due to higher equity income from DIRECTV and lower interest expense. Cash from operations came in at $7.7 billion for the quarter. Overall spending was up year-over-year with stand-alone AT&T capital investments of $6.1 billion.

Free cash flow was $2.9 billion. As expected, cash flow this quarter was affected by several factors. First, higher capital investments as we ramp fiber deployment and prepare to deploy our 5G mid-band spectrum bands in the back half of the year. Second, the absorption of 3G shutdown impact. Third, increased employee incentive compensation benefits paid in Q1. Fourth, lower proceeds from securitizations.

DIRECTV cash distributions were $1.8 billion in the quarter, which is modestly better than the $1.5 billion contribution in last year's first quarter. We continue to expect about $4 billion distribution from DIRECTV for the year, so we do expect some moderation.

Given that Q1 is a seasonally low quarter for free cash flow and many of the factors impacting free cash are not expected to repeat, we remain confident in the guidance we provided to you during our Analyst Day to achieve free cash flow in the $16 billion range for the year and on a stand-alone basis.

Looking forward, we expect to incur restructuring charges over the next few quarters as we continue to execute our transformation initiatives. The cash impact of these charges has already been contemplated in our full year free cash flow guidance.

Now let's turn to our subscriber results for our market focus areas on Slide 7. Diving a bit deeper into our business unit level performance, the story continues to be simple and straightforward. The consistent, disciplined go-to-market strategy we implemented almost 2 years ago continues to work very well, and we're delivering strong momentum and growing customer relationships with 5G and fiber.

In the quarter, we had 691,000 postpaid phone net adds. As John said, this marks our best first quarter in more than a decade. This total also excludes impacts of 3G network shutdown of more than 400,000 postpaid phones. Consistent with industry practice, we have treated this reduction as an adjustment of our base at the beginning of the period.

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Churn also remained near historically low levels, thanks in part to our improving NPS, which is being driven by an enhanced customer experience, the strength of our network and our consistent and simple offers. We're growing our customer base with this disciplined approach. Our teams have maintained a strong focus on growing the right way with high-quality intake and by investing in existing customers. As mentioned in March, we're focused on incentivizing customers to shift to our current unlimited rate plans, which are designed for the 5G era and to better meet each customer's unique needs and provide greater value to both existing and new customers.

Looking at AT&T Fiber, our customer base continues to grow as we expand availability of the best access technology across our footprint. We had 289,000 AT&T Fiber net adds in the first quarter and we expect to accelerate growth from here.

To say we're excited about the underlying momentum of the business would be an understatement. Where we have Fiber, we win and gain share and our deployment plans remain on track. We now have 6.3 million AT&T Fiber customers, up 1.1 million compared to a year ago and we expect customer momentum to accelerate from these already stepped-up levels. We continue to see strong demand for AT&T Fiber as customers seek out faster broadband speeds at an attractive price. And our Fiber churn remains low as AT&T Fiber continues to offer a great experience and a consistently high Net Promoter Score.

Now let's take a deeper look at our Communications segment operating results, starting with Mobility on Slide 8. Our Mobility business continues its record-level momentum. Revenues were up 5.5%, with service revenues growing 4.8% due to subscriber growth. Impressively, this growth in service revenue comes despite impact on service revenue of our 3G shutdown and without a material return of international roaming revenues.

Consistent with our comments on Analyst Day, Mobility EBITDA declined 1.8% year-over-year, largely due to a number of onetime-related factors. EBITDA was negatively impacted by over $300 million due to 3G shutdown costs and the absence of FirstNet and CAF II reimbursements. We remain confident in our stated expectations for Mobility adjusted EBITDA trajectory to improve through the course of the year as these impacts moderate through the balance of the year.

Overall, we continue to see healthy Mobility demand. While our guidance does not factor in industry demand levels replicating the strength that we experienced in 2021, our Q1 results came in better than anticipated. Both our postpaid phone and prepaid phone churn remained near record low levels despite a modest uptick among lower-income cohorts as certain pandemic levels benefits wear off.

Now let's turn to our operating results for Consumer and Business Wireline on Slide 9. Our fiber growth was solid as we continue to win share where we have fiber. Even with expected declines from copper-based broadband services, our total Consumer Wireline revenues are up again this quarter, growing 2% due to higher broadband ARPU and fiber revenue growth.

Our fiber ARPU was approximately $60 with gross addition intake ARPU in the $65 to $70 range. We expect overall fiber ARPU to continue to improve as more customers roll off promotional pricing and on to simplified pricing constructs we introduced earlier this year.

In addition, with the launch of our new multi-gig speeds in January, we have even more opportunity to move customers to higher speed tiers. Over time, we expect these factors to serve as a tailwind to the trajectory of our fiber ARPU.

We also continue to accelerate our Fiber footprint build and now have the ability to serve 17 million customer locations. As you heard us share on Analyst Day, our plans center on pivoting from copper-based products to fiber. As we make this pivot, we expect positive EBITDA growth in 2022, driven by growth in broadband revenues.

Also to help provide you with greater insight into the performance of our Consumer Wireline Fiber operations, we've provided additional metrics in our trending materials that can be found on our IR website.

Looking at Business Wireline, we continue to execute on our rationalization of low-margin products in our portfolio. In the first quarter, we experienced some impacts by the timing of government sector demand due to the delays in passing the federal budget, which caused deeper-than-expected revenue declines. However, we expect demand to rebound later this year.

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While the rationalization of our Business Wireline portfolio creates incremental pressure on our near-term revenues, it also allows us to focus on our own and operated connectivity services as well as growing 5G and fiber integrated solutions. Both areas, business 5G and fiber, continue to perform well, benefiting our Mobility segment with Business Solutions wireless service revenue growth of 8.4% and a sequential increase in our FirstNet wireless base by about 300,000.

We remain comfortable with our guidance of Business Wireline EBITDA down mid-single digits in 2022.

Shifting to Slide 10, I'd like to reiterate our overall capital allocation framework moving forward. With the completion of the WarnerMedia transaction, AT&T received $40.4 billion in cash and WarnerMedia's retention of certain existing debt. Additionally, AT&T shareholders received 1.7 billion shares of Warner Bros. Discovery, representing 71% of the new company. This transaction greatly strengthens our balance sheet and provides us with financial flexibility going forward. We now have a simplified capital allocation framework.

First, we plan to invest in our strategic focus areas: 5G and Fiber. As previously said, we expect stand-alone AT&T capital investments of $24 billion in 2022 and 2023. Starting in 2024, we expect our capital investment to begin tapering to around the $20 billion range as we surpass peak levels of investments in 5G and transformation.

The completion of the WarnerMedia transaction also marks a significant step towards achieving our established goal for net debt to adjusted EBITDA in the 2.5x range by the end of 2023. We've shared, as we get closer to this target, we expect our financial flexibility to improve. This increases our ability to pursue other ways to deliver incremental value for our shareholders.

As previously said, we expect to deliver annual total dividends of around $8 billion, which represents $1.11 per common share. This remains an attractive dividend and places AT&T among the very best dividend-yielding stocks in the U.S.

Now let's take a step back and look at the free cash flow generation expected from our business. As outlined at our Analyst Day, we expect to generate in the range of $20 billion of free cash flow in 2023. After paying dividends and noncontrolling interest commitments, we expect to have at least $10 billion of cash remaining. And beyond 2023, this pace of cash generation will be helped by the tapering down of our capital investment. This is why we continue to feel very comfortable with our capital allocation plans.

As I've stated, we're in a much stronger financial position to pay down debt. And at the end of the first quarter, more than 90% of our debt portfolio was fixed and we do not have near-term needs to issue debt. In April, we improved our net debt by about $40 billion and paid down over $10 billion in bank loans, providing us with a lot more financial flexibility. We also provided notice that we plan to redeem an additional $12.5 billion of bonds by mid-May, reducing our near-term maturities.

For the balance of the WarnerMedia proceeds, we plan to reduce our outstanding debt by focusing on pay down of commercial paper to improve our liquidity and opportunistically using the higher-rate environment to redeem debt at lower prices. So we feel really confident in our ability to pay down our current debt maturities in an effective manner and reach our goal for net debt to adjusted EBITDA.

Amir, that's our presentation. We're now ready for the Q&A.

Amir Rozwadowski - *AT&T Inc. - Senior VP of Finance & IR*

Thank you, Pascal. Operator, we're ready to take the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from the line of John Hodulik of UBS.

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John Christopher Hodulik - *UBS Investment Bank, Research Division - MD, Sector Head of the United States Communications Group and Telco & Pay TV Analyst*

A couple of questions on margins, if you could. First, maybe on the consumer side, numbers were a little bit better than we thought. I mean if you look back to 2019, you guys were generating margins in the sort of 39%, 40% range. Given the change in the business and the mix there and the higher ARPUs, do you think you can eventually get back to those kind of levels?

And then I guess on the other side of the ledger, consumer -- or the business segment continues to be weaker than expected, thanks for the color there. But how much visibility do you have in the improvement in the margins and the declines there? Any other color on that sort of rationalization of the portfolio you guys keep talking about? And should we see this improvement even if we see some economic headwinds later in the year?

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

Consumer Wireline first, let's -- the thing to keep in mind is in repositioning this business, we had -- over the last several years, we've been investing in our Fiber footprint and investing and launching in new parts of our footprint. What happens going forward is as the business add subscribers, we expect margins to continue to improve. And our cost base is relatively fixed once we've laid fiber out, so we do expect improvements over time. We haven't guided in terms of specific margins expected to generate, but we feel really good about the long-term view of this business. I mean you look at others in the space, margins are really attractive.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

And John, I'd add to that, if you go in and you kind of decompose what's in the transformation program and where we're targeting improvements in our operations in our business and things like reduction of call center activity that ultimately moves online, et cetera, all those things feed directly into that business that will -- it will allow us to scale that into the right kind of margin structure that I think we've historically been accustomed to, given the long-live nature of the asset base that we're deploying.

To answer your question on the business side, I'll tell you what we have visibility to. As we've shared with you, our move is to be driving harder owned and operated infrastructure into the low end of the mid part of the market. And in order to do that, that's highly correlated to where we're deploying new fiber or where we have existing infrastructure deployed. We have good visibility to that part of it. So we know, as we deploy what we open up in terms of new market opportunity.

In some cases, in order to get that market, we're shifting our distribution channels. So there is work going on around how we ultimately position to distribute the product both directly through our own sales force as well as through other third parties. That's an execution issue. While we have control over how we progress on that, obviously, any time you scale up new channels and you work through things, there's things that you run into that are unexpected or that allow you to move left to right that you have to adjust to. But that's nothing new, that's the kind of thing we work with. And I think in terms of working through those issues, they usually are cycles that matter from a quarter or 2. They're not the kind of things that you hit a brick wall and can't work your way through.

That's the area that I would say maybe we don't have perfect visibility over, but it's a question of whether you trust we can execute. And I would tell you, my view is we know how to do these kinds of things. I think I shared with you on the Analyst Day one thing that is very clear as we walk into the segment with the AT&T brand on the product and service, it's incredibly well received. And as I mentioned in my opening remarks, when we walk into these customers and we have the opportunity to talk to them about a new product, it oftentimes leads to a second discussion about possibly moving other parts of their services, like wireless, in that transaction. And that's the power of us in the business segment being able to go on with a complete portfolio of owned and operated wireless and direct fixed transport.

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Operator

Michael Rollins from Citi.

Michael Ian Rollins - *Citigroup Inc., Research Division - MD & U.S. Telecoms Analyst*

As you look at the postpaid phone volume growth in the quarter, how much of that do you attribute to better market share versus just better overall industry growth? And can you frame how the economics of these mobile postpaid phone customers are evolving when you consider the ARPU, churn as well as the cost of acquisition?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Mike, sure. Obviously, we don't -- we're first, so we don't have information as to how others are going to report this quarter. We, clearly, from the way we look at data, have some view of what's going on in the market. And I can tell you without backing that up with the actual reports from others, we believe the overall market still remains pretty strong. And we're seeing, what I would say, consistent volumes to what we saw in 2021 in terms of gross add pool that is occurring in the market. And I think we shared with you as we were guiding, we expected that to maybe taper down a little bit this year as we were giving you our estimates and our expectations. And so far, at least through the first quarter, we haven't seen that materialize at this juncture.

And I would expect, I don't know, but my guess is after everybody reports, I won't be surprised if trends are similar to what you've seen in previous quarters in terms of flow share overall for our business. I don't want to overdrive my headlights on that, I could be surprised by what somebody puts on the table. But from my market sensing and data, I didn't see a material shift in overall flow share this quarter versus previous quarters. And I feel really good about that, especially given the nature of some of the promotional activity that occurred during the fourth quarter of last year, that we chose not to chase, stayed very consistent in the first quarter of this year with our strategies and approach and others are throwing a lot of different things at it.

I don't see us out there with BOGOs and I don't see us out there with $1,000 incentive to switch that others are using in the market. We've been very stable in our approach. And I think the thing that I would point to in terms of the overall economics is, look at ARPUs, they remain very, very stable, as we told you they were going to remain despite all the gains that are coming in here.

And as we shared with you at Analyst Day, our cost per gross adds are getting better, not worse, because we're scaling that away now, where our fixed cost structure is obviously being spread across a larger number of subscribers on any given quarter. That's a good dynamic that's going on there. And our churn numbers continue to be very, very strong. With our customer life cycle is actually looking better than what they've historically looked. That means better value.

So as we've been sharing with you all along, we feel really comfortable that the economics of these customers that we're bringing in are no different right now than they were a quarter ago or 2 quarters ago or 3 quarters ago, and we'll take these customers all day long.

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

Mike, I would also just add, as a reminder, our fastest-growing plan is our Unlimited Elite, which is our top-tier plan. So that tells you the quality of what's happening in the overall wireless base.

Operator

Brett Feldman, Goldman Sachs.

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Brett Joseph Feldman - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

It's actually sort of a two-part question on inflation. The first part is we saw one of your competitors earlier this week announced they were going to be increasing or have increased minimum wage for their retail workforce and a big part of their customer-facing workforce. So I was hoping you can maybe comment on what you're seeing in terms of labor cost and labor supply and whether or what you've anticipated in your outlook for this year for inflationary cost pressures on the workforce.

And then second, John, I think you've made some comments recently that if you did see inflationary pressures persist, you might look at what your pricing was, and I think it was implied that you could take price up. I was hoping you can maybe just elaborate on how you think about your pricing model if we were to remain in the sustained inflationary environment? And what gives you confidence you can execute a degree of pricing leverage even as the market remains competitive?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Sure, Brett. So look, there is no question there's wage inflation in the environment. And frankly, it's 7% inflation. There is no question there's pressures across a broad segment of goods and services and we're not insulated from that. I don't think anybody in the industry is insulated from that, and it's not a good position for the overall economy to be in. And I think from a policy perspective, it needs to be addressed.

We were pretty deliberate when we did planning for '22, acknowledging that we expected we'd see some wage inflation. And we compared to previous years as we built the plan, we assumed upticks in wages as a result of that. And we did several revisions late in the planning cycle that I would say those amounts added something with the B into overall cost structure into our expectations around that.

We're in the middle of -- as you know, we have labor contracts. Labor contracts are extended and ultimately program out wage increases. And we have the luxury in some cases, given the way the current wage market or job market is set up, that people stick around and work here because we have great benefits for middle class folks and they often go beyond the wage that somebody gets paid. And as a result of that, we've been managing through the dynamics of the wage -- the labor market pretty well.

I will tell you, we're in the middle of some negotiations right now. Those negotiations are likely to land in a place that I think is consistent with how we built the plan this year, which was a stepped-up wage level from previous historic levels. I'm not happy about the fact that wages are rising as fast as they are. We're having to deal with it. It is going to drive a bit of an uptick in what I would call per individual wages. The good news is we're doing a lot of investment in other forms of mechanization and automation in our business. And some of that investment is helping us keep a lid on some of the wage-related inflation costs.

I would also point out that as you look at other parts of our business where people deploy long-lived infrastructure like fiber networks, wages are a portion of that deployment cost, not all of that deployment costs, and they are capitalized and they are taken over the life of a product that stays in service for many, many, many years.

So well, obviously, we'd like to pay less in wages. It's not the end of the world when we're seeing a little bit of an uptick. It's a small portion of the cost of deployment and we can ultimately recover that over the long life cycle of the product, especially if prices ultimately go up in the market.

Now to your question of pricing, I'm not going to give away or announce anything here that -- it's not appropriate to do that. But I'll go back to the comments I made a couple of weeks ago, which is broadly across the board in the economy right now, we are seeing inflationary pressures and the consumer is seeing that every place they go. It's my belief, if we do not see some moderation in this fairly quickly that I think every business in the United States is going to be dealing with the cost of inputs. And I don't see the wireless industry being immune from that nor any other industry being immune from that.

And as I shared earlier, there's a lot of different ways you can deal with price adjustments. There's a lot of different tactics and approaches you can use. But when we're looking at the customer base as satisfied as we are, when we look at a customer base with some of the value we've been putting back into the product and service over time, when we look at our current churn levels do we believe we're in a position if we're forced into

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a situation where we have to start maybe taking some price that we can do that and move it through? Our history would suggest that we know how to do that, and we can do that. And we'll be very smart and judicious as we have to apply it. But running this business and not sitting here and evaluating where we have options to move on pricing and be successful, I wouldn't be doing my job properly.

And I want to maybe go back to a comment I made in my opening remarks. If you look at what we've done in our fiber product this last quarter, we went to a simplified price structure. I want everybody to understand what this means. We are not out in the market right now selling on 12-month promotional pricing on broadband. We are selling the customer on a stable price to the duration of the relationship with us. In many cases, we're in the market at a minimum of $10 higher to the promotional price that cable or the other broadband competitors have in the market. And our volumes were still stellar and they're continuing to grow, and we're doing incredibly well in that market. And it's a reflection of the value of the product and the service that we're bringing in that we're able to do that. It's an example of us being able to smartly understand where there's value and where there's opportunity for us to work the overall value equation, including price, to be able to manage our business effectively and we'll continue to do that.

Operator

Phil Cusick, JPMorgan.

Philip A. Cusick - *JPMorgan Chase & Co, Research Division - MD and Senior Analyst*

A couple of follow-ups first. Let's dig into the postpaid phone adds a little more this quarter. Was there any impact from your own 3G shutdown on the reported adds? And what about the shutdown of T-Mobile CDMA network? Do you see any impact there in the first quarter or maybe second quarter?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Phil, the short answer is no on the first one. As you know, we don't -- when we count net adds, a migration of the 3G customer to another service plan isn't a net add. That's just the migration. And so there wouldn't be any impact to that. And as we've shared with you, we restated our base numbers. Those are out there for you to see. And so I think everything you can look at, including looking at ARPU characteristics after the restatement, you should look at it. And I would actually say, this is probably one of the best air interface transitions I've ever seen. When I think about the shutdown of the 2G network and now the shutdown of the 3G network on a proportional basis and the number of subscribers and what we're able to do here, I think the team executed incredibly well.

Relative to the flow share in the market today, I think we have seen over the last several quarters, Sprint is -- had an issue for T-Mobile to migrate and manage. And I know they're having to touch that base as they're shutting down the CDMA network and moving things through. And any time you do that, that can be disruptive to a customer base. And I think we've benefited in some flow share from Sprint customers who have been evaluating what they want to do and see AT&T as a good choice and a good value as they make that decision to whether or not they want to get a new handset and who they want to get it with. And there has been an element of that in the flow share in the market over, not just this last quarter, but several quarters as this has been going on. And there was an element of it in this quarter, but I don't think it was anything that was out of pattern from what we saw in previous quarters.

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

Yes. Phil, just as a reference point, 300,000 of the net adds this quarter were from FirstNet. Again, nothing to do with the 3G migrations.

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Philip A. Cusick - *JPMorgan Chase & Co, Research Division - MD and Senior Analyst*

Okay. And then second, if I can. You've got a guide out there for 3% plus service wireless service revenue growth. You did 4.8% this quarter. Is there -- I mean, there's comping issues. But anything in the numbers that we should think is going to be a headwind that would drive a significant deceleration?

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

We feel really good about how the business is performing. And we guided to 3% plus. As you've heard from John previously, this management team is in the realm of trying to put up guidance on a conservative end of a spectrum.

With that said, the one thing I would remind you, as you move through next quarter, we're going to have a full 3-month impact of the 3G migration, so that is going to hit ARPU some. But we feel really good about the overall pace of the business and how we're executing.

Operator

Simon Flannery, Morgan Stanley.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

I wonder if you could talk about C-band a little bit. I think you said that you would be ramping the deployment later this year. If you could just give us some updates on when we expect that to really start scaling and what you're seeing in the supply chain then. And there's been a lot written about fixed wireless recently, and we've seen some good momentum in that market. As you get the C-band up, what do you think in terms of out-of-market opportunities or even the opportunity to upgrade some of your DSL base that may not be getting fiber anytime soon or non-fiber based?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Simon, so the scaling on C-band is happening now, and it will continue. We're not -- as we told you, we're deploying midyear. That's when we have the right kind of equipment for our ONETOUCH work between the 2 different spectrum bands that we can touch the tower once and move through. We have capabilities to do prework on that. Obviously, there are things that we can deploy today to get ourselves ready, make sure that we're in the right position. And we can start spending on and be in a position to scale that, turn up pretty rapidly as we hit midyear.

So I'd say, as we told you, you're already seeing it move into some of the capital numbers in this quarter and it will continue to ramp as we move through the middle of the year. And then that positions us to do the rapid turnup in the second half of the year and hit the POP targets that we've communicated to you through the Analyst Day.

On supply chain, I'm conservative on this. I don't ever want to say we're in good hands, but here's the dynamic that I think is occurring. I actually think for the industry in aggregate globally, there are going to be some supply chain pressures, at least from what I know, where chip manufacturing is, it's going back into some of the key OEMs.

However, I think what you should keep in mind is that the North American market is an incredibly profitable market for providers of equipment on a global basis. If you were to start ranking it relative to other continents, it is the most profitable market of any continent out there. And so as a result of that, if you're into a situation where there's some degree of constraint, I think if you're an equipment manufacturer, you have the motivation to make sure that you supply your most profitable market first. And as a result of that, I don't want to say that we're out of the woods, but I think that we're likely to see a prioritization given the dynamics of this market that may put other parts of the globe a little bit lower down the list in terms of availability of equipment and services moving forward.

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So right now, I think we have a good handle on things. Our vendors are telling us they can meet our build expectations. We've done a lot of second order diligence on our equipment. We're not just taking their word for it. We look at sourcing on key components within if we can't do every element. And sometimes it's the smallest and silliest things that end up causing a problem.

We've looked at the harder things like at chip levels and feel that there's confidence in those estimates right now that they can bring them through. And so I'm not expecting that to be a problem. But as you know, the global supply chains are fragile right now and crazy things happen, whether it's neon gas coming out of the Ukraine or whatever, and we'll continue to work through that.

On the fixed wireless side, I think you hit the nail on the head. Look, we have hundreds of thousands of fixed wireless subscribers already. We've used it pretty aggressively in parts of the business segment where a particular business customer that we support finds it to be the right and best solution for how their particular business is set up. We continue to believe that there are going to be applications for fixed wireless deployment moving forward, and we think our network will be well suited to do that after we get through the mid-band deployment.

But to your point, it's going to be what I would call use specific. I don't intend to go into dense urban and metropolitan areas where I can build fiber infrastructure and offer broadband and try to use fixed wireless as the solution to serve broadband customers where we see estimates of traffic growing 5x over the next 5 years and performance requirements needing to get significantly better. And we watch our Fiber base, we watch our customers and we don't believe -- we watch our copper base of customers, and we don't believe a product that's doing sub 100 megabits is going to be a viable product in the market over the next couple of years based on how we're seeing consumers use the service and what they expect to do in some of these urban areas where there's broader and more dense environments, with more people in a living unit.

But there are clearly places in more rural areas where fixed wireless will be the best way to get the most amount of bandwidth out to a customer. And we believe we can play in those spaces, and there'll be some former ADSL locations where fixed wireless will be a substantial step-up in opportunity. And there's going to be places where the government comes in with subsidy in very less densely populated areas that fixed wireless is going to be the solution.

And sure, there may be some niche customers who can live on a very niche-oriented product for their particular use characteristic and find it interesting, but I don't believe that's the main part of the market. I think it's really hard to market niche broadband products, frankly, over time. And I think market performance of what we're able to do is we blanket an area with a robust fixed fiber broadband service are showing in the numbers that we're putting up in our performance in the market right now.

Operator

David Barden, Bank of America.

David William Barden - *BofA Securities, Research Division - MD*

A few higher-level questions about the new AT&T, John -- or maybe the old AT&T, depending on how you think about it. Is the new AT&T -- maybe -- I'm going to be greedy, I have three questions.

Number one, is the new AT&T a dividend yielder or a dividend grower?

The second question is, John, last -- I think at the Analyst Day, you previewed that your plan was -- after the separation, that you would kind of refresh AT&T's go-to-market plan. I was wondering if you could kind of maybe share an evolution of those thoughts or set some expectations around what we should see.

And then finally, Pascal, could you kind of describe and maybe share a little of the geography about how the go-forward financial relationship between AT&T and WarnerMedia Discovery will work, i.e. offering HBO Max for free in the wireless business and those sorts of things? That will be super helpful.

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John T. Stankey - *AT&T Inc. - CEO, President & Director*

Dave, let me give the front end. I'll try to do all 3 of them and Pascal can jump in and offer anything he wants.

I think we're a dividend competitor moving forward, meaning I want the dividend to remain at a competitive level relative to others out in the market, which means I'll pay attention to the yield of the dividend. As we've told you, as we move past 2023 and we start to think about what we do with discretionary capital, as we have the balance sheet where we want it to be, the Board is going to evaluate where the best returns come back into the business. And there's a lot of choices at that point. That could be what we choose to do on equity, could be choose on what we choose to do with dividend, it could be choose -- could be choices on we make -- what we make within the deployment on new business opportunities within the business for organic growth. We'll evaluate those in the complete portfolio where we stand and the relative competitiveness of the value proposition of the AT&T equity with others in the market and adjust accordingly.

And so to answer your question, we'll pay attention to the yield, but I don't necessarily intend to every quarter look at it and say my expectation is that I have to grow the dividend in any given quarter relative to not answering the question of how do we stand competitively in the market and whether or not we think we've got the right kind of mix of how we're investing our capital and deploying it within the business.

When you ask about refreshing the go-to-market plan, it could possibly be 2 things you're driving that. One could be comments I've made about what we're doing to refine the brand. If that's kind of the angle that you're going after, is that where your question is?

David William Barden - *BofA Securities, Research Division - MD*

I think more specifically, John, the market's seen your kind of -- and you highlight this as a positive, your very consistent go-to-market plan on customer retention, the new and existing customer, hence that upgrade plan. It's been pretty solid for almost 2 years now. And I think you hinted that there would be a change. And I think people were interested in hearing a little bit more about it.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Well, there'll be a change when it doesn't work, and it's working just fine. And I'm probably not going to tell you what the change is going to be when it doesn't work anymore because that would kind of be self-defeating. But it's working just fine.

And I would have guessed maybe last year that we might be hitting a point where we had to think about it differently, we're not. And I think that's great. We have thoughts on where our next path will go if we need to go down that path. But we're not at that point at this juncture. I love the momentum we're seeing. I think it was a great quarter. I like what we're seeing right now. And I like that we're watching others having to, in any given week or month, adjust their approach in the market while we continue to do exactly what we're doing.

And as we continue to have the opportunity to grow our footprint between the 2 services, it opens up even more opportunity for us to do things on a combined basis that we're seeing really good progress on. Admittedly, our new footprint is still relatively small. It will grow over time. But I'm really excited about what that means for us moving forward in the future.

And I think as I would stress, one of the things that's really important to understand is we're not getting our growth just through one set of go-to-market actions here. I know you're focused and you're thinking about what we're doing in the consumer space right now. But I want to stress, FirstNet has been really strong for us. What we're doing in the business customers that we have close relationships have been really strong for us. We're going to see us start to grow in some wholesale revenues later this year that we have not had in our mix up to this point in time.

So our growth portfolio is a balanced portfolio and it's not hinging on any one strategy. And I've been saying this all along, you need to understand that there's not any one thing we're doing, it's a variety of things that we're doing on distribution that are adding up to the sum total of this and feel good about that.

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Your last question on financial relationship with Warner Bros. Discovery. We expect there's going to continue to be a relationship with Warner Bros. Discovery going forward. I expect that, that relationship will still be important to both companies. But I don't expect over time that it's going to be ultimately exclusive. I think Warner Bros. Discovery will want flexibility to be able to do things with a variety of players in the market. I think I understand why they'd want to do that. I think there are things that AT&T can do to accommodate that and still have the right value proposition for our customers moving forward. But I still expect there'll be a strong trading relationship given what we've had in the market is a portion of the success that we've had in being able to keep and retain customers moving forward. And we'll fine-tune that a bit as we move forward and make sure it's right for both companies. But I don't expect that it will continue to be what I call a captive or exclusive arrangement.

Pascal, do you want to add anything?

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

The only point, Dave, I'd say on your first question on the dividend yield growth. We've said this, the way we're thinking about generating returns going forward, dividends are only one part of it. We're going to hold ourselves accountable to growing earnings at the stock price. And it's a mix of overall return to our shareholders. And that's what we are looking to optimize over time.

Operator

Doug Mitchelson, Credit Suisse.

Douglas David Mitchelson - *Crédit Suisse AG, Research Division - MD*

Sort of, John, following up on the media side with regards to media streaming piracy, is there a place for AT&T to gain any economics by helping streaming services reduce piracy given the breadth of your broadband footprint? I mean, Netflix losing $50 billion in market cap yesterday suggests there might be value to the streamers. And I would think it would be important to the value you're giving your customers of HBO or however that evolves. And to help size that, how much password sharing did you see with HBO in the U.S.?

And then if I could just sort of follow up, Pascal, I just wanted a clarification. The CapEx guide, $20 billion of cash spend plus paying down $4 billion of vendor financing in 2022, what should we anticipate for CapEx purchased on new vendor finance?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Doug, so if I go back -- I don't know, I don't play a story in here, but if I go back probably 3 years ago, there were several comments I made or observations I made about the SVOD business, one of which was that managing customer subscriptions was going to be an important element of the long-term sustainability of the business. And that was at a time when I think somewhere in the industry may be advocating that rampant password sharing was somehow a good thing for these products. And I had a little bit more jaded view of that. I think there were probably some articles that were written to criticize me for having a little bit more jaded view of that. But it drove a lot of the thought process at the front end of the HBO Max product where we were thoughtful about how we built the product.

We were thoughtful about making sure that we give customers enough flexibility, but we don't want to see rampant abuse. And so I'm not going to go into all the details, but there were a lot of things and features built in to the product that are consistent with the user agreement, that has terms and conditions of how they can and can't use it. And we've enforced it, and we've enforced them obviously in a way that I think has been customer-sensitive. You don't see anybody complaining massively about it. But I can tell you that we actively, in any given month, are looking at how particular users are using the product and have features and capabilities technically to limit what I would call rampant abuse.

And so I would tell you that I think that's the right way for the industry to be managed. And I think maybe some are going to adjust practices and approaches over time to try to get their arms around that, but I don't think it's the broadband providers' role in making that happen. I think it's the

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owner of the applications role in making that happen. And I don't necessarily expect that we'd be trying to work on a product or service to market back to other providers to say we can help you manage that. I think there are adequate tools available in software and then how you manage your application to be able to do that. And I can tell you from our own experience, we feel like we've done that reasonably effectively in the interest of the product.

I'll let Pascal go ahead and maybe pick up the second part of the question.

Pascal Desroches - *AT&T Inc. - Senior Executive VP & CFO*

Doug, here's the way I think about. We haven't provided guidance specifically on how much better financing commitments will enter into each year, but we provided overall cash payment guidance. And so we provided for '22 and '23, both years is $24 billion. So anything we do this year, we'd have to pay next year and that would be captured in that $24 billion guide.

And so while we haven't provided guidance, you should have a pretty good sense about where the overall trajectory should be.

Operator

Walter Piecyk, LightShed Partners.

Walter Paul Piecyk - *LightShed Partners, LLC - Partner & TMT Analyst*

Pascal, I was hoping to unpack some of the fiber comments you made earlier. You talked about rising subscriber growth over the course of the year. And then, John, you talked about basically higher ARPUs or basically charging $10 higher than cable. I guess first, when you look at the 289,000 that you did this quarter, what was the mix of conversions from your own customers versus taking it from other competitors that are out there?

And then secondly, in terms of fiber, if you think about higher pricing, are you still seeing that kind of the penetration rate after year 1 and year 2 that we've historically seen when other companies have built out fiber? Or is the higher pricing changing kind of the penetration rate that you think you can achieve for a second, third year of rolling out these new services?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Yes. Walt, let me see if I can answer your question, and Pascal can jump in if he wants to. First of all, we don't disclose the mix. But what I would say to you is what you should understand is we do give you some information that you should be able to understand that we're getting a healthy growth of new subscribers to AT&T. You know, I think our aggregate share numbers in broadband in the market today and you know where those stand. We shared with you that our pen rates after we're in the market about 3 years has roughly an equal split of market share which is a substantial increase to where our aggregate market share in our broadband business previously stood. You can't, in a 3-year period of time of fiber growth to get to equivalent market share in an area, do that without taking customers from the other side of the house. It's mathematically impossible to do that.

And so I think the way you think about it, if I were in your shoes, being an analyst, and you look at cash flows over a 3-year period and you look at footprint expansion and you see that market shift, you should conclude over time that we're actually picking up, as I've described it, share points in a way that I've never seen a product move in my career.

Now admittedly, we put a lot of money into this infrastructure. And we should expect to see that kind of share point move, and we're getting that. So we are winning our share of new customers as a result of this.

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And we report to you as well our aggregate revenues, and we report to you our growth and decline in our fiber and our copper base. And I think it's pretty easy for you to see the motion of what's happening in the copper basis to how much of it is likely moving to fiber and how much of it isn't.

And I feel really good about how we're competitively performing. I see nothing in our performance that suggests we should be tamping down ultimate pen rates because of our approach. Quite the opposite, as we shared with you, our pen rates are accelerating, they're not declining. If you look at where we were several years ago. And a lot of our new builds right now, we're achieving year 2 pen rates in year 1. And there's a lot of reasons behind that, not just one. The great product is the foundation of it.

The part of it is how we're building right now, we're much less Swiss cheese, which allows us to be a lot more effective in our marketing. And we've developed much better tactics as we move into a neighborhood to be able to get early adopters to move in at a much higher rate and pace. And that has a huge impact on the economics of the business case.

If we sustain that moving forward, I'm going to frankly be relooking kind of the overall economics of the Fiber business case because one of the big variables on leverage in the business case, is if you can accelerate your penetration by a year, it dramatically improves kind of the return characteristics.

So I'm really proud of what the team has done in that regard. And we have no expectation by the time we get to year 3 that, that's going to suggest that we shouldn't expect our split of the market as a result of that.

Remember, we're not charging more to the customer. We're giving the customer a better experience. We're getting rid of promotional pricing, it is a pain point for customers. They hate it. They hate the 12-month mark. And when they're using another service, that 12-month mark means their price is going up $15 or $20, and that's just a really bad thing for a customer.

And so now we put out a very simple, straightforward constant price, where the customer isn't going to see that step up for 12 months. They know what the equipment pricing is on the front end. They're getting the square deal. They're getting a great product. And they're happiest clams and it shows in the data.

Walter Paul Piecyk - *LightShed Partners, LLC - Partner & TMT Analyst*

And apparently, I guess the high split investments, if you can call it that by cable, is not really helping to fight those shifts. Can I just switch to wireless, John? You mentioned about wholesale as another component of growth. And then I looked at the wholesale revenue this quarter, and it didn't move much from Q1. I guess that just implies that you're in the very early stages of the shift of that DISH wholesale traffic to your network. How do we expect that to ramp? Is it linear? Is it -- I know you've already started to connect to DISH. How should that play out over the course of 2022 and 2023?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

That's an accurate assumption, Walt. It has to do with the ramp directly from DISH. And I think the way you should think about this, it's public information, that I think DISH got a little bit of a reprieve from T-Mobile on some of the legacy network availability and some help on that slowed down the front end a little bit. And I think you're aware of where DISH is in their deployment and debugging their network so that it actually can function and work properly.

I think they recently announced a milestone as to what they're doing around that. Those 2 things are the drivers of when that transition occurs, a combination of when those customers need to move off of another network as well as, as DISH starts to move people on to their network, new customers coming in, those all play in the wholesale arrangement as that volume starts to ramp. So I think a surrogate for understanding that trend line, we'll be watching the loading of new customers on to DISH's new network capabilities.

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Amir Rozwadowski - *AT&T Inc. - Senior VP of Finance & IR*

Thanks very much, Walt. And with that, I'll turn it over to John for some final comments.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Just really briefly to all of you. First of all, thanks for joining us today. And I really want to extend my thanks and appreciation to all of you on the call. I know it's been going on internally at AT&T in terms of the number of filings, schedules we've had to develop, the information we've had to put out over the course of the last month or so. And I know that, that puts a lot of work on all of you to kind of parse through that, get through this transition that we've been working through as a business. I want to extend my appreciation for your patience in that regard. And what I can promise is it should settle down here a little bit going forward. And I'm as excited about that as I'm sure you are. So thanks very much for being with us today, and we'll talk to you again in 90 days.

Operator

Ladies and gentlemen, that does conclude our conference call for today. On behalf of today's panel, we'd like to thank you for your participation, and thank you for using AT&T. Have a wonderful day. You may now disconnect.

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