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CTL - Q3 2012 CenturyLink, Inc. Earnings Conference Call

EVENT DATE/TIME: NOVEMBER 07, 2012 / 10:00PM GMT

OVERVIEW:

CTL reported 3Q12 consolidated operating revenues of $4.57b and adjusted diluted EPS of $0.66. Expects 4Q12 total operating revenues to be $4.56-4.61b and adjusted EPS to be $0.64-0.69.

CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to CenturyLink's third quarter 2012 earnings conference call. At this time, all participants are in a listen only mode. Later we'll conduct a question and answer session and instructions will be given at that time.

(Operator Instructions)

As a reminder, this conference call is being recorded. I'd now like to turn the conference over to Mr. Tony Davis, Vice President of Investor Relations. Mr. Davis, you may begin.

Tony Davis - *CenturyLink, Inc. - VP, IR*

Thank you, [Sayeed]. Good afternoon, everyone, and welcome to our call today to discuss CenturyLink's third quarter 2012 results released earlier this afternoon. The slide presentation we will be reviewing during the prepared remarks portion of today's call is available in the Investor Relations section of our corporate website at www.ir.centurylink.com. At the conclusion of our prepared remarks today, we will open the call for Q&A.

On Slide 2 you will find our Safe Harbor language. We will be making certain forward-looking statements today, particularly as they pertain to guidance for fourth quarter and full year 2012, some outlooks for 2013, the integration of Qwest and Savvis and other outlooks in our business. We ask that you review our disclosure found on this slide, as well as in our press release and in our SEC filings, which describe factors that could cause our actual results to differ materially from those projected by us in our forward-looking statements.

We ask that you also note that our earnings release issued earlier this afternoon and the slide presentation and remarks made during this call contain certain non-GAAP financial measures. Reconciliation between the non-GAAP financial measures and the GAAP financial measures are available in our earnings release and on our website at www.CenturyLink.com.

Now turning to Slide 3, your host for today's call is Glen Post, Chief Executive Officer and President of CenturyLink. Joining Glen will be Stewart Ewing, CenturyLink's Chief Financial Officer, and also available during the question and answer period of today's call will be Karen Puckett, CenturyLink's Chief Operating Officer, who leads our Region market segment; Bill Cheek, President of our Wholesale market segment; and Jim Ousley, Chief Executive Officer of Savvis and President of our Enterprise market segment.

Our call today will be available for telephone replay through November 14, 2012 and accessible by Webcast through November 28, 2012. Anyone listening to a taped or Webcast replay or reading a written transcript of this call should note that all information presented is current only as of November 7, 2012 and should be considered valid only as of this date regardless of the date heard or viewed. As you move to Slide 4, I'll now turn the call over to your host today, Glen Post. Glen?

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Thank you, Tony. Good afternoon, everyone. Thank you for joining us today. First, I want to express my sympathies to those affected by the storm along the East Coast last week. Located in Louisiana, we of course are all too aware of the devastation hurricanes and tropical storms can create and our thoughts are with all of those affected.

CenturyLink did experience some operational destructions as a result of the storm, however, we are pleased that all of our East Coast data centers remained fully functioning during the storm so we could continue to serve our customers through this difficult time. Early indications are that we experienced about $5 million to $6 million of operating and capital expense as a result of the storm, so we were relatively displaced less than I know many were. Also want to thank our employees for their hard work and dedication to insuring the best possible service for our customers during this difficult time.

Now, I'll turn to discuss CenturyLink's third quarter 2012 results and guidance for fourth quarter and full year 2012 as we provide other updates -- as well as provide other updates about our business. During the third quarter, CenturyLink achieved solid results and we continued to make progress on a number of fronts. We remain on track to meet our synergy targets for the Qwest and Savvis transactions and continue to make progress with the integration of these two acquisitions. We continue to see solid growth in our enterprise markets and regional markets business segment with continued demand for integrated network, colocation managed hosting and cloud services.

We also continue to invest in additional data center capacity to drive further growth from these services in the months ahead. With our fiber to the tower initiative, we continue to make excellent progress in completing fiber builds and enabling high bandwidth ethernet data services to support the growing demand for wireless data back haul capacity. We are experiencing some near term revenue pressure resulting from the transition from additional copper based data service to fiber and ethernet connectivity, however, we are confident our investment in fiber to the tower will generate good returns and provide solid revenue growth over the lives of these agreements.

We are pleased to announce a soft launch of our Prism TV service into the Phoenix market. By the end of this year, this will be our first legacy Qwest market that will offer the service. We anticipate a commercial launch in the first half of 2013 and additionally, we expect to enter a second legacy Qwest market in mid 2013. Finally, in October, we launched our click to buy and managed hosting and cloud service platform for businesses of all sizes, and we'll talk a little more about that later on.

Now turning to Slide 5, we made continued progress in improving our top line revenue trend. In the third quarter we generated revenue of $4.57 billion, a 1.3% year-over-year decline, comparing favorably to the 4.6 decline for pro forma third quarter 2011. Excluding data integration revenues, which widely fluctuate from quarter-to-quarter, the annual revenue decline in third quarter was 1.4%. For full year 2012, we remain on track to reduce our annual revenue rate of decline of 1.5% to 2% range.

The integration of Qwest and Savvis remains on track and we will continue to leverage these assets to strengthen our competitive position throughout operating areas. As of the end of the third quarter, we achieved an annual synergy run rate of $450 million related to Qwest integration. We now expect the end of 2012 with an annual synergy run rate of $480 million related to Qwest, up from $465 million previously anticipated as operating expense savings are being achieved earlier than expected.

Also in the third quarter, we achieved strong improvement in access line loss and continued subscriber growth in broadband and Prism TV services. And during the quarter we generated strong strategic data growth from business customers in both regional markets and enterprise market segments, so in the third quarter business customers drive more than 60% of our total operating revenues. As we move forward, we remain focused on making disciplined investments in our strategic initiatives to drive growth in top line revenue and over time EBITDA and free cash flow improvement.

Turning now to Slide 6. I'll briefly discuss our preliminary outlook for 2013. We expect to provide full guidance for 2013 in mid February when we release our fourth quarter 2012 results. That said, we believe the investments made in our key strategic initiatives have been successful in driving additional strategic revenue, growth in 2012 and we expect to continue investing operating capital dollars in these key areas. We anticipate further improvement in the top line revenue trend in 2013 with a year-over-year rate of decline in the range of 0.5% to 1.5% compared with full year 2012. We now believe we will reach revenue stabilization in 2014.

As I mentioned, we expect to continue to invest in the key strategic initiatives in 2013. These strategic investments and the continuing shift in the Company's revenue mix, along with the lower level of incremental annual synergies in 2013, are anticipated to negatively impact operating and free cash flows for 2013 as compared with 2012. Currently, due to the high level of synergies achieved in 2012 and late 2011, we anticipate approximately $150 million to $200 million lower incremental synergies in 2013 compared to the level achieved in 2012.

On Slide 7, the chart illustrates the steady improvement we have made in operating revenues and strengthening strategic services and lower access line losses have helped reduce the quarterly rate of decline. For the third quarter, we achieved 1.3% rate of revenue decline and we remain on track for a 1.5% to 2% annual revenue decline for full year 2012, a significant improvement over the 3.8% pro forma revenue decline in 2011.

Now turning to Slide 8. The third quarter revenue declined 0.9% from second quarter 2012 as growth in strategic revenue was offset by lower legacy revenues due to access line losses and lower minutes of use. Our strategic revenue growth was driven by strength in high speed internet and high bandwidth business data services. Additionally, during the quarter, we experienced a small net decrease in legacy revenues due to the implementation of the calf order in which the rate step down was largely offset by access recovery charges implemented beginning July 1, 2012.

Third quarter 2012 revenue declined 1.3% from pro forma third quarter 2011. Again, growth in strategic revenue was offset by lower legacy revenues due to access line losses and lower minutes of use. MPLS and ethernet services, high speed internet and managed hosting products, and Prism revenue continued to grow.

Now moving to Slide 9, I will provide a few highlights regarding our strategic initiatives. As we have outlined over the past several quarters, we are focused on continued strategic investment in broadband expansion enhancement, Prism TV, fiber to the tower and managed hosting cloud computing services. Our third quarter results reflect the solid progress we are making in these key initiatives.

Starting with broadband expansion enhancement, we continue to make significant investments in this area and during the third quarter we added over 44,000 high speed internet customers. This represents a solid rebound in new subscribers from the seasonally weak second quarter of '12. With these new subscribers, we now have more than 5.8 million broadband customers.

Our customer retention efforts and the growth benefits of bundling broadband with other products and services attributed to the continued decline of the rate of access line loss, which improved from 7.1% in the third quarter 2011 to 5.8% in third quarter 2012. We also expanded our fiber to the node infrastructure to more than 310,000 new living units during the quarter. We now pass over 6.8 million living units with fiber to the node and we expect to pass approximately 7 million living units by end of this year.

As a result of our network investment enhancements, broadband speed availability has continued to improve. Over 70% of our enabled access line receives speed of six megabits or higher. More than 57% of enabled lines receive 10 megabits or higher and 29% have speeds of 20 megabits or higher. Additionally, during the quarter, we continue to expand our ethernet over copper footprint which has increased nearly 70% year-to-date. We expect to continue to make investments in our network to enhance speed capabilities and to deliver competitive broadband product and services across our markets.

Turning to Slide 10. Our Prism TV service represents a very compelling entertainment alternative to cable. In the eight markets where it is currently available, it continues to perform well. We added over 10,000 Prism TV subscribers during the third quarter, ending the period with more than 104,000 subscribers. Of the new subscribers we've added over the past 12 months, approximately 55% are new customers to CenturyLink. We now have a penetration rate of over 10% across state markets in which the service is available. In addition, we continue to enhance our IP TV experience for introducing new functionality and application.

Prism TV continues to have a positive impact on churn and line loss trends. We experienced greater than 90% broadband pull through rate with our Prism TV sales to new customers. We continue to expand our Prism TV enabled footprint and expect to drive additional subscriber growth in the months ahead. As I mentioned, we are on track, by the end of the year, to soft launch Prism TV in Phoenix which will be our first legacy Qwest market to receive the service. The Phoenix market will be commercially launched in the first half of 2013 and we expect our second legacy Qwest market in mid 2013.

Continuing onto Slide 11. A third key strategic initiative is investing in fiber builds to as many towers in our service area as economically feasible. During the third quarter, we completed approximately 1,335 fiber builds for a total of over 3,300 year-to-date, and we currently anticipate completing 4,000 to 4,500 builds in 2012. This initiative supports the anticipated long term growth and data transport, much of which is driven by wireless data traffic. And also expands our addressable customer footprint by enabling fiber access points to other strategic locations where viable along these routes. We believe our fiber to the tower program helped solidify our wholesale access revenue for the long term and assist in the stabilization of our revenue trends.

As we've discussed with you before, we are experiencing some revenue compression as our wireless wholesale customers transition into copper based DS1 facilities to fiber based ethernet services; however, we anticipate that wireless bandwidth growth will result in expansion of ethernet consumption, reversing the revenue current revenue compression by late 2013.

Moving on to Slide 12. We continue to invest in managed hosting and cloud services to increase our data center capacity, as well as expand our product portfolio to meet customer needs and expand our market opportunity. During the quarter we opened a data center in Singapore and expanded capacity in the data center in New York -- in the New York and New Jersey market. We ended the quarter with 53 data centers in North America, Europe and Asia with total sellable floor space of approximately 1.4 million square feet as we continue to expand the global reach of our managed hosting services.

While we continue to see strong demand in the hosting market, third quarter bookings came in lighter than expected as we believe a handful of potential large deals pushed to the fourth quarter. We are working hard to improve our prospect close ratio. We expect stronger bookings in the fourth quarter and we are focused on opportunities for growth from new prospects and our current client base.

Savvis was recently recognized as a leader in Gartner's magic quadrant for cloud infrastructure as a service. We also anticipate increasing hosting and cloud expansion opportunities as we further train enable enterprise markets, region markets and wholesale market sales channels. We expect to see incremental revenue for these channels in 2013. In the months ahead, we will focus on aligning hosting product offerings and solutions bundles with existing region markets and enterprise markets network client needs.

In October we announced the beta launch of savvisdirect, our simplified approach to cloud computing for businesses of all sizes. And finally, on October 15, we closed the acquisition of certain assets of Ciber's global IT Outsourcing, or ITO, business. In addition, these assets will complement Savvis' existing ITO assets by expanding our capabilities for application management services and help desk support.

And now, on Slide 13, in summary I am pleased with the third quarter results. We continue to improve our top line revenue trend. Our employees did a good job of containing cost and we generated solid cash flows during the quarter. We reduced our access line losses by 22% compared to the pro forma third quarter 2011 and we achieved high speed internet subscriber growth, as well as solid increase of Prism customers.

Also the focus investments we have made in our key strategic initiatives have positively contributed to strategic revenue growth and continue to improve our top line revenue trend. We believe the soft launch of Prism TV into the Phoenix market towards the end of this year will position us well to grow video subscribers in 2013 and beyond. And lastly, we feel good about leveraging the acquisition of Savvis to generate organic growth. Our new savvisdirect product offers the opportunity to gain market share in the fast growing cloud space across our entire range of customers.

With this, I'll turn this call over to Stewart for an in depth look at our financial results. Stewart?

Stewart Ewing - *CenturyLink, Inc. - CFO*

Thank you, Glen. I'll spend the next few minutes reviewing the financial highlights from the third quarter and then conclude my remarks from an overview of fourth quarter and full year 2012 guidance we included in our earnings release issued earlier this afternoon.

Turning to Slide 15, first in order to provide more relevant comparisons, I'll be reviewing the financial results on a pro forma basis as if Savvis were included in the results for all periods. I will also be reviewing the results excluding special items as outlined in the earnings release and associated financial schedules. With that, let's turn to our results for the third quarter.

As you can see, we generated strong operating revenues and solid cash flows. Operating revenues were $4.57 billion on a consolidated basis, which was in line with our guidance for the quarter and represented 1.3% decline from pro forma third quarter 2011 operating revenues. This also represents a solid improvement from the 4.6% annual decline in the year ago period.

Strategic revenue in the quarter increased to 46% of total revenue from 43% in the pro forma third quarter a year ago, due to growth in strategic products such as high speed internet, high bandwidth data services, Prism TV and managed hosting services. Adjusted diluted earnings per share for the second quarter was $0.66, exceeding the mid point of our guidance by about $0.095. The difference from our expectations were driven primarily by lower depreciation and amortization, lower than expected seasonal plant maintenance, lower property taxes, and a slightly better than expected impact from implementation of the calf order, along with higher synergy achievement.

As we've discussed on prior earnings calls, adjusted diluted EPS excludes special items and certain non-cash purchase accounting adjustments. Total cash operating expenses decreased from pro forma third quarter 2011 to third quarter 2012 with synergy achievement, lower marketing and advertising cost and other cost reductions, partially offset by continued investments in our key initiatives, as well as other costs related to revenue growth. We generated solid operating cash flow of approximately $1.9 billion for third quarter and achieved an operating cash flow margin of 41.5%.

Additionally, we generated $905 million of free cash flow during the quarter which is defined as operating cash flow less cash paid for taxes, interest, and capital expenditures and additional adjustments to other income. Our strong cash flows continue to provide us with the financial strength and flexibility to meet our business objectives and drive long term shareholder value.

Now turning to Slide 16, I'll begin my operating segments discussion today with our regional market segment. Regional markets generated $2.47 billion in operating revenues, which represents a decrease of 2.1% over pro forma third quarter a year ago. Strategic revenues grew to $912 million in the quarter, up 7.9% pro forma year-over-year. Excluding the impact of private line revenue, strategic services grew approximately 9%.

Legacy services revenues for the segment declined $108 million, or 6.8% from pro forma third quarter 2011 due primarily to a continuing decline in revenues related to access lines, partially mitigated by implementation of the access recovery charge. Our expense reductions for the quarter compared with the previous year were mainly driven by lower employee related expenses, which were partially offset by higher Prism TV expenses.

Moving to Slide 17, our wholesale market segment generated $908 million in operating revenues, a decline of 7.6% from pro forma third quarter 2011. Strategic revenues for wholesale markets declined 1% to $568 million from pro forma third quarter 2011, primarily driven by the rate compression in special access services as customers transition to ethernet-based services.

Wholesale markets legacy revenues declined by 17% to $340 million, reflecting the continued decline in access and long distance revenues and the implementation of the calf order rate step down. Operating expenses for the quarter were $273 million, 11% below the pro forma period from the prior year driven by lower access expense and allocated cost.

Moving to Slide 18, enterprise markets network segment generated $658 million in operating revenues during the third quarter, which represented an increase of 5.6% from pro forma third quarter 2011. The third quarter represented the third consecutive quarter of sequential growth in recurring revenues from a network services segment.

Third quarter strategic revenues for enterprise markets network increased by $23 million, or 7.2%, to $341 million from pro forma third quarter a year ago, driven primarily by strength in high bandwidth services such as MPLS, ethernet and DWDM. Excluding private line services, strategic revenue grew more than 13% from the pro forma year ago period.

Legacy revenue declined by $3 million from pro forma third quarter 2011 due primarily to declines in logo and legacy wide area network services, while data integration revenues increased $15 million, or 17%, due to higher equipment sales and professional services revenue from government and enterprise customers. Our total segment expenses declined $13 million from the same period a year ago.

Now turning to Slide 19 and enterprise markets data hosting segment, which is primarily the Savvis legacy operation, legacy Savvis operations. This segment generated $280 million in operating revenues, representing an increase of 8.1% from pro forma third quarter 2011 revenues of $259 million. This growth came primarily from year-over-year increases of 7.6% in colocation revenues and 9.2% in managed hosting and cloud services revenues, and a 7.1% increase in network services revenues.

Strong first half 2012 bookings in hosting services helped drive this revenue growth in the third quarter. While churn was in line with expectation for third quarter, we do anticipate a slight increase in fourth quarter churn due to bankruptcy related issues. Enterprise markets data hosting and operating expenses were $219 million in third quarter, compared to $193 million in the pro forma third quarter a year ago. This increase of 13.5% is driven by added headcount to support revenue growth, including our Savvis direct operation.

Slide 20 addresses our fourth quarter and full year 2012 guidance, which includes the acquisition of Ciber. The Company expects fourth quarter 2012 operating revenues and cash flow to increase compared to third quarter 2012 due to anticipated continued growth in strategic revenues and lower outside plant, maintenance and utility cost. Additionally, we expect depreciation and amortization to be $20 million to $30 million higher for fourth quarter 2012 than it was for the third quarter due to higher balances of plant and service and a one-time adjustment to software amortization that occurred in the third quarter.

For the fourth quarter 2012, CenturyLink projects total operating revenues of $4.56 billion to $4.61 billion and operating cash flow between $1.9 billion and $1.94 billion, and adjusted EPS is expected $0.64 to $0.69. To reflect the year-to-date performance in fourth quarter expectations, we've also updated our previously given full year 2012 guidance and this is provided in our press release.

Turning to Slide 21, in summary, we are generating solid strategic revenue growth. We achieved good cost containment during the quarter and achieving Qwest synergies earlier than originally anticipated. Finally, we continue to believe a solid balance sheet is important to our financial flexibility and feel confident about our cash flow generating ability, which allows CenturyLink to return meaningful cash to our shareholders.

That concludes our prepared remarks for today so at this time, I'll ask the Operator to provide instructions for the Q&A portion of the call.

QUESTIONS AND ANSWERS

Operator

Thank you.

(Operator Instructions)

David Barden, Merrill Lynch.

David Barden - *BofA Merrill Lynch - Analyst*

Hi, guys. Thanks for taking the questions. Congrats on the quarter. I wanted to ask maybe a couple more strategic questions if I could, Glen.

Obviously in the last couple months there's been some erroneous reports that CenturyLink was trying to buy TW Telecom and your stock took it on the chin to the tune of a couple dollars as a result of some of those reports, which I think were later actually retracted. But I was wondering if you could kind of set the table a little bit, based on where you are in the integration and what your appetites are. When we see these kinds of reports, how should we be reacting to them?

The second question is obviously the free cash flows are coming in ahead of expectations, the guidance is going up. I know that you guys have talked about stock buybacks as a priority for cash, but could you revisit your thinking about how you consider the dividend -- being a dividend paying company versus maybe being a dividend growth company looking into maybe next year, thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, David. First of all, regarding the acquisition rumors and where we are with leads to organic growth, we are really focused on the investing in our four primary growth initiatives that we've talked about, the broadband expansion, enhancement fiber to the node, fiber to the tower initiative, the managed hosting cloud service and our Prism TV services. The integration of Qwest and Savvis is going well, but there's still a lot to do and we're achieving, expect to hit our objectives in terms of synergies but there's a lot of work to do. These are large acquisitions and do them right it's going to take more time, as we've stated previously, so there's a lot of focus there.

We don't feel the need to acquire in order to drive growth. Our four initiatives have strong potential for driving growth and our side is good. We don't need additional synergies necessarily that additional acquisitions would bring. We'll continue to evaluate investment opportunities that arise, both organic and inorganic, but we don't feel compelled to make an acquisition. We'll be focused on ways to have value for shareholders but there's no -- we don't feel compelled or we aren't out beating the bushes looking for an acquisition, so I'll leave it at that. That's pretty much how we feel about our position here.

As far as the increase in the dividend or stock buybacks, that's obviously a question that we consider continually with our Board. We'll continue to evaluate the best ways to create value for shareholders and obviously how to utilize our cash is a key component of that process. We'll consider opportunities to reduce debt and the value of debt reduction. We'll look at the benefits or increasing the dividend or buying back stock, what that can mean to value for shareholders and we'll continue to consider investment opportunities for organic and inorganic that can drive value for shareholders. These are obviously important and complex considerations and we'll continue our very disciplined approach to these types of investment decisions and again, with the objective of really maximizing long term shareholder value.

David Barden - *BofA Merrill Lynch - Analyst*

Glen, if I could just follow-up real quick, obviously we saw about a 2.3% increase in the dividend from AT&T today and I think investors tend to look at dividend growth companies as being a higher value proposition than simply companies that pay out a dividend. Do you agree with that statement and do you think that CenturyLink has it within its financial wherewithal to maybe support that kind of limited amount of dividend growth, but growth nevertheless?

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

I'm sorry, do I support what, agree with what statement?

David Barden - *BofA Merrill Lynch - Analyst*

The idea that there's a higher value to companies that grow their dividend, even if it's only a small amount, as opposed to just simply keeping a dividend steady through time.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Well, yes, I have seen some studies that indicate that companies grow the dividend to drive value, good value for shareholders. So yes, I have seen some of that and don't disagree with the studies. It's something that we consider as we talk about our use of free cash flow, basically every quarter and certainly every year we talk in detail about what's the best way for us to drive long term shareholder value and we realize that growing dividends is one way that companies have done that over time so it is part of our consideration.

David Barden - *BofA Merrill Lynch - Analyst*

Thanks, guys.

Operator

Thank you. Batya Levi, UBS.

Batya Levi - *UBS - Analyst*

Great, thanks. A question on revenue trends. Revenue decline has been consistently improving every quarter for a while now. You mentioned in Q4 you are expecting some churn from Savvis. Can you clarify do you still expect Savvis revenue growth to accelerate to double digits in Q4?

And your Q4 guidance suggests that revenue decline will stay at flattish. Is that a function of this churn that we talked about or what else is in there? And then maybe just a clarification for your longer term guidance for revenue stabilization in '14. Do you expect some stabilization at the end of '13 and flat revenues in '14 or will we see some declining trends in '14? Thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

This is Glen. I'll talk on Savvis and ask Jim Ousley to also comment. The churn absolutely impacted us, a couple companies that were in bankruptcy impacted us during the quarter. Also, just the longer decision-making process that we're seeing with some enterprise customers, we think that impacted the -- affected bookings for the third quarter.

That will, of course, roll into the fourth quarter for us as far as our revenue growth into early next year; however, we feel very good about the demand that's out there and the potential, the interest from customers, the potential funnel that we have out there, so we still feel very good about the growth here. It's just a matter of getting some of these deals closed and secondly, just the churn that we've experienced in the latter part of this year. Jim?

Jim Ousley - *CenturyLink, Inc. - CEO, Savvis, President Enterprise Market*

Yes, this is Jim Ousley and I would just support what Glen said. We would expect fourth quarter posting revenue will be double digit kinds of growth levels, so we still stand by that what we've been saying. And the effects of two major churn events in the fourth quarter, which were bankruptcies, will flatten it a little more but it will still be double digits.

And we see no downturn in demand. As we and some of our competitors have stated before, the only issue we're seeing is elongation of decision-making for -- Savvis large enterprise customers are clearly taking longer. They aren't buying, they are just taking longer to make decisions. Hopefully that will ease with the election and all the other issues in the macroeconomic issue, but we're still seeing strong demand.

Batya Levi - *UBS - Analyst*

Maybe the question about longer term revenue decline, would you expect some stabilization in 2013?

Stewart Ewing - *CenturyLink, Inc. - CFO*

Yes, with respect to the statement that Glen made in the release in revenue stabilization in '14, we really hopefully will have revenues such that in 2014, it will be equivalent to 2013 revenue on a full year basis.

Batya Levi - *UBS - Analyst*

Thanks.

Operator

Thank you. Simon Flannery, Morgan Stanley.

Simon Flannery - *Morgan Stanley - Analyst*

Thank you very much. Good afternoon. Glen, can you just update us on the labor negotiations, where are we at this point? Any hope of a near term resolution? We've obviously seen Verizon strike a deal, presumably there's a little bit of a template there. And Verizon and AT&T have made some differing proposals on their pension. Have you got any interest in pursuing either of those sort of approaches?

And maybe if you can just talk a little bit about CapEx levels for '13, we obviously saw AT&T increase their capital spending. Are you likely to hold capital budgets pretty similar to 2012, what's implied in your initial guidance? Thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, Simon. First of all, on the pension of AT&T and Verizon has done the stabilization there, we're evaluating that, made no decisions there. Stewart may want to talk a little bit more about that in a moment, but it's an area we are looking at and evaluating.

As far as labor negotiations, the current contracts with the legacy Qwest unions were set to file on October 6. We and the unions agreed to extend the current agreements day-to-day as we continue the negotiations. Our primary focus on these discussions, of course, is to more closely align our cost structure with competitive marketplace, the revenue streams that we are seeing and operating in, while continuing to provide our employees a competitive wages and benefits so that's our goal here.

We have a number of issues to work through, but we believe we're making progress with these negotiations. We're not targeting a specific date that we want to complete this agreement by, but we are hopeful that the process can be resolved without too much further delay. We believe we are, again, making progress in these discussions.

The final question on CapEx, we expect CapEx to be in the range it is in 2012. It can be slightly higher as we do some expansion of the data center expansion and along with the Prism TV investments, and pursuing our strategic initiatives. We are going to take a very disciplined approach to those investments and where you'll see any increase will be where we expect revenue gains in the relative near future from those investments.

Simon Flannery - *Morgan Stanley - Analyst*

Thank you.

Stewart Ewing - *CenturyLink, Inc. - CFO*

Simon, just a couple quick comments. On the negotiations, Qwest, either the last time they renegotiated the contract or the time before last, they moved new bargaining unit employees that were hired subsequent to that day over to a cash balance plan, so there's no longer really a defined benefit plan for the new Qwest employees. And again, secondly, we are reviewing what others have done with respect to the plans and we'll decide at some point if we want to try to execute a transaction similar to what has been done.

Simon Flannery - *Morgan Stanley - Analyst*

Great, thank you.

Operator

Thank you. Frank Louthan, Raymond James.

Frank Louthan - *Raymond James & Associates - Analyst*

Hi, thank you. Just quickly on the Savvis side, I understand you're working on some more customer facing cloud products for SMB customers and a little simpler interface and so forth. Where does that stand? How successful is that?

And then just on a bigger picture, we've been consistently hitting and exceeding the guidance targets on top line and cash flow and so forth, which is refreshing. What would it take for you to get to positive top line growth in 2013? You're guiding to maybe negative 0.5%, that's getting pretty close. Is that a possibility and what would have to change? Is that more of a macro issue? Thank you.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, Frank, first of all savvisdirect, we've got our soft launch in October and it's going well thus far. We have a lot of high hopes, anticipation for the success of this product. It's one click, easy to use, web-based solution and we're seeing lots of interest from customers. Of course, we'll start in the small and mid size businesses where we see the most interest but also there will be the large enterprise business that will eventually use more of the public cloud in this point and click type that we're providing there. So it is a significant rollout for us and we believe it's going to have a major impact in the years ahead on the growth.

As far as top line growth, what would have to take place, we just have to see some of these new initiatives take off a little faster than we anticipate. We're going to be conservative with those but if they were to take off faster, if the rollouts were more quickly done and the penetration rates exceeded what we're anticipating, that could change -- we would see some increases. That's what it would really require.

Frank Louthan - *Raymond James & Associates - Analyst*

Okay, great. Well good luck with that.

Operator

Thank you. Mike McCormack, Nomura Securities.

Mike McCormack - *Nomura Securities Intl - Analyst*

Hi, guys, thanks. Just thinking about the sort of 2013 look that you've given us and I know, Glen, you've mentioned obviously the Qwest synergy opportunity won't be there obviously in 13 but if it weren't for the Qwest headwind, would you have expected EBITDA to be flat absent that sort of 200 to 250 headwind on synergies year-over-year? And then, Stewart, just thinking about cash taxes, what's your current thought process on when that starts to kick in and also maybe wrapping the discussion about potential pension funding, thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Mike, regarding the EBITDA, if we had the same level of incremental synergy, we would have been close to flat, right around even there, breakeven on the EBITDA. That's correct. We just saw basically a lot of those initial start up costs, expenses and investments in the new initiatives especially.

Mike McCormack - *Nomura Securities Intl - Analyst*

Okay.

Stewart Ewing - *CenturyLink, Inc. - CFO*

And Mike, with respect to cash taxes in '13, probably around $100 million or so will still be using the Qwest NOLs. We'll continue to use the NOLs in 2014 and probably complete the utilization of all of the NOLs. We don't have a cash tax number to talk about yet for '14. Pension funding required contributions for next year, 2013 is a little over $100 million. We may possibly look at doing that towards the end of this year as we did last year for the 2012 contribution that we made.

Mike McCormack - *Nomura Securities Intl - Analyst*

Great, thanks guys.

Operator

Thank you. Scott Goldman, Goldman Sachs.

Scott Goldman - *Goldman Sachs - Analyst*

Hi, guys. Thanks for taking the questions. Want to look at the EBITDA for this quarter and you guys exceeded the top end of your guidance by a pretty healthy mark, which I think is the second time you've done that this year. What I'm trying to figure out is I've gone through the different quarters this year, what's changed as you go through and you issue your guidance and then you come out with a higher number on the quarters?

Are these costs that are merely being pushed out perhaps on the Prism IPTV into next year? Are these the more seasonal maintenance costs and lower property taxes that you highlighted on the EPS side that really drove that? And of those costs, sort of which ones are one-time in nature versus sustainable cost improvements?

Stewart Ewing - *CenturyLink, Inc. - CFO*

Yes, so Scott, I think what's happened is we've exceeded the top end of the guidance because we've been able to get some of the Qwest synergies quicker than we had otherwise expected in the guidance that we gave, and it's really in the strategic sourcing area, network integration area, and some headcount as well.

In terms of one-time items that we had in the third quarter, probably the larger one-time item that we had that's reflected is we had about a $20 million reduction in property taxes below what we expected for the third quarter. $12 million of that was related to a true-up for finalization really of a prior year property tax issue in the state of Florida that came to us from Embarq. And then basically, the remainder of it was really related to a state where we were able to successfully reduce an assessment that they had previously provided to us.

Scott Goldman - *Goldman Sachs - Analyst*

Okay, great, and then just listening to AT&T at the analyst day today they laid out a path for investment in broadband whereby they plan to bring speeds up to 100 megabits per second on U-verse platform, probably 75 megabits or even higher on using IPTV technology. Glen, you laid out sort of the coverage where your speeds are up to say 20 megabits per second for a quarter or more of your territory. Just wondering longer term, how comfortable you are with the speeds you're driving towards now. Do you feel the need to maybe have to drive to the 50 megabit or 100 megabit bite or driving fiber out deeper or utilizing pair bonding or some of the other technologies that may be out there?

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, Scott, we do think we need to continue to drive additional speeds. We think we're shooting for the 20 megabit, 25 megabits for very large percentage of our areas but with bonding, we can virtually double the capacity of the broadband capacity of speeds in our markets. We are already doing bonding in a number of markets today so where we have 20 megabits, basically you could have 40 and where you have 10 you could have 20, so that is a major area we're looking at.

We look at, of course, our fiber to the node work where we are bidding 25 to 40 megabits and depending on the distance to our customers trim and we can double that to the 80 megabits and the fiber to the node work there and it's a large percentage of those customers. So we are doing the same, looking at ways to economically reach that customer base with higher speeds and it's important to us, so it's why our broadband investment is one of our key initiatives. We're expanding our broadband capabilities. It's a key investment for us and it helps drive our penetration level as well with our broadband products.

Scott Goldman - *Goldman Sachs - Analyst*

Great. Thanks guys.

Operator

Thank you. Michael Rollins, Citi.

Michael Rollins - *Citigroup - Analyst*

Hi, thanks for taking the questions. First question is if you could just size the revenue that you get, the access revenue you get from towers from the combination of copper and fiber.

And then secondly, I was wondering if you could -- just going back to the cloud and managed services business that you have -- what are you seeing in terms of the learning, the ability to cross-sell telecom services to your cloud customers and vice versa? Are there other areas that you need to develop to further create this cross-selling opportunities either sales force wise, customer service, any other kind of infrastructure that you need? Would be great just to get your perspectives there, thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, Mike. We haven't given, and I actually don't have right now, the access revenue that we get from towers, whether they be fiber or copper, but we obviously serve a very high percentage of the towers in our legacy local exchange areas either with copper, fiber and we'll have -- by the end of the quarter we had about 13,500 towers that we had built fiber to. So it's a good -- they're all under long term contracts, so it's good growing revenue stream for us as bandwidth demands increase.

Jim Ousley - *CenturyLink, Inc. - CEO, Savvis, President Enterprise Market*

This is Jim. On the second part on the cloud and managed services crossover. We clearly see the opportunity there and in fact, we have put a major organization in place, roughly 10% to 15% of the Savvis sales and marketing group are now dedicated to enabling the CenturyLink sales organization to start selling hosting cloud services so we see a lot of pull through there.

I would say it's not a surprise to us. I would say that it's not an overnight process. It's going to take a couple quarters of training programs, certification programs, et cetera, to get the organization up to speed to take on that challenge but the full through going both ways, major network customers that need hosting and major hosting customers that need network, we see significant opportunity and we will start realizing that based on the training programs in the first quarter of 2013.

Michael Rollins - *Citigroup - Analyst*

Thanks very much.

Operator

Thank you. Kevin Smithen, Macquarie.

Kevin Smithen - *Macquarie Research Equities - Analyst*

Yes, I wondered if you could talk about the enterprise business. We've seen a series of weak results across-the-board from your competitors so far in enterprise and SME, and I wanted to know if you could talk about -- they cited specifically weakness in Europe. What are you not seeing that others have seen so far this quarter?

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Well, Kevin, we're seeing longer decision cycle times. We have benefited from some pretty large customer deals we've had coming in over the last few months, last few quarters that really came to fruition the last few months, so we've been fortunate we've had a lot of demand in our areas.

I don't know that we're seeing anything different. We aren't seeing a lot of improvement in the economy. We are seeing businesses be willing to spend more but in recent months, we're seeing that, just like the other carriers said, we're seeing same thing. It's just that our revenue has not been impacted like those because of some deals we had going that have really been good.

Our salespeople, our management folks and enterprise group have done a great job of penetrating that market and continuing to grow our revenues in that sector. So it's certainly a challenge, but our folks are doing a good job and the issue we see is lack of job growth and what's that going to do longer term to this demand and decision cycle for these. Jim, do you want to add anything to that?

Kevin Smithen - *Macquarie Research Equities - Analyst*

Can you also give us a little granularity as to your exposure to Europe as a percentage of revenue now, because others have clearly cited Europe and multi-nationals with exposure to Europe as a big area of weakness.

Jim Ousley - *CenturyLink, Inc. - CEO, Savvis, President Enterprise Market*

I'll try and address both your questions. One, CenturyLink in total has very little exposure here to Europe. Savvis has some exposure to Europe but it's fairly minimal and most of our business is in the UK, so we're not affected by the Southern Europe issues going on. So minimal impact in Europe to speak of.

On the enterprise piece, I would say two things are going on. One, we're smaller than our other two major competitors so we have the ability to go after segments that they aren't really paying attention to and so we put some very focused programs in place that we're seeing very positive results from on a quarter-to-quarter basis on winning business away from those competitors that, to be honest, just aren't paying attention to so I'd say it's an execution. That organization enterprise network group has executed some focus programs quite effectively.

Operator

Thank you. Timothy Horan, Oppenheimer.

Timothy Horan - *Oppenheimer & Co. - Analyst*

Thanks, two broad questions. One for Jim. With Savvis, how important is it for you to have the bandwidth of fiber connectivity? How much benefit is Qwest long distance network and fiber connections brought you?

And second for Glen, some of the carriers are talking about using wireless to be able to shut down copper and replace the copper to save expenses, I know both in the US and globally. Do you think that's feasible from a regulatory perspective and an economic and quality perspective? Thanks.

Jim Ousley - *CenturyLink, Inc. - CEO, Savvis, President Enterprise Market*

On your first question, the fiber connectivity, the whole cloud agenda if you will is network-based and for enterprise, which Savvis is focused on, it's high speed connectivity. So Savvis used to buy those services from third parties and one very good at providing them so we had to subcontract those, et cetera, now as part of CenturyLink, one, we have a cost advantage compared to what we had before and we have a parent that is in the business. And so it should be extremely important to us and we believe it will be and was part of the rationale on the acquisition.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Tim, regarding the wireless displaced copper, from a regulatory standpoint, that can be a tough go. There may be some areas that will have better service with wireless in some ways. As far as a competitive threat, we don't see that being a real issue for us because just the bandwidth requirements and the wireless limited wireless access capability in a lot of areas, obviously the most rural areas it could be an issue, but we're not seeing -- we don't see that as being a major issue right now for CenturyLink. We are looking at the opportunity to use broadband data in some different ways to serve these customers but right now, we don't see that as a major investment for us, or a major risk at this point.

Timothy Horan - *Oppenheimer & Co. - Analyst*

Thank you.

Operator

Thank you. Brian Turner, JPMorgan.

Brian Turner - *JPMorgan - Analyst*

Hi, guys. Just in the context of the initial '13 guide and the continued improvement towards top line stability, any sense as to whether that provides incremental flexibility around the balance sheet and M&A with respect to the rating agencies? And then along those lines, can you help us think about how you'd manage potential opportunities for growth and organic opportunities for growth within the context of maintaining IG ratings at both Moody's and Fitch? Thanks.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Yes, Brian. I don't think, given where Moody's is and we'll go and talk with them probably actually after the year-end so that we can talk fully about 2012 and '13 as well, but not sure that really offers too much flexibility if you understand where Moody's is with respect to the requirement to get down to their three times debt to EBITDA using their formula.

Brian Turner - *JPMorgan - Analyst*

Okay, I think that they've certainly given a few different parameters and one of them I know was stabilization of the top line but certainly, the balance sheet remains the focus. I just didn't know if that would give you guys any sense of incremental flexibility to do something but it sounds like --

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

I don't think it gives us significant incremental flexibility.

Brian Turner - *JPMorgan - Analyst*

Okay and then the second part on how you'd think about inorganic opportunities in M&A within that context, and how you'd think about maintaining investment grade versus opportunities out there that may pressure that.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

We've always valued investment grade rating and we still value it. It really depends on the opportunity, what it could do. Future acquisitions would be more -- if we were to make another acquisition in the future -- it would be more focused in an area that could drive growth for us, so we have to weigh that opportunity with the issues around credit ratings. We hope we would find ways to maintain our investment grade credit rating. Every time we do a transaction now it's a factor that we consider, so there's no firm answer, every deal is different.

Brian Turner - *JPMorgan - Analyst*

Great. That's helpful, thank you.

Operator

Thank you. I will now turn the conference back over to Mr. Glen Post for any closing remarks.

Stewart Ewing - *CenturyLink, Inc. - CFO*

Just one comment too. Someone asked what our required contribution was for pension for 2013 and I said well over $100 million, about $100 million. It's actually about $35 million, the required contribution for 2013.

Glen Post III - *CenturyLink, Inc. - Chairman and CEO*

Okay, thank you, Stewart. So thank you, Sayeed. We're pleased with the continued progress we made during the third quarter towards stabilizing the top line revenues and believe our continued investment in key strategic opportunities will help us continue to drive growth, both near term and long term. Our strategic revenues continue to grow and our guidance reflects our expectation that our revenues from strategic services will continue to grow in the months ahead.

We also remain focused on insuring our operating costs align with our revenue mix and on achieving our operating expense synergy targets through the successful completion of the Qwest and Savvis integrations. Additionally, the expansion of our Prism TV service later this year and recent launch of managed hosting and cloud services for small and mid size business customers will further strengthen our product portfolio and provide us additional revenue growth opportunity as we look into 2013. Thank you for joining our call today and we look forward to speaking with you in the weeks ahead.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes our program for today. You may all disconnect. Have a wonderful day.
