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CenturyLink, Inc. NYSE:CTL

FQ1 2016 Earnings Call Transcripts

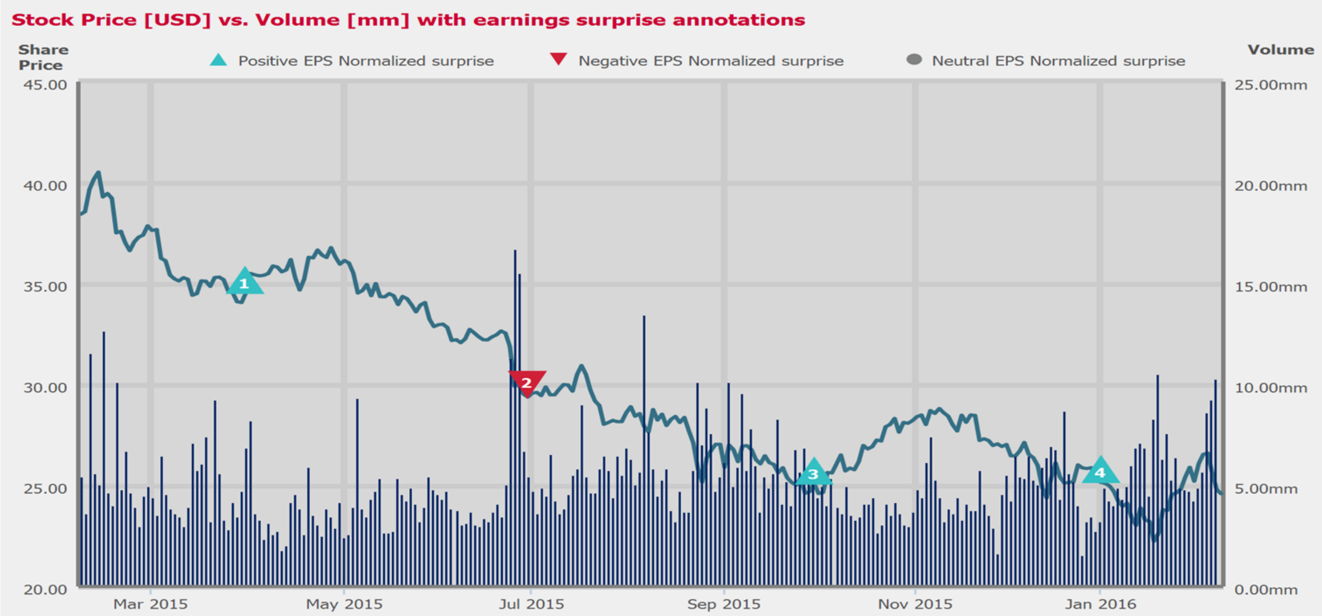
Wednesday, May 04, 2016 9:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2016-			-FQ2 2016-	-FY 2016-	-FY 2017-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.68	0.71	▲4.41	0.63	2.60	2.51
Revenue (mm)	4425.72	4401.00	▼(0.56 %)	4415.01	17666.80	17600.38

Currency: USD

Consensus as of May-03-2016 6:09 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ1 2015	0.58	0.67	▲1 15.52 %
FQ2 2015	0.60	0.55	▼2 (8.33 %)
FQ3 2015	0.69	0.70	▲3 1.45 %
FQ4 2015	0.65	0.80	▲4 23.08 %

Call Participants

EXECUTIVES

Dean J. Douglas
President of Sales and Marketing

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Tony Davis
Vice President of Investor Relations

ANALYSTS

Amir Rozwadowski
Barclays PLC, Research Division

David W. Barden
BofA Merrill Lynch, Research Division

Forrest Wilson
JP Morgan Chase & Co, Research Division

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

Matthew Niknam
Deutsche Bank AG, Research Division

Simon Flannery
Morgan Stanley, Research Division

Timothy K. Horan
Oppenheimer & Co. Inc., Research Division

Presentation

Operator

Good day, ladies and gentlemen, and welcome to CenturyLink's First Quarter 2016 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to Mr. Tony Davis, Vice President of Investor Relations. Mr. Davis, you may begin.

Tony Davis
Vice President of Investor Relations

Thank you, Sayeed. Good afternoon, everyone, and welcome to our call today to discuss CenturyLink's First Quarter 2016 Results released earlier this afternoon. The slide presentation we will be reviewing during the prepared remarks portion of today's call is available on the Investor Relations section of our corporate website at ir.centurylink.com. At the conclusion of our prepared remarks today, we will open the call for Q&A.

As you move to Slide 2, you'll find our safe harbor language. We will be making certain forward-looking statements today, particularly as they pertain to guidance for second quarter and full year 2016 as well as 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.

As you move to Slide 3, 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 these non-GAAP financial measures and the most comparable GAAP financial measures are available in our earnings release and on our website at ir.centurylink.com.

And now as you turn to Slide 4, your host for today's call is Glen Post, Chief Executive Officer and President of CenturyLink. Joining Glen today will be Stewart Ewing, CenturyLink's Chief Financial Officer; and also available during the question-and-answer portion of today's call will be Dean Douglas, CenturyLink's President of Sales and Marketing. Our call today will be available for telephone replay through May 12, 2016, and a webcast replay of our call will be available through May 27, 2016. Anyone listening to a taped or a webcast replay or reading a written transcript of this call should note that all information presented is current only as of May 4, 2016, and should be considered valid only as of this date, regardless of the date heard or viewed.

So now as we move to Slide 5, I'll turn the call over to Glen Post. Glen?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

Thank you, Tony, and thank you for joining our call today as we discuss our first quarter results and operational initiatives as well as provide guidance for next quarter.

Beginning on Slide 6, our first quarter 2016 results were solid. Core revenue, operating cash flow and adjusted diluted earnings per share were all in line with our guidance for the quarter. Our high-bandwidth data services revenue provided to business customers grew more than 7% year-over-year, and consumer strategic service revenues grew approximately 5% year-over-year. Additionally, since the beginning of the year, we successfully placed over $1.2 billion in debt, which we will use primarily to refinance 2016 debt maturities.

Continuing on Slide 7, we entered 2016 with a renewed focus on our key objective: "To improve the lives of our customers by connecting them to the power of the digital world," whether it's providing network connections or adjacent services on top of that connection, enabling the power of the digital world to improve our customers' lives and business, is really what we are all about. Obviously, we are operating in a challenging and quickly evolving industry. Customer expectations are growing. Technology is rapidly advancing and we face strong competition on multiple fronts. But change brings opportunity, and we believe we have the assets, the financial strength and the people necessary to deliver critical broadband capabilities and related services our customers require. Our delivery on this opportunity and our efforts to drive long-term free cash flow growth is anchored in 4 operational objectives.

Continuing on to Slide 8. First, we expect to maximize market penetration of enabled network and adjacent services. The network is our key strategic advantage and is the foundation of value we deliver to our customers. We will leverage our localized marketing initiatives to drive penetration of the investments we've made to date in GPON and other broadband technology, and we will drive further penetration of our fiber-enabled multitenant commercial buildings and businesses. As of quarter-end, we have over 1.5 million fiber-enabled homes and businesses within our net speeds of up to 1 gigabit per second. And we provide more than 30% of our addressable units with speeds of 40 megabits or higher, a speed that today in the market is sufficient to address most of our customers' actual needs. Additionally, we remain committed to enhancing our sales through partnerships with major software, computer and technology companies and with our large alternative partner channel. It is also important for us to be more aggressive in our customer and revenue retention efforts as the cost of acquiring new customers is typically much higher than retaining current customers.

Our second operational initiative is to create exceptional customer experiences. We have always operated with a customer-centric focus, where we know there are ways we can improve our customer experience. Now we're simplifying our product offerings, and with our existing capital program, we're investing to drive higher levels of automation and self-service into our service delivery platforms. We expect the outcome of these improvements to enhance the products and services that we deliver to our customers. We expect them to reduce our overall delivery time frame as well as improve our managed services delivery and service model.

Continuing on to Slide 9. Our third operational initiative is to invest with discipline and with a focus on network first. We believe the greatest potential returns on our capital investment are in building and delivering broadband service capacity on our markets. We will focus our investment on enabling fast, reliable broadband connectivity to our customers, and we will further enhance our core network access capabilities for consumers with a variety of network enablement techniques, including bonding, vectoring and further deploying fiber-to-the-home. Second, we will complement our strong access position by deploying less capital-intense, higher-growth solutions to deliver our customers a full range of technology-focused services such as managed network and hosting, cloud, IT services and video along with over-the-top applications and content. We believe this approach will allow us to deliver the full range of services our customers want, while also allowing us to prioritize capital to improve the network service offerings at the heart of our customer relationships.

Finally, our fourth operational initiative is to optimize operating and capital efficiencies. We know that our long-term success will require ongoing realignment of our legacy call structure. Realizing those efficiencies and ensuring our capital is aligned to those investments that will drive the highest returns is crucial to driving CenturyLink's future cash flow, our cash flow growth, through aggressive simplification and automation of our product portfolio and customer experience. Not only will we enhance service to our customers, we'll also drive cost out of our business and operate more efficiently. Also, we're focused on increasing the discipline and rigor of our capital allocation process to generate the best returns in our capital and operating investments. An example is the strategic review process currently underway for the data center and colocation business. While we expect colocation services to continue to be a service our customers will look to us for, we believe there's potentially more efficient ways to enable these services for our customers. And we have a clear strategic direction, and we believe by focusing on our key objectives in these key operational initiatives, we will successfully build CenturyLink's strong foundation and deliver value for both our customers and our shareholders.

Moving to Slide 10. There remains tremendous amount of colocation services in both the U.S. market as well as the international markets we operate in. While we like the colocation business, we believe our priority for capital investments is in the network to protect and grow our consumer and business network market position. Therefore, we launched the strategic review process for our data center and colocation business last year. Our strategic review is ongoing. We have received a strong level of interest from numerous strategic and financial parties. We expect to start narrowing this down to a shorter list over the next few weeks, and we expect to finalize the process in late third, early fourth quarter of this year. This strategic review could result in a sale of all or a portion of our data centers. It could result in a partnership with a joint venture as well as possibly keeping these assets as part of CenturyLink's portfolio. In all cases, we look for the best way to create accretive value for CenturyLink and our shareholders and continue to provide a strong colocation competitor in the market for our customers.

Now I'd like to turn the call over to Stewart to discuss our financial results and guidance and liquidity position. Stewart?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Thank you, Glen. Over the next few minutes, I'll review the financial results for the quarter, provide an overview of second quarter 2016 guidance we included in our earnings release issued earlier this afternoon and conclude my remarks with a discussion of CenturyLink's liquidity position.

Now moving to Slide 12. I will review a few highlights from our first quarter results. Please note that I will be reviewing the results, excluding special items, as outlined in our earnings release and associated financial schedules. As Glen mentioned earlier, we achieved solid results for the first quarter and operating revenues were $4.4 billion on a consolidated basis, a 1.1% decrease from first quarter 2015 operating revenues. The decrease was primarily driven by lower legacy and low-bandwidth data services revenue, offsetting an approximate $50 million increase in high-cost support revenues due to CAF Phase 2 higher consumer strategic services and increased high-bandwidth data services revenues. Core revenue, defined as strategic revenue plus legacy revenue, was $3.98 billion for the first quarter, a decrease of 1.9% from a year ago period. Strategic revenues grew 1.5% year-over-year primarily driven by strengthened high-speed data revenues, high-speed Internet and Prism TV. In the first quarter, we added approximately 16,900 Prism TV customers, while high-speed Internet customers increased nearly 7,800 during the quarter.

We generated operating cash flow of approximately $1.69 billion for the first quarter and achieved an operating cash flow margin of 38.4%. The cash expenses for the first quarter declined $5 million year-over-year primarily due to lower employee-related costs.

Starting in the first quarter of 2016, we have revised our free cash flow calculation to include the cash impact of pension and OPEB costs as well as stock-based compensation. We believe this calculation provides additional detail and insight into the company's ongoing cash requirements. For the first quarter of 2016, free cash flow was $824 million. Adjusted diluted earnings per share for the first quarter of 2016 was $0.71, an increase from $0.67 in the first quarter of 2015. Although operating cash flow declined in the first quarter of 2016, compared to the first quarter of 2015, lower depreciation and the impact of our share buybacks in 2015 resulted in a net increase in adjusted diluted earnings per share.

Moving to Slide 13 in our Business segment. In the first quarter, the Business segment generated $2.6 billion in operating revenues, which decreased $93 million or 3.4% from the same period a year ago. First quarter strategic revenue for the segment was flat at $1.58 billion compared to first quarter 2015, driven primarily by the continued growth in high-bandwidth data services, being offset by the declines in low-bandwidth data services and hosting revenues. Legacy revenues for the segment declined 6.9% from first quarter a year ago due to primarily a continuing decline in voice and switch access revenues. Total Business segment expenses decreased $36 million or 2.5% from the year-ago period, driven primarily by lower employee-related costs.

Now turning to Slide 14. The Consumer segment generated $1.49 billion in total operating revenues, a slight decrease of $8 million or 0.5% from first quarter 2015. Strategic revenues in this segment grew 4.9% year-over-year to $774 million, driven by year-over-year growth in high-speed Internet and Prism TV revenues.

Legacy revenues for the Consumer segment declined 5.8% from first quarter 2015 as voice revenue declines were partially offset by select price increases. Operating expenses increased $16 million or 2.6% compared to the same period a year ago due primarily to higher Prism TV content costs and marketing expenses.

Now turning to our guidance on Slide 15. For the second quarter 2016, we expect operating revenues of $4.38 billion to $4.43 billion; core revenues of $3.94 billion to $3.99 billion; and operating cash flow between $1.59 billion to $1.64 billion. Adjusted diluted EPS is expected to range from $0.57 to $0.62. Second quarter 2016 operating revenues are expected to be in line with first quarter 2016 operating revenues, primarily due to anticipated growth in data integration, high-bandwidth data services, high-speed Internet and Prism TV revenues being offset by the expected declines in legacy and low-bandwidth data services revenues.

Our anticipated sequential decrease in second quarter operating cash flow compared to first quarter 2016 is primarily due to expected higher seasonal cash expenses. For full year 2016, we remain comfortable with our previous guidance, although continued pressure on business strategic revenues and our decision to defer certain price increases will likely result in our core and total revenue coming in toward the lower half of our range for the year than we previously provided.

Now turning to Slide 16. And as we discussed last quarter, our liquidity position remains very strong. Since the beginning of the year, we've completed debt issuances for a total of over $1.2 billion, which will be used to refinance substantially all of our 2016 maturities. Our 2017 maturities are comparable to the amount in 2016, and as you can see, the following 3 years maturities are materially lower.

As indicated by our 2016 guidance, we expect $1.8 billion to $2 billion of free cash flow, which should result in our dividend payout ratio for full year 2016 to be in the low to mid-60% range. So our solid cash flows continue to provide us with the financial strength and flexibility to meet our business objectives and drive long-term shareholder value.
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.

Question and Answer

Operator

[Operator Instructions] The first question comes from Simon Flannery from Morgan Stanley.

Simon Flannery
Morgan Stanley, Research Division

Okay, great. Stewart, I wonder if we could come back to that last comment on the revenue guidance for 2016. You cited pressure on business service revenues and deferral of price increases. Can you just go through that in a little bit more detail and how that relates to your path to revenue stability?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Yes. So, Simon, yes, if you take our first quarter actual results and the midpoint of second quarter guidance, you'll see that if you leave in the annual guidance where it is, you'll see that we would require to have revenue growth in the last half of the year to be able to get to the midpoint guidance. So we think we'll be in the bottom half of guidance based on the things I mentioned. In terms of the business strategic revenues, we've seen some weakness in MPLS revenues as well as our hosting revenues. We expect to be able to turn that around and grow these revenue streams later in the year. But at this point, based on where we are, we think that we need to give you guidance that -- or indicate that it'll be towards the lower half of the guidance. The other part, I guess, is that the price increases. Some of the increases that we're going to put in place, probably in the $40 million range, we've decided at least to defer at this point. We're still talking about them, but we feel it's fair to call that out as possibility that we'll not implement those increases. Some of our...

Simon Flannery
Morgan Stanley, Research Division

What products were those on?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

They were really across the board, but mostly directed towards high-speed Internet or facility charges and things like -- of that nature.

Simon Flannery
Morgan Stanley, Research Division

Okay. And the pressure in businesses, is that competition or macro or...

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

I think, it's -- I think, we're winning. I think -- I'm going to let Dean talk about that a little bit.

Dean J. Douglas
President of Sales and Marketing

Okay, sure. Some of the pressures that we're facing in the business have to do with a slight adjustment in strategy, for example, in high-speed Internet realm. What we did was we pivoted from an approach that was pure broadband to one that is more traditional bundled broadband. We did that in the latter part of fiscal year '15, and so we're starting to work through what that means in the first part of fiscal year '16. And we expect that, that will continue to work through the middle part of the year of fiscal year '16. But that pivot to the more traditional approach to high-speed bandwidth, in the Consumer segment especially, should allow us to have customers that have less proclivity to churn and a higher ARPU. So we think that, that's going to be something that we're going to benefit from in the second half of the year and into 2017.

On the high-speed -- I'm sorry, the MPLS circuits and the Ethernet circuits for the business marketplace, we actually are doing pretty well with that. In the first quarter, it's generally slower than we see in the second quarter and other parts -- or other quarters throughout the year. And we saw that once again in the first quarter this year. Having said that, we did focus on driving our business and market approach from an enterprise standpoint to really take advantage of opportunities that we think are much nearer term, and so we're focused on those nearer-term opportunities. And you should start to see those nearer-term opportunities manifest themselves in the second half.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

I'd point out, too, Simon, on the business services, MPLS and Ethernet, we had good -- we still had 7% growth. We just expected more. We wanted it to be higher than 7%. So it's growing, it's just we'd expected to see that little pickup in the latter half of the year.

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

And that was the case.

Operator

Our next question comes from Amir Rozwadowski from Barclays.

Amir Rozwadowski
Barclays PLC, Research Division

Just following up on Simon's question on sort of the 2016 outlook. Does that sort of change the trajectory in terms of your expectation for stabilization in the top line? And then I've got a bit of a follow-up question, if I may.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Yes. I think we can still get close, if not get there. And the other thing that we're going to do is work on the expense side as well to try to make sure that we keep our operating cash flow more towards the midpoint of the guidance that we'd provided.

Amir Rozwadowski
Barclays PLC, Research Division

And then on initiatives around the data center assets, you'd mentioned we should think about sort of a wrap-up around the Q3 or Q4 time frame, if I'm not mistaken. How should we think about the primary use of cash once those -- that comes in? And at this point, you'd mentioned there is some -- that you've seen a lot of interest. You've mentioned in the past that you'd be open to a sale or potential JV or other opportunities. Has there been sort of an area that a lot of this interest is focused on? Is it a sale? Or how should we think about that?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

I'll take the last part. There's been more focus on the sale from our interested parties. There are some who are proposing possible joint ventures. We expect in the next 2 weeks to have that -- those structures available to us, which are really due next week. And when we have that, we'll know more about, not only the structures and the partnership opportunities versus the sale, but also is the level of interest in terms of valuation. In terms of the use of proceeds, we're going to wait until we get closer to understanding what that might be. But basically, one option is to -- if we do dispose of the properties in the business, we will be -- our EBITDA will be reducing. And we want to try to keep our debt-to-EBITDA ratio at about 3x, so we may repay certain amount of the debt that we have outstanding over a period of time. The other opportunity that we'll look at is to look at -- to the extent that business is generating free cash flow to potentially look at a share buyback to mitigate the negative impact of any free cash flow per share that would be associated with the disposal of that business. And then we'll look at investing in our business as well, potentially the network to try to drive our speeds faster and drive more customers to the network.

Operator

Our next question comes from David Barden from Bank of America.

David W. Barden
BofA Merrill Lynch, Research Division

I guess, first, just a short term kind of picture, Stewart. If I go line by line through the strategic services, legacy services, data integration quarter- to-quarter, the businesses that are declining went down $88 million and the businesses that grew, grew $14 million for a negative $74 million sequential. And the guidance range suggests that, that goes from minus $74 million to a range of minus $20 million to plus $30 million. So that like a plus $100 million swing is in the realm of possibility. If you could kind of walk us through this kind of these line items and tell us where all these big changes are continually be coming from, I think it would give people a little more conviction about what's supposed to happen next quarter. And then, longer term, obviously one of the big questions a lot of people have is a couple of years ago, you guys were looking into the future, saw mid-80% types of payout ratios in your future as a full cash taxpayer, and you decided to cut the dividend. And people are doing the math now. They're looking into the future. They're seeing bonus tax depreciation reverse and payouts going at least into the mid-70s. And there's fears that you guys are going to go back and cut the dividend again because that's what you did last time. Could you kind of talk about that issue as well?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

David, let me just pull the line item information, and I'll just talk about the dividend issue. The dividend is a key part of the value proposition that we have for shareholders. And we -- there's no guarantee, but I know our board and management team feels like we're very much committed to the dividend. And we think with the additional approval of bonus depreciation, if you look at our -- even though the payout ratios are going up, we believe we certainly have adequate free cash flow to continue the dividend. So I can tell you, our board has not discussed reducing the dividend. I think it never happened, but we're committed to our dividend. Again, our primary factor is our value proposition to shareholders, so we're committed to that dividend.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Yes. And the other thing that we said as well, David, on the dividend is that versus where we were a few years ago when we reduced the dividend, as long as we can see a path to EBITDA stability and EBITDA growth down the road, it's okay for our dividend payout ratio to float up higher than we talked about before. In terms of the increase in the strategic services and what that implies, basically, a fair amount of that is due to rate increases that we've put in and expect to put in, in the second quarter of the year. So that's driving quite a bit of it. The rest of it is due to unit increases that we expect to see in our IPTV products as well as our high-speed Internet. In general, that's pretty much it. It's really -- I can't really go line by line, but just in general, it's basically price increases on those products, predominantly high-speed Internet.

David W. Barden
BofA Merrill Lynch, Research Division

And so your comments earlier about not putting through some price increases, that there are, in fact, some other price increases that are going in?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Yes, there are other price increases. We -- of the total amount that we expected to do and that we kind of put -- baked into our guidance that we gave for the full year at the end of the fourth quarter, we chose to not do about $40 million of the total amount. But there are other price increases that are going in and have gone in sometimes during the first quarter as well as we expect to put in throughout really the second quarter or third quarter. That will drive some of the revenue in the back half of the year

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

David, and just a little more color on the revenue. We've got the rapidly expanding GPON markets. We've gone up again. Now we're up at 1.5 million homes and businesses we're passing. We've got -- with the exclusion of the last couple hundred thousand, I know we were at 21% penetration at the end of March, and that's -- we just started with it last year with that GPON work. So we believe there's significant upside going forward with those GPON markets as well as the new Prism markets we entered just late last year, and now with those markets. So that, along with the MDU and MTU focus we have now, we've got fiber to a number of MDUs and MTUs that are going to help drive revenues. So we think there's really upside here in the last half of the year to drive greater penetration, as Stewart said, additional revenue there.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

Yes, and we think our MPLS revenues will grow in the back half of the year based on installations that we can do of customers that we have sold and expect to sell, as well as our IT services business is small, but it's growing and contributing to expected revenue growth in the back half of the year as well.

Operator

Our next question comes from Matthew Niknam from Deutsche Bank.

Matthew Niknam
Deutsche Bank AG, Research Division

Just 2, if I could. First, on consumer broadband. So revenues were effectively flat sequentially. Can you just give us some more color on what's driving that slower growth? And then just bigger picture, on your asset mix, as you think about the business over the long term, are there areas you think you may need greater scale to begin competing more effectively? And then conversely, are there other opportunities like the colo business, where you may not necessarily need ownership or where you'd look to maybe move away from over time?

Dean J. Douglas
President of Sales and Marketing

So let me take the first part of the question, which is with regard to the consumer broadband business. As I mentioned earlier, in the second half of last year, we actually pivoted from a model where we focused on pure broadband to move to a more traditional broadband mix. And so as we do that, we've moved the marketing funds from focused on pure broadband to taking on the more traditional broadband or bundled broadband kind of services. And so we expect that to -- that business to recover as I mentioned in the second half of the year, because we'll still see some marketing spend and investment in marketing that we need to do to drive that broadband business. So we're seeing it flat sequentially, but we don't think that the business is going to be flat sequentially based upon where we're focused and the drive we have. And as I mentioned, and I'll reiterate, it does drive a churn model that's significantly lower than the churn model that we would see in the pure broadband. So not only would we get new customers going forward with the marketing efforts we have in place to drive the traditional broadband business, but we'll also retain more of those customers that we drive to that business model as well.

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

I'll just talk about asset mix for a moment. As I pointed earlier on the sale of the colo, which really a matter of really prioritizing where we're going to invest our capital. We think we can drive the best returns. We think there are ways to increase our revenue drive, revenue using partners and different technologies such as over-the-top technologies for what we call our asset light businesses, the hosting and IT services, those types of businesses that we believe that we can drive growth in. We think there's some functionality we would like to have. I don't think the scale is necessarily the issue here as you asked, but I think it is or some functionality that we would like to gain and we think there's some opportunity for us to do that. On the network side, we think we have great scale there, and we'll just continue to invest in GPON and higher speed vectoring and bonding, and we think we can drive a lot of opportunity throughout our markets for the broadband growth and Prism growth as well. So that's really our focus there, and we think we have a real opportunity to drive both the returns as well as the revenue growth over time with the asset base we have.

Operator

Our next question comes from Frank Louthan from Raymond James.

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

Great. Can you comment on special access? What's sort of your net exposures there and thoughts on some of the action that the FCC is taking? And then you mentioned in the prepared remarks about better investments in your network versus where the data center opportunities are there. Where do you see the highest returns in investing your network? And where are you going to be placing your CapEx for the next 12 months?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

Yes, Frank. So this week, the FCC concluded its special access tariff investigation on -- and really, that will have a minimal financial impact and, in fact, tariff impacts to this as well. And of course, they opened a special access notice for full rules making that could potentially impose more regulations, special access pricing, terms and conditions. It appears that the FCC is seeking to impose additional price regulation on the industry as well as redefining what constitutes a competitive market between the market participants. The most concerning financial issue in the proceeding, as we appreciated at this point, is the potential imposition of a productivity factor or an X factor that could require CenturyLink to lower its special access rates on an annual basis. We believe the market for high-bandwidth data services is highly competitive as evidenced by the fact that we're not getting all the special access that's going away and converting to Ethernet. The cable companies get some, the other fiber companies get some, CLEC gets some, so there's plenty of competition. We don't believe that heavy-handed regulation included an arbitrary market and bandwidth definitions as well as on more price regulation. We think that, that will only serve to just hinder further investment in broadband, especially in rural areas, where it's tough to make the investment work anyway. So we don't know what the outcome will be at this point, and really haven't quantified -- been able to quantify the financial impacts because, again, we really don't know where they're going to end up from the standpoint of having a productivity factor or an X factor or not.

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

Can you tell us what sort of your net exposure is between special access revenue versus any costs you have for network -- for access?

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

I mean, it's the wholesale revenue basically, and its high margin, Frank. So there aren't a lot of continuing incremental expenses associated with providing that service. It's mostly in the investment that was required to build a service out. There's some maintenance costs, but it's probably pretty minimal.

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

Well, there's also costs you have, say, in outside your region where you're buying special access is where I was getting to.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

That's true. And that would...

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

You'd benefit on the cost side as well.

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

That would be a benefit on the cost side as well, Frank. And we haven't really been able to quantify that either, and frankly, I'm not sure exactly of the relationship now between what we spent with our third parties versus our revenue. I think, when we look at this in years past, it basically -- there was some benefit, but the benefit wasn't enough to offset the potential reduction. And especially this time when they may bifurcate the special access between urban areas and rural areas, so you really just don't know what they'll end up doing there and what the implications would be to us until we really get a better understanding and get more detail and have the notice for both rule-making and reply comments made and all. I think, then, we'll have a better feel, maybe towards the end of the third quarter or so.

Frank G. Louthan
Raymond James & Associates, Inc., Research Division

Got it, okay. And on the network investment focus?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

Yes. In terms of our network, I mean, we believe our best returns come from where we're increasing the speed availability in the network that allows us to be more competitive with the cable companies and others that provide high-bandwidth data services and Internet services. So that's where our best opportunity is, I believe, and we'll continue to really do the things that we need to do to improve our network and improve the speeds that our customers are able to take advantage of on the network. We have quite a bit of work going on, really starting a year or so ago, really spearheaded by Aamir Hussain, our CTO, in terms of really increasing the end, and really utilizing to get more life out of the old copper networks. So it's not -- we realized fiber is the way to go and is a good way to go when you can afford it from a density standpoint. But we believe there's a lot of life left in the copper network and a lot of things we can do with bonding and vectoring and other technologies that are coming down the pipe that will help us be able to stay competitive and enhance the experience that our customers are seeing.

R. Stewart Ewing
Chief Financial Officer, Executive Vice President and Assistant Secretary

I'll just give you an example of that, Frank. If you look at just when we have a GPON investment last year or so, and we've got 20% penetration already in those GPON markets that have been there for several months. So it's really encouraging also where we get the vectoring. Now we're seeing great take rates there. So we really have in the, especially, in the -- well, it's really both, but especially in the business side, we have very little market share from a data revenue standpoint in our legacy markets. And as we roll out the GPON capabilities as well as the vectoring-type capabilities in these larger and midsized markets, we're seeing a really good success. That's why we believe in the second half of the year, we're going to see better growth than we've seen in a while in MPLS, Ethernet-type services.

Operator

Our next question comes from Tim Horan from Oppenheimer.

Timothy K. Horan
Oppenheimer & Co. Inc., Research Division

Just 3 quick ones. Can you give some examples of what you mean by more advanced broadband services or more bundled, more advanced services? Also, how does your ARPU -- maybe you can talk about your broadband average ARPU and maybe how does that compare to your competitors. And then, third, can you just give us a sense of how deep the fiber is in the network at this point? It seems like vectoring and a bunch of these other technologies you've got to get down to a couple of thousand feet. And I know you talked about 1.5 million homes passed with GPON, maybe where are you in terms of the dollar amounts of fiber deployment a year or some other metric to give us a sense of where we can get to a point where the broadband speeds are really more comparable to the cable companies?

Dean J. Douglas
President of Sales and Marketing

All right. So let's talk about the examples of what we mean by bundled broadband services. So the traditional high-speed Internet services are really what you'd expect in a double play or triple play. So it's not only a high speed, but it's also video and some voice technology as well. And so that's pretty much a typical broadband suite of services. When you look at the Prism ads that we did in the first quarter of this year, 53% of them were with new customers. And so you're now starting to see services like Prism attract new customers that were not customers of CenturyLink, and they're dragging along broadband services with that video play. So 98% of those customers that signed up for Prism in the first quarter also signed up for our broadband services. And so we see in those markets that bundling the technologies, broadband, video and the like, really do provide a much more compelling offering for both our customer base as well as our -- the folks that were with either competitors or didn't have the service at all, but nonetheless were not customers of CenturyLink. And so as we think about how we go forward with -- to the marketplace, we obviously do a lot of competitive analysis. So I would tell you that our ARPUs are consistent with what you'd see from an ARPU level in our competitors. And we see competition adding a lot of fees, and so that's where there might be a little bit of a delta. But we're working through and constantly monitoring what our competitors are doing in the marketplace with regard to the average ARPUs in our business. The fiber deployment, well, we talked about fiber deployments, 1.5 million homes passed from a fiber standpoint. But vectoring and bonding does provide a compelling level of service for many of our customers, especially those that don't have access to fiber or where they really don't need the speed of fiber. And so there's obviously an economic equation there for those customers, but also it's, at 40 megabytes, sufficient enough to get Prism services and to do a lot of broadband activity that they're going to need in the consumer space especially. And so they should be very, very comfortable with what we have to offer, and I think they are comfortable with what we have to offer when we do the vectoring and the bonding in order to provide them high-speed broadband access.

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

And Tim, let me just add on the vectoring. Today, we only have about 250,000 households passed. We expect to be close to 600,000 by year-end. And we're looking at a plan that could reach over 14 million households in the next few years. And it was costing about $160 per home passed at vectoring, but it's getting 100 megabits out here too, and it can be more than that. But certainly, 100 megabits is very possible vectoring that we believe can cover a lot of our customers' needs for the next few years.

Timothy K. Horan
Oppenheimer & Co. Inc., Research Division

So are you basically saying you can reach a vast majority of your homes passed with vectoring with 100 megabits in a few years?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

We could reach the majority of the addressable homes passed, as we described them, or we have. They're occupied and they are addressable with broadband.

Timothy K. Horan
Oppenheimer & Co. Inc., Research Division

Yes, that would be a game changer. Good luck.

Operator

And our final question comes from Phil Cusick from JPMorgan.

Forrest Wilson
JP Morgan Chase & Co, Research Division

It's Forrest, in for Phil. As you see more over the top video offers coming, does it make sense to stay at your own full video platform in new markets rather than just bundling a DTV OTV [ph] product, for example, with the great broadband speed offering? How do you think about that?

Dean J. Douglas
President of Sales and Marketing

So we think it's a very, very, very interesting proposition, and so we're piloting that capability in 4 markets. And we're going to evaluate how that plays out in those markets. But we think it's a very, very intriguing opportunity, and we're definitely looking at that as an alternative to some of the other opportunities we have in the video space.

Operator

I'm showing no further questions at this time. I'd like to hand the conference back over for closing remarks. Mr. Glen Post?

Glen F. Post
Chief Executive Officer, President, Director and Member of Special Pricing Committee

Thank you, Sayeed. We're confident that CenturyLink is well positioned to help our customers realize the promise of the digital economy, as we've stated as our goal. We have a strong set of assets. We have dedicated and passionate employees. We have a financial strength to continue to invest in our future. And we have the strategic clarity of how we will grow our business by connecting our customers to the digital world. And we are really inspired by the opportunities we see for our customers, for our employees and our shareholders in the months and years ahead. So thank you for joining our call today, and we look forward to speaking with you in weeks ahead.

Operator
Thank you. And ladies and gentlemen, thank you for participating in today's event. This concludes our program. You may all disconnect, and have a wonderful day.