WOW!

Moderator: Rich Fish
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8:00 a.m. MT

Operator: Good morning, ladies and gentlemen and welcome to the Second Quarter 2014 WOW! Internet, Cable and Phone Earnings Release Conference Call.

As a reminder, I want to advise everyone that this call is being recorded. At this time, I would like to turn the call over to Mr. Rich Fish, WOW's Chief Financial Officer. Please go ahead, Mr. Fish.

Rich Fish: Thanks Stephanie. Good morning everyone and thanks for joining our second quarter earnings call. With me today is WOW! CEO, Steven Cochran, who will be giving an update on our operating activities and then I'll cover the financial results for the quarter. And then after that, we'll open it up for Q&A.

Before we get started, we need to remind everyone that in our call, we'll be making some forward-looking statements about our expected operating results, our business strategy and other matters relating to our business. We disclaim any obligation to update those forward looking statements.

Those statements involve known and unknown risks, uncertainties and other factors that may cause our actual operating results, financial position or performance to be materially different from those expressed or implied in our forward-looking statements.

We discuss in our most recent Form 10-K some important assumptions in business risks that could cause our actual results to differ materially from those in the forward-looking statements and you should refer to that filing for a complete discussion of those risks.

In addition please note that in our call today and in our earnings release, we refer to certain non-GAAP financial measures including adjusted EBITDA which is reconciled in our earnings release to the most comparable GAAP measures in our financial statements that's filed with the SEC.

So with that out of the way, I'll turn it over to Steven to give everyone an update on the business.

Steven Cochran: Thank you, Rich. Good morning to everybody. Thanks for joining us. We're halfway through the year now and while we had a couple of challenges early in the year, we feel like we're making really good progress as we move forward.

From a customer activity standpoint during the second quarter despite what is normally a pretty tough acquisition quarter, we felt really strong as our connects stayed strong throughout the quarter. We were impacted by the normal seasonal churn as well as we implemented the second rate increase this year which impacted churn as well.

Our total customers and total RGU growth was about 15,000 during the quarter. The growth was driven by our continued positive trends in HSD subs as well as we also included customer and subscriber data related to Anne Arundel Broadband.

We don't disclose market specific information and so we won't be giving the exact numbers of what that contribution was, but the total investment we made for this system was only $5.6 million. We increased our investment in an entity we already had from 5% to 75% for the $5.6 million, for an overall valuation of the business of $8 million. So, that system is in Anne Arundel County, Maryland and is now part of our operations although we are continuing to operate it under the Broadstripe name.

From an Ultra standpoint, our video platform of the future, we continue to see strong growth there. We saw our "sell-in" move from 30% to 32% in the quarter. And we added an extra 7,000 Ultra customers during the quarter which also equated to almost 42,000 from a year over year perspective.

We mentioned the rate increases, we've had a cycle of rate increases this year and it continues. Our first customer rate increase took place on January 1st which is our normal rate increase. It cycles through, you really don't get the full effect of it until February.

We then had incremental rate increases in Mid-Michigan and Lawrence just because their timing cycle is off due to the previous rate increase timings prior to our acquisition. We then implemented an ancillary fees type rate increase in the second half of the second quarter which the quarter was impacted by a little bit, but it's not fully implemented or wasn't fully implemented until sometime in June and so we're starting to see the impact of that.

We also have a sports tier fee that's coming in the middle of the third quarter really tied to the launch of the SEC network, not particularly priced to that, but in connection with the timing of that. So, the second set of rate increases were implemented in May and June. We've seen some of the impact I think we expect to do much better from a realization standpoint on that just from the lessons we learned in the first quarter.

Part of that though also, as we'll talk about, impacted churn a bit just because of our desire to make sure the majority of that rate had a better stick rate than what we experienced during the first quarter. We continue to – in addition to that, because of some of the rate challenges we had early in the year we continue to work on other opportunities to offset and mitigate that Q1 impact.

From a customer churn standpoint, as always the second quarter is a tough quarter for us. We see just overall seasonal moves so from the customer churn standpoint we saw our churn at 2.8% for the quarter compared to the first quarter of 2.4% obviously impacted by the seasonality, impacted by the rate increase and also impacted pretty significantly in our college towns, which we have several, where you see pretty significant move activity.

From the business services standpoint, we continue to make a lot of progress. We have launched some new products early in the quarter in the Legacy WOW! markets, it's a slower sales cycle and it's a slower install cycle and so it took a little bit of time to see that starting to hit the financials, but as we move throughout the second quarter we're starting to see a lot of transactions associated with those new products.

We're also in the process of launching hosted VOIP in the third quarter that's kind of the next product that our people are excited to get out and sell, and then we'll continue to move forward from there.

From a sales standpoint, we continue to see nice progress with our sales funnels and our booked MRC. March had represented our best month ever. We built on that in the first quarter and the second quarter is now our best quarter ever and we're excited about that trend. We also can see that continuing into the third quarter in a very good way.

We're also really excited to announce that we signed a very large wireless back haul deal in the quarter. We'll connect over 450 towers in two regional hubs. And that will really just be the baseline from the business we do. We have significantly more towers than that are kind of in progress and so we feel very good about that.

Not only what's going to do from a standalone business just for that piece what allows us to offer to other wireless carriers down the road. But what that does that from our overall network standpoint. It'll allow us opportunity to continue to go and sell off of the network that we're going to build as part of this process. So we feel – we're very excited about what that opportunity is going to do for us.

We continue, just overall, to build the infrastructure; to build the scalability; it's a work in progress, but we've made a lot of progress on it. We continue to improve the types of the account executives we have, the sales managers that we have and really improve the infrastructure from a technology standpoint and from a team standpoint. And they are really excited that we're headed with that piece of the business.

From an integration standpoint we continue to move forward on our all digital conversion in the Legacy Knology markets. We completed Pinellas, Huntsville, Columbus, Valley and Auburn. We're now in the process of completing Montgomery. We've had two of the channel drops. The last one is next week. That will be all that we do from an all digital conversion for this year. We'll continue to complete the simulcast and the complete the seeding and move forward with the remainder of the markets as we move into early part of next year. But what's really been good is we've been able to take what we learned in each market and move forward to make each of them less and less impactful.

And lastly we also announced in the quarter that we're selling our South Dakota markets. We announced that we'll be selling them for $262 million to Clarity Telecom. We think this is good for us, and good for them. This is a deal where probably our least – we were putting the least priority on these markets.

They were the least geographically synergistic to us. They are kind of the most spread out and looked unlike the rest of our systems more than any we had, and because of that made it hard to be as competitive as we needed to be there.

And with that we sold it to a company that's going to have that as their only market and their only priority. So we feel good about that. We feel good about the price we were able to get for it. We're going through regulatory and municipal approvals right now and we expect this will close either late in the third or early in the fourth quarter.

So with that I will turn it back over to Rich.

Rich Fish: Thanks Steven. For the quarter we reported total revenue and adjusted EBITDA of $319.8 million and $111.5 million, respectively. Total revenue was up $7.7 million sequentially or 2.5% and represented an increase of $18.4 million or 6.1% on a year over year basis. Adjusted EBITDA was up sequentially $2.5 million or 2.3% and was an increase of about $400,000 on a year over year basis.

On a combined basis, total subscription revenue for the quarter was $288.3 million which was an increase of $6.6 million or about 2.3% sequentially.

And of that quarterly increase $4.2 million of it was attributable to increased volume as a result of the strong subscriber activity during the quarter specifically, as Steven mentioned, as it relates to our HSD connect activity as well as the inclusion of customer data related to the Anne Arundel Broadband.

The remainder of the sequential increase or $2.4 million was derived from the realization of the full quarterly impact of the first quarter rate increase and the smaller ancillary rate increase that we implemented during the second quarter.

On a year over year basis, total subscription revenue was up $9.3 million or 3.3% which was driven primarily by the increases to the customer base that we've been able to garner over the second quarter of last year.

Other Commercial Revenue for the quarter totaled $6.1 million which was down $400,000 sequentially, as a result of a dark fiber sale that we had in the first quarter of this year and represented an increase of $2.3 million or about 61% on a year over year basis. And that's as a result of the acquisition of Bluemile that we made in the third quarter of last year.

Other revenue for the quarter totaled $25.4 million that was an increase of $1.5 million or 6.3% sequentially and up $6.8 million or about 36.6% on a year over year basis. Both of which are attributable to the increased ancillary customer billings that we implemented during the second quarter.

And finally as it relates to CAPEX, gross capital expenditures for the quarter totaled $72.3 million. During the quarter we had an increase in CAPEX related working capital payables that totaled $7.2 million so that was an offset, a positive offset to the capital amount.

So our statement of cash flows shows total cash outlay related to CAPEX during the quarter of $66 million which is an increase on a sequential basis of about $13.1 million due to the timing of projects during the quarter and as our capital spend gets off of and moves out of the planning phase out of the first quarter into implementation phase during the second and third quarters.

So that concludes our remarks. And I'll turn it back over to (Stephanie) now to open it up for questions.

Operator: Certainly. At this time if you would like to ask a question, please press star then the number one on your telephone keypad. We will pause for just a moment to compile the Q&A roster.

Our first question comes from the line of Mike Pace with JP Morgan. Your line is open.

Mike Pace: Hi, thanks. Good morning, guys. Question on the South Dakota sale, I guess of the 262 gross so will you be paying any taxes on that or can you shield that entirely?

Steven Cochran: Yes, we have enough NOL to offset that completely.

Mike Pace: OK. And then what is the EBITDA multiple that you sold that for?

Steven Cochran: It went for 8.2 times 2013 EBITDA.

Mike Pace: I'm sorry, what was the multiple in this?

Steven Cochran: 8.2 times 2013 EBITDA.

Mike Pace: OK. Thank you. On the operating cost line item I guess that came in the little higher than what we were thinking, I'm just wondering I'm assuming this is largely programming but can you just add a little more flavor on that and was there something, were there any affiliates agreements that were redone during the second quarter or was that all done in Q1?

Steven Cochran: Yes, the big one, Mike, was Viacom that was out there and we ended up with almost 40 percent or 42 percent increase in that account by itself so that was the biggest driver of it and then some staffing costs as we continue to ramp up on the commercial side.

Mike Pace: And anything in the second half of the year related to those affiliate agreements coming up?

Steven Cochran: Yes, there are two others. ESPN/Disney deal expired August 1st and we just renegotiated that deal. You know it was in line with what we budgeted. So there's not a big shot to our budget, but from a quarter increase you'll see some associated with that and the, I believe, it's our Scripps deal expires at the end of September.

I think once again I think based on where we are we feel that's going to come in line with we had budgeted for that. And that's not nearly as impactful as the Disney deal or the Viacom deal for that matter.

Mike Pace: And then just on the rate increases that you guys are doing this year, I guess you do one in January, you have a small ancillary increase in the second quarter and another sports tier increase in Q3 so I'm just wondering if you look back over a your history, have you ever had three – two or three different rate increases during the year and when it came time for that third one or last one, was there bigger impact then you might have thought so…

Steve Cochran: Yes and just for clarification too – the ancillary fee doesn't necessarily hit everyone. It hits segmented people, people who are using certain things, people who are in our service protection plan, those kinds of things. So it doesn't hit everybody.

The sports tier we're actually only implementing in the Southeast markets now and will probably roll out, or we will roll out as part of our overall rate increase but we felt that the timing of that was acceptable given that we're carrying the SEC network which was pretty highly demanded in the market.

And so, so no we haven't done three in the year, we have done at least, we've done at least two where its similar to this, where you did a rate increase and then you change some other fees and services and so we don't have the third one but like I said the third one is at least a little bit more well received than some might be because of the nature of what it is and what it's for.

Mike Pace: Got you. And then last one I guess back to my first question. You know do you have any other assets that you might consider parting ways with I guess on flipside to what you're looking at the other small acquisitions maybe in the commercial space?

Steven Cochran: I would say - I mean do we have assets we could sell? Sure. Are we actively engaging in that? No we're not. You know we had a couple people actively approach us on and there is really not a desire to sell right now.

I think from a standpoint of from the liquidity if we had a great opportunity and one of the liquidity you'd be able to do something we definitely we have assets that we could sell to do that but we're not in any kind of active discussions to do anything right now.

We do continue to look at small acquisition opportunities. We look at commercial services opportunities as well as those kind of small more tuck in type things where we see them fitting in because of the geographic synergy we would get.

Mike Pace: Sure. And I'm sorry you saw proceeds from the Dakota selling? I forgot to ask that one?

Steven Cochran: There is no specified use of proceeds at this point. You know we - like I said continue to look at some small acquisitions and are hoping we have the opportunity to re-deploy some of those proceeds into those acquisitions but otherwise there's not a specific use for the proceeds.

Mike Pace: Is there a period of time or you'd have to pay down bank debt if you don't…

Steve Cochran: Yes, we have a year that we have to do it. I mean, clearly, if we don't see something coming, we would do it sooner than that but if we feel that we have some real acquisition opportunity or something that it seems that at the least there's a decent chance of doing it and then we'll probably hold on to it and so we get that chance.

Mike Pace: Thank you.

Steven Cochran: Sure.

Operator: Again, if you would like to ask a question, please press star and the number one on your telephone keypad. Our next comes from the line of David Phipps with Citi, your line is open.

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Operator: Our next question comes from the line of Michael McCaffery with Schenkman Capital. Your line is open.

Michael McCaffery: Hey, guys. Can you just update us on where you are or as far as synergy from the original deal with Knology and any additional cash expenses that are still to be incurred as part of that?

Rich Fish: Yes. We have about at the end of the second quarter we have about $6 million, roughly, in unrealized synergies that are still left to come in to the P&L.

So we have, in total, identified total synergies related to Knology as well as adding in the small amounts from Bluemile and Anne Arundel we've got total annualized synergy impact of approximately $56 million so about $6 million of that is still unrealized at this point.

We think we have roughly about one and a half year payback on that relative to the cost of integration/implementation. So, we should see by the end of this year cost of integration should be kind of winding down by the end of the fiscal 2014 into early 2015.

Michael McCaffery: And is that entire – is that $56 million is that largely OPEX or how much is that is CAPEX?

Rich Fish: No, that's exclusively OPEX and SG&A.

Michael McCaffery: OK, great. Thank you.

Steven Cochran: Thanks Michael.

Operator: Our next question comes from the line of Jonathan Lavine with Neuberger Berman. Your line is open.

Jonathan Lavine: Thanks. I may have missed this I was wondering, did you provide RGUs for the South Dakota assets sell?

Steven Cochran: We did not. It's approximately 110,000 RGUs.

Jonathan Lavine: Can you break that out?

Steven Cochran: I don't think we really should from the buyer's standpoint. I mean we – same way that we don't disclose our own kind of independent market stuff you know for competitive reasons I wouldn't want to do that for those guys either. They're, you know, going to be in competitive markets with MidCo Mediacom and Charter as they move forward.

Jonathan Lavine: OK, thanks.

Steven Cochran: Sure.

Operator: Again, if you would like to ask a question, please press star then the number one on your telephone keypad. Your next question comes from the line of David Phipps with Citi. Your line is open.

David Phipps: Hey, guys. Sorry about that earlier.

Steve Cochran: I thought we had answered your question Dave.

David Phipps: Yes, I had the phone on mute sorry. This is (inaudible) on behalf of David Phipsps by the way. Just a quick question on ARPU. You guys could give some more color in terms of video or creative the trend their growth sequentially because it looks like it is, is it going to sequential growth going forward.

Rich Fish: Yes. ARPU for the quarter was up a little over three dollars. The components of that, David, were we kind of break it into the subscription ARPU which is tagged to total subscription revenue line item and then in total. So at the total subscription in line item ARPU was up a little bit over to two and a half dollars.

And the increase in other was approximately sixty cents. So the total increase in ARPU was three dollars and roughly fifteen cents something like that. So ARPU trends within the year generally follow a fairly consistent pattern on a historical basis which is to say that in the beginning of the year as the customer rate increases are effected in the first and the second quarter we experience an increase in ARPU.

And then throughout the balance of the year there is continued pressure, downward pressure on ARPU as we are churning out legacy embedded base customers which may have higher ARPU and replacing them with acquisition pricing customers which are lower than the embedded base. So that's a fairly consistent historical trend and not one we would expect to be significantly different this year into next year.

Steven Cochran: And I'd say one other thing that may move it a little bit so we continue to move up market on the commercial side. We're starting to see nicer sized sales that will help with ARPU a bit, obviously that's pretty small piece of overall revenue so it doesn't have a huge impact but should help.

David Phipps: Got it, thank you. And also, was the mix of video vs. high speed data different at South Dakota from the WOW average. You know what I mean just to get an idea…

Steven Cochran: It's a little more skewed to – because there's some ILEC in there. It's a little more skewed on the phone side and so – but not hugely different.

David Phipps: Got it and you know for CAPEX for the rest of the year, is there any incremental CAPEX that we should think about or is it going to be in the 120ish million range for the rest of the year?

Steven Cochran: 120 is that compared to what was in the first half of the year?

Rich Fish: For the balance of the year, David is that your question?

David Phipps: Yes.

Rich Fish: Yes, we'll see an elevated amount of CAPEX in the second half relative to the first simply as, it's just a timing when projects kind of move from the planning and the permitting stage really in the first quarter is always is the lowest and then the second and the third it really picks up as the projects move in to full implementation.

So second quarter we're higher than or second half of the year rather, excuse me, will run higher than first half.

David Phipps: OK. And lastly just on the HSD side, the sub-growth, first quarter you say was mostly product improvement driven. Is that the same case in the second quarter or was that – how much was from the AAB? Can you give any idea?

Steven Cochran: As we said, we don't disclose the market specific impact of anything. That market in particular we're competing with Verizon and Comcast so we don't like to sit and talk about those specific numbers but in general what we're seeing is much better growth and just HSD only customers we're having a pretty significant impact on that base.

The number of those customers are improving or are increasing at a pretty good pace. So I don't think it has anything to do with the product – I think we're just seeing growth and I think that growth that we're going to continue to see because of, just because of the usage and the need that people have for it and just continue to drive penetration overall as new customers come on board.

David Phipps: Got it, thanks a lot guys.

Steven Cochran: Sure.

Operator: OK. If you would like to ask a question, please press star one on your telephone keypad. I'm currently showing no further questions at this time, I'll turn back the call over to the presenters.

Steven Cochran: Well, thanks everybody for participating. I hope you enjoy the end of your summer and looking forward to talk you next quarter. Thanks.

Operator: This concludes today's conference call, you may now disconnect.

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