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LEAP - Q2 2007 Leap Wireless International Earnings Conference Call

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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to the second quarter 2007 Leap Wireless International conference call. My name is Katina, and I will be your coordinator for today. At this time, all participants are in a listen-only mode. We will conduct a question-and-answer session towards the end of this conference, at which time you may press star-one on your touchtone telephone to participate. (OPERATOR INSTRUCTIONS). As a reminder, this call is being recorded for replay purposes. I would now like to turn the presentation over to your host for today's call, Ms. Jeanie Herbert, Director of Investor Relations. Please proceed.

Jeanie Herbert - *Leap Wireless International - Director of Investor Relations*

Thank you Katina. Good afternoon, and welcome to Leap's second quarter 2007 conference call. This call is being recorded and will be available for play back in the U.S.,through the close of business August 14th by calling 1-888-286-8010. Callers from outside the U.S. will need to dial 1-617-801-6888. The pass code for both calls is 20884537. This conference call is also being webcast live, and will be available for replay on the Investor Relations section of our website, at www.leapwireless.com throughout September 7.

Joining me on the call today to discuss our second quarter results are Doug Hutcheson, our President and Chief Executive Officer and and Amin Khalifa, our Executive Vice-President and Chief Financial Officer. Following our prepared remarks, Katina will come back o line with instructions for the Q&A portion of the call. Al Moschner, our Executive Vice President, and Chief Marketing Officer and Glenn Umetsu, our Vice Executive Vice President and Chief Technology Officer will join Doug and Amin for the Q&A session.

As used in today's conference call, existing markets refers to the company's markets in operation as of December 31, 2005. New markets refers to those markets launched or acquired after December 31, 2005 but does not include any Auction 66 markets. During our call today we will discuss some non-GAAP financial measures. For a GAAP reconciliation of non-GAAP financial measures please see the financial reports page of the Investor Relations section of Leap's website, at www.leapwireless.com.

Statements made today that are not historical in nature include statements about future events and performance and statements including words like, expect, plan, intend, and similar terms, are forward-looking statements. Our actual results could differ materially, from those stated or implied by such forward-looking statements. Factors that could cause actual results to differ from our forward-looking statements are detailed in the section entitled; risk factors, included in our annual report on Form 10-K for the year ended December 31, 2006, and in our other publicly filed reports including our Form 10-Q for the quarter ended June 30th, 2007, which we plan to file shortly. With that, I now want to turn the call over to Doug.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you for joining us this afternoon. As we complete the first half of 2007, we have crossed two major milestones in the plans we outlined back in 2005 to double the size of our business. First this quarter, we completed the launch of our remaining new markets bringing the business to nearly 51 million covered POPs. While that itself is a significant accomplishment, more importantly, this quarter, our new markets in aggregate, began to contribute positive adjusted OIBDA, even though the average weighted life of these markets is less thatn ten months at quarter end.

Also in the second quarter, we have several additional major accomplishments. The company launched new service plans across most of our markets, which were well received by both new, and existing customers. To enhance customer value, and give us a continuing attractive competitive position, we added three unlimited text picture and instant messaging to all of our service plans. We completed a senior notes offering that raised approximately $71 million in proceeds and in June, the company held its first Analysts' Day in many years outlining our plans for the future. Throughout today's call we will be highlighting and reinforcing some of the key topics that we discussed at that meeting.

Second quarter results demonstrate our continued ability to move our business ahead in a focused manner. In terms of our performance, we added 127,000 net customers during the quarter, more than double the amount we added in the second quarter of 2006. Of significance is the fact that we grew net customer additions in the existing markets by 30% in the first half of the year, when compared to the same period last year. Service revenue reached approximately $350 million driven by an increase in weighted average customers, and continuing growth in ARPU. And our adjusted OIBDA for the quarter was approximately $115 million, driven not only by our performance in the existing markets, but by the contribution from our new markets.

The progress we had made in our business is further demonstrated in our results for calculated contribution per user. CCPU, is a measure of customer economics, that demonstrates the approximate net margin we realize per customer, each month. For the second quarter CCPU was $17.84 an improvement of approximately $1.18 from the second quarter of last year, even as we supported the costs associated with expanding and optimizing the company's footprint. Our existing market CCPU was $20.37. An improvement of $2.05 from the prior year quarter. As we discussed today's results, this quarter represents an important transition point for the business.

Now that we've completed our new market launches, and these markets have begun to contribute positive adjusted OIBDA in the aggregate, this will be the last quarter, in which we will separately characterize the results of our existing markets, and our new markets. As we said at our analyst day, 2007 is a year of optimization for our company. Our focus is to increase the opportunity for growth, by continued efforts to provide high-value service plans, expanding coverage in our operating markets, moving ahead on the Auction 56 build-outs and evolving our higher-speed data offerings, all while maintaining relentless attention to our cost leader position. In our outlook today and going forward, we'll provide insight into the impact and contributions that these activities will have on our business. After Amin reviews our financial results, I'll return to customer activity, provide an overview of our major new initiatives and update on our outlook. Amin.

Amin Khalifa - *Leap Wireless International - CFO, EVP*

Thank you, Doug, we are pleased with our second quarter results. We completed the new market launches and believe that we have put a growth engine in place, for our business. As you look at the optimization opportunities, and potential growth ahead, we believe that we are in a good position for continued success.

Through mid-year, the company continues to deliver improving adjusted OIBDA, robust customer growth, and improved margins. Second quarter service revenues were $350 million, up 52% compared to the same quarter last year. The increase was driven by two key factors. First, a 45% increase in weighted average customers, from new market launches, and existing market growth. Second, a $2.16 increase in ARPU, over the prior year quarter, due to strong uptake over higher end service plans, and our return to pay-in-advance billing, for new customers.

Equipment revenues for the quarter were $43 million, an increase of 16% or $6 million, compared to the same quarter last year. Increased revenues from a 68% increase in handsets sold, were largely offset by increases in promotional incentives for customers, and an increase shift in handset sales to our exclusive indirect distribution channel. Cost of equipment was $81 million, an increase of $29 million over the second quarter of 2006, due to the increase in the number of handsets sold. Cost of service for the quarter was $90 million and decreased by .5% as a percentage of service revenues over the second quarter of 2006. Variable product costs increased by 2.3% of service revenues, due to increased customer usage of our value added services. We expect that this trend will continue as more customers choose our higher-end service plans, and we also expect the increased revenues from these plans, will more than offset the increase in variable product costs.

Network infrastructure costs declined by 2.1% of service revenues compared to the prior year quarter. Primarily because of reduction in liabilities for self site remediation costs, and the benefits of scale. During the quarter, we negotiated amendments to agreements, which reduced our liability for the removal of certain of our cell sites at the end of the lease turn. This change resulted in a net reduction of cost of service, of $6 million or 1.7% of service revenues, and will also slightly reduce go-forward network expenses. Sales, marketing, and general administrative expenses were $113 million in the aggregate, and decreased by 3.4% as a percentage of service revenues over the second quarter of 2006, due primarily to the reduced market launch expenses, benefits of scale from our new markets, and increasing revenues.

Stock-based compensation expense before tax, was $6 million for the second quarter of 2007 compared to $5 million for the second quarter of 2006. We delivered $115 million of adjusted OIBDA, up from $78 million in the prior year quarter, and up from $81 million in the first quarter of 2007. Reflecting expected improvements, as we grew our business and generated positive contributions, in the aggregate from the newly launched markets.

In the second quarter our new markets delivered $3 million of adjusted OIBDA contribution, and we expect that to continue to grow in future quarters. Operating income for the quarter was $37 million, compared to operating income of $16 million for the second quarter of 2006. The increase in operating income from the prior year quarter, primarily reflects the increase in our revenues, and the leveraging of our operating expenses for the benefits of scale.

The company achieved net income of $3.2 million compared to net income of $7.5 million for the corresponding quarter of the prior year, reflecting the impact of higher interest expense associated with financing activities, and higher income tax expense. Compared to the net loss of $8 million in the first quarter of 2007, net income in the second quarter improved by $11 million, diluted earnings per share for the quarter was $0.05. In terms of capitalized interest and tax for 2007, our capitalized interest for the year should be between $45 million and $55 million which has been included in our capital outlook.

Our projected tax expense for the year is estimated to be between $40 million and $48 million assuming we adopt a potential change in tax accounting method that I'll describe in a minute. This amount consists primarily of the deferred tax effect of the amortization of wireless licensed tax and good will. Similar to prior periods we project that our cash taxes will be minimal. We continue to record a full valuation allowance on our deferred tax assets. At June 30, 2007, the company has cumulative pretax income of approximately $50 million, since our emergence from bankruptcy in August of 2004. Accordingly, we will continue to closely monitor the positive and negative factors concerning the likelihood that our deferred tax assets will be recovered, to determine whether the valuation allowance, should be released.

We expect to remain at near breakeven from a pretax income perspective for the remainder of 2007. We are currently evaluating a change in tax accounting method, which would accelerate certain tax deductions related to the amortization of wireless licenses and increase our net operating loss carry-forwards, we, expect to complete our analysis of the potential tax accounting method change, during the third quarter. Do to this potential change, deferred tax expense, and net loss may increase in the second half of the year.

Capital expenditures were $106 million for the second quarter, primarily due to ongoing investments associated with operating our business, continuing build-out of our new markets, implementation of data network upgrades to EV-DO and capitalized interest of $11 million.

Now, let's review our key operating metrics. In the second quarter ARPU was up 5% over the prior year quarter, to $45.13. We saw customer migration to our $50, $55 and $60 service plans with approximately 90% of all new customers this quarter, adopting the $45 and above service plans. As a result, build ARPU for new customers, increased 8% from the prior year quarter. However, this growth in new customer build, ARPU, was somewhat masked by the seasonal rhythms in our business, and the impact of customer deactivations, associated with less tenured customers added in our recent market launches. The company disconnects customers 30 days after a bill is due but not paid, for service. One of the shorter periods for wireless carriers. The company does not recognize revenue associated with the bill until payment has been received, and services provided to the customer, because customers who have not paid their last bill, and have yet to disconnect service are included in our calculation of weighted average customers, ARPU tends to appear lower during those quarters which we have significant disconnect activity. The effect is likely to continue through the rest of 2007, masking the underlying improvement we expect to see in ARPU, over time.

With the launch of the Charleston, Rochester and Raleigh markets in the second quarter, our customer acquisition expenses were as expected, at $180. As we move to the third quarter of 2007 we expect CPGA to be about $180 again, reflecting the normal seasonality of our business. We achieved the cash cost per user or CCU of $19.55 for the second quarter which included $1.39 in operating costs, associated with new market development. Compared to the prior-year quarter, CCU in our existing markets was relatively flat. During the quarter we experienced increasing leverage in our operating expenses from customer growth, any benefit from the reduced remediation liability discussed earlier, offset by the increase in the variable product costs from our value-added services.

Going forward we continue to expect our CCU and coming quarters to benefit from the advantages of scale from the newly launched markets offset by the costs associated with increase customer use of these value-added services. We expect CCU to be about $21 for the third quarter of 2007. On the network and systems front, our business planning for Auction 66 is nearly complete. In fact, we recently signed agreements with infrastructure providers for both our Auction 66 markets, and existing footprint expansions. We expect to launch between 20 and 28 million new covered POPs in 2008, including both the planned coverage expansion, and Auction 66 market development. We continue to expect capital expenditures associated with the Auction 66 buildout, to average $28 or less, for covered POP.

We build our networks for efficiency and capacity and we are now prepared for the increased opportunities in data services. EV-DO capabilities embedded in our networks, and can be launched once, applications and devices are available. We completed a major upgrade to our enterprise resource planning system during the second quarter which included improvements in our procure-to-pay, and asset management functionality. This significant project was completed on time, and budget.

Other systems are also undergoing enhancements for the growth ahead, including our reporting and activation systems. We also continue to review long-term solutions, for our billing system. On the liquidity front, as of June 30th, 2007, total unrestricted cash, cash equivalents and short-term investments were $685 million, an increase of $356 million, during the quarter. After adjusting for the $371 million in proceeds from our offering of senior unsecured notes in early June, we generally broke even, on cash generated, during the period. All in all, the company's performing well, while we are preparing to double our covered POPs beginning in 2008. I would now like to turn the call back over to Doug.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you, Amin. We continue to operate in a very competitive industry, something we reflect upon daily. Last April, we again led the industry by offering free text picture and instant messaging, in all of our service plans to fill our customers' voice, messaging, and data needs. Even as we've seen other unlimited concepts for voice and messaging spread with the industry, we continue to make progress in driving further value, and bringing new customers to our business.

Also, we believe the business has, to date, absorbed the effects associated with financial pressure on sub prime (inaudible), and rising gas prices. However, we do not discount the potential future impact of these factors and continue to monitor macroeconomic trends as we have in an economically sensitive customer base. We continue to operate on the basis that we'll be opportunistic during those time periods where net customer additions are readily available and we'll be patient in other periods, when conditions indicate customer activity may be reduced.

In the second quarter, over 127,000 net new customers selected our services. A 112% increase over the 60,000 customers added in the second quarter of 2006, after adjusting for the sale of Toledo and Sandusky, Ohio. Net customer additions in the second quarter from new markets, totaled approximately 115,000, 121% increase over the same period last year. The existing markets added nearly 12,000 net new customers in the second quarter, and approximately 60% increase over the previous year quarter, and a approximate 30% increase year-over-year for the first half of the year. As we look to third quarter of 2007, we again expect the business to experience its normal seasonality with respect to gross additions, and to be further influenced by increased customer deactivations. These expectations are in contrast to the third quarter of 2006, when we enjoyed the benefits of a large number of new-market launches, such as Houston, San Antonio, Austin, Louisville, Lexington and Cincinnati. As a result we expect net customer additions in the third quarter of 2007, to be in the range of 40,000 to 120,000. Turn for the second quarter, was 4.3%, up by 0.7% from the prior year quarter, and in line with our expectations based on seasonality, upgrade activity, and our increasing number of less-tenured customers. Over the past year we have noted that we expected churn to increase, and the business would over time, return to more traditional levels.

Most recently at our analyst's day we provided additional information regarding the two principle reasons for this trend. First, we continue to see customers upgrade their handset by buying a new phone, activating a new line of service and let their existing line of service lapse. Which accounted for 0.4% of the 0.7% increase. We expect this trend will continue for several additional quarters, and believe that this upgrade activity is a positive for the business, since these customers choose to stay with Cricket. As previously disclosed, we are implementing a new customer lifetime value management system, later this year. This system will provide the business with additional information, and customer management tools, that we can use to both manage and direct this customer upgrade activity.

Second, the large number of new customers from our recent market launches has resulted in a significantly less tenured customer base. In fact, average customer tenure has dropped by approximately 20% since the second quarter of 2006. We recently provided information about the deactivation characteristics of our customers by tenure, and highlighted that lower tenured customers have up to double the deactivation rates, of some of our more tenured established customers. The increase in churn that we reported today, is a direct byproduct of the success we enjoyed in our newly launched markets, and the addition of correspondingly less tenured customers. To the degree that new customers follow the patterns of customers who have been with the business over the past several years, we anticipate that churn from these customers will decline, as the newly launched markets mature. Viewed with that backdrop, the business continues to see core churn improve, which we believe that indicates that our efforts are addressing many of conditions that we have discussed that may cause churn.

As we look to the third quarter, we expect churn will be between 4.9% and 5.4%, and we would summarize our expectations for churn with these three observations in mind. First, consistent with normal seasonal rhythms, Q3 is typically our highest churn quarter. Second, we anticipate an increasing number of customers who will upgrade their handsets by buying a new phone, activating a new line of service, and let their existing line of service lapse. Third, the business will continue to absorb the increased churn from the large number of less tenured customers added from our new market launches. We expect churn to trend downward again as the new markets mature over the next several quarters. However, once our new Auction 66 markets reach critical mass, we may see the effect of less tenured customers deactivating at a higher rate for some time period with their launches.

The company recently outlined several significant initiatives, including our coverage expansion, Auction 66 new market development and efforts around our higher-speed data service offerings. The company expects to add nearly 600 new cell sites over the next year, to expand coverage to better meet the needs of our customers. We expect that this will not only lead to additional new customers, but will also help reduce churn, and lower the cost of off-network calling. For certain markets, these expansion plans represent the first major coverage enhancements since the market's initial launch, over five years ago. The expansion process we have deployed will be disciplined and thoughtful, and as we demonstrated on previous significant investments. As to the 110 million of new license POPs that we in Denali purchased in Auction 66, and the overlay of additional 10 megahertz of spectrum in many of our markets for data offerings, we have set the stage for another significant round of expansion. We now have spectrum in 35 of the top 50 markets. The highest number of any carrier in the unlimited space. We estimate that our Auction 66 spectrum portfolio includes up to approximately 85 million incremental covered POPs in markets suitable for our service.

Approximately 50 million that we are currently developing plans to build out, and another 35 million which may be developed in conjunction with others. As I've said before our Auction 66 markets reflect the characteristics of our better performing existing markets, including, first an appropriate footprint either on a stand alone basis, or in close proximity to other markets. Second, ethnically potential customer base, and third, attractive employment prospects. As a result, we expect to achieve attractive terminal penetration rates in our new markets. Rates that we expect to be similar to the rates that may be achieved by others who operate our business model. However, we believe that predictions of long-term penetration rates should not be the focus of investors, as there are significant opportunities and challenges, that will need to be resolved before we reach terminal penetration.

We expect to continue our focus on the business we had built and on the development of new markets over the next several quarters. We will concentrate on our execution to ensure that the new markets are launched on time and budget, and that they contribute to building the company's financial performance. With respect to Auction 66 spectrum clearing, we continue to await information from their government, regarding how their current usage of the spectrum will be transitioned or eliminated. While we do not have comprehensive details at this point, and continue to work at all levels to obtain the information, we are making progress. We believe that we have improved visibility regarding the availability of the cleared spectrum, allowing us to move ahead, with our planned market launches in the first half of 2008. Additionally we have seen further progress on the development of AWS capable handsets and are working together with our suppliers, to develop an attractive portfolio of handsets, also set for the first half of 2008. As a result of these developments and reflected in our outlook, we have begun to increase our activities to move ahead, on our planned Auction 66 build-outs.

The final initiatives we recently discussed is our initial efforts to develop higher-speed data products. Over the past two years, the company has seen substantial benefits from our continued effort to provide data services. Another recent data-related success involves our introduction of ringback tones, in early July. While it is still early it appears we will have achieved industry typical penetration levels, for this product, within the first month of launch.

We expect to launch additional data services in the second half of the year for our customers. Another development in the higher-speed data area revolves around our introduction of a broadband product. This summer we began trials, and this fall we expect to begin a more extensive market test to increase our understanding about customer needs. As always, we intend to follow a disciplined approach as we determine the viability of this product offering and decide if and when, we will offer these services in additional markets. At this time we have not yet determined the extent of our participation in the 700 megahertz Auction which is now expected to occur in January of 2008. We're studying last week's FCC order regarding the Auction, and evaluating its effect on our decision to participate. We expect to update you on our the plans for the Auction at our next conference call.

Let me turn to our outlook for the third quarter full-year 2007, and for the first time our initial outlook at 2008. We will now report on a combined basis a results for all the markets in operation at the end of the second quarter of 2007. As we discussed our outlook, we will report the performance of the major initiatives we're developing, similar to what we have done over the past several quarters, with Auction 58 and related new markets. The major new initiatives included, are planned coverage expansion, Auction 66 market development and the new higher-speed data product discussed.

In our earnings release today we provided an adjusted OIBDA outlook for the third quarter, and outlined our initial perspective on the financial effects of our initiatives. We expect third quarter adjusted OIBDA will between 110 and 120 million for our operating market, reflecting the continued improvements year-over-year and or average weighted customers, and improvements in ARPU from service offerings. This outlook does not include 10 million to 15 million in negative adjusted OIBDA that we expect to incur in conjunction with major new initiatives. Taking into account the effect of these initiatives, we expect total company adjusted OIBDA to be 100 million and 110 million for the quarter.

Looking ahead for the full year 2007, adjusted OIBDA is expected to be between 430 million and 460 million for our operating markets. Again, this outlook does not include 25 million to 35 million in negative adjusted OIBDA we expect to incur in connection with these major new initiatives. Taking into account the effect of these plans, we expect total company adjusted OIBDA to be between 400 million and 430 million for the full year. Next quarter and thereafter, our outlook will include costs associated with these major initiatives.

Capital expenditures for 2007 are expected to be 280 million to 320 million for the existing business. The costs associated with our launched markets to date, and the EV-DO network upgrades. In addition, the company expects to invest 200 million to 250 million to support the major new initiatives we have outlined. Therefore, including total 2000--therefore, total 2007 capital expenditures are expected to be between 480 million and 570 million including capitalized interest.

Today we provided our first outlook for 2008. We anticipate further adjusted OIBDA growth from our existing business, with some of our growth, offset by the effect of the major new initiatives. We expected adjusted OIBDA will be between $550 million and $650 million, which includes the impact of the planned coverage expansion, and Auction 66 market launches. This outlook does not include any impact at the higher-speed data service offerings beyond the initial trial markets launched in 2007. We expect capital expenditures to be between $650 million and $850 million in 2008. Including the investments associated with our existing business, the coverage expansion, the Auction 66 market launches and the initial higher-speed data service trials. This excludes capitalized interest.

In closing, we expect to continue to enhance our value proposition by introducing expanded functionality, and capabilities into our service offerings, that meet our customers' needs. As we said time and again, unlimited is our monitor and it drives our brand promise. We expect to achieve continuing customer growth, and strengthening financial performance in the coming quarters as a result of a persistent and disciplined approach of meeting our customer needs. We have completed a major set of milestones around the business expansion that we just started over two years ago. With the new initiatives outlined today, we're poised for continued growth. I want to thank our employees, partners and suppliers who have helped us achieve this success, and are supporting our future efforts. I would now like to turn the call, over to our conference call host, Katina, would you please come back on the line to review instructions and open the call for Q&A?

QUESTIONS AND ANSWERS

Operator

Yes, sir, and thank you. (OPERATOR INSTRUCTIONS). Your first first will come from the line of Romeo Reyes, representing Jeffries. Please proceed.

Romeo Reyes - *Jefferies & Company - Analyst*

Good afternoon. Couple of quick questions here. First, with respect to Q3 churn guidance, if you give us a sense of, you think, that jump between Q3-- Q2 and Q3 seems fairly dramatic here. Give us a sense of how much of that is handset upgrades, and also just the fact that you have less tenured customers, and I guess the third element, would be the seasonality. I don't know if you can break out the delta in those three buckets, but that would be very helpful. Secondly, with respect to the 2008 guidance on EBITDA-- or OIBDA, rather--how much of new initiative new EBITDA burn are you anticipating from those 20 or 28 million POPs that you expect to launch? Should we assume most of those are launched towards the latter half so there isn't a lot of burn associated with that. If you can give us more color, that would be helpful.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Sure, let's start, if you want to look at churn year-over-year. You know, second quarter was up about 0.7 year-over-year. If you look at where we're at for third quarter, and you look at where we're at last year, versus this year, it is fairly close in the same range. We think we'll see a little bit more upgrade activity, and we'll see that continue for a little bit longer. And then we'll continue to work through the subscribers associated with less tenured customers. We think that will probably take another three or four sometime in the middle of next year, when you will really see that mature its way through. So I think you see a jump that is similar to what we saw in second quarter, and we expect to see that in the third quarter. And it's consistent, with what we've expected to see. We've flagged that we would see higher churn, as these younger customers come on, as we move ahead.

As far as OIBDA, we expect that the new initiatives, and we'll update this, so this is an approximation, represent about $100 million related to the launch of new Auction 66 markets. Now, that probably has a fair amount of range. We actually think we'll see some launches in the first half of the year, and remember, we tend towards seeing a fair amount of the burn, associated with new market launches fairly quickly after launch. And so we're expecting that we'll move through a fair number of POPs as we move through the year.

Romeo Reyes - *Jefferies & Company - Analyst*

Okay. And then just a quick follow-up. On Q3 ARPU, for either Amin or Doug, are you guiding toward lower churn, I'm sorry, lower ARPU for Q3, here based on your comments, Amin? You said that you expect the-- as the denominator becomes smaller because some of the customers outlined. Your ARPU has, I guess, lower pressure when you have higher churn periods. As you see that in Q3, would you expect a decline in ARPU, as well?

Amin Khalifa - *Leap Wireless International - CFO, EVP*

No, we do expect that the underlying ARPU is on an upward trend right now as I spoke about before. So ARPU should increase throughout the rest of the year, but the effect will be muted. It won't be as strong as one would expect, because of the calculation with, with the disconnects that we talked about earlier.

Romeo Reyes - *Jefferies & Company - Analyst*

Is it going to be flattish or up on a reported basis?

Amin Khalifa - *Leap Wireless International - CFO, EVP*

It should be up.

Romeo Reyes - *Jefferies & Company - Analyst*

Okay. Thank you.

Operator

Your next question will come from the line of Phil Cusick, representing Bear Stearns. Please proceed.

Phil Cusick - *Bear Stearns - Analyst*

Hi, guys, thanks for taking my question.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hi, Phil.

Phil Cusick - *Bear Stearns - Analyst*

I wonder, first, if we could talk about the macro environment overall. You made a comment in your release about the economic environment. And if you could talk about what you're seeing in terms of sub prime, if anything. And how you see things going forward, just a start?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Yes, it is certainly a lot of people ask about it and one of the comments that I made in the prepared part, is we seem to be comfortably absorbing that. So I don't think that we, at this point, have seen any meaningful impact in that area. We've seen the normal--we've seen some market fluctuation as we watch gas prices move around, but we haven't seen anything that's been materially different, than what we have seen before. So at this point we're feeling like that part is moving through fairly well for us, and don't see large, you know, macro environments affecting us. With that said, we always watch that, and we keep watching, and which is why I flagged that we are part of that environment, and to the degree, there is material changes, it may affect our business.

Phil Cusick - *Bear Stearns - Analyst*

Okay. Second, on the churn side, you break out net ads between the two different types of markets, but you don't break out churn. I wonder if in this case, if we can talk about a relative increase, quarter to quarter, in the core markets. Because the big delta from 1Q to the 2Q in the overall, given your commentary, was driven by, the really big ramp in the new markets, where you've got a younger customer base. Can you give us a relative increase quarter to quarter, from the core markets?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Core markets continue to perform as we have seen them perform typically. In fact, they have absorbed--we went through that--we went through that. They absorbed even the upgrade activity, and performed at about the same level, which is why I pointed out that we've actually seen improvements in our core churn levels.

Phil Cusick - *Bear Stearns - Analyst*

On a year-to-year basis?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Yes. In fact, all of the impact that we're seeing, which is why, at our analysts day we actually put the charts up and asked-- worked through with people. We-- most of the increase you've seen is in the new-- in fact all of the increase you've seen is in the new markets and it's related to customer tenure. And it is why we think it passes, and works its way through.

Phil Cusick - *Bear Stearns - Analyst*

I apologize if you said that. There was a lot of information on that call. And then, from there I wonder if we can talk about the overall-- you talked again, about the relative increase year-to-year and churn from, upgrades. Can you give us some idea as to what you think that is in the overall churn level, and then I'll stop?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, in the first quarter it was a 0.3% increase, and this quarter was 0.4%, year-over-year increase. So it has been a 0.3%, 0.4%, year-over-year increase. And I think, we believe the upgrades are value enhancing, for us. So we have decided, that we have been talking again for the last several quarters, that we wanted to absorb that impact. What we intend to do, is roll out some systems at the point of sale that will give us some new tools that will, you know, allow us to apply some things at the point of sale that might allow us to adjust customer behavior on that. But I think we feel pretty good right now that customers that are choosing to upgrade their handset, and staying with us, we want to continue to encourage that behavior, so we'll be fine-tuning the behavior, not trying to eliminate it.

Phil Cusick - *Bear Stearns - Analyst*

I'm sorry, let me just make sure I asked the question. Can you give us within the 4.3% what you think that upgrade activity actually is?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Total for the period was 0.7%, for the period.

Phil Cusick - *Bear Stearns - Analyst*

So the year ago there was nothing in there?

Doug Hutcheson - *Leap Wireless International - President, CEO*

No, the change from a year ago was 0.4%.

Phil Cusick - *Bear Stearns - Analyst*

Okay. I'm sorry.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Year-over-year change was 0.4%, the total activity was 0.7%.

Phil Cusick - *Bear Stearns - Analyst*

Got it. I guess I'll stop. Thank you.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you.

Operator

Your next question will come from the line of Brad Feldman, representing Lehman Brothers, please proceed.

Brad Feldman - *Lehman Brothers - Analyst*

Thank you for taking the questions. I was hoping you could just clarify some of the comments you made about the cost of service impact, you had, due to revision of your CALA leases. Can you review what that represented? Is that one-time, or is it recurring? And then maybe I'm just curious why you're planning to take some sites down, or if it is just housekeeping, around the contracts?

Amin Khalifa - *Leap Wireless International - CFO, EVP*

Well, what we were talking about was in our contract negotiations, we were able to remove a liability that we had been responsible for, and as you know, we have to reflect the cost of bringing down our equipment from towers, at the end of life, whenever that may be, in the future. And we were able to negotiate some of our leases to remove that liability. In other words, we will no longer have to incur costs sometime in the future to do that. So that's-- that meant our liability was removed from the books and future periods--and that was at $6 million that I spoke about. And in future periods, we'll benefit by several hundred thousand dollars additionally, on reducing that cost.

Brad Feldman - *Lehman Brothers - Analyst*

So is that a couple hundred thousand dollars per quarter, would be lower than it previously would have been?

Amin Khalifa - *Leap Wireless International - CFO, EVP*

Correct.

Brad Feldman - *Lehman Brothers - Analyst*

Okay. Thanks for clarifying that. Separate question. I know you've talked a lot about seasonal patterns. I was hoping you could talk about patterns you exhibit in markets during the periods shortly after you launched them? For example, we've come to learn that shortly after launching to market, you're going to experience a period of very strong growth activation. How long do those periods last? Is it first quarter is very, very strong, and second quarter is a little less, and then maybe 5 or 6 quarters out you hit a period of seasonal activity? Or does it extend longer than that?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Yes, I think, Al, do you want to answer that?

Al Moschner - *Leap Wireless International - EVP, Chief Marketing Officer*

Sure, absolutely. You're absolutely correct. What we see is a strong performance as we initially launched the market, and it takes several quarters to settle out. It varies by market. But I think as a general rule, you know, we see the seasonality impacts come into the patterns about 9-- I'm sorry, 9 to 12 months or three to four quarters out.

Brad Feldman - *Lehman Brothers - Analyst*

Great. Thank you.

Al Moschner - *Leap Wireless International - EVP, Chief Marketing Officer*

Thank you.

Operator

Your next question will come from the line of Simon Flannery representing Morgan Stanley. Please proceed.

Simon Flannery - *Morgan Stanley - Analyst*

Okay. Thank you very much. Good afternoon. Can you first talk about the broadband offerings, and just elaborate a little bit more. Is this intended to be a laptop card type, solution? And, you know, what is your expectations for timing of that rollout. And secondly, coming back to the upgrade issue, what have you learned from your market research about exactly why people are doing this? Is it, that you've brought some very attractive handsets in? And what is the typical time from when somebody has first bought your service, to when they come and upgrade to a new phone? Is it six months or 15 months? What is your research telling you there? Thanks.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Let me take a shot first on the what we're looking at on the higher-speed data. We believe our customers are likely going to be interested in products, including laptops, where broadband service would be available to them. So our expectation is we will be in market trials, late in the third quarter, and through the fourth quarter and we'll just watch that evolve. I think we've done a fair amount of friendly-user trials at this point, to get an idea, and we plan on rolling that out and seeing where that goes. So, we're optimistic. The research says that it is promising, and it is something that really gives us a shot to deliver our cost structure to the industry in another way that is attractive to us, and it is embedded in the networks that we have billed. On the upgrade front, Al, do you want to take that?

Al Moschner - *Leap Wireless International - EVP, Chief Marketing Officer*

Sure. Again, there is a several reasons why customers upgrade their handsets. We call them upgrades, but they come from various sources. One of the primary reasons that customers deactivate, is they have issues with their handsets, either a loss or damage. Others find that their initial purchase didn't quite fit their need from a technology or data perspective, as we are increasing our functionality. They're finding that the functionality that we provide, is something that they would like to pursue. And, again, there is quite a bit of variability around that, but we see customers upgrading as early as six months after their initial purchase, and the range could be as high as 18 months. But the newer markets, our Auction 58 markets, are demonstrating a little bit of a higher upgrade rate than our core markets, and I'm not sure that that is something that we fully understand the difference is not significant, but again the range is anywhere from as early as six months up to 18 months.

Simon Flannery - *Morgan Stanley - Analyst*

Okay. Do you think this will ease after you've obviously brought a lot of data products on line in the last sort of year or two. You'll be able to see this settle down, as--or virtually all the handsets you sell in the next year or so, will be data capable.

Doug Hutcheson - *Leap Wireless International - President, CEO*

We'll see, that is one of the reasons we've been interested in watching this, or introducing the customer lifetime management. What Al said, and I want to make it clear, the one that we had been pleasantly surprised not only by the uptake on our new service plans, by new people joining the company, but the migrations. And so we've seen a lot of, when people come in and they've upgraded, they've also gone on to a new higher ARPU rate plan, which is one of the reasons that we see it as attractive step for the business to take.

So what we will do with the customer lifetime value management system, is that we'll fine-tune. If people want to do a go into a rate plan, we may try to work with them to avoid doing it through a churn-related upgrade. There may be other ways that we can work to provide and meet that customer need. We think it is a net positive, so that is why we have been signaling for the last several quarters, that we're probably going to let this continue, and we'll manage it as we put these new systems in place.

Simon Flannery - *Morgan Stanley - Analyst*

Great. Thank you.

Operator

Your next question comes from the line of David Barden, representing Banc of America. Please proceed.

David Barden - *Banc of America Securities - Analyst*

Hey, thanks a lot. Can you hear me okay?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Yes, we can.

David Barden - *Banc of America Securities - Analyst*

Thanks. Couple questions, I guess. You know, the stock trading off $11 in the aftermarket, and clearly, you know, as typical and as expected as the churn and the subscriber performance in the quarter may have been, I think people are looking back and going, you know, on May 8th, we had a call, there was guidance given. The lowest end of that for a subscriber perspective, was 125,000. Presumably it wasn't the, you know, the target for management to kind of hit this-- the lower end. And I guess the-- you know, we look at the sub prime market, and we see softness there. We look forward to your third quarter guidance, and we see some softening up of the subscriber number, sequentially. And then we have the upgrade issue where, we're having to spend more to keep the same customers, and we're having the costs go up to keep them. So, you know, is there a reason for deeper concern that something about the business model is changing, in this environment? And that rather than higher highs in the first quarter and lower lows in the second quarter, we're going to see lower lows kind of in perpetuity in the model? Or what is giving you guys the comfort level, to give very-- at the higher end pretty good guidance for 2008 on a financial basis? Where does that come from? What are you seeing in the business today, that will let people latch on to that?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, I think it rings through the entire thing. We're pretty positive with what we've seen go on. We've seen the new markets come up to speed. We're seeing attractive customer uptake of the products. We're seeing those customers behave no differently than other new customers, behave. We're seeing poor churn for the reasons other than tenure and upgrade. We're seeing that coming down. We're seeing strong interest in our new rate plans. We're seeing the new programs that we're rolling out likely to continue to provide increased improvement in the expected company performance.

And we're also reflecting that, you know, the seasonality that we've seen in our business, has been here, since its inception, and we go through not only reminding people in Q1, every year, about you know, it is seasonal and good things are happening. We remind people that it is a seasonal business and we find every year we work through Q2 and Q3, and see that business move through. We feel we're doing pretty good. I have to tell you. We're pleased with where we see things going. We expected some of the things that we're seeing to work our way through. All of the information that we've given out today, on our outlook was-- is contained within the guidance that we've expected to see, so we're feeling like we're delivering, what we had expected to come through. We see time periods--I did flag-- we see time periods where, you know, customer activity is reduced, and our experience has been repeatedly that, you know, that we work our way through those, and things come back. I don't know, David, if that helps answer your question.

David Barden - *Banc of America Securities - Analyst*

Yes, thanks, Doug. I guess I want to ask too, if I could, have two follow-ups related to that. If you give a free month to people who upgrade and buy a new phone, that, you know, it may be that process might need to be managed a little better. Six months seems like a pretty short time to give a guy a free month, and then buy a new phone and gets another free month. It seems like the CPGA for those customers might be going up-- I was wondering if you could kind of outline how do you plan to manage this upgrade process? And then--

Doug Hutcheson - *Leap Wireless International - President, CEO*

Al said in his, it could be as early, but he also pointed out, it could go out for quite a bit longer than that, as well. So let's not pick the worst data, and point out that upgrades occur, over a period of time. And think about it, that when a customer is deciding to upgrade , that customer is also in play. And so we certainly would like to see customers, you know, continue to stay with us, so we can advance that. So what we're introducing, the next step that we're introducing on that, is this customer lifetime value, which is introduced at the point of sale, and will be available in all of our branded presence, which is we're nearly 70%, that we see nearly 70% of our-- of our new customers come through those, and I think we're optimistic over a time period that, that will allow us to better manage things. Also, I do want to flag that the company, does tend towards using its guidance ranges. We have exceeded our guidance ranges and such, so the fact that we've used our guidance range this quarter, is not untypical. It is what we have generally done as we have moved through building our business in a thoughtful

David Barden - *Banc of America Securities - Analyst*

I apologize. If I could ask one last one. Given that there is an awful lot of volatility, and maybe misunderstanding about the rhythms of the business, from quarter to quarter, this would be a great forum to give us a picture of, as we look into the fourth quarter, which of these general trends are going to be moving in which direction, to kind of get to the subscriber numbers, which are really the growth driver of the business?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, we typically see net customer additions increase during the fourth quarter. And that's generally because there is both higher gross activity. So front-door activity, and lower churn activity. So third quarter is typically where we see, you know, the reduction in churn, or the peak in churn and a little lower gross activity and then it starts to build back. So we think that all conditions are lined up and will move through the same cycle.

David Barden - *Banc of America Securities - Analyst*

All right. Guys, good luck. Thanks, much.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you.

Operator

Your next question will come from the line of Ric Prentiss, representing Raymond James. Please proceed.

Ric Prentiss - *Raymond James - Analyst*

Yes, good afternoon, guys.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hey, Ric.

Ric Prentiss - *Raymond James - Analyst*

Hello. Couple of questions. Following on a fairly similar theme, I guess. If you look at the second quarter you launched the 3 million POPs, you had Rochester, Raleigh, and a couple others out there. How did you feel about the ads within those newly launched markets within the quarter. Did you see the typical spike up in those?

Al Moschner - *Leap Wireless International - EVP, Chief Marketing Officer*

Yes, we did. We saw the same typical patterns that we've seen when we launched other markets sell. The business performed similar to what we have seen it perform previously.

Ric Prentiss - *Raymond James - Analyst*

Okay. And then on the major new initiatives, the increased footprint , the Auction 66 and the higher data offerings. Can you help us parcel a little bit-- I'm trying to figure out, what about the higher-speed data offerings implies CapEx and OpPex burns, and then looking at more footprint versus Auction 66. Should we use the rule of thumb, $28 per covered POP, and refresh our memory on what's the OpEx burn rate we should expect. Is it in the 5 to 10

Doug Hutcheson - *Leap Wireless International - President, CEO*

What we have typically seen and what we guided to today, is that CapEx is $28 or less for a new covered POP. And that the associated impact to the OIBDA is $5 or less. But generally been in the $5 range. So those numbers are in place, and we are now as a result of the information that we have gotten from the FCC, are in fact, moving ahead. We think we have enough information at this point, to see the channels in our initial market launches that we needed to, so we're pleased, we're seeing good progress. We're ready to move ahead on that, and have the information we've need. The guidance we've provided previously continues to be appropriate, for people to think about that. You know, the data--higher-speed data initiatives are really involved in two markets at this point, where we expect a launch. And what those entail is not only-- is a little bit of a increased capacity that may come in the way of self-identity, but there are operating costs associated with adding some of the backbone around that. And then you have to acquire customers, so there would be CPGA, and marketing expense.

Ric Prentiss - *Raymond James - Analyst*

As far as OpPex and CapEx impacts, higher-speed data would rather be diminimous compared to the other two, I would guess.

Doug Hutcheson - *Leap Wireless International - President, CEO*

That is why we pointed out in our guidance that, all we-- the impact of that is only the initial, and the implication, when you're talking about launching 20 upwards of 28 million new covered POPs, the implication there, with that being closer to 100 million, is that you wouldn't expect a lot-- as much impact from that.

Ric Prentiss - *Raymond James - Analyst*

And then also the guidance for '08 on capital, I think you mentioned does not include capitalized interest, but the '07 guidance does. Any thoughts about why you included in one, and not in the other? I assume you're still going to capitalize some interest even in '08.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, we are, but here's the-- we tipped, you know-- from a utilization of cash, we provided a lot of information historically about our interest expense in total. And so for 2007, we provided additional details today, that capitalized interest. So of that total interest expense, between 45 million and 55 million of that would move through the capital line. What happens in 2008 is still contingent on launch schedules, and so the 2008 number may still move, depending upon how we launch. So the burn, the utilization of cash, is still all on the interest expense line, all we're doing now is giving details for '07, about how that closes out. So if you looked at the '07 guidance, there is $50 million of roughly midpoint of guidance of capitalized interest in it.

Ric Prentiss - *Raymond James - Analyst*

And the final question, speaking of cash and funding, given the plans you've laid out for the second half of '07 and '08, and the cash balance you have on the balance sheet right now, how do you feel about fully funded process? Are you still fully funded for the build program?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, where we're at is we certainly have felt comfortable that on the guidance range that we put out right now for the 20 to 28 that we have, to adequate resources on that, and we also feel comfortable that we have adequate resources to complete launching the remaining POPs by sometime in late 2010, utilizing our own resources. So we'll continue to make progress. We'll let the business build, and then we can take adjustments to either self-fund our way through that, or look at other alternatives, if there is a desire to-- a desire and a reason, to move along more quickly.

Ric Prentiss - *Raymond James - Analyst*

Great. Thanks, guys. Have a good day.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you.

Operator

Your next question will come from the line of Chris Larsen representing Credit Suisse. Please proceed.

Chris Larsen - *Credit Suisse - Analyst*

Thanks.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hi, Chris.

Chris Larsen - *Credit Suisse - Analyst*

Good afternoon. The Auction 66 development, I know you mentioned that it was going to be part of the incremental costs, but I thought that would be capitalized. Secondly, as you look at the new data products, do you feel a need to have incremental distribution, and/or does the ITC band, have any impact on that? And then I have a third question on churn?

Doug Hutcheson - *Leap Wireless International - President, CEO*

The guidance on launching a new market is remain-- remains the same, which is about up to $28 per capital.

Chris Larsen - *Credit Suisse - Analyst*

I'm sorry. I was talking about 10 to 15 of incremental expenses, expected to be incurred in the third quarter?

Doug Hutcheson - *Leap Wireless International - President, CEO*

That is all related to-- we're accelerating coverage, so we're launching up to 600 cell sites, over the next year. And those markets in operation before the middle of 2007. That is what we outlined on our analysts day and we think that is an attractive, value creating potential. And when you launch new cell sites there are costs that are associated with that. Look at 600 cell sites, on the basis of our total footprint, and that is a substantial number of new sites that we will-- I think you'll see a return come to the business fairly quickly. We are moving ahead with 66. We pointed that out. And as a result of that, we started as we have previously, we started to incur costs, ahead of the launches that will happen in the first half of 2008. And we'll give more detail on those launch dates, as we get a little closer.

Chris Larsen - *Credit Suisse - Analyst*

I understood the coverage expansion would have the 10 to 15 of incremental expenses that you're going to incur in 3Q, that that would go in there. I'm just surprised that 66 development would wind up going-- would wind up hitting the income statement as opposed to being capitalized expense.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Well, remember, that there is lease costs already included, as we're starting to develop some markets, and those flow through the P&L. They're part of $5 of operating expense, that we run through the P&L. And so there is no-- it is the same process that we went through on the 58 expansion.

Chris Larsen - *Credit Suisse - Analyst*

Got you.

Doug Hutcheson - *Leap Wireless International - President, CEO*

And, you know, we started to incur costs on that, a couple quarters ahead of when we started to see activity, on launches. And so, I think you're seeing the same process begin, and we have throughout the year pointed out that the Auction 66 expenses we would update, when we start to get comfortable. We have launch dates, and what you're seeing is, that we're starting to get comfortable that we have markets that are going to be ready to launch. You're seeing progress, and optimism on, based on fact, on where we see spectrum clearing progressing. The effect on ITC does cause us to be thoughtful, relative to the devices, and we are doing the same thing that other carriers have done, trying-- working to address the different intellectual property issues, to the degree we want to go ahead with devices that are impacted.

Chris Larsen - *Credit Suisse - Analyst*

Okay. And then in the past you talked about churn going down, as your footprint expands. I wonder if you could talk a little bit about, maybe put some numbers around that, as you see in the 600 cell sites what we might see out of that, as you go from 50 million POPs, to 100 million POPS, what kind of churn reduction you might see there, and then if you were to go from 100 to say, pairing up with somebody who had a similar footprint, what kind of churn reduction you would get out of that?

Doug Hutcheson - *Leap Wireless International - President, CEO*

The first piece--

Chris Larsen - *Credit Suisse - Analyst*

I'm smiling.

Doug Hutcheson - *Leap Wireless International - President, CEO*

The first piece I want to flag is that we're already seeing poor churn, reduce. When I talked about how year-over-year we see similar churn performance in the existing markets, even though we're absorbing the upgrade activity, that gives you a message that a lot of what has been going on is laying good strong fundamentals for us. We're pretty comfortable that as these customers we've added, the 700,000 customers that we've added in the last year, mature. They follow the same profile as the rest of our business. So we have been consistent in pointing out that we expected this year would be higher churn, and then it would come back down as those customers mature.

We have an underlying business that's doing robust and doing well on churn. We see that underlying fundamental advancing, and we see every reason as time passes, that you'll see churn go down.

Now, we also pointed out relative to the new sites, we haven't given Chris specific guidance, but as you would think about that investment, we think you should think about it, not just focused on adding net new gross ad customers, but also we have put a lot of effort into looking for those customers that buy our service, but may not have coverage where they are, where they live, and going ahead and adding cell sites there, and we think that is the driver that gives us confidence that we'll see improved deactivation characteristics and it will affect our tenure curves over time, positively. And then the last piece is always managing our costs, and in this case, it would be a way to manage our off-network calling.

So we haven't given specific numbers. We think it will lead into the continuing decline we've seen in core churn year-over-year, and it will continue to keep that moving ahead. So we think we're on the right track with that and we'll see good benefits.

Chris Larsen - *Credit Suisse - Analyst*

Thanks a lot.

Operator

Your next question comes from the line of Thomas Lee representing JPMorgan. Please proceed.

Thomas Lee - *JPMorgan - Analyst*

Hey, guys.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hey, Tom.

Thomas Lee - *JPMorgan - Analyst*

How are you?

Doug Hutcheson - *Leap Wireless International - President, CEO*

We're fine.

Thomas Lee - *JPMorgan - Analyst*

You know, you know, I think after kind of like seeing some of the investor reaction from the metro PCS quarter, and the reaction to some of your headline numbers, and then hearing all of these investors ask questions about seasonality, and churn, I guess the one thing that's really jumping out at me is that at your Analysts Day, to me, it just struck me as you guys think about your business, I kind of got the sense that a subscriber was less important a metric, in terms of how you view your business, and more about, as you said, up-selling your customer base or driving additional revenues. And I'm just wondering, you know, could you just give us an idea of like-- here we have, you know, almost you know nine out of ten questions focus on churn and unit , what is a better way for us to think about your customer? Because I know in the past you've talked about this CPGA adjusted cash flow per customer. Kind of other metrics, that really look less at the subscriber as a unit, but more as a revenue producer.

A, I'm curious, could you just tell us what you think about, how you create value in your business? And, secondly, is, do you think there might be some logic in the way--I know you guys count customers as customers, and I know metro tends to use ESN phone method as their method for counting customers. Do you think there is a better way to measure your unit and your penetration? Because I think the net adds will be volatile. You have gross adds, and you have churn. Your net is always your original calculation. There is no reason like, and I think it is hard for you guys to have precision of what 3Q ads would be anyway. I would love to hear your thoughts.

Doug Hutcheson - *Leap Wireless International - President, CEO*

I start out every call talking about the, what we call the calculated contribution per user. And talk about how year-over-year that has come up. An example is, in our existing business, with all of the stuff that we've worked our way through, it is up year-over-year, about $2 or 10%. Now, that's applied across all customers. Not only the new customers, but the-- our existing customers. And so we focused on providing products and services, that allow us to meet their needs, and in the process we've typically seen that they have actually improved our competitive positions.

So those pieces are in place. They're working well for us, and expect them to continue. And it also shows the results of how we have optimized our cost structure. Talked about year-over-year existing business growth went up 30% on new customer additions, so we see momentum, in not only the margins that we're making per customer, but we see momentum in improvement in the rate that we're adding customers, so we think there is good progress being made by the teams there, as well. So those two tell us that the growth engine that we have over time for OIBDA, seems to be intact, and moving ahead.

On the new markets, in 10 months-- 10 months weighted average time period, they broke even. That's well inside typical time period that you would see with others. And we see them moving through the normal rhythms, both of how customers mature, and how our business has this seasonal rhythm where we tend towards adding more customers in the fourth, and the first quarter. And so, again, we-- and we're watching those go from in less than 10 months, going from consuming cash to contributing profit. Or OIBDA margin.

So I think that's-- we have two levers that we're always focusing on, and how do we drive the increased margin, and how do we drive increased customers. I would point out also, that the that the build ARPU, the people walking in the door over--went up in the second quarter year-over-year 8%. So we're pretty comfortable that the new rate plans that we have are robust, they're working well for us, and that 90% of our customers chose the $45 and higher rate plan. So that's why we feel comfortable as we look ahead that we think we've got a business that will continue to grow and move ahead.

Thomas Lee - *JPMorgan - Analyst*

Got it. Thanks.

Doug Hutcheson - *Leap Wireless International - President, CEO*

You bet, Tom. Thank you.

Operator

Your next question will come from the line of Michael Rollins, representing Citigroup. Please proceed.

Michael Rollins - *Citigroup - Analyst*

Hi, good afternoon.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hey, Mike.

Michael Rollins - *Citigroup - Analyst*

Just a couple of questions. I guess the first is, what are you seeing from the weekly plan, that you've launched. Any material impacts to whether it is customer retention or sales from that-- that plan? Second question I had was, just looking out more broadly, I think, Doug, you had mentioned that you thought there were significant upside opportunities for penetration, particularly in the core markets, and you were comparing yourself to, some of your peers with similar models.

So I was curious if you could talk about what would be the catalyst to accelerate that incremental gain in penetration in those core markets, and as you look at the new markets, how should we expect the pacing to go? What do you think the timeframe is for the newer markets to hit, for example, a 5% covered penetration of POPs, and then, maybe even say what would be the longer opportunity in terms of the years to get to that 10% milestone? Thanks.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Cricket by week is primarily in place right now as a retention tool, and we have it operating as an acquisition tool in a couple of markets, and we'll be rolling that out based on what we see. So I think the results on Cricket by week are really promising, and we'll let that continue to evolve. In fact, if you think about it, it is likely that that 5% number that you're talking about, may frequently be achieved within a year, on a new market we don't give specific guidance, but if you look at the total number of subs and think about the information that we disclosed, you will see that you have robust customer growth, and we see average penetration in those new markets, that approaches those levels, within a year.

What I have said, you said it slightly different than what we said publicly, so let me make sure, I say, where we see us. We see continued growth in our existing markets, which we're not going to break out separately. But those initial 25 million POPS and we seen an acceleration of customer activity, a 30% year-over-year increase in customer activity, so not only have we said that it is fair, we're now seeing the acceleration of customer activity. And in addition to that, we're now telling you for the first time, in over five years, we're going to go back and make some investments in those markets, that we think will help further move them ahead. So feeling pretty good that we're already seeing progress on those, and that as we add the additional cell sites, that we'll see more.

The other part of your question, I actually pointed out that new markets, so new markets not only include 66, but include the Auction 58 markets, and really don't have any different long-term likely, long-term penetration characteristics as compared to others, that might operate the model. We don't believe people should be focused right now on long-term penetration. We don't think we should do anything that de-optimizes that, but we're more focused on how we grow it quarter-over-quarter.

But we shared a lot of data, actually in June, that showed why the markets looked the same, as compared to others. And we think that data, we're very confident that data is valid, and we're-- we expect to continue to grow those not in a quarter or two, but over the next several years, we expect to see attracted, increasing, long-term penetration rates for the business. We don't see elements in place that cause us to believe additional growth isn't available.

Michael Rollins - *Citigroup - Analyst*

If I can follow up with one other question on that. If you think about this digestion period where you have a rapid period of gross growth, is that digestion period that may, hold back this incremental penetration rate, like if you look at the 2Q number in the new markets, specifically, is this an indigestion period that can, last call it six or twelve months, so that in some respects you're taking a little bit of a step back from the churning effect of this-- of some of those gross ads, and then when you get through that, then you're in a normalized period of growth? Or do you consider the second quarter a more normalized period of incremental penetration for the June quarter?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Yes, the former, not the latter. So we would expect we would work through this tenure issue, and this business would go ahead, and into the latter part of 2008 you would see it start to look more similar. All of the different pieces of the business look more similar, and exhibit normal seasonal rhythms.

Michael Rollins - *Citigroup - Analyst*

What you'resuggesting is it might take six or twelve months. Once you have this rapid pace of expansion, to then digest a little bit. You're still growing, but you're also digesting a little bit. And after six to twelve months, you get back to a more normalized pattern?

Doug Hutcheson - *Leap Wireless International - President, CEO*

Absolutely. That is why we provided the tenure chart for people, so that they can get an idea to think about how that works, and that's why we gave you data that said, our average tenure customer is 20% lower than a year ago. And you'll see that number actually be fairly high for the next few quarters, and then it flexes its way back through, as we digest that growth. That is why we pointed out, when we started the expansion process, that is why we made it clear, that we thought we would see this effect. So this is now, we've been outlining that we would see the effect we're experiencing for five, six quarters, that we would see an increase in the number of lower-tenured customers, and we would see that work its way through the business.

Michael Rollins - *Citigroup - Analyst*

Thank you for taking my questions.

Doug Hutcheson - *Leap Wireless International - President, CEO*

You bet. Thank you.

Operator

Your next question will come from the line of Ana Goshko, representing Banc of America. Please proceed.

Ana Goshko - *Banc of America Securities - Analyst*

Hi, guys, thanks for taking the question, I know this is getting to be a long call and you're probably running out of steam. I'll try to be brief. On your new roaming buckets which were implanted recently, you said that 90% of your customers now are-- of the gross ads are taking a $45 or higher plan. I wonder what the take rate is, on a plan with a roaming bucket. And then, secondly, I think the part of your intention in implementing those plans, was as potential churn reduction tools, and I know it is early but I'm wondering if you've been able to mine the data yet. And of the similarly tenured younger customers, in terms of their tenure, I mean, is there any evidence that there is lesser churn with someone with a roaming bucket, than one with not?

Doug Hutcheson - *Leap Wireless International - President, CEO*

The--we don't give specifics, but, on rate plan uptake, but we've seen not only at or higher than expectations of customers on the higher rate plan, but we've been pleasantly surprised at the rate of migration, and that may have entailed an existing customer migrating, going to a higher ARPU plan, and getting a new handset in the process. That was what I was trying to point out, with some of the earlier questions, and that is a pretty attractive proposition for the company to work its way through. The-- as far as differences between churn rates on customer, different rate plans, I think it is premature for us to say that-- to give any detailed information on how tenure or-- or how the rate plans affect churn characteristics. What we have found, is that we have driven, brought better products and services to our customers, churn goes down. Which is why we have pointed out, that the core churn, less these two issues, continues to come down, and that is why we feel good the business is well in hand, and moved through this transition.

Ana Goshko - *Banc of America Securities - Analyst*

Okay. Thanks. A second thing is that I thought today the FCC came out with an order on automatic roaming, which appeared to be a nice gesture, but there wasn't any relief in there, on roaming rates. So my initial read is that it is something you will take, but it is probably not going to have a concrete impact on you. I just wanted to run that by you, and see what your take is on the order.

Doug Hutcheson - *Leap Wireless International - President, CEO*

It is premature for us to interpret the order. I think that--and so we are in the process of looking at it. I don't--our initial read, is that it tends towards looking promising at this point, and I think we feel best if we just continue to take a look at it, and figure out where we go with it next?

Ana Goshko - *Banc of America Securities - Analyst*

Okay. Great. Thanks, very much Doug.

Doug Hutcheson - *Leap Wireless International - President, CEO*

You bet. Thank you.

Operator

Your next question comes from the line of Jason Armstrong representing Goldman Sachs. Please proceed.

Jason Armstrong - *Goldman Sachs - Analyst*

Great, thanks. Hi, thanks, guys. I'll just ask one, given the time. Can you help us think through, if sub prime or economic factors do get worse, and start to, you know, impact the business a bit more, how do you think about dis-aggregating the risk? Would your expectation that it shows up more in absolute disconnects, or maybe more in sort of rate compression, with subscribers migrating down to lower rate plans. Just helping us think through that.

Doug Hutcheson - *Leap Wireless International - President, CEO*

We've talked over the last couple of years about what we would expect to see not just with sub prime. I do think people-- what we've expected to see on the sub prime issue has been very low impact, and we think that's what we've seen, the businesses absorb that. If there were broader economic conditions, we think we would see two effects, and if not, right now, we don't have data that would indicate there is an ARPU effect, or downward migration. What we actually would see is those customers that, run out of economic means, you would see an increase in their de-activation rates. If you think that through, however, we're probably the least expensive alternative for them to come back to. And so to--and having a phone where 60% of your-- having a service where 60% of your customers don't have a landline phone, I think you would see, increased volatility in that area, but you would see a lot of those customers come back with re-activations over a period of time. So we think that part worked its way through.

The part we find, that is a little bit more interesting, is actually more that other customers with other carriers, start to look at what they're going to do to manage their costs, and as contracts lapse off for those customers, our ability to be in front of those customers with our services, we actually think, opens up the-- and expands our opportunity that customers will take a look at us. So, you know, I think right now I-- it was our conversation outlined today, that we think sub prime is not a major factor on our business. But if there was a major factor like that, I think that is how it would affect us.

Jason Armstrong - *Goldman Sachs - Analyst*

That's helpful. Thanks.

Operator

Your final question will come from the line of Will Power representing Robert W Baird. Please proceed.

Will Power - *Robert W. Baird - Analyst*

Great, thanks. Good afternoon.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Hey, Will.

Will Power - *Robert W. Baird - Analyst*

You covered a lot of ground here, already. If I look at Q2, it looks to me like the churn number basically came in line, with guidance. I guess I was wondering if you would give us a sense of what the trajectory of gross ads look like, over the quarter. Did gross ads improve, worsen, et cetera? That might just help provide some flavor around Q3. Secondly, in the update, just on the boost unlimited product, and what kind of impact that might or might not be having in those markets where they are. Thanks.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Sure. Well, we actually tend towards seeing second quarter being a little bit of back-end-loaded quarter. And so what you would have seen, what goes along with the back-ended quarter, you see an acceleration, that happens later in the quarter, versus earlier in the quarter. We have several quarters that are like that. I would point out as an example, fourth quarter, is absolutely another example of a back-end-loaded quarter. So we tend towards having those effects.

And so I would tell you that there was plenty of strength at the end of the second quarter, and I think hitting our guidance where we're at on our-- on our gross additions in the second quarter, seems like to us, that we're moving in, and working through things. I won't comment to any one competitor specifically. I won't-- I will comment in general. We seem to be doing fine dealing with competitive issues at this point. I certainly don't want to introduce that we think any variability that we're seeing in, how customer activity is competitive related, at this point. Now, we're in the middle of a drop-dead competitive industry. We're investing left and right on, you know, different things that we think that improves the strength of our proposition, and we change our rate plans, recognizing that we're in a-- in a competitive industry, but I don't think we see things at this point, that are relative to, actions of any one individual competitor.

Will Power - *Robert W. Baird - Analyst*

Okay. Great, thank you.

Doug Hutcheson - *Leap Wireless International - President, CEO*

Thank you.

Operator

There are no further questions at this time. I would now like to turn the presentation back to Ms. Jeanie Herbert for closing remarks.

Jeanie Herbert - *Leap Wireless International - Director of Investor Relations*

Thank you for joining us on the call. We look forward to updating you on our business on the next quarterly conference call. If you have further questions, about our second quarter results, or need additional clarification, please feel free to call me at 858-882-6084. Thank you and good night.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes your presentation. You may now disconnect. Good day.