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LEAP - Q4 2007 Leap Wireless International Earnings Conference Call

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PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to the Leap Wireless Q4 2007 earnings conference call. My name is Lisa, and I will be your coordinator for today. At this time, all participants are in a listen-only mode. We will be facilitating the question-and-answer session towards the end of this conference. (OPERATOR INSTRUCTIONS) I will now like to turn the presentation over to your host for today's call, Mr. Jim Seines, Director of Investor Relations. Please proceed, sir.

Jim Seines - *Leap Wireless International - Director of Investor Relations*

Thank you, Lisa. Good morning. Welcome to Leap's fourth quarter 2007 conference call. This call is being recorded and will be available for playback in the U.S. for the next 30 days by calling 1-888-286-8010. Callers from outside of the U.S. will need to dial 1-617-801-6888. The pass code for both calls is 215-53799. This conference call with accompanying presentation is also being webcast live and will be available for replay on the investor relations section of our website at www.leapwireless.com shortly after the completion of our live call today.

Joining me on the call today to discuss our fourth quarter results are Doug Hutcheson, our President and Chief Executive Officer and acting Chief Financial Officer, and Stefan Karnavas, our Vice President of Finance and Treasurer. Following our prepared remarks, Lisa will come back online with the instructions for the question-and-answer portion of the call. Al Moschner, our

Executive Vice President of Sales and Marketing Operations, and Glenn Umetsu, our Executive Vice President of Engineering and Technical Operations, will join Doug and Stefan for the question-and-answer session.

Turning to slide three, during our call today, we will discuss the non-GAAP financial measures. For GAAP reconciliation of non-GAAP financial measures, I would like to refer you to the notes to financial statements contained in our earnings release today and also the financial reports page of the Investor Relations section of the Leap's website. The results and data we will discuss today, including customer information, reflect the consolidated results of Leap, its subsidiaries and it's not controlled joint ventures LCW Wireless, LLC and Denali Spectrum, LLC for the periods indicated. Also, as used in today's conference call and accompanying presentation, new initiatives refers to the company's costs associated with this coverage, expansion initiative billed out of auction 66 markets, high-speed data offerings, and strategic M&A activities.

Turns to slide four, on our forward-looking statement slide, I would like to remind you that statements made today that are not historical in nature, including 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, 2007, which we expect to file tomorrow. For anyone listening to a tape or webcast replay or reviewing a written transcript of our fourth quarter call, note that all information presented is current only as of today's date, February 28, 2008. The company disclaims any duty or obligation to update any forward-looking information, whether as a result of new information, future events or otherwise unless as required by law. With that, I would now like to turn the call over to Doug.

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

Thanks, Jim, and thanks to all of you for joining our discussion today of our fourth quarter 2007 performance. We ended the year with a strong performance as we added increased customers by 152,000 net additions. Churn was nearly flat year-over-year and 100 basis point improvement quarter-over-quarter, better than expectation. This resulted in the 28% year-over-year increase and, in the period, customers. The strong momentum that we have built has resulted in today, us adding our 3 millionth customer. Turning to ARPU, it grew year-over-year by nearly $2 as expected, and increased $1.06 from the prior quarter. Both service revenue and total revenues increased with service revenues being higher due to increased customers and ARPU driving improved service revenues with an increase of 38%.

Operating income improved by $37 million as we enjoyed the increasing contributions from the markets we launched in 2006 and the first half of 2007, as well as the increasing contribution from our more mature markets. Lastly, OIBDA increase year-over-year by 115% as we achieved 30% adjusted margins even including $15.2 million of spending related to the new initiative. As we turn to our customer profitability, we make our money customer-by-customer, month-by-month. We believe the calculated contribution per user is an important metric that sums up the results of our key operating metrics. As we look to the far right of the chart, you see the fourth quarter 2007 results where our ARPU of $45.57 when you take off our $21 CCU. And churn adjusted CPGA results in a $17.09 calculated contribution per user per month, including the $1.70 of the new initiative costs included in this number. The contribution was $18.79 for our operating business. As you look towards the full-year 2007, you see we reported an ARPU of just below $45 and cash costs just below $21 with the calculated contribution per user resulting in about $16.34 of monthly contribution per user. Including the new initiative spent, this number was $17.20. The yearly growth rate on that was 2 1/2% and our quarterly growth rate was 7%.

Our business is built around providing a high strong-valued proposition supported by an attractive cost structure. If you look at the industry average ARPU of a little over $51 and divide that by the industry average delivered minutes, you see the current yield is a little less than $0.6. That cost of delivery is about $2.6 cents and is delivered at a 56% gross margin. Our ARPU of $45.57 when divided by the 1450 minutes we deliver, resulted a yield of a little more than $0.3 and we deliver that at about $0.15. This results in a 52% margin. We sell our services at 53% of the average selling price and we achieve comparable operating margins. We believe we have the ability to provide nearly twice the value at comparable margins.

Turning to customer growth, we continue to reflect our seasonal patterns; however, it's important to note that the uncovered POPs in our business over the past three years has increased nearly 28 million. A portion of this comes from POP growth within our markets, a large percentage from the auction of 58 markets that we launched in 2006, and the related launches in early -- in the first half of 2007, and we now see the results of the expanded footprint with our first meaningful launches in the fourth quarter of 2007, related to the Rocky Mountain high initiatives we discussed. This resulted in 1.3 million new customers over the past three years. In the fourth quarter, we added 152,000 net additions, and as we discussed, we expect to achieve 3 million customers today. Churn improved this quarter to receive these normal seasonal rhythms of our business and the expected improvements we had been looking for in customer tenure. But the performance we experienced at 4.2% was better-than-expected and resulted from strong reactivation trends late in the fourth quarter. As we look ahead, we expect the tenure effect and upgrade activity will perform as we have expected and as we have seen in the fourth quarter and churn will continue to follow the typical seasonal rhythms that we see through 2008. The remaining effects of the tenure should be through the business by mid-2008.

As we turned towards ARPU, I think the business has clearly achieved some attractive results and demonstrate the ability to manage ARPU. We've achieved this by building an attractive array of service plan and set a goal to achieve an ARPU objective in the mid-$40 range, something we have now achieved over the past few quarters. This has resulted in an increased ARPU of $6.54 over the last three years. There has been a variety of competitive moves that the industry have seen, not only the introduction of new, unlimited offerings, but some targeted offers in the by-the-minute category, something that we discussed in our last earnings call. We believe the company has built an attractive value proposition over a range of price points that will allow us to compete and continue to strife the balance the relationship between ARPU, customer growth, and costs.

When we look at the ability to continue to drive margin growth and balance our pricing, the chart here shows that, in fact, our lower price rate plans are fairly narrow and our higher priced rate plans really add a lot of value that we bring to our customer. At least, we have conducted service plans trials that are designed to appeal to a broad range of customers by balancing price and value. And as we have demonstrated, we have seen attractive uptake over the last several years of our higher value rate plans, a trend we expect will continue. Our objective is and remains to maximize total returns by increasing customer growth while maintaining ARPU in the mid-$40 range.

Turning to CPGA, it's performing as expected. Our CPGA for the quarter was reported at $178, including $8 of spending related to our new initiative. Our spending levels were as expected and we expect that 2008 CPGA trends to be consistent with our prior results. One piece in particular on CPGA that we're excited about on CPGA is the introduction of our first low-cost handset, the Cricket EZ, a handset that we worked to source and white label from overseas during the first quarter of 2008. This handset along with the variety of other initiatives allows us to support a competitive promotional pricing without affecting our subsidy materially. And this will be our first handset retailing for less than $100 will allow us to provide promotional pricing between $49 and $69.

CCU is expected to continue to improve as we continue to gain scale. It performed during the second fourth quarter as expected at about $21. This includes $1.34 of expenses that are related to our new initiatives. Expect CCU to remain in the $20 range through 2008, which will reflect the cost associated with our new market launch activities. And in addition, as we look out over the longer-term horizon, we expect further decline to occur as the business gains scale as a result of customer growth in ongoing cost control initiatives. Stefan?

Stefan Karnavas - *Leap Wireless International - Vice President of Finance and Treasurer*

Thanks, Doug. Turning to slide 16, you can see that while we significantly grew adjusted OIBDA during the fourth quarter of 2007, we also expanded our margin substantially. Adjusted OIBDA margin improved by 11.1 percentage points to 30.2% on an as-reported basis. Included in reported adjusted OIBDA was $15.2 million in new initiatives spent, which represents costs associated with new market launches, core footprint expansion, broadband trials and other costs. Excluding these costs, adjusted

OIBDA margin grew by over 15 percentage points to 34.3% for the quarter. In addition, adjusted OIBDA margin, excluding new initiatives was approximately 30% for the full-year 2007.

The margin improvement was broad-based. Our cost-of-service for non-product costs benefited from the scale on fixed costs including leases, utilities, back haul, and employee-related costs. These improvements were enough to absorb increases in the costs-of-service related to product costs, which are associated with third-party services that enable our delivery of directory assistance, text messaging, MMS, WAP, long distance, roaming, ring tones, et cetera. Net equipment subsidy improved as we reintroduced activation fees for new customers which were not charged during the prior-year period. Sales and marketing benefited from lower advertising spent from the year-ago period, and customer care and billing margins improved due to efficiencies from further offshoring at our outsource call centers and some billing efficiencies. The G&A margin on an adjusted basis for new initiatives was about flat and was negatively impacted by increased D&O insurance costs, professional services, and employee-related expenses. In summary, we're achieving margin improvement through scale as we expected and believe we will continue to expand margins as we further penetrate our markets. The delivery of adjusted OIBDA margins that are at or exceed 40% in our more mature markets bodes well for margin expansion opportunities driven by growth in our recently-launched markets.

Turning to slide 17, operating income in the fourth quarter of 2007 improved by about $38 million from the year-ago period as revenue improved by $115 million and total operating expenses, including depreciation and a motorization, increased by around $77 million. While operating income grew by $38 million, net loss improved by $27.6 million. Over half of the $10.6 million difference is explained by higher interest expense, primarily due to an increase of $350 million in face amount of senior unsecured debt for the period offset somewhat by lower interest income. Please note that 72% of our debt is currently fixed and we have executed $355 million of floating to fixed rate swaps under our term loan. At December 31, 2007, the effective interest rate on our term loan was 7.9% including the effective picture of the swaps. Minority interests in consolidated subsidiaries increased by $1.9 million and reflects our partner's interest in the net income or loss of joint ventures that are consolidated for financial reporting purposes, primarily LCW and Denali. The equity in that loss is $1.5million reflects our share of losses in a joint venture providing wireless service in Puerto Rico. And finally, what Leap does not pay taxes for federal income tax purposes, we do report tax expense on our income statement. During the fourth quarter, income tax expense was $8.5 million in line with our expectations outlined in last quarter's conference call and a reduction of $2.5 million from the previous year.

Turning to slide 18, we provided a summarized cash flow statement which reconciles the cash, cash equivalence, and short term investments. As can you see in the column that reconciles that three months ended 12-31-2007, we used over $40 million in cash during the fourth quarter, leaving the ending balance at $613 million at year end. Cash from operating activities was around $120 million or capital expenditures for the quarter were around $160 million. For the full-year, cash increased by $173 million the primary sources being $318 million in cash from operating activities and $367 million in cash generated from financing activities. These amounts were reduced by capitol expenditures of $505 million for the full-year which included approximately $46 million in capitalized interest. Our guidance range for capital expenditures for 2007 was $505 million to $545 million, including around $50 million in capitalized interest. Of the total capital expenditures, around $100 million was spent on Auction 56.

A couple of items to note. First, cash from operating activities of $318 million for the full-year was less than the reported adjusted OIBDA of $392 million, primarily due to a swing in our accounts payable and a crude liability balances associated with the crude invoices for heavy launch activity in late 2006, which were paid in early 2007. Second, I want to briefly review our current cash investments. We are currently investing in three areas. Around 40% is invested directly in U.S. government treasuries and short-term federal agency notes. Around 40% is invested in money market reserves that invest primarily in U.S. treasuries and federal agency notes and the remainder is invested in straight commercial paper from industrial companies and includes no banks or investment banks. We currently hold no auction rate securities. Our joint venture partner Denali holds two issues of asset-backed commercial paper with an aggregate face amount of $21.6 million.

During the fourth quarter, we adjusted the fair market value of these securities by approximately $1 million bringing the full-year adjustment of fair market value to $5.4 million. We may see further deterioration in the fair market value of these two securities;

however, our maximum exposure is $16.2 million should these securities be written down to 0. In closing, the financial overview section of today's call, I would like to reiterate that between our cash position of over $600 million at year-end, our ability to generate cash from operating activities in 2008 and the flexibility inherent in the business to modulate the launch of new markets forged Leap with adequatability and the ability to flex its capitol outlays if need be. The resources include our $200 million revolver which, we typically don't rely upon when planning future funding needs. In addition to a healthy liquidity position, our total leverage came down to 5.2 times at year-end, a reduction of over 25% since the senior unsecured add-on closed in June of this year. As we look to fund future growth, we remain focused on a disciplined approach that balances investment in our existing markets with expansion opportunities in new markets in order to maximize value for all stakeholders. Now I'll turn it back over to Doug.

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

Thank you, Stefan. As we look to the future, I think we wanted to take a minute and discuss what we have achieved over the last three years. In early 2005, we laid out a plan to double the size of our business. Relative to footprint, we increased our footprint by 108%, $3 million of this increase through POP growth in the existing footprint we then operated. About $23 million through new market launches and $2 million through the expanded footprint that I will discuss later as we added new cell sites to our more mature markets. Our customers grew by nearly 1.3 million, an 82% growth. The modest increase, we had an initial modest increase between 2004 and 2005, as we completed our preparations for growth and enhanced our product portfolio.

However, since then, we have seen a substantial acceleration with 2006 being a little less than 600,000 incremental customers and 2007 being 633,000 net new customers. As we look at service revenues, our CAGR has been 28% on service revenues as they have grown over or at 100% in the last three years. The service revenues doubled as a result of the 82% increase in customers and the $6 increase that we have experienced in ARPU. But it all culminated in the improvement that we have seen in our adjusted OIBDA. We have improved our adjusted OIBDA by over 141%. When you adjust for the new initiatives that will allow us to consider the next doubling of our business. This results in a 34% CAGR over the last few years and operate. Our business operated at a 34% adjusted OIBDA margin when we look at the business without the new initiatives. Our guidance as we look ahead says, expects that we will have an adjusted outlook of 30 to 40%.

Now, we believe we're in an attractive market segment. We believe that no contract area allows us to not only be in the largest growth area which is the additional customers that will join in the industry without a contract, but also as we have seen over half of our customer comes from other carriers. Many of them that had been on post paid plans. So we see an expansion of the segment from 16% in 2007 to over 24% in 2012. We think as we see this continued improvement in penetration that Cricket has a substantial opportunity with our low-costs, high valued services. In times of economic stress, we believe that we also provide an attractive alternative as we provide the best value for the rate plans that we have -- that we provide. These numbers exclude the effects of mobile broadband penetration. The next, as we set up our next phase of expansion, I want to point out the company acquired ing is can't portfolio spectrum.

We have available to us up to 15 million additional covered POPs and we overlaid most of our footprint with additional spectrum to allow us to grow not only our voice business and introduce a mobile broadband opportunity. The result is we have 186 million licensed pops, inspection in 35 of the top 50 U.S. markets. This portfolio has been built as we focused on value and executed a disciplined approach to acquisitions in the past. Leap and our DE partners have achieved average acquisition prices in Auction 58 of $1.11 , a megahertz POP and for the most recent completed Auction 66, $0.41, the lowest price bidder of all the major bidders in the auction.

We have three new initiatives that we believe provide the opportunity to build our business further. Continued coverage expansion, higher speed data offerings and the new market expansion. In May, we discussed our plan to improve our network by enhancing the footprint that we believe complements many of the other growth initiatives we're executing. The effective increasing footprint not only improves the market quality score but continues to execute the clustering strategy we have used over the last three years as we have combined markets together. In 2007, we completed over 300 of the planned new cell sites, of the planned new 600 total sites and expect the remaining sites to be completed in the first half of 2005. What's most significant is the early results on this are yielding the expected outcome. We increased year-over-year sales in those markets that had been launched with the major of their sites by over 20%. And we have seen the improved customer retention. We believe the expected benefits of this program over time will yield higher long-term penetration and lower off network costs.

As we turn toward the product portfolio, we have seen continued success with our major new product initiatives, particularly as the businesses continue to focus on data. As a proxy for the behavior that you see with our younger, more ethnically-diversed customer base, I think ringback tones need, the results we have seen on ringback tones are very compelling. In six months after launch, we have seen a 67% higher than the industry average usage of ringback tones. Our current offer includes a $5 monthly recurring charge that allows two ringback tones a month. There is more ahead. We see the opportunity to expand our data applications to mobile video, music, social network, and e-mail. Our customers continue to show the propensity to be early adopters and large users of appropriate data services.

In the second half of last year, we announced a broadband trial and we want to provide an update on the progress we've made. We finalized our pricing with a $40-per-month charge per new customer and $35 when bundled with the Cricket voice service. The trial now operates in five market customers, market clusters and we can report that 60% of the subscribers are new to Cricket. We launched initially with the product primarily in our brand of distribution but recently have expanded to include regional consumer electronics stores. We have reached an important milestone in the second quarter with the expected launch of our USB device that we think will broaden the appeal of our product and we continue to expect, to follow a disciplined as we see further success come with this new offering.

We have talked for sometime about how we have improved the market quality that the business operates through the variety of initiatives. As we look at what is ahead, we have increased those market-quality scores by 14% as a result of the actions that we have taken in Auction 58 and Auction 56. The effect of these improvements increases by nearly 25% the increased long-term penetration potential of our total business as we continue to launch and move these marks ahead. The Auction 66 markets continue to progress with an expectation of up to $12 million POPs launched by the end of the summer and $12 to $28 million POPs launched by 2008. We're pleased to report we have the initial handset and believe that no longer in our path to hold us up on continuing to launch as well. Spectrum clearing is progressing. We have some markets clear today and we expect that we will have additional markets available in 2008, as we make further progression with the government. The company reiterated its guidance for the new market buildouts with a CapEx per covered POP of $26 through the first full year of operation and an operating impact of approximately $5. Again, as we experienced it with our previous launches, Auction 58 launches, we expect that those will be OIBDA break even within the first full four quarters of operation. Leap has done well and continues to be a strong growth story. With our results that we've delivered today, we see attractive year-over-year growth in our financial performance. We see and we see improving margins. Further, our business is resilient. We've shown the ability to grow with a proven scalable business model that delivers nearly unparalleled value in the market place. And We have an attractive array of future growth opportunities. Growth, not only from our existing business, but from the expansion of our footprint as we continue that with quite execute this point of approach. With that, I'll turn it over for questions and

QUESTIONS AND ANSWERS

Jim Seines - *Leap Wireless International - Director of Investor Relations*

Thank you, Doug. Lisa, can you review the instructions for the Q&A portion of today's call?

Operator

Thank you. (OPERATOR INSTRUCTIONS) Our first question comes from Romeo Reyes from Jeffries. Please proceed.

Romeo Reyes - *Jefferies & Company - Analyst*

Hi. Good morning. A couple of questions. First on, I guess, before anybody asks about competitive landscape, can you give us a quick update, Doug, on boost and other alternatives out there that are in the marketplace and then secondly, with respect to broadband, can you give us a little bit more, I guess, information if you can on, otherwise, subsidies, CPGA? I think you said churn is lower than your core business. I think -- as you have said it's a lower CCPU, potentially lower CPGA and lower, I guess, churn CPGA and overall cost of array distributed lower and the margin should be higher? But can you you give us a little bit more color on that if you can? Thanks.

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

You bet. Well, thanks, Romeo, and I know people have had a busy morning already. We have clearly watched and I am sure, I think a number of people have watched a very active period in the marketplace from a competitive landscape. But I think some of the early things we have seen, particularly some of the announcements today really give us, I think, a lot of headroom. We think we have a really attractive competitive position, and so I have not seen any changes that cause us to change, how we believe the business is comparatively positioned. We think we have real attractive growth prospects in front of us and I think we have quite a bit of value differentiation that's available to us. I think we have discussed those that we have operated our business with other unlimited competitors in a whole host of our different markets and what we have seen in many of those markets is that effectively expands the pie and we have done quite well of taking our fair share of that. So at this point, we're feeling like the business is positioned for growth.

The broadband initiative is in a trial phase and so I think it's a little premature to give you some specific operating metrics on that. Clearly, we think there is an attractive margin growth opportunity for us. We think the costs associated with delivering that product should be very attractive for us. I think we'll get a better idea on the acquisition once we roll out the USB device. We think that is an important milestone and us validating whether or not we want to proceed and expand this business, but what we have been interested in on that or what we have been pleased with is we thought we would see adoption by our existing customers and we have seen of the limited customers that we have about 40% of those are existing customers, but it also brings, it allows other customers to look at the business and we have seen interesting data that yet improves how all customers, those customers that are aware certainly take a look at our brand. And so it also helps improve our brand and how people see it in the marketplace as we bring value, not only in our voice and mobile data services, but we add in the mobile broadband services. Thanks, Romeo.

Operator

Our next question comes from [Scott Millert] from Goldman Sachs. Please proceed.

Scott Millert - *Goldman Sachs - Analyst*

Good morning. Thank you. I know a lot of people have talked about the $25 plan. So I wanted to hear your thoughts on the promotional $25 plan you ran in December and why it was taken away and what are the effects we can expect going forward. And then I noticed that $30 plans have been taken off the website. I was surprised by that piece and I just wanted to get an understanding what may be the sweet spot is for an opening price point in terms of voice plan?

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

Well, it's been a little historical. First off, the company has consistently had service fines or regularly had service plan promotions particularly in the fourth quarter, and we typically had those promotions be real narrow subset of what we offered. Not a lot of additions or flexibility on those. We do that first because it generates customer interest and second, we believe based on the results that we demonstrated that over time customers really want the value that we provide in our higher value rate plans and so we really set up an interesting opportunity for the customer to see additional growth. In addition, the business has -- and I do want to point out that that was a promotional plan, which means it's not a plan that is available if you either disconnect or routinely offered. No different than what we have done previously particularly during the fourth quarter. In addition, the business has regularly trial business rate plans. I think last year we discussed the whole series of trials that we did as an example in advance of introducing our roaming products, would be one area. You have also seen the trial bolt-ons, what we call bolt-ons as we looked at adding in and creating value with some of the additional data services. During the first quarter, we were trialing new rate plans. We expect that you will see a new rate plan rollout come sometime either in the late in the first quarter or second quarter. We feel pretty pleased with the results that we're seeing, clearly as we pass through the 3 millionth customer and we think we'll continue to see attractive prospects for the business. So, I think we're feeling that we're in pretty good shape at this point.

Scott Millert - *Goldman Sachs - Analyst*

Okay, and just one other question. It seems like a lot of the national carriers might be tightening the credit standards. I'm just wondering if it's seen the effect to this and has it added to your first ad channel. Thanks.

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

Well, to the degree there is a tightening of credit standards and we created and operate a business model that doesn't require contracts or long-term credit checks and by managing our cost structure, both on the acquisition churn, NCCE side, clearly we provide an attractive alternative for many customers. We don't require a contract and we provide industry-leading value with a lot of services that we provide. We'll see how the year progresses. I think we feel like in a little bit of a setup from where we're at looks promising. We feel like we have got a good fourth quarter behind us and we'll see how the first quarter continues to evolve, certainly through the end of February as we have announced. We see good results and we look forward to continuing the progress through the year, rolling out our next round of rate plans and service plans and seeing how we move ahead.

Scott Millert - *Goldman Sachs - Analyst*

Thank you.

Operator

Our next question comes from Ric Prentiss from Raymond James. Please proceed.

Ric Prentiss - *Raymond James - Analyst*

Thanks. Good afternoon or good morning, depending on where you're at.

Stefan Karnavas - *Leap Wireless International - Vice President of Finance and Treasurer*

Good morning, Ric.

Ric Prentiss - *Raymond James - Analyst*

First, can you hear me okay?

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

We can.

Ric Prentiss - *Raymond James - Analyst*

Okay. First, yes, I appreciate the 3 million subscriber number. That is a nice milestone to hit. It gives us an indication of how the economy is going, kind of how your first quarter is going. If there is anymore color you can give us along that front door with the requisite of an economy question, and should we expect seasonality that first quarter ad might be higher than the fourth quarter ad is the first question.

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

Well, the overall, our net ads are seasonal. We tend towards seeing higher net ads in the fourth quarter and highest in the first quarter. And I think what we said today is we would expect that seasonal trend to continue and I think what you see is that we're certainly a long ways down the path at this point of having the first quarter be the higher number. We have had an attractive run rate through the first few months. So I think from an economic standpoint, at this point, I think we have seen the normal cycle that we see in the first quarter with attractive customer additions and look forward to looking ahead. This year's a little interesting. I am sure many people are looking at the economic stimulus package and we are, too and that is clearly one of the reasons why we see attractive first quarter in some of the income tax returns that go on and so to the degree that there is an economic stimulus package that provides a potential opportunity that will certainly look at it as the year progresses a little bit later as well. I don't want to suggest that that changes the overall seasonal rhythm to the business. I think that would be inappropriate, but it certainly provides an interesting opportunity that we are going to take a look at pretty hard.

Ric Prentiss - *Raymond James - Analyst*

Second question for you guys is appreciate the update on the cash balance and your operating cash flow and the flexibility to modulate existing launches, also the history of you guys, as far as being pretty diligent and disciplined bidders in auctions about 58 and 66, a kind of a side question might be though, would you consider yourself fully funded for your buildout and knowing what you know and what we don't know about Auction 73 participation. Is that something you guys would feel comfortable saying you're fully funded, do you think?

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

Well, I'm going to be pretty careful here. I think we believe that the business has adequate cash reserves for our $12 million POP buildout plant and we'll look at what other alternatives are available as things developed here.

Ric Prentiss - *Raymond James - Analyst*

The final question, a bit awkward, sorry about that, but I always have to ask. The final question is obviously Vegas is one of the markets you got on your map with a flag on it. Phily is one of the maps with flags on your future markets, both of those are metro PCS-intended markets as well. As you look at your prioritization of the POPs to build out the $12 to $28 to $58 million POPs, how do you think about the competitive landscape? Does it affect you at all as far as prioritizing your POPs and just kind of a thought of I know you competed against them and a couple of Americans. But just kind of -- as your priority POPs. Does the fact that metro factor into your scale?

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

We have operated with other unlimited carriers in a variety of our market and we have found that the fact there is another carrier there is not the key driver on whether or not that market is going to be successful. I want to reiterate that some of our deepest penetrated markets which are clearly in the double digits have had unlimited competitors in them for their entire time. The priority that we have, based on what we learned most recently on market launches is to really roll out a solid footprint that meets the needs of our customers and to the degree we can deliver that on a timely basis with the adequate spectrum is really where we have been focused. The flags we had, we've clearly said previously there at Las Vegas and Phily we were on our launch schedule. We would expect them to roll out in due course but we also have a number of other markets that we discussed as well, such as Chicago and St. Louis and Oklahoma city, South Texas, Washington and Baltimore. So I think we have a variety of opportunities to go out and launch these markets and see some continued growth.

Ric Prentiss - *Raymond James - Analyst*

Sounds good. Good luck, Doug.

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

Thank you. Next question?

Operator

Our next question comes from [Brad Saldemon] from Lehman Brothers. Please proceed.

Brad Saldemon - *Lehman Brothers - Analyst*

Thank you for taking my question. I have two this morning, or this afternoon, I guess. First, I think you mentioned that one of the reasons why you did particularly well in the fourth quarter on your net ads is that you had strong reactivation toward the end of the quarters. I thought maybe we could start talking about what was behind the trend.

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

Sure. We put out a guidance for churn for the fourth quarter in early December and beat that guidance. I think what we're trying to point out is that we certainly saw a change in trends and remember, that the way we calculate churn is the customer that reactivates is not a gross edition. The customer that reactivates with the same handset is a deduct to churn and what we saw around the holidays was a pretty significant increase in reactivation, particularly post the holidays and I think we don't have concrete data that gives all the inside and outs of why that occurred but what is frequent particularly now as the holiday giving of gift cards is expanded that we see an influx of dollars that come in and because of the value we provide, we see acceleration and reactivation. So it was a little more than what we had anticipated and clearly recognizing that we had, as a result of the tenure effect we sue through the business, ceded handsets into the marketplace and to see those handsets come back to us now, which is really what you see when you see these reactivation time periods. To see those come back and give us an opportunity to make additional margin off that is something that it's hard to be disappointed about at this point. I think the business has done well there.

Brad Saldemon - *Lehman Brothers - Analyst*

I'm going to to ask you, guys, going to turn the first question into a two-part questionality because you mentioned tenure effect. Could you maybe give us a little more color on how you think the tenure effect is going to play out over the course of this year?

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

It would seem early in 2008 it would become beneficial because you'll be getting further away from some of your 2007 market launches. But once you begin the progress on your [Adal-U.S.] launches, will that turn around again? I also want to make sure we properly anticipate how the tenure issue could impact this normal season or rhythm to churn this year. We didn't. We provided, I think over the last three, four -- three quarters, we provided the tenure chart a bunch of times so that it's in investors' hands so that you see you can see as you accelerate new customer additions. You can see that you have higher tenure earlier in your life and then as they mature out, you get down to pretty low, pretty attractive levels. In today's call, we mentioned that we expect the tenure effect that we discussed that by midyear and I don't know if that is at the end of the second quarter or midyear that we would see those curves if you looked at them, if they would have worked through the business and you would see a more normal tenure profile for the business reflecting our seasonality. Clearly, we do and we would expect that as you look at our business, that would be appropriate for you to think about that as well you launch a new market and you see the early strong uptake that comes along with the market launch for us and that you would see for the markets, you see the tenure effect reflected and it would work through on the same curves. I'll bet it was differences based on changes that you see that it would work its way through.

Brad Saldemon - *Lehman Brothers - Analyst*

Okay, thanks. The second question can you give us an update on where you are and the AWS market build and you commercially launched. What I'm really driving towards is estimating capitol expenditures for 2008. We think about how many POPs you're going to build and multiply it by 26. I wonder if some of the cost is captured in the fourth quarter CapEx dollars?

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

Yes, in our fourth quarter number, I think we said 100 million was related to not only Auction 66 but the other strategic initiatives we're discussing with you and we gave you a bit of background and the answer to your question is yes. And we also said we expect up to $12 million of those to launch by the end of the summer and that should give you perspective on how to look at timing when we might see launches and the third piece in our last call we outlined that we expect to a degree that we have launched later in the year that they're chunky launches and we suggested that if those were to move a quarter or two, you could see the difference between $12 and $28 million, just looking at the timing of those launches. So, that was trying to go of a a launch timing view so people could think about when we would see POPs for less.

Brad Saldemon - *Lehman Brothers - Analyst*

Great, thank you for taking the question.

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

You bet. Thank you.

Operator

Our next question comes from Simon Flannery from Morgan Stanley. Please proceed.

Simon Flannery - *Morgan Stanley - Analyst*

Nice to hear about the easy handset. Can you give us more details on the descent functionality and will it have worked on the AWS funds as well as the legacy funds and also if you could update us on distribution, your distribution strategy, how are you thinking about spreading it between the exclusive stores and the national retailers and so forth. Thanks.

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

Why don't I let Al answer both of those since he did such a good job of putting the EZ handset for us.

Al Moschner - *Leap Wireless International - EVP and CMO*

Sure, Doug. Thank you. A quick update on the EZ. Yes, we're excited about this. It is a de-featurized handset, however, it supports voice and text and it's really meant as an entry handset with entry pricing. At this point, it does not support multiband so, therefore, it's not intended at this point for AWS. We're looking at that as a potential for the future but as it stands today, it does not support that. The second question was the distribution. Distribution for us, Simon, continues to evolve and we are, as you know, have stated in the past about 2/3 to about 70% of our gross ads now come through the exclusive channels. This includes both our company-owned stores as well as our premier dealers. We're committed to those, that strategy as we continue to look at Auction 66 launches this year and the Premier Channel is a part of our mix but, however, we still complement that with what we call our standard dealers that help complement a full distribution range and we have also, at the end of last year, introduced our direct channel which is our web and outbound telesales capability. We were very pleased with the initial rollout last year, we're expanding that this year and you should expect -- we will expect to see a greater percentage of our ads coming through that as well as the year and future progresses. So that is a quick update on decrease.

Simon Flannery - *Morgan Stanley - Analyst*

Thank you. Is the EZ handset, is this sort of a start of a group of new lower-priced handsets? Will we see other products, yes, with similar sort of price points as the year progresses or is it a 1-all?

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

No, I think this is our first attempt to -- obviously, this is new for us and based on how well it performs, clearly this, our demographic appreciates entry level pricing that is more competitive and if this is successful, I would think that we would see this kind of concept evolve.

Simon Flannery - *Morgan Stanley - Analyst*

Great. Thanks, all.

Operator

Our next question comes from Chris Larsen from Credit Suisse. Please proceed.

Chris Larsen - *Credit Suisse - Analyst*

Hi. Thanks. A couple of questions. First, on the few million that you have today, I just wanted to clarify. Maybe if you just sort of run rate. They're probably talking, knowing that the January is a little stronger than March. Probably 175 to 200,000 subs for one quarter and from 1Q, '08. I just want to make sure I did that right. On Arko, that is probably one of the biggest questions we seem to get, particularly the $25 promotional plan and there is three things going on. You have the $25 promotion plan. A lot of net ads were at the end of 4Q. So you could actually get a benefit of the full quarter on a straight-line basis to ARPU and lastly, what are you seeing in terms of trends, ignoring the $25 promotion plans. Are people taking more of the higher, continue to take more of the higher revenue-generating plans and lastly, I spent $15 million on strategic initiatives in '07. Any thoughts for that type of spinning for '08 -- spending for '08. Thanks.

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

Sure. And thanks, Chris. The first, I don't know that one month-quarter struck or one month is that much different than the other so I don't know that I can give you verification where 2/3 away to the quarter and have another month to go through. I think what we're saying is we're seeing -- it's progression. We're doing fine. I think we would expectedly would seek continued growth in March as we would move things ahead. You know, the business, the $25, I think, and people need to move past that. The $25 was a promotion. We have done promotions before, we'll do promotions again. It brings us customer-basing advice of the holidays and that it's unique. When those customers come in and they get a very, very narrow range of services and they look at the rest of the value propositions that we have, they move, they move up toward time. I mean, it's all the way you build and bring customers in and build a franchise. And would we expect a $25 customer to be in the near-term have an impact on ARPU? Yes, we can all do the math on it but we said we expect the ARPU to be in the mid-$40 range and we've managed it the last three years up $6 over $6.50 bucks and I think we feel comfortable. We know how to manage ARPU and add customers and create OIBDA growth over a period of time. So, it is what it is but we're going to keep progressing and expect to pull out a rate plan mix that, a service plan mix that continues to put us in an industry-leading value position and is reflective of the fact that we figured out how to grow ARPUs over the last three years and managed that. What I have said for quite awhile is that ARPU growth doesn't occur forever and I said in the second half of 2007, that was when the business would make a decision about what we would do and next that line and clearly, what we said and continue to say is that we're getting comfortable in the range we're at now and we will probably look to operate with our seasonality and all the things that go on, and the effects that what we have in the range that we're at will increase. We found a spot that is appropriate for us to be and we'll work on it. Does that mean every quarter lines up exactly? No, remember, our business will progress our way through and we feel like we're okay. The $15 million spent that we announced for the fourth quarter had not only spending related to Auction 66, it also had the initial costs with rolling out a couple of million additional covered pots and the broadband trials, and the new initiative. Our focus for 2008 will be 66 and broadband. We have given you guidance on the broadband or on Auction 66. The $5 per colored POP is how that would work its way through the OIBDA line. We think it's premature on the broadband right now. I mean, I think we've given you some flavor on that and would we have committed to a disciplined approach and how we would move through that and I think we would rather let that build before we start giving a lot of specific guidance around that so thanks, Chris.

Chris Larsen - *Credit Suisse - Analyst*

Thanks. It sounds like you are able to -- you're still able to upsell those customers as their coming in. I guess I was that was the approximate one.

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

Clearly even a customer coming in on a promotional rate plan buys other services. They may also buy those over the next year or two. So, remember, if you can't reconnect to a promotional plan. You can only reconnect to a service plan and so we have had a lot of section doing this previously and continue to believe that business is in good stead and will continue to progress.

Chris Larsen - *Credit Suisse - Analyst*

Great, thank you.

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

Thanks, Chris. Sorry. Lisa, we have time for one more question.

Operator

And our last question comes from from Phil Cusick from Bear Stearns. Please proceed.

Phil Cusick - *Leap Wireless International - Analyst*

Hey, guys, thanks for taking my call. Just another wire, alright?

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

How are you, Phil?

Phil Cusick - *Leap Wireless International - Analyst*

Good, thanks. It's been a crazy morning, huh?

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

Yes, it has.

Phil Cusick - *Leap Wireless International - Analyst*

As we hear chatter and I am sure everybody's heard about this, whether boost is going to come out on unlimited or CDMA, I think that the question is becoming much more about the whole package than it is about just what's the voice for us and as I think about that in terms of you guys, ARPU's going up by a great amount and data seems to be becoming more important both on the handset and also on the lap card trial. But can you update us on where you see your spectrum position in one of these markets where you have only 10 megahertz? Are you sitting with an open carrier or are we pretty much built out in a lot of those markets? What are you thinking about that space?

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

Yes. Let me go at it from two directions on the spectrum availability. The first is we have cleared a carrier across all of our markets and that is inside what that initial launch spectrum would be. And other than a marketer too during Auction 66, we overlaid our entire footprint with another 10 megahertz. So i think the business is certainly has adequate spectrum to continue to roll out the services that we discussed relative to the social networks, e-mail, mobile video, and those -- i think we look forward to those rolling out and moving ahead and we remain with another second 10 megahertz untouched, providing us another three carriers. It's all AWS spectrum so it needs to work through that process of getting launched and added on. But we feel positive that if we do that, we're going to have a pretty attractive business case that we're rolling out on that. So we feel like we're in good shape on spectrum, Phil.

Phil Cusick - *Leap Wireless International - Analyst*

Okay. And since you bring up AWS, how many handsets do you think are available now and at what point is that going to be a descent selection across the entire footprint?

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

Well, we're going to end up with a portfolio of handsets. From not one or two manufacturers but a variety of manufacturers. I think they need to make their announcements about who is going to be where and we're pretty pleased with the broad array of manufacturers that we see. Before we went into the AWS spectrum, one of the things that we looked at was the chip set that was going to be developed on that. There was a new chip set coming out that was going to manage up to four frequencies simultaneously, four different bands that is really going to make that process of having a pretty broad array of handset choices to the business be pretty attractive and be as complicated for the manufacturers to achieve that. With that said, you know, when you start AWS, you start with one handset and you build that portfolio. But we see the portfolio handsets available on that building pretty quickly and looks to us like it's going to move through in an appropriate time period for us.

Phil Cusick - *Leap Wireless International - Analyst*

Okay, good. Thank you, guys, see you soon.

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

I want to end, before I pass it back to Jim, to say also thank you to all employees and customers and the team that's here today to help push through things on the business. We appreciate the effort. Jim?

Jim Seines - *Leap Wireless International - Director of Investor Relations*

Thank you. And thank you all for participating in our call today. We appreciate your interest and support and we look forward to updating you on the business progress during the next quarterly conference call. If you have any questions about the fourth quarter results or need further clarification on the information we presented and discussed today, please feel free to contact us at 858-882-6084. Thank you.

Operator

Thank you for participating in today's conference. That concludes the presentation. You may now disconnect. Have a great day. Thank you.