

AT&T Inc.

FICC Research Dept

Generating rich cash flows

- 4Q23 Revenues increased 2.2% y/y to \$32bn; Adjusted EBITDA increased 3.2% y/y to \$10.6bn driven by higher Mobility, Consumer Wireline and Mexico, partially offset by lower Business Wireline
- Free operating cash flow increased 11.4% y/y to \$6.8bn due to higher operating cash flows, partially offset by higher CapEx
- Credit positive given the large and growing revenues, healthy profit margins and the firm's commitment to continue to deleverage

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Credit Opinion

We maintain our credit positive outlook given AT&T's large and growing revenues, healthy profit margins and the firm's commitment to continue to deleverage. Revenues continue to grow with 4Q23 revenues up 2.2% y/y to \$32bn. The main revenue growth drivers are Mobility and Fiber which continue to expand their customer base, more than offsetting the declines for legacy voice and data services. Mexico also showed a strong performance in the quarter with revenues growing 26.6% y/y due to growth of both services and equipment revenues. Postpaid phone churn rate remains at historical low levels (0.84% in the quarter), reflecting AT&T's strong market position.

AT&T maintains healthy profit margins, with adjusted EBITDA margins increasing 0.3pp y/y to 33%. Mobility segment continues to be the most profitable segment with EBITDA margins of 37.4%. The growing profit margins are also supported by the cost savings actions that AT&T has been taking over the past years. AT&T achieved the target of over \$6bn of run-rate cost savings ahead of schedule and set a new target to achieve over \$2bn of incremental cost savings by mid-2026.

AT&T has a strong financial position with \$8.5bn of cash and marketables on its balance sheet as end of 4Q23. Total debt decreased 0.5% q/q to \$137.3bn. We expect AT&T to continue to deleverage given the target to achieve a net debt-to-adjusted EBITDA ratio in the 2.5x range in the first half of 2025. AT&T's liquidity profile is also supported by the company's high ability to generate cash flows. In 4Q23, free operating cash flows increased 11.4% y/y to \$6.8bn due to higher operating cash flows, partially offset by higher CapEx. For 2024, AT&T expects adjusted free operating cash flows to be in the \$17-\$18bn range.

4Q23 Financial Highlights

Revenues increased 2.2% y/y to \$32.0bn driven by 5G and AT&T Fiber subscribers gains, partially offset by lower revenues from the legacy voice and data services.

Mobility revenues increased 4.1% y/y to \$22.4bn due to both higher service and equipment revenues. Service revenues increased 3.9% y/y to \$16bn mainly driven by subscriber and postpaid phone ARPU growth. Equipment revenues increased 4.7% y/y to \$6.4bn driven by sales of higher-priced phones. Mobility subscriber base continues to grow with 526,000 of postpaid phone net adds. Postpaid phone churn rate (the percentage of subscribers who canceled during the period) was stable y/y at 0.84%. Postpaid phone ARPU increased 1.4% y/y to \$56.23 due to a mix shift to higher-priced unlimited plans and pricing actions.

Business Wireline revenues decreased 10.3% y/y to \$5.1bn due to lower demand for legacy voice and data services and product simplification, partially offset by growth in connectivity services.

Consumer Wireline revenues increased 3.8% y/y to \$3.4bn as gains in broadband surpassed declines in legacy voice and data services. Broadband revenues increased 8.3% y/y due to fiber growth of 21.9%, partially offset by non-fiber revenue declines of 8.4%. AT&T Fiber subscriber base continues to grow with 273,000 of net adds in the quarter.

Latin America (Mexico) revenues increased 26.6% y/y to \$1.1bn due to growth of both service and equipment revenues. Service revenues increased 15.9% y/y to \$671m driven by favorable foreign exchange and subscriber growth. Equipment revenues increased 48.6% y/y to \$419m due to higher sales from subscriber growth and favorable foreign exchange rates.

Adjusted EBITDA (EBITDA less certain items that are non-operational or non-recurring in nature) **increased 3.2% y/y to \$10.6bn** driven by higher Mobility, Consumer Wireline and Mexico, partially offset by lower Business Wireline. Adjusted EBITDA margin increased 0.4pp y/y to 33%. AT&T continues its efforts to cut expenses and achieved the target of over \$6bn of run-rate cost savings in mid-year 2023. It also set a new target to achieve over \$2bn of incremental cost savings by mid-2026.

By business segment, Mobility EBITDA increased 5.6% y/y to \$8.4bn and EBITDA margin improved 0.5pp y/y to 37.4%. Business Wireline EBITDA decreased 19.3% y/y to \$1.5bn and EBITDA margin decreased 3.3pp y/y to 30.4%. Consumer Wireline EBITDA increased 10.2% y/y to \$1.1bn and EBITDA margin increased 1.9pp y/y to 33.1%. Latin America EBITDA increased 61.2% y/y to \$137m and EBITDA margin increased 2.7pp y/y to 12.6%.

Free operating cash flow (FOCF= cash from operating activities- CapEx) increased 11% y/y to \$6.8bn due to higher operating cash flows, partially offset by higher CapEx. Cash from operating activities (CFO) increased 10% y/y to \$11.4bn, reflecting operational growth, lower mobile device payments, and lower voluntary benefit plan contributions, partly offset by higher cash tax payments. CapEx increased 8.8% y/y to \$4.6bn. Capital investment was \$5.6bn, including \$1bn of cash payments for vendor financing.

Net debt was almost flat q/q at \$128.9bn at the end of 4Q23. Total debt decreased 0.5% q/q to \$137.3bn. Total cash and marketables decreased 8.8% q/q to \$8.5bn. Net debt-to-adjusted EBITDA was almost flat q/q at 3. AT&T maintains its target to achieve a net debt-to-adjusted EBITDA ratio in the 2.5x range in the first half of 2025.

Financial Guidance for 2024

AT&T expects 5G and Fiber growth to continue. In 2024, AT&T expects wireless service revenue growth in the 3% range driven by a larger subscriber base and modest growth in postpaid phone ARPUs. Broadband revenue is expected to grow over 7% y/y driven by fiber subscriber growth and higher ARPUs from the mix shift to fiber. Adjusted EBITDA growth is expected to be in the 3% range driven by Mobility and Fiber, partially offset by Business Wireline. Capital investments are expected to be in the \$21-\$22bn range. Adjusted free operating cash flows (cash from operating activities- capital investments) are expected to be in the \$17-\$18bn range. Adjusted EPS is expected to be between \$2.15-\$2.25 vs \$0.54 in FY23.

Chart 1: Financial Results

(\$m)	Q4 2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	YOY	QOQ	FY 2022	FY 2023	YOY
Period End	'22/12	'23/3	'23/6	'23/9	'23/12			'22/12	'23/12	
■ P/L										
Revenues	31,343	30,139	29,917	30,350	32,022	2.2%	5.5%	120,741	122,428	1.4%
Operating Income	▲ 21,092	6,002	6,406	5,782	5,271	---	-8.8%	-4,587	23,461	---
Interest expense	▲ 1,560	▲ 1,708	▲ 1,608	▲ 1,662	▲ 1,726	10.6%	3.9%	▲ 6,108	▲ 6,704	9.8%
Interest Coverage Ratio	▲ 13.5	3.5	4.0	3.5	3.1	16.57	▲ 0.43	▲ 0.8	3.5	4.3
Pretax Income	▲ 23,197	5,767	6,165	4,980	2,936	---	-41.0%	-3,094	19,848	---
Net Income	▲ 23,571	4,176	4,437	3,444	2,135	---	-38.0%	▲ 8,727	14,192	---
EBITDA	▲ 16,497	10,633	11,081	10,487	10,037	---	-4.3%	13,434	42,238	214.4%
EBITDA margin	-52.6%	35.3%	37.0%	34.6%	31.3%	▲ 84.0	-3.2	11.1%	34.5%	23.4
Adjusted EBITDA	10,231	10,589	11,053	11,203	10,555	3.2%	-5.8%	41,465	43,400	4.7%
Adjusted EBITDA margin	32.6%	35.1%	36.9%	36.9%	33.0%	0.32	-3.95	34.3%	35.4%	1.1
■ C/F										
Cash from operations	10,313	6,678	9,922	10,336	11,378	10.3%	10.1%	32,023	38,314	19.6%
Depreciation & Amortization	4,595	4,631	4,675	4,705	4,766	3.7%	1.3%	18,021	18,777	4.2%
Cash from investing	▲ 3,823	▲ 3,818	▲ 5,423	▲ 4,545	▲ 5,874	53.6%	29.2%	▲ 25,805	▲ 19,660	-23.8%
CapEx	▲ 4,229	▲ 4,335	▲ 4,270	▲ 4,647	▲ 4,601	8.8%	-1.0%	▲ 19,626	▲ 17,853	-9.0%
Cash from financing	▲ 5,191	▲ 3,711	2,181	▲ 7,754	▲ 6,330	21.9%	-18.4%	▲ 23,741	▲ 15,614	-34.2%
Dividends	▲ 2,014	▲ 2,014	▲ 2,083	▲ 2,019	▲ 2,020	0.3%	0.0%	▲ 9,859	▲ 8,136	-17.5%
Free cash flow (FCF)	6,490	2,860	4,499	5,791	5,504	-15.2%	-5.0%	6,218	18,654	200.0%
Free operating cash flow (FOCF)	6,084	2,343	5,652	5,689	6,777	11.4%	19.1%	12,397	20,461	65.0%
Dividend payout ratio	33.1%	86.0%	36.9%	35.5%	29.8%	▲ 3.3	▲ 5.7	79.5%	39.8%	
RCF (CFO-CapEx-Dividends)	4,070	329	3,569	3,670	4,757	16.9%	29.6%	2,538	12,325	385.6%
Net cash flow	1,299	▲ 851	6,680	▲ 1,963	▲ 826	---	-57.9%	▲ 17,523	3,040	---
■ B/S										
Assets	402,853	400,873	408,453	406,698	407,060	1.0%	0.1%	402,853	407,060	1.0%
Current assets	33,108	29,903	36,672	35,620	36,458	10.1%	2.4%	33,108	36,458	10.1%
Cash&Marketables	3,701	2,821	11,328	9,290	8,472	128.9%	-8.8%	3,701	8,472	128.9%
Goodwill	67,895	67,895	67,854	67,854	67,854	-0.1%	0.0%	67,895	67,854	-0.1%
Liabilities	296,396	292,527	290,408	286,871	287,645	-3.0%	0.3%	296,396	287,645	-3.0%
Current liabilities	56,173	58,150	54,159	51,684	51,127	-9.0%	-1.1%	56,173	51,127	-9.0%
Total Debt	135,890	137,484	143,280	138,003	137,331	1.1%	-0.5%	135,890	137,331	1.1%
ST Debt	7,467	13,757	15,268	11,302	9,477	26.9%	-16.1%	7,467	9,477	26.9%
LT Debt	128,423	123,727	128,012	126,701	127,854	-0.4%	0.9%	128,423	127,854	-0.4%
Net Debt	132,189	134,663	131,952	128,713	128,859	-2.5%	0.1%	132,189	128,859	-2.5%
Equity	97,500	99,396	101,903	103,703	103,297	5.9%	-0.4%	97,500	103,297	5.9%
■ Financial Ratios										
Equity Ratio	24.2%	24.8%	24.9%	25.5%	25.4%	1.17	▲ 0.12	24.2%	25.4%	1.2
NetD/E	1.36	1.35	1.29	1.24	1.25	▲ 0.11	0.01	1.36	1.25	▲ 0.1
NetD/ EBITDA	10.70	10.37	8.38	8.20	3.05	▲ 7.65	▲ 5.15	9.84	3.05	▲ 6.8
NetD/adjusted EBITDA	3.19	3.22	3.10	2.99	2.97	▲ 0.22	▲ 0.02	3.19	2.97	▲ 0.2
ROA	-2.1%	-2.3%	-2.2%	-2.8%	3.5%	5.59	6.31	-1.8%	3.5%	5.3
ROE	-7.9%	-9.5%	-8.9%	-11.2%	13.7%	21.65	24.91	-6.6%	14.1%	20.8

Source: Company materials, Bloomberg; compiled by Daiwa.

Chart 2: Segment Results

(\$m)	Q4 2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	YOY	FY 2022	FY 2023	YOY
Period End	'22/12	'23/3	'23/6	'23/9	'23/12		2022/12/31	2023/12/31	
Operating Revenues	31,343	30,139	29,917	30,350	32,022	2.2%	120,211	121,970	1%
Communications	30,365	29,152	28,845	29,244	30,797	1.4%	117,067	118,038	1%
Mobility	21,501	20,582	20,315	20,692	22,393	4.1%	81,780	83,982	3%
Business Wireline	5,635	5,331	5,279	5,221	5,052	-10.3%	22,538	20,883	-7%
Consumer Wireline	3,229	3,239	3,251	3,331	3,352	3.8%	12,749	13,173	3%
Latin America-Mexico	861	883	967	992	1,090	26.6%	3,144	3,932	25%
Corporate and others	117	104	105	114	135	15.4%			
Adjusted EBITDA	10,231	10,589	11,053	11,203	10,555	3.2%	43,749	45,747	5%
Communications	10,835	11,032	11,490	11,623	11,019	1.7%	43,417	45,164	4%
Mobility	7,929	8,369	8,736	8,897	8,376	5.6%	32,010	34,378	7%
Business Wireline	1,900	1,708	1,729	1,695	1,534	-19.3%	7,604	6,666	-12%
Consumer Wireline	1,006	955	1,025	1,031	1,109	10.2%	3,803	4,120	8%
Latin America-Mexico	85	145	146	155	137	61.2%	332	583	76%
Corporate/ eliminations	▲ 689	▲ 588	▲ 583	▲ 575	▲ 601	---			
Adjusted EBITDA Margin	32.6%	35.1%	36.9%	36.9%	33.0%	0.4	36.4%	37.5%	1.1
Communications	35.7%	37.8%	39.8%	39.7%	35.8%	0.1	37.1%	38.3%	1.2
Mobility	36.9%	40.7%	43.0%	43.0%	37.4%	0.5	39.1%	40.9%	1.8
Business Wireline	33.7%	32.0%	32.8%	32.5%	30.4%	-3.3	33.7%	31.9%	▲ 1.8
Consumer Wireline	31.2%	29.5%	31.5%	31.0%	33.1%	1.9	29.8%	31.3%	1.4
Latin America-Mexico	9.9%	16.4%	15.1%	15.6%	12.6%	2.7	10.6%	14.8%	4.3

Source: Company materials, Bloomberg; compiled by Daiwa.

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