



AT&T Inc. (T)

Updated July 22nd, 2021, by Eli Inkrot

Key Metrics

Current Price:	\$28	5 Year CAGR Estimate:	13.4%	Market Cap:	\$199 B
Fair Value Price:	\$36	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	07/08/21
% Fair Value:	78%	5 Year Valuation Multiple Estimate:	5.1%	Dividend Payment Date:	08/02/21
Dividend Yield:	7.4%	5 Year Price Target	\$41	Years Of Dividend Growth:	36
Dividend Risk Score:	B	Retirement Suitability Score:	A	Last Dividend Increase:	2.0%

Overview & Current Events

While the history of AT&T dates to Alexander Graham Bell and the original telephone in the late-1800's, the current iteration of the firm is rooted in a spun off "baby bell," SBC, that acquired AT&T Corp. in 2005 and changed its name to AT&T Inc. Today AT&T is the largest communications company in the world, operating in three business units: AT&T Communications (providing mobile, broadband and video), WarnerMedia (including Turner, HBO, Warner Bros. and Xandr) and AT&T Latin America. The \$199 billion company generated \$172 billion in revenue in 2020.

On February 25th, 2021, AT&T announced it will spin off a separate company called 'New DIRECTV' that will own 'old' DIRECTV, AT&T TV, and U-verse video. AT&T will receive ~\$7.8 billion from New DIRECTV and TPG Capital will contribute \$1.8 billion for a 30% stake. AT&T will own 70% of the company after contributing its U.S. video business.

On May 17th, 2021, AT&T announced an agreement to combine WarnerMedia with Discovery, Inc. to create a new global entertainment company. Under the terms of the transaction AT&T will receive \$43 billion in a combination of cash, securities and retention of debt. In addition, AT&T shareholders receive stock representing 71% of the new company, with Discovery shareholders owning 29%. The company will combine HBO Max and Dsicovey+ to compete in the direct-to-consumer business, bringing together names like HBO, Warner Bros., Discovery, CNN, HGTV, Food Network, TNT, TBS and more. The new company expects \$52 billion in 2023 revenue and the transaction is expected to close in mid-2022.

Following the close of the transaction, the remaining AT&T business expects low single digit revenue growth, mid-single digit adjusted earnings-per-share growth and a resized dividend of ~\$1.15.

On July 21st, 2021, AT&T announced that it was selling its Latin America digital entertainment unit, Vrio, to Grupo Werthein. The transaction is expected to close in early 2022.

On July 22nd, 2021, AT&T reported Q2 2021 results for the period ending June 30th, 2021. For the quarter the company generated \$44.0 billion in revenue, up 7.6% from \$41.0 billion in Q2 2020, reflecting a partial recovery from the prior year impacts of the COVID-19 pandemic. Reported net income equaled \$1.5 billion or \$0.21 per share. On an adjusted basis, earnings-per-share equaled \$0.89 compared to \$0.83 in the year ago quarter. AT&T ended the quarter with a net debt-to-EBITDA ratio of 3.15x.

AT&T also updated its fiscal 2021 guidance, anticipating low-to-mid single digit adjusted EPS growth.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$2.20	\$2.33	\$2.50	\$2.50	\$2.69	\$2.84	\$3.05	\$3.52	\$3.58	\$3.18	\$3.25	\$3.77
DPS	\$1.72	\$1.76	\$1.80	\$1.84	\$1.88	\$1.92	\$1.96	\$2.00	\$2.04	\$2.08	\$2.08	\$2.28
Shares¹	5,927	5,581	5,226	5,187	6,145	6,139	6,139	7,282	7,255	7,126	7,125	7,125

AT&T is a colossal business, easily generating profits of \$20+ billion annually, but it is not a fast grower. From 2007 through 2019 AT&T grew earnings-per-share by 2.2% per annum, with 2020 being a down year. The company had been optimistic about generating growth, but that has not yet come to fruition.

After paying \$65 billion for DIRECT-TV in 2015 and \$85 billion for Time Warner in 2018, AT&T reversed course in 2021, deciding to spin off both businesses. The company's strategy of integration clearly did not work and now AT&T is in the

¹ In millions.

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unfavorable position of unwinding assets shortly after those transactions were completed. The DIRECT-TV spin-off price tag, implying an enterprise value of \$16.25 billion, sticks out in particular.

Still, AT&T will receive significant cash from each transaction, enabling it to reduce its debt. Furthermore, the company is focusing on its roots and has growth opportunities in the way of building out its 5G network. We are forecasting \$3.25 in EPS for this year to go along with a 3% annual growth rate, until the above transactions are finalized.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Avg. P/E	13.4	14.5	14.2	13.8	12.6	13.8	12.7	9.5	9.5	9.8	8.6	11.0
Avg. Yld.	5.8%	5.2%	5.1%	5.3%	5.6%	4.9%	5.1%	6.0%	6.0%	6.7%	7.4%	5.5%

During the past decade shares of AT&T have traded with an average P/E ratio of about 12 times earnings. We believe 11 times earnings is a fair baseline, given that growth prospects are unknown, the dividend is robust for now, and the payout ratio is getting better. At the current valuation, there is the potential for an uptick in valuation.

AT&T has a record of not only paying but also increasing its dividend for 36 consecutive years. This payout will be reduced with the WarnerMedia spin-off, and it is not clear what the combined payout will be yet.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	78%	76%	72%	74%	70%	68%	64%	57%	57%	65%	64%	61%

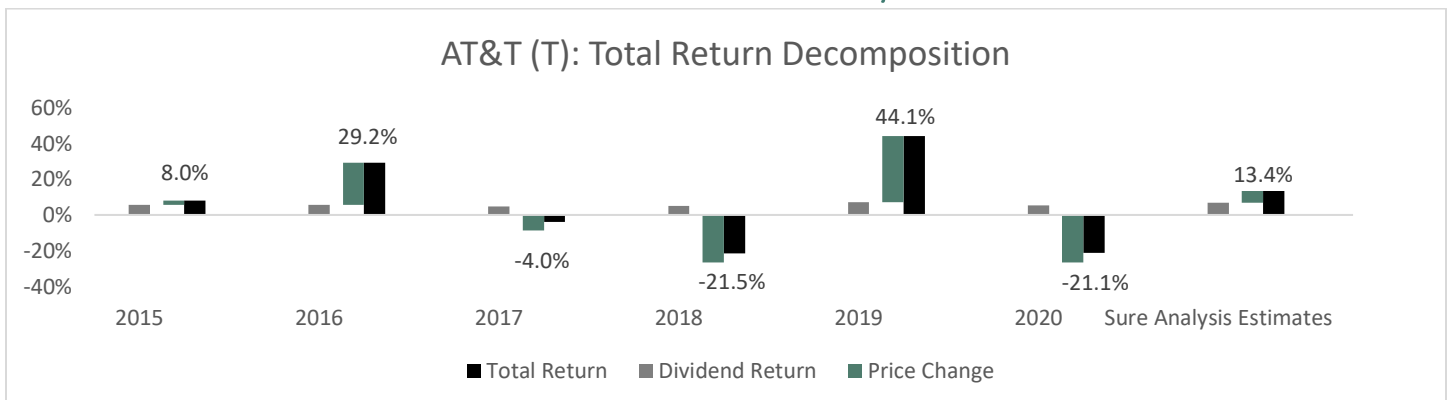
AT&T has a competitive advantage with its entrenched position in various important industries. However, this will change once the WarnerMedia, and DIRECT-TV spin-offs are complete. Debt has always been a sticking point for the business. At the close of the Time Warner merger, it equaled \$180 billion, and the net-debt-to-adjusted EBITDA metric came in at 3.0x. At the end of 2018, 2019 and 2020 this figure was 2.8x, 2.5x and 2.7x respectively.

During the last recession AT&T posted results of \$2.76, \$2.16, \$2.12 and \$2.29 in earnings-per-share for the 2007 through 2010 period. The company did not eclipse \$2.76 in EPS until 2016, but the dividend continued to grow.

Final Thoughts & Recommendation

Shares are down marginally since our last report. In our view AT&T faces two main challenges: a slow-moving business and a material debt load. The company is trying to address these by spinning off businesses, but it is not yet clear if the legacy business will see reignited growth as a result. Total return potential of 13.4%, stemming from 3% growth, a 7.4% dividend yield and a valuation tailwind, is appealing. However, the uncertainty related to the proposed transactions, and a likely lower dividend payout, make us a bit more cautious. Even so, shares continue to earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue (\$B)	126.7	127.4	128.8	132.4	146.8	163.8	160.5	170.8	181.2	171.8
Gross Profit	71819	72206	77561	72302	79755	86596	82736	91337	97052	91840
Gross Margin	56.7%	56.7%	60.2%	54.6%	54.3%	52.9%	51.5%	53.5%	53.6%	53.5%
SG&A Exp.	41314	41066	28414	39697	32919	36845	35465	36765	39422	38040
D&A Exp.	18377	18143	18395	18273	22016	25847	24387	28430	28217	28520
Operating Profit	12128	12997	30752	14332	24820	23904	22884	26142	29413	25280
Op. Margin	9.6%	10.2%	23.9%	10.8%	16.9%	14.6%	14.3%	15.3%	16.2%	14.7%
Net Profit	3944	7264	18418	6442	13345	12976	29450	19370	13903	-5176
Net Margin	3.1%	5.7%	14.3%	4.9%	9.1%	7.9%	18.3%	11.3%	7.7%	-3.0%
Free Cash Flow	14633	19711	13852	10139	16662	16926	17363	22844	29233	27460
Income Tax	2532	2900	9328	3619	7005	6479	-14.7B	4920	3493	965

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets (\$B)	270.4	272.3	277.8	296.8	402.7	403.8	444.1	531.9	551.7	525.8
Cash & Equivalents	3045	4868	3339	8603	5121	5788	50498	5204	12130	9740
Acc. Receivable	13231	12657	12918	14527	16532	16794	16522	26472	22636	20220
Goodwill/Int. (\$B)	130.2	128.5	131.5	136.7	225.3	222.1	219.7	310.2	303.9	281.6
Total Liab. (\$B)	164.6	179.6	186.3	206.6	279.0	279.7	302.1	338.0	349.7	346.5
Accounts Payable	10485	12076	11561	14984	21047	22027	24439	27018	29640	31840
LT Debt (\$B)	64.8	69.8	74.8	81.8	126.2	123.5	164.3	176.5	161.1	155.2
Total Equity (\$B)	105.5	92.4	91.0	89.7	122.7	123.1	140.9	184.1	184.2	161.7
D/E Ratio	0.61	0.76	0.82	0.91	1.03	1.00	1.17	0.96	0.87	0.96

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	1.5%	2.7%	6.7%	2.2%	3.8%	3.2%	6.9%	4.0%	2.6%	-1.0%
Return on Equity	3.6%	7.3%	20.1%	7.1%	12.6%	10.6%	22.3%	11.9%	7.5%	-3.0%
ROIC	2.3%	4.4%	11.2%	3.8%	6.3%	5.2%	10.6%	5.7%	3.8%	-1.5%
Shares Out.	5,927	5,581	5,226	5,187	6,145	6,139	6,139	7,282	7,348	7,183
Revenue/Share	21.30	21.89	23.91	25.37	26.00	26.46	25.97	25.09	24.65	23.91
FCF/Share	2.46	3.39	2.57	1.94	2.95	2.73	2.81	3.36	3.98	3.82

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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