



AT&T Inc. (T)

Updated October 28th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$39	5 Year CAGR Estimate:	10.6%	Volatility Percentile:	29.2%
Fair Value Price:	\$44	5 Year Growth Estimate:	4.0%	Momentum Percentile:	82.3%
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.5%	Growth Percentile:	27.7%
Dividend Yield:	5.3%	5 Year Price Target	\$53	Valuation Percentile:	82.6%
Dividend Risk Score:	B	Retirement Suitability Score:	A	Total Return Percentile:	78.9%

Overview & Current Events

While the history of AT&T dates back 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 four distinct business units: AT&T Communications (providing mobile, broadband, video and other communications services to more than 100 million U.S. consumers and more than 3 million businesses), WarnerMedia (including Turner, HBO and Warner Bros.), AT&T Latin America (offering pay-TV and wireless service to 11 countries) and Xandr (providing advertising). The \$285 billion market cap company, with over 260,000 employees, generated \$170 billion in annual revenue last year.

On October 28th, 2019 AT&T reported Q3 2019 results for the period ending September 30th, 2019. For the quarter the company generated \$44.6 billion in revenue, down from \$45.7 billion in the year-ago quarter, as declines in legacy wireline services, WarnerMedia and domestic video were partially offset by growth in strategic and managed business services, domestic wireless services and IP broadband. Net Income came to \$3.7 billion or \$0.50 per share versus \$4.7 billion or \$0.65 per share prior. On an adjusted basis, earnings-per-share equaled \$0.94 compared to \$0.90 previously.

AT&T also provided a 2020 outlook and 3-year financial guidance and capital allocation plan. For 2020 the company expects revenue growth of 1% to 2%, adjusted earnings-per-share of \$3.60 to \$3.70 and a dividend payout ratio in the low-50% range. By 2022, AT&T expects 1% to 2% revenue growth, \$4.50 to \$4.80 in earnings-per-share, continued dividend increases making up less than 50% of free cash flow and a net-debt-to-adjusted EBITDA ratio of 2.0x to 2.25x.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$2.12	\$2.29	\$2.20	\$2.33	\$2.50	\$2.50	\$2.69	\$2.84	\$3.05	\$3.52	\$3.65	\$4.44
DPS	\$1.64	\$1.68	\$1.72	\$1.76	\$1.80	\$1.84	\$1.88	\$1.92	\$1.96	\$2.00	\$2.04	\$2.24
Shares¹	5,902	5,911	5,927	5,581	5,226	5,187	6,145	6,139	6,139	7,282	7,356	7,300

AT&T is a colossal business, easily generating profits of \$20+ billion annually, but it is not a fast grower. From 2007 through 2018 AT&T grew earnings-per-share by 2.2% per annum. While the company is picking up growth opportunities, notably in its recent acquisitions of DirecTV and Time Warner, we are cognizant of both the premiums paid and the fact that the company's legacy businesses are steady or declining. AT&T is optimistic about generating reasonable growth and the payout ratio is falling, resulting in excess funds to divert toward paying down debt. Moreover, after the debt is under control, management has indicated the potential for share repurchases down the line. While the company put out strong growth expectations through 2022, we are somewhat cautious forecasting 4% annual growth instead.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	12.1	11.7	13.4	14.5	14.2	13.8	12.6	13.8	12.7	9.5	10.6	12.0
Avg. Yld.	6.4%	6.3%	5.8%	5.2%	5.1%	5.3%	5.6%	4.9%	5.1%	6.0%	5.3%	4.2%

¹ In millions.

Disclosure: This analyst is long the security discussed in this research report.



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During the past decade shares of AT&T have traded with an average P/E ratio of around 12 to 13 times earnings, with a range of 8 to 16. We believe something in the middle of that range is fair, given that new growth prospects are not yet proven, the dividend is robust and the payout ratio is getting better. At the current valuation, there is the potential for a moderate uptick in valuation.

AT&T has a record of not only paying but also increasing its dividend for 35 consecutive years. Granted this payment has only been increasing by 4 cents annually for the last decade, but it remains an important driver of shareholder returns. From this point, with a well above average dividend yield, protecting the payout is more important than growing it.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	77%	73%	78%	76%	72%	74%	70%	68%	64%	57%	56%	50%

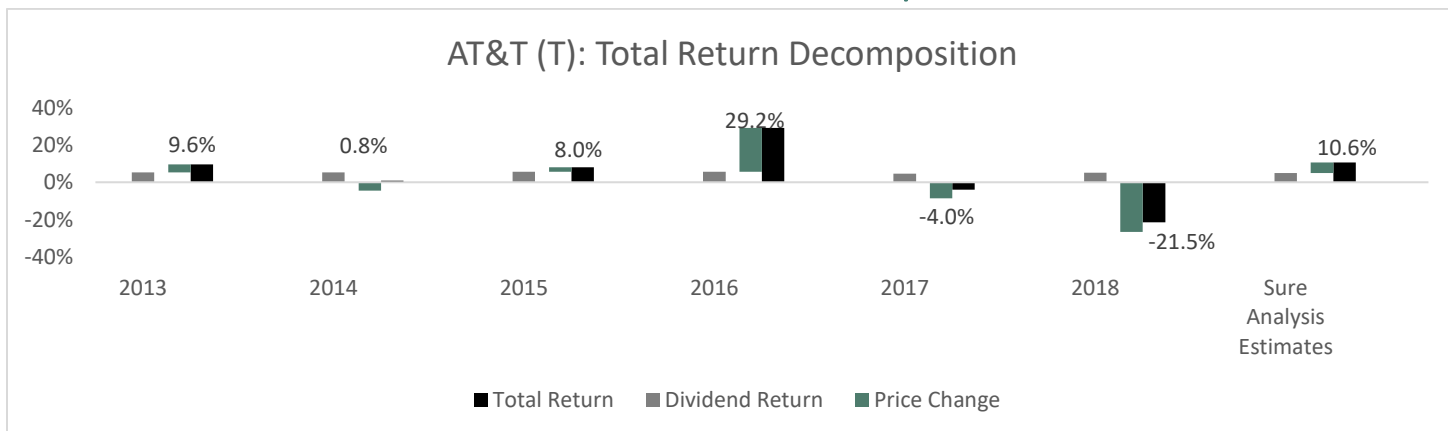
AT&T has a competitive advantage with its entrenched position in various important industries. Although this position could be eroding due to technological change, it remains that the company has direct contact with 170 million customers. However, the debt is an issue. At the close of the Time Warner merger it equaled \$180 billion and the net-debt-to-adjusted EBITDA metric came in at 3.0x. By the end of 2018 this number got down to 2.8x. The goal is to get it down to 2.0x to 2.25x by 2022. This is a great goal, but the execution of this plan will still be key.

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 its pre-recession high on an earnings basis until 2016, but the dividend did continue to grow throughout the entire period. Speaking of which, we are encouraged with the progress made on the dividend payout ratio, moving from 77% in 2009 down to 56% today. Some bemoan the slow rate of dividend growth, but we believe it has (and will continue to be) prudent given the company's current financial position.

Final Thoughts & Recommendation

Shares are up 18% since our last report, while earnings expectations have improved as well. In our view AT&T faces two main challenges: a slow moving business and a significant debt load. If it can overcome these obstacles the valuation multiple could expand. Indeed, management has put forth a plan to grow materially in the coming years. Total return potential is appealing, with a 5.3% starting yield, a 4% expected growth rate and the potential for a small improvement in valuation, adding up to a 10.6% prospective annual gains. The much higher share price in the last three months has been somewhat justified, with a significantly improved business outlook as well. We acknowledge the risks in the business, especially as it relates to the transition away from legacy businesses, but we believe the current value proposition makes up for a lot of this. We continue to award the security with a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue (\$B)	122.5	124.3	126.7	127.4	128.8	132.4	146.8	163.8	160.5	170.8
Gross Profit	71942	74023	71819	72206	77561	72302	79755	86596	82736	91337
Gross Margin	58.7%	59.6%	56.7%	56.7%	60.2%	54.6%	54.3%	52.9%	51.5%	53.5%
SG&A Exp.	31427	34986	41314	41066	28414	39697	32919	36845	35465	36765
D&A Exp.	N/A	19379	18377	18143	18395	18273	22016	25847	24387	28430
Operating Profit	21000	19658	12128	12997	30752	14332	24820	23904	22884	26142
Op. Margin	17.1%	15.8%	9.6%	10.2%	23.9%	10.8%	16.9%	14.6%	14.3%	15.3%
Net Profit	12138	19085	3944	7264	18418	6442	13345	12976	29450	19370
Net Margin	9.9%	15.4%	3.1%	5.7%	14.3%	4.9%	9.1%	7.9%	18.3%	11.3%
Free Cash Flow	17111	15692	14633	19711	13852	10139	16662	16926	17363	22844
Income Tax	6091	-1162	2532	2900	9328	3619	7005	6479	-14.7B	4920

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets (\$B)	268.3	269.4	270.4	272.3	277.8	296.8	402.7	403.8	444.1	531.9
Cash & Equivalents	3741	1437	3045	4868	3339	8603	5121	5788	50498	5204
Acc. Receivable	14845	13610	13231	12657	12918	14527	16532	16794	16522	26472
Goodwill/Int. (\$B)	134.4	134.1	130.2	128.5	131.5	136.7	225.3	222.1	219.7	310.2
Total Liab. (\$B)	166.3	157.4	164.6	179.6	186.3	206.6	279.0	279.7	302.1	338.0
Accounts Payable	21260	7437	10485	12076	11561	14984	21047	22027	24439	27018
LT Debt (\$B)	76.3	66.2	64.8	69.8	74.8	81.8	126.2	123.5	164.3	176.5
Total Equity (\$B)	101.6	111.6	105.5	92.4	91.0	89.7	122.7	123.1	140.9	184.1
D/E Ratio	0.75	0.59	0.61	0.76	0.82	0.91	1.03	1.00	1.17	0.96

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	4.5%	7.1%	1.5%	2.7%	6.7%	2.2%	3.8%	3.2%	6.9%	4.0%
Return on Equity	12.3%	17.9%	3.6%	7.3%	20.1%	7.1%	12.6%	10.6%	22.3%	11.9%
ROIC	6.9%	10.7%	2.3%	4.4%	11.2%	3.8%	6.3%	5.2%	10.6%	5.7%
Shares Out.	5,902	5,911	5,927	5,581	5,226	5,187	6,145	6,139	6,139	7,282
Revenue/Share	20.68	20.93	21.30	21.89	23.91	25.37	26.00	26.46	25.97	25.09
FCF/Share	2.89	2.64	2.46	3.39	2.57	1.94	2.95	2.73	2.81	3.36

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

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