



Lumen Technologies (LUMN)

Updated May 13th, 2022 by Quinn Mohammed

Key Metrics

| | | | | | |
|-----------------------------|------|--|------|--------------------------------------|------------|
| Current Price: | \$12 | 5 Year CAGR Estimate: | 9.3% | Market Cap: | \$12 B |
| Fair Value Price: | \$12 | 5 Year Growth Estimate: | 1.0% | Ex-Dividend Date¹: | 05/27/2022 |
| % Fair Value: | 93% | 5 Year Valuation Multiple Estimate: | 1.5% | Payment Date²: | 06/10/2022 |
| Dividend Yield: | 8.6% | 5 Year Price Target | \$13 | Last Dividend Increase: | 0 |
| Dividend Risk Score: | F | Retirement Suitability Score: | B | Rating: | Buy |

Overview & Current Events

Lumen Technologies traces its roots to 1930 when the Oak Ridge Telephone Company was purchased by the Williams family. They would eventually expand exponentially into what has become Lumen, which serves customers in over 60 different countries today. It has an \$12 billion market capitalization and produced \$19.7 billion in revenue in 2021. The name Lumen was brought about in September 2020 to rebrand and reposition the company as a critical partner in leading enterprises through the 4th Industrial Revolution – or the smart technology revolution. Lumen will help customers deliver things such as smart cities, retail and industrial robots, real-time virtual collaboration, and automated factories.

Lumen Technologies reported first quarter 2022 results on May 4th, for the period ending March 31st, 2022. Total revenues for the quarter were \$4.68 billion, down from \$5.03 billion in the prior year first quarter. Adjusted earnings per share of \$0.63 was a 43% increase over \$0.44 earned in the same prior year period.

Long-term debt of \$28.4 billion remains outstanding. Mass markets broadband subscribers fell from one year ago to 4,470 as of March 31st, 2021.

At the end of the quarter, Lumen had cash and cash equivalents of \$366 million.

The company experienced some adjusted EBITDA margin contraction, as it stands at 40.9% vs 42.9% last year.

Management increased its 2022 outlook, where adjusted EBITDA is seen coming at \$6.9 billion to \$7.1 billion (up from a mid-point of \$6.6 billion at previous outlook). Free cash flow outlook is roughly \$2.0 billion (up from \$1.7 billion at previous outlook) expected in 2022.

Growth on a Per-Share Basis

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | \$1.25 | \$1.64 | \$2.61 | \$2.72 | \$2.45 | \$1.58 | \$1.19 | \$1.32 | \$1.51 | \$1.91 | \$1.56 | \$1.64 |
| DPS | \$2.90 | \$2.16 | \$2.16 | \$2.16 | \$2.16 | \$2.16 | \$2.16 | \$1.00 | \$1.00 | \$1.00 | \$1.00 | \$1.00 |
| Shares³ | 626 | 584 | 569 | 544 | 547 | 1,069 | 1,067 | 1,078 | 1,080 | 1,067 | 1015.0 | 1015.0 |

Lumen has struggled in recent years with competition as well as profitability. The Level 3 acquisition has seen the company's share count doubled in 2017. In addition, it took on another \$13 billion in debt with the transaction onto a balance sheet that was already in poor shape.

That said, we see 1.0% annual growth going forward as it has some catalysts for earnings expansion. Revenue should continue to move higher from the Level 3 merger. The company is also investing to expand its network footprint and enhance its product portfolio. Lumen is ramping up its quantum fiber enablements in 2022, with an addressable fiber opportunity of over 12 million. Reduced leverage should help improve margins over time as well as less of the company's earnings will be consumed by interest expense.

¹ Estimate

² Estimate

³ In millions

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Following the dividend cut in early 2019, we do not believe management will raise the payout anytime soon given the aggressive leverage target of around 3.0 times EBITDA.

Valuation Analysis

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | Now | 2027 |
|-----------|------|------|------|------|------|------|-------|-------|------|------|------|------|
| Avg. P/E | 31.4 | 21.3 | 14 | 11.6 | 11.4 | 13.9 | 13.3 | 10.8 | 8.8 | 6.6 | 7.4 | 8.0 |
| Avg. Yld. | 7.4% | 6.2% | 5.9% | 6.9% | 7.7% | 9.8% | 11.4% | 13.0% | 9.5% | 7.8% | 8.6% | 7.6% |

Lumen's volatile price-to-earnings ratio stands at 7.4 now as earnings remain below record levels. We estimate fair value at 8 times earnings given the weakness in the company's recent results, which implies the potential for a valuation tailwind. We see the yield falling as a result of a higher share price and flat payout, but it will still be strong, at 7.6%. The recent rebranding of the company as a "technology" company may push the estimated PE slightly higher in the near term, but we would like to see solid growth first.

Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 232% | 132% | 83% | 79% | 88% | 137% | 182% | 76% | 66% | 52% | 64% | 61% |

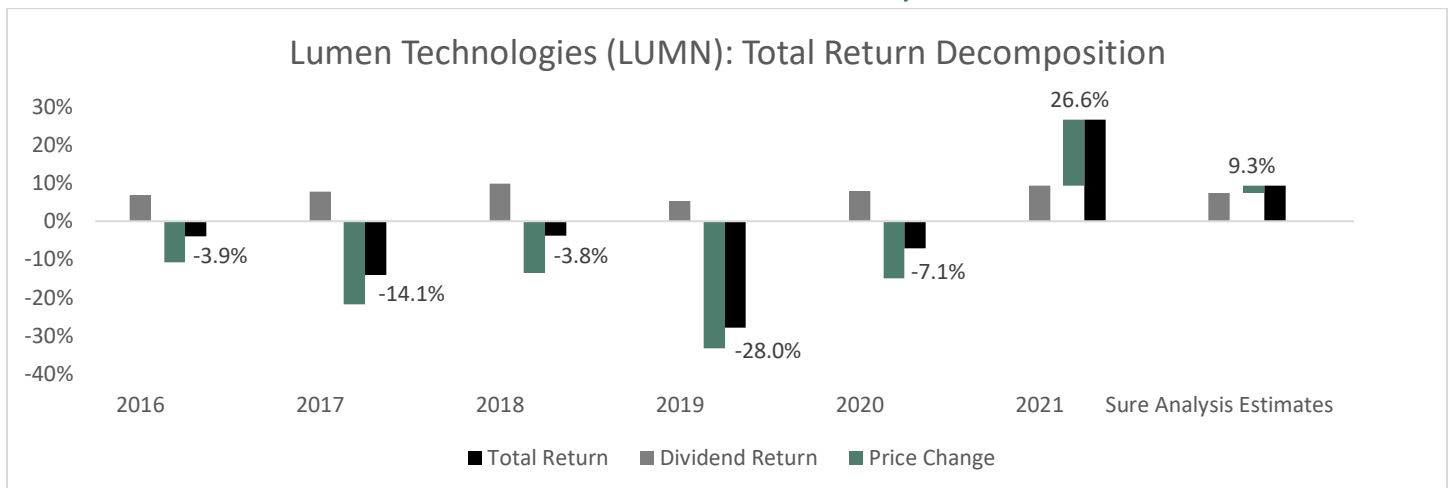
Lumen's payout ratio is now back under 100% after the dividend cut, and we expect the dividend will remain at \$1 per share for the foreseeable future. Management has made it clear the priority is reducing leverage, so we see the payout ratio drifting lower over time as earnings grow but the dividend remains steady.

Lumen's competitive advantage is in its diversified model as well as its tremendous size and geographic reach. It can negotiate in ways smaller competitors cannot and its global footprint provides valuable diversification. While the COVID-19 pandemic overhangs the economy, CTL has a large and diversified customer base with only a small amount of total revenue coming from highly impacted customers (retail, restaurants, hotels, etc.).

Final Thoughts & Recommendation

Lumen Technologies is a stock that offers minor growth potential but a large yield. We see annualized total returns of 9.3% going forward, most of which comes from the dividend. Thus, it is a buy for aggressive investors, but we caution conservative dividend growth investors that it remains a high-risk, high-reward situation, particularly considering the recent dividend cut and declining revenue.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Revenue | 18,376 | 18,095 | 18,031 | 17,900 | 17,470 | 17,656 | 23,443 | 22,401 | 20,712 | 19,687 |
| Gross Profit | 10,737 | 10,588 | 10,185 | 10,122 | 9,696 | 9,453 | 12,581 | 12,324 | 11,778 | 11,199 |
| Gross Margin | 58.4% | 58.5% | 56.5% | 56.5% | 55.5% | 53.5% | 53.7% | 55.0% | 56.9% | 56.9% |
| SG&A Exp. | 3,244 | 3,502 | 3,347 | 3,354 | 3,447 | 3,508 | 4,165 | 3,715 | 3,464 | 2,895 |
| D&A Exp. | 4,,780 | 4,541 | 4,428 | 4,189 | 3,916 | 3,936 | 5,120 | 4,,829 | 4,710 | 4,,019 |
| Operating Profit | 2713 | 2,545 | 2,410 | 2,579 | 2,333 | 2,009 | 3,296 | 3780 | 3,604 | 4285 |
| Operating Margin | 14.8% | 14.1% | 13.4% | 14.4% | 13.4% | 11.4% | 14.1% | 16.9% | 17.4% | 21.8% |
| Net Profit | 777 | -239 | 772 | 878 | 626 | 1,389 | -1,733 | -5,269 | -1,232 | 2,033 |
| Net Margin | 4.2% | -1.3% | 4.3% | 4.9% | 3.6% | 7.9% | -7.4% | -23.5% | -5.9% | 10.3% |
| Free Cash Flow | 3,146 | 2,511 | 2,141 | 2,281 | 1,627 | 772 | 3,857 | 3,052 | 2,795 | 3,601 |
| Income Tax | 473 | 463 | 338 | 438 | 394 | -849 | 170 | 503 | 450 | 668 |

Balance Sheet Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|----------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Total Assets | 5,3940 | 51,787 | 49,103 | 47,604 | 47,017 | 75,611 | 70,256 | 64,742 | 59,394 | 57,993 |
| Cash & Equivalents | 211 | 168 | 128 | 126 | 222 | 551 | 488 | 1,690 | 406 | 354 |
| Accounts Receivable | 1,782 | 1,862 | 1,821 | 1,789 | 1882 | 2,245 | 2,094 | | 1,962 | 1,544 |
| Inventories | 125 | 167 | 132 | 144 | 134 | 128 | 120 | | | |
| Goodwill & Int. Ass. | 30,597 | 28,411 | 27,295 | 26,225 | 23,978 | 43,248 | 38,810 | 21,534 | 27,089 | 22,956 |
| Total Liabilities | 34,651 | 34,596 | 34,080 | 33,544 | 33,618 | 52,120 | 50,428 | 5,1272 | 48,232 | 46,153 |
| Accounts Payable | 1,207 | 1,111 | 1,226 | 968 | 1,179 | 1,555 | 1,933 | | 1,134 | 758 |
| Long-Term Debt | 20,605 | 20,966 | 20,503 | 20,225 | 19,688 | 37,726 | 36,061 | 34,694 | 31,837 | 28,982 |
| Shareholder's Equity | 19,289 | 17,191 | 15,023 | 14,060 | 13,399 | 23,491 | 19,828 | 13,470 | 11,162 | 11,840 |
| LTD/E Ratio | 1.07 | 1.22 | 1.36 | 1.44 | 1.47 | 1.61 | 1.82 | 2.58 | 2.85 | 2.45 |

Profitability & Per Share Metrics

| Year | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 |
|------------------|-------|-------|-------|-------|-------|-------|-------|--------|--------|-------|
| Return on Assets | 1.4% | -0.5% | 1.5% | 1.8% | 1.3% | 2.3% | -2.4% | -7.8% | -2.0% | 3.5% |
| Return on Equity | 3.9% | -1.3% | 4.8% | 6.0% | 4.6% | 7.5% | -8.0% | -31.6% | -10.0% | 17.7% |
| ROIC | 1.9% | -0.6% | 2.1% | 2.5% | 1.9% | 2.9% | -3.0% | -10.1% | -2.7% | 4.9% |
| Shares Out. | 626 | 584 | 569 | 544 | 547 | 1,069 | 1,067 | 1,078 | 1,080 | 1,067 |
| Revenue/Share | 29.53 | 30.11 | 31.65 | 32.25 | 32.31 | 28.08 | 21.99 | 20.91 | 19.19 | 18.45 |
| FCF/Share | 5.06 | 4.18 | 3.76 | 4.11 | 3.01 | 1.23 | 3.62 | 2.85 | 2.59 | 3.38 |

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