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PRESENTATION

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Okay. Good morning, everybody. Thanks for joining us. I'm delighted to welcome Jeff McElfresh from AT&T. Welcome, Jeff. Thanks for being here.

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Thanks for inviting me.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Before we get started, let's do the research disclosures, for important disclosures please see the Morgan Stanley research disclosure website at www.morganstanley.com/researchdisclosures. If you have any questions, please reach out to your Morgan Stanley representatives.

Jeffery Scott McElfresh - *AT&T Inc. - COO*

And I have one as well. You're not the only one. That's why I'm pulling my phone out here to keep the attorneys happy. Before we begin, I need to call your attention to our safe harbor statement, which basically says some of our comments today may be forward-looking. As such, they're subject to risks and uncertainties. Results may differ materially. Additional information is available on our Investor Relations website.

QUESTIONS AND ANSWERS

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. Well, we've got a lot to talk about today. You put out some pretty constructive guidance around the wireless business for 2023 despite concerns about the overall industry slowing. But let's start just broadly with the strategy and with the key priorities for '23 and beyond.

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. So Simon, I think as our CEO announced in the fourth quarter earnings, we're really pleased with the progress that we made as a company. And our go-forward strategy is the same as what we've been executing over the last year or so. We clearly are investing to grow the business. And as you think about it as an investor, the investments that we're making are not only in our networks, but also in attractive customers across our growth segments.

Second priority of the company continues, and it's really kind of my core job is to take cost out of the business, improve the operating leverage of the operation, and we're on a multiyear transformation journey, and we're just now starting to see the fruits of that come to the bottom line, as you probably noticed in our fourth quarter results.

And then last, but very important to us. Our third priority is a very deliberate capital allocation strategy and to achieve our leverage targets that we've committed to the Street. So those balancing acts continue to drive our core strategy in the business.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. And macro has been on a lot of people's minds today. And you had some cautious comments a few quarters ago. Where do we stand today with your consumer customers and with your enterprise customers?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes, we did, Simon. In fact, I think our CEO, John might have been one of the first to kind of call out, hey, we're looking at this. I can tell you, though, we don't know how to predict what's going to happen, but I am confident we've proven we know how to manage through any kind of turbulence that we see there as we experienced in 2022.

And all of that's basically factored into the guidance that we offered in the fourth quarter earnings. I will say from the health of the consumer or enterprise customers, we haven't really seen anything that is dramatic. It's been relatively stable over the course of the back half of last year. But we're watching it every day. As you would expect us as operators to do. We look at intake quality, credit levels, we look at churn. We look at those metrics on a daily basis as leading indicators. And so far, we don't see anything that's going to change the way we are going about with our operating plan for 2023, and I'm here to reassert that the guidance that we offered in the fourth quarter still holds.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. Right. So let's start with mobile, if we can, 4% plus wireless service revenue growth. What gave you the confidence to provide that guidance -- about in this uncertain environment?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Well, we've achieved better than that, as you noticed in our fourth quarter results. But we know what we've done operationally with our distribution and our go-to-market offers in the segments at which we are finding some success in 2022, and we're calling that to continue even in the competitive market that we've experienced.

Growth of high-quality subscribers, coupled with many other levers that haven't fully recovered. International roaming, for example, still isn't at the magnitude it was prior to the pandemic. And we've seen some recovery of that, but there's still room there. And I'd offer we're not complete as an industry with the 5G conversion, and we still have customers coming up on contract and upgrading to our best rate plans.

And if you think about all those levers, our ARPU growth and our subscriber growth gives us confidence that service revenue growth 4% is an appropriate number.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. Great. Well, I think you've surprised a lot of people would also ourselves to some extent, with the sustainability of the ads, you'd call for a slower momentum, but [that it] come in stronger. What is it that's allowing you to continue to deliver these numbers and you're expecting some of that for next -- this coming year?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Well, of course, I'm not going to disclose all the great stuff that we're doing. All kidding aside, we -- if you go back a couple of years and you think about the consistency that AT&T has been approaching the market, I hope by now that the public and the investment community can see the consistency at which we've gone about with our offer strategy and our go-to-market strategy.

That consistency is important to us because the changes that structure and efficacy in these points of distribution, such that if the market does happen to surprise us all and the growth rates are higher, I get to flex up. If we see a more [temperate] growth, which is what we've called for in our guidance, then I can flex down and not have a high burden of the carrying cost in a fixed cost structure. That's an example of why we've got the right kind of leverage ratios in our wireless business and the execution of our frontline where we're winning.

Second, I would say we look at the customer and the feedback they're giving us. Our network quality is better. Our churn is running at record levels. We printed the most profitable year ever in our wireless business last year. Those -- the things that have created that momentum for AT&T aren't temporary. That's part of our operating plan, and those will continue despite what occurs in the economy.

So lastly, I would tell you, because of the consistency of how we've gone to market, it's given our frontline and our teams a bit more time to look at pockets of growth where we are not industry leading, where we still have plenty of room to go and offer a nice value equation to those customers. And you're seeing some of that in the subscriber growth that we're printing on a quarterly basis.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

One element of your growth strategy has been FirstNet. Can you just update us on where you are and the runway you see there?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

We still have a lot of runway to go. I think the first responder community is a lot larger than even maybe we had expected when we started the program. We're roughly at 4.4 million subscribers, 24,000 agencies. And I would tell you, if we had accomplished all of the growth that we can with FirstNet, and that one's tapped out, I would tell you if that were the case, that is nowhere near the case.

We see market expansion and actually not a share take play, but an actual revenue expansion for our industry with some of the solutions that our product teams are bringing in to [life] for the first responder community. So I like that growth, because it gives us as a scaled fixed and mobile operator TAM expansion.

It's not from share steel, but actually getting the industry to participate in ecosystems that we typically have. That's one growth element in our business. I would tell you, our mid-markets. AT&T still today does not enjoy any shared leadership in the mid-market enterprise space. And we've got work to do on that, and we're underway right now this year doing that with an organization dedicated to it.

So yes, there's many options for us, Simon, that we've got in our operating plan, and that's why we're confident in subscriber growth with attractive churn rates and good return profiles and the service revenue growth of 4%.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

You're building out 5G. You talked about moving people up to higher ARPU plans. But more broadly on 5G monetization, what's your -- what do you think the opportunities are there?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. If you think we, like many others, are participating in edge compute and private networking solutions with some of the enterprise customers. But Simon, I would probably back up a bit and say that our enterprise customers, when we meet with them, they don't approach us with a -- I want to get into the 5G game. They approach us with what's on their mind, the CIOs of our very large accounts.

And I can tell you, security is number one, multi-cloud is a second for them. Disaster recovery or service continuity is third and probably fourth is how do you support remote hybrid workforce because that's still a challenge. And as we think about it at AT&T, our 5G solutions that we're offering, I think growth is actually going to come tonnage-wise from our ability as a provider to leverage 5G in the right areas of a solution.

So serving architecture to an account could be a combination of fiber to 70% of their locations and a 5G access point to 30% of their locations, stated maybe even a little bit more eloquent. Having the ability to fail over to 5G is a high-value proposition for an enterprise customer when they're concerned about service continuity.

And as we start to see more 5G chipsets getting embedded in edge equipment, not just devices that we use with our hands, I think you're going to begin to see a larger growing revenue stream from the 5G spectrum deployed in the enterprise space with those basic services.

It doesn't require a lot of really high science in private networking, for example, to achieve that monetization. I'm encouraged because that's the trends that I'm seeing in the discussions with our largest enterprise accounts.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

We've had the cable companies here earlier. They were talking about their entry into the wireless business and the success they're having with their new bundles, lower price bundles. So 2 questions. How does that impact you? And what's your thoughts on a converged offering?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Well, I mean, obviously, we're a converged carrier. We're somewhat of a unique competitor to cable and vice versa, I think. First question on their entrance into mobile, I mean, they've been in mobile for quite some time. We've been competing with cable. And I can tell you that they are enjoying some success and the heightened competitiveness that you see play out in the market, it exists.

What we see in our business is any trend that gives us pause or concern about that, the share take or the share change isn't a material number for us. And having said that, for us, we look at having owner's economics in both the fiber and wireless business, and we get to enjoy those economics as we go to go grow the business.

I couldn't say the same for others. And certainly, cable at some point is going to have to tackle the cost of continuing to service a growing wireless customer base and the handset evolution and the cycling of that. So I think they've got potentially some margin questions coming. And those are things that, for me, I look at where we sit as a company, and I like the position that we sit in, where we're building fiber and competing head up with cable, we're winning. We're winning both with our fiber product and our wireless product, as you might expect.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. Well, we'll come on to that. One last thing on wireless. Just on the pricing side of things, you made some moves on legacy plans last year, like...

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes, we did.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Do you see opportunities to continue to? We've obviously got persistent inflation environment, wages are going up. So how do you think about not just the cost, but also passing through some of that?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes, certainly, I think when we look at any kind of pricing actions very carefully, as a scaled operator. And as we demonstrated last year, we were quite effective in that. You shouldn't expect anything different from AT&T. There are many levers that we have in the way that we combine our offer strategy and our pricing strategy, and we feel confident that we've got plenty of room with our growth and our ARPU guide that will accomplish what we need to accomplish.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. So on the consumer wireline, we've seen some good momentum there as your fiber rollout has continued. Help us understand what '23 looks like on the fiber build side, first in region and then out of region?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. So thanks for that question. I thought John did a really nice job in our earnings, laying out 3 prongs to our fiber strategy. First one is we are right down the fairway -- I like to use this way. We're right down the fairway on our 30 million passings commitment that we laid out at Analyst Day.

My network team that I operate day in and day out is a building toward that. We ended the year last year at $24 million. And so if you do the math this year, '23, '24, '25, you can assume about what the minimum build needs to be for us to achieve that $30 million passings commitment. Where we're building, we are seeing better pen rates than we expected.

We are seeing strong ARPUs. ARPUs on our fiber product are about $10, above that on our nonfiber broadband customers, and intake ARPUs are even stronger than that. So we like the ARPU mechanics in the fiber business very much where that's one part of the strategy in-house. We announced a joint venture building out of footprint, and that's the second leg of the strategy.

What we like about this is the following: we have forever, kind of focused just inside of our footprint itself, where we were licensed as a local carrier, yet I enjoy this nationwide scaled wireless network. And so as I look at the economics and as John and the team as we look at the return profile, where we have fiber, we enjoy stronger market share in wireless.

We enjoy better economics in the combined converged home as I think is probably well understood. And so if that play works where we've got fiber, then let's get fiber everywhere we can, how do we expand in a capital-light model that gives us optionality to expand the footprint. And so the first tranche that we're building in Arizona, we're going to see.

We're going to see how well we do with that. If we have the same kind of penetration performance and we get the right kind of lifts in my returns of my invested capital in my wireless business and that equation holds true, I would hope that you as an investor would want us to do more of that.

Why I also like that play is it gets our ability, our coverage, our surface area of our build further than just our own footprint. And as you think about the bead funding that's going to start to unlock here at the back half of this year for the next several years, we have not only our home team, but we also have a joint venture team that can participate in that, and hopefully, we'll have some nice news to share on that as that progresses.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

And how do you think about what is a good market? Look, what was it that attracted you to me? I know there's a Corning factory that you've got a partnership with there, but what's the...

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. No, there's no correlation there. That's just -- that was coincidence.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Fiber central. Yes.

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. I mean as you might expect, we've got a fairly straightforward model where we look at what the demographics are in the neighborhoods, what the build construction looks like, what the cost to actually install the service, what the market share looks like for us from a wireless perspective, we throw in our enterprise presence.

And if we have enterprise customers that are in or nearby, we put all of this into a very large data model, and that kicks out what's the next best place for us to go build in. We've been doing this in an integrated way as a converged carrier now for about 2.5 years, whereas before, we used to have a network team for wireless that would go engineer and build, and we had a wireline team that would go engineer and build.

And even though they were part of the same company, they were 2 different divisions of the company. Now that we're a more simplified, focused organization, we have consolidated that into an integrated build model. And that gives us scale and efficiency in our capital for both fiber and wireless. And it gets -- makes our dollars a little bit more productive.

We have taken that very same model, and we apply that to the entirety of the nation. And that gives us areas where we think there could be a really nice return. But for our joint venture partners, they are the ones that have to make the decision on where to go build because it's not just us, but we certainly offer that insight.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

You've really ramped your fiber build plans in the last couple of years, and you've got a big -- you've got a $30 million goal here ahead of you. What are you seeing in cost per passing cost to connect supply chain?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. They're -- they've increased from where we thought they would be when we started, but I think that is probably fairly intuitive. Gas prices are up, labor prices are up. We've had supply chain disruptions. But for us, we've got such a large scale procurement arrangement with our suppliers and our labor partners. And we have such diversity of our build that we're not immune to the rising cost, but we actually have a little bit more flexibility and protection against that, I would tell you, in our procurement agreements.

And then you couple that with the penetration that we're seeing, the 12-month penetration that we're seeing and the ARPUs that we're seeing, we're actually able to overcome that pressure. So if you're asking, are you seeing anything economically that is slowing you down in your aspirations to build fiber? I would tell you no.

I mean, yes, moves in the housing markets, probably not as vibrant as it once was, and it makes our marketing teams have to work extra hard to get in there and to take a neighborhood and get them excited about converting their service over, which would normally happen with a mover as a natural change of ownership of a home.

But saying all that, we don't see anything that's telling us the economic return or the demand has shifted. It's just let's get it built, let's get it penetrated. And Simon, we're going to be on this journey for a while. I mean we think there's 50 million homes, urban, suburban in America that deserve fiber.

And so the $30 million that we've got in our footprint is not the entirety of what I think the market opportunity is there. So for us, we're playing a long game. We're not sitting here looking at just this year or next year. We're looking long term, what our end goal as a business is.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

And BEAD presumably expands that?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

BEAD does. BEAD gives you the opportunity to probably fill in areas that economically you might not have had high on the priority list. It gives you an opportunity, if you're an AT&T where you operate a 511,000 square mile copper network that has a carrying cost associated with it in low revenues because it's pretty legacy. And as you think about AT&T's cost transformation, investments in fiber, having 3 legs to the fiber stool, BEAD being the third of that.

You should expect AT&T as we go to make our copper transformation occur at certain distribution areas, about half of that square mileage footprint I just quoted, will be covered with fiber or served another way. And the cost that we pull out of the business as a result of no longer serving that copper footprint and putting that investment into the things like fiber, what we're seeing here 2, 2.5 years in is the cost to maintain fiber is actually exceeding our expectations in terms of efficiency. So it's lower cost to maintain. It gives us really nice conversions of the profit of AT&T long term, and we end up with a future-proof network footprint that has got industry-leading performance.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Right. So we've talked a lot about fixed wireless. We've heard both sides of the argument already. You're somewhere in the middle, you're obviously leading with fiber, but you have provided fixed wireless. You -- it sounds like you will use it judiciously. So what is the best uses for fixed wireless in your view?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

I think there's many. I mean, obviously, our lead offer and where we're putting the majority of our capital and our focus is in our mobility product and our fiber product, but we recognize there are certain areas and certain customers where fixed wireless probably is a nice solution, even if it is temporary.

And so areas where we have fallow capacity in wireless, and we're happy to be making a conversion of a footprint area that will take a year or 2 to bring fiber into. You may see us transition a customer today onto a fixed wireless product that we might backfill that footprint with fiber at a later date.

When you think about the application of fixed wireless in the enterprise space, I alluded to this, how as a facilities-based fiber and 5G company, (inaudible) solution for these large enterprise accounts, they're not telling us, I want that fiber or I want that fixed wireless or I want that 5G or 4G. Here's my problem, serve me.

And I bring a serving architecture that's a hybrid mix of fiber and a fixed wireless access solution. And for them, it's kind of seamless. Their service and applications work across both. I, within my network, make that seamless. And so you'll see us, I think, spend a little bit more energy in the areas of those kinds of use cases. We do not -- as we have stated we will not be a large-scale fixed wireless service provider. That's not the solution for solving for the bandwidth needs in our opinion.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. So you touched on enterprise a couple of times already -- you still have some legacy product roll off there. So help us understand and how much visibility do you have in being able to bend the curve on that over the next several years?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Well, I mean over the next several years, I sure hope to be in that curve. That's a core tenet of my job here. Right now, even though we've experienced some slightly better EBITDA performance over the last several quarters, I'd just say point to our guide. We expect that here in 2023, it's going to be high single digits decline on EBITDA.

And that's in part because of the transformation that we're making. It -- if you think about our consumer wireline business as a proxy for it, today, we've got more fiber revenues than we do copper revenues, and you're seeing that fiber revenue growth in the mid-20s, and you're starting to see EBITDA stabilize and grow a bit.

That's kind of the leading cursor of what you should expect from our enterprise business. We've curated out all the products and services that were revenue-oriented and low margin. We're investing in expanding our fiber and our performance in our fiber selling of our owned and operated services. And as we get that volume of that increase is when you'll see the stability of the EBITDA curve in a similar way to what you've seen us execute on consumer wireline.

We haven't disclosed when we think that's going to happen. We've been challenged in this space. We are hard at work at getting this to a position where we can walk you through a little bit more visibility into what's legacy, what's the future growth. I'll just remind you, Simon, it's been less than a year since we've become really this more focused telecom company.

I mean it was a year ago, we still had a media company. We still had a video distribution business, and so we're kind of in early innings here on that.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Right. You've talked again about the cost imperative there. Help us understand what are the big buckets here of savings? And what's the time frame to realize those?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. We announced in the fourth quarter that we had achieved over $5 billion of the $6 billion cost takeout target. And I can recognize how that's kind of like a black box for a lot of investors. I don't really understand how, where that comes from. I'd say the way I would think about it is a 1/4 came out of our network, 1/4 came out of our customer-facing operations, think distribution.

And about half of that is coming from what I might call support, back office or parent and overhead. We have the $6 billion target well in hand. That being said, we're not really public about how we've curated our operations. But since January '21, our headcount and the communications business is down 30,000.

We were down in the fourth quarter, 7,000 just in the quarter. And no headlines, no service disruptions, performance, the key operating metrics looked really great in the fourth quarter. The trends look fantastic, and you should expect us to continue to find ways to get more efficient because I'm here to tell you, we are not best-in-class when it comes to cost structure.

We still have room to improve. And that's -- that's really my main charter in the company. I alluded to it earlier, if you think about the actual carrying cost of an underutilized copper network that is across 511,000 square miles, think about all the access circuits. You think about all the maintenance and support. You think about all the energy that we use. We are in the early innings of that wireline transformation. And so over the next 2 to 3 years, you will see us draw costs out of this part of our franchise, reinvest them into the future of the company, and it should be a nice virtuous cycle of great returns for investors.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Right. And you've guided to CapEx dropping from $24 million to $20-ish billion next year. What are the drivers of that?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Well, mainly, it's the -- we're investing right now at very high levels with our C-band deployment going on in wireless and obviously, our fiber build.

What we've guided to is our design target is to get to mid-teens in terms of capital intensity. And it's trade-off, Simon, as you know. If I can get revenues growing at a rate then the tonnage of capital can be a flexible number. But we are committed in our disciplined capital allocation approach to investing in growth, covering the dividend and paying down debt.

And we are -- part of that equation requires us to get more efficient on our capital. And to do that, we've got to get better penetration rates, which we are doing in our fiber deployment. We've got to make our capital dollars stretch a bit further operationally with our wireless build, which we are seeing in better-than-expected C-band coverage performance in our wireless investment last year, all of this goes into our ability to get better return on a lower capital number next year.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

A year ago, you gave guidance, stand-alone guidance that was for $20 billion of free cash this year. You -- and you guided down for '22, and you're guiding now up for $2 billion to $16 billion for this year. So how do you feel confident that $16 billion is the right number? And what were the big elements both versus the prior guidance and versus 2022?

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. For us, as we exited 2022 at $14 billion, and we've guided to $16 billion, I can tell you that guidance still holds firm. And the 2 elements of that, that should give you confidence, we've spoken about today. We continue to see attractive subscriber growth at great ARPUs. We exited the fourth quarter printing the best profit year in history for our largest business, wireless.

I've shared with you that I don't see while the economic uncertainties are all around us, I don't see any major trend change in that. And so subscriber growth, ARPU growth, cost reduction, cost takeout translates to improved EBITDA and that improved operating EBITDA is the difference between $14 billion and $16 billion. And I've got confidence we're going to deliver that.

Simon William Flannery - *Morgan Stanley, Research Division - MD*

Great. Well, that's a great place to stop. Jeff, thank you so much for your time today.

Jeffery Scott McElfresh - *AT&T Inc. - COO*

Yes. Thank you, Simon.