Q3 2023 Earnings Call *(Corrected version)*

Event Details

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Company: Crown Castle, Inc.
Ticker: CCI-US

Company Participants

Kristoffer Hinson - Crown Castle, Inc., Vice President-Corporate Finance & Treasurer
Jay A. Brown - Crown Castle, Inc., President, Chief Executive Officer & Director
Daniel K. Schlanger - Crown Castle, Inc., Executive Vice President & Chief Financial Officer

Other Participants

Simon Flannery - Analyst
Michael I. Rollins - Analyst
Nicholas Ralph Del Deo - Analyst
Jonathan Atkin - Analyst
Ric Prentiss - Analyst
David W. Barden - Analyst
Gregory Williams - Analyst
Matthew Niknam - Analyst
Brandon Nispel - Analyst

MANAGEMENT DISCUSSION SECTION

Operator

00:00:15 Good morning and welcome to the Crown Castle Third Quarter 2023 Earnings Conference Call. All participants will be in listen-only mode. After today's presentation there will be an opportunity to ask questions. Please note this event is being recorded.

00:00:31 I would now like to turn the conference over to Kris Hinson, VP of Corporate Finance and Treasurer. Please go ahead.

Kristoffer Hinson

00:00:38 Thank you, Kate, and good morning, everyone. Thank you for joining us today as we discuss our third quarter 2023 results. With me on the call this morning are Jay Brown, Crown Castle's Chief Executive Officer; and Dan Schlanger, Crown Castle's Chief Financial Officer. To aid the discussion, we have posted supplemental materials in the Investors' section of our website at crowncastle.com that will be referenced throughout the call this morning. This conference call will contain forward-looking statements which are subject to certain risks, uncertainties and assumptions and actual results may vary materially from those expected. Information about potential factors which could affect our results is available in the press release and the risk factor sections of the company's SEC filings. Our statements are made as of today, October 19, 2023, and we assume no obligation to update any forward-looking statements.

00:01:24 In addition, today's call includes discussions of certain non-GAAP financial measures. Tables reconciling these non-GAAP financial measures are available in the supplemental information package in the Investors' section of the company's website at crowncastle.com.

00:01:38 With that, let me turn the call over to Jay.

Jay A. Brown

00:01:41 Thanks, Kris, and good morning, everyone. Thanks for joining us. Our third quarter results continued to demonstrate our ability to generate consistent growth in the face of changes in the industry environment allowing us to maintain our full year 2023 outlook for revenue, adjusted EBITDA and AFFO. Based on the multi-year strength of our business model, we are confident in our ability to grow our dividend beyond 2025 once we get past the Sprint-related churn. Therefore, we are committed to maintaining our dividend in 2024 in the midst of the impacts from the non-recurring Sprint cancelations and lower contributions from services. Based on the timing of these headwinds, we expect the low point of AFFO to occur during the first half of 2024 before returning to growth in AFFO in the second half of next year and beyond.

00:02:35 Demand for our assets has consistently been driven by our customers investing in their networks to keep pace with the rapid growth in mobile data demand. Through our shared infrastructure model, we have helped our customers maximize the benefits of their investment by lowering the cost of deploying networks, networks that have significantly improved our ability as consumers to connect with the people and the world around us. The combination of persistent data demand growth and our ability to provide low-cost shared infrastructure solutions has enabled resilient underlying growth for us throughout generational upgrades and across macroeconomic cycles. Our full year 2024 outlook demonstrates the benefits of complementing our tower business with a leading portfolio of small cells and fiber.

00:03:27 As our customers increasingly focus on 5G network densification so that they can meet the needs of their end users, we expect the total demand for our diverse portfolio of assets to increase. For towers, we expect to generate organic revenue growth of 4.5% in 2024. For small cells, we expect to generate organic growth of 13% driven by around $60 million of core leasing activity as we increase new nodes from 10,000 in 2023 to 14,000 in 2024. And for fiber solutions, we expect continued acceleration of leasing activity combined with a lower churn to generate organic growth of 3%. Excluding the impact of Sprint cancelations, the combination of organic revenue growth across our business is expected to generate consolidated organic growth of 5% in 2024, up from 4% in 2023. While our growth remains robust, we know we need to continue to get better.

00:04:37 Therefore, we continue to simplify, streamline, and centralize our business processes and operations which will reduce our long-term costs and improve our customer experience. Since announcing the restructuring plan in July, we have reduced our workforce and achieved $105 million of annual run rate savings. Having completed that plan, we have identified additional opportunities to drive further efficiencies, including a plan to move approximately 1,000 employee positions from several locations nationwide to a centralized location by the end of the third quarter 2024. The strong organic growth and improved operating leverage from the actions we continue to take to reduce costs supports our maintaining our current annualized dividend of $6.26 per share. As reflected in our results and outlook, our differentiated strategy to invest in and build an unmatched portfolio of assets diversifies our sources of growth.

00:05:43 Our 40,000 towers, 115,000 small cells on-air and under contract, and 85,000 route miles of fiber concentrated in the top US markets make us well-positioned to capitalize on long-term growth and data demand regardless of how carriers deploy spectrum and densify their networks. At the beginning of 5G, our customers moved quickly to deploy record amounts of newly acquired spectrum; this drove record tower activity levels. As this initial surge in tower activity ended, our small cell growth is accelerating as customers shift focus to densifying portions of their network that have experienced the most traffic. In 2024, we expect to deploy a record 14,000 small cell nodes. Our ability to capture the accelerating growth in small cell demand is driven by the assets and core capabilities that we have built as the largest operator of shared infrastructure in the United States.

00:06:47 Our 85,000 route miles of fiber include high strand counts in heavily populated areas where the density of data demand is the highest, which make them the most desirable locations for small cell deployment. We are a highly reliable operator of that fiber network. If fiber goes offline, small cells go offline; and for our wireless customers, network quality and reliability are paramount. We have a world-class team of network operators and engineers that ensures our network is designed to mitigate the impact of any outage and is capable of fixing these outages quickly and efficiently. We have also developed expertise in navigating the permitting processes with multiple municipal organizations, regulatory agencies, and utility companies across hundreds of disparate local markets, each with a unique set of regulations and stakeholders.

00:07:42 This expertise allows us to navigate the difficult process of building small cells in the markets across the United States. Finally, we are consistently finding ways to build small cells and fiber more efficiently. These efficiencies allow us to provide the most cost-effective and reliable network solutions for customers. We look to deliver the highest risk-adjusted returns for our shareholders through continuously building on the core capabilities that I just mentioned that generate unique value in the businesses we own and operate. These capabilities reduce the overall cost of deploying and operating communications networks, which becomes even more compelling for our customers, in times of increasing capital costs. Of course, higher capital costs impact us as well. Our disciplined approach to capital allocation means that as our cost of capital increases, so must the returns we require from our investments.

00:08:42 We are continuously evaluating the expected returns of all of our investments against the rising cost of capital and other potential investment opportunities, including repurchasing our own shares. Consequently, we allocate capital to whatever we believe will generate the highest long-term returns. Being disciplined allocators of capital means that we appropriately adjust the scale and economics of our investments based on changes in technology, customers and macroeconomic conditions. It doesn't mean that we stop investing. We apply a consistent, rigorous approach to pursue opportunities that generate superior, expected returns for their given level of risk. Long-term value is created when we invest in those opportunities. We have a long history of success in towers built on investing through various macroeconomic cycles.

00:09:38 And we believe the small cell business is another great example of how we can build a business where our unique capabilities drive sustainable advantages that can grow significant long-term value. In 2024, we plan to capitalize on these opportunities, resulting in approximately $1.2 billion in discretionary capital expenditures net of customer contributions with $1.1 billion in our fiber segment. This capital is supporting the acceleration of expected 10,000 nodes in 2023 and 14,000 nodes in 2024, reflecting a 40% increase in new nodes with only a 20% increase in capital, as we expect more than 50% of the nodes to be co-location nodes. Importantly, we expect to fund this with discretionary CapEx in 2024 without issuing equity.

00:10:37 Compared to 2022, this means that we expect nodes deployed in 2024 will be up three times, while fiber CapEx is only up 30%, again, reflecting creasing co-location on our existing assets. The co-location and increasing yields on multi-tenant systems continue to be similar to the development of the tower business over the last 25 years. There is one more item I wanted to discuss. As you saw in the release, Dan will be departing Crown Castle next March. While he's not leaving for another five-plus months I wanted to take the opportunity to thank him for the contributions that he has made to the company over the last seven years. He has been integral to the growth of our business and strategy. We are benefiting from the work he has led to increase the duration and predictability of our balance sheet and he has developed a strong finance team. We will wish him all the best in his next endeavors.

00:11:38 We have begun a search to find his replacement and will be considering both internal and external candidates. As I wrap up, we believe the low point for AFFO will be in the first half of 2024 as we work through the non-recurring Sprint cancelations and the services headwinds that I mentioned earlier. The consistent growth of each of our lines of business, driven by persistent growth in data demand, gives us confidence in our ability to fund our CapEx budget in 2024 without issuing equity, to maintain our current dividend in 2024 and to pursue sustainable dividend growth beyond 2025.

00:12:21 And with that, let me turn the call over to Dan.

Daniel K. Schlanger

00:12:24 Good morning, everyone, and thanks for the kind words, Jay. I just wanted to start by saying how grateful I am for having opportunity to work at Crown Castle the last seven years. It's a great company and I continue to strongly believe it is pursuing a strategy that will generate significant value for shareholders. As a large, at least for me, shareholder I'm excited to see that strategy play out over the next several years and look forward to the company's continued success. Turning to the results. Our third quarter was in line with expectations and demonstrated the resiliency of our business. With our customers transitioning beyond the initial surge in 5G deployments, we were able to deliver 4% consolidated organic growth in the quarter, including nearly 4.5% organic growth in towers and accelerating growth in small cells and fiber solutions.

00:13:12 Following third quarter results, we updated our outlook for 2023 to reflect the impact on our expected net income of approximately $110 million of charges related to our restructuring plans announced in July, as well as a $100 million reduction in tower CapEx. All other items remain unchanged as shown on page 5. Moving to our 2024 outlook. There are three significant issues that are negatively impacting our results. First, the $165 million of Sprint cancelations payments we have received in 2023 will not recur in 2024. Second, we will see a combined $240 million reduction to our straight line adjustment and amortization of prepaid rent, both of which are non-cash items; and lastly, a combination of exiting the construction services business and lower tower activity levels causes a reduction of approximately $55 million in our services gross margin.

00:14:11 Due to these impacts, our 2024 outlook shows year-over-year declines in site rental revenues of $140 million, adjusted EBITDA of $260 million and AFFO of $275 million. Excluding these headwinds, the strong organic growth across each of our businesses contributes $220 million to 2024 adjusted EBITDA resulting in $65 million of AFFO growth. Turning to page 6. Looking ahead we expect attractive revenue growth trends to continue with consolidated organic growth accelerating from 4% in 2023 to 5% in 2024 as we are seeing an increase in demand for our small cell and fiber assets. Contributing to our organic growth is $305 million to $335 million of core leasing, an increase of $30 million at the midpoint compared to full year 2023. Our 2024 consolidated core leasing of $320 million at the midpoint includes $110 million from towers compared to $130 million in 2023, $60 million in small cells compared to $35 million in 2023, and $150 million in fiber solutions compared to $125 million in 2023.

00:15:26 This year-over-year increase in core leasing results in an increase in organic contribution to site rental billings excluding the impact of Sprint cancelations of $265 million at the midpoint or 5% which includes 4.5% from towers, 13% from small cells and a return to 3% growth in fiber solutions. The organic growth is offset at site rental revenues by the non-cash decreases that impacted the Sprint cancelations I referenced earlier, along with an additional $10 million of Sprint cancelations-related small cell churn. This is primarily related to approximately 5,000 nodes that were terminated midway through 2023, which creates a roll over effect in 2024. Turning to page 7. We're delivering this increase in organic contributions to site rental billings with a limited increase in expenses of only 2% or $45 million at the midpoint, which benefits from $35 million of savings related to the restructuring we announced in July.

00:16:27 When combining this $35 million in expense reduction in 2024, with a $30 million we expected to achieve in 2023, and $40 million of cost savings embedded in the 2024 change in service margin, the total annual run rate savings of our restructuring program is expected to be $105 million. Inclusive of the $40 million decrease in costs, and the impact from exiting the installation services business, we expect services margin to be $65 million to $95 million in 2024. Margins as a percentage of revenue in our services business are expected to improve from approximately 25% in the third quarter of 2023 to nearly 50% by the end of 2024 as we phase out installation services activity and benefit from our cost reduction initiatives. Moving to interest expense. We expect an increase of approximately $105 million at the midpoint as we fund our 2024 investments with incremental debt.

00:17:28 When forecasting interest expense, we assume a cost of borrowing implied by the current rate environment slightly above 6% to fund our 2024 capital requirements. Our 2024 AFFO growth excluding the impact of the Sprint cancelations and outsized non-cash movements, which more closely reflects the underlying growth of the business, is expected to be $40 million to $90 million. With contracted long-term tower leasing agreements, a backlog of 60,000 small cell nodes and a largely fixed cost structure, we have visibility into this underlying growth continuing over a multi-year period, providing a solid foundation both for our current dividend and for our expectation of returning to sustainable dividend growth after 2025. As our wireless customers increasingly expand their 5G network investment focus to include both coverage and densification, we are seeing a growing number of value-creating investment opportunities.

00:18:25 And as Jay already mentioned, our 2024 discretionary capital program is $1.5 billion to $1.6 billion or $1.1 billion to $1.2 billion net of $430 million of prepaid rent received. Importantly, we believe we can fund these investments without issuing equity in 2024. We recognize the collective impact of the reduction in non-cash items and the Sprint cancelations payments not recurring in 2024, results in our leverage ratio exceeding our target of five times net debt-to-EBITDA. However, we expect our durable cash flow growth to organically reduce our net-debt-to-adjusted EBITDA ratio over time to levels in-line with our investment-grade credit profile, as we have seen our business do on multiple occasions throughout our investment-grade history.

00:19:11 Since transitioning to investment-grade in 2015, we have intentionally strengthened our balance sheet to mitigate risk by extending our weighted-average maturity from five years to eight years, decreasing the percentage of secured debt from 47% to 7%, and increasing the percentage of fixed rate debt from 68% to 86%. Further, we ended the quarter with approximately $5 billion of availability under our revolving credit facility and only $750 million of debt maturities occurring through 2024, providing us with ample liquidity to fund our business for the foreseeable future. To wrap up, the underlying growth of the business remains solid and the contracted agreements we have in place provide line of sight into continued underlying growth over a multi-year period.

00:19:58 We believe this growth provides a stable foundation for our current dividend and the ability to continue to pursue our value-creating investments in 2024 without issuing equity. Longer-term, our unparalleled domestic portfolio of tower, small-cell, and fiber assets, provides unique access to a growing number of opportunities with superior risk-adjusted returns, which we believe will create value for our shareholders and increase our long-term total shareholder return.

00:20:40 With that, Kate, I'd like to open the call to questions.

QUESTION AND ANSWER SECTION

Operator

00:20:45 We will now begin the question-and-answer session. The first question is from Simon Flannery of Morgan Stanley. Please go ahead.

Analyst: Simon Flannery

00:20:56 **Question – Simon Flannery:** Great. Thank you and good morning. And, Dan, all the best for the future. Great working with you. I guess you've got one more call with us. Perhaps we could start just talking about leasing activity and the guidance expectations. It seems like it's a pretty tricky year. I know you always guide before your peers, but we've got a lot of moving parts with the 5G CapEx cycle kind of winding down here. So could you just characterize when you set your guidance for next year, particularly on towers, how you characterize the current activity and the expectations for next year in terms of what we expect to see from the major carriers and from the likes of DISH? Is there less visibility, say, than in prior years and has that caused you to perhaps just be somewhat conservative?

00:21:30 And then you talked about the leverage being above-trend. Any kind of ability to sell assets, anything that you might be looking on the strategic side? And also, any opportunities on the M&A side given some of the strategic moves by some wireless carriers out there? Thank you.

00:21:58 **Answer – Jay A. Brown:** Sure. Good morning, Simon.

00:21:59 **Question – Simon Flannery:** Good morning.

00:22:00 **Answer – Jay A. Brown:** On your first question around leasing activity, the tower guide for 2024 assumes a similar level of activity to what we've seen in the second half of 2023, so underlying our view is basically a consistent level of activity as the surge, the initial activity from 5G came to an end during the first half of the year. We saw the level of activity stabilize and we think that carries into calendar year 2024. I think we have good visibility around that. Much of the work given the nature of the business, we go into the year with a significant portion of that revenue already contracted and we have good visibility as to when we think it will actually come online.

00:22:46 So I would characterize our visibility from a reported results standpoint pretty similar to what we've seen historically and feel like that level of activity is sustainable over the long-term as the carriers continue to upgrade the sites that they're already on with 5G equipment as well as densify the network using towers that they're not currently on. As I noted in my comments, we think that we will see and have seen a shift and a focus from the carriers as they start to use small cells to a greater degree to densify their network, so our view is based on a pretty holistic view of the way the carriers are thinking about their networks as we wrap up 2023 and get into 2024 and feel good about the organic growth that we're showing in both segments there related to the wireless carriers.

00:23:50 On the second question around the leverage trend, as Dan mentioned in his comments, obviously with some of the headwinds that we talked about and our comments, it's going to cause the leverage to tick up a bit. That's happened in the past and we would expect over time that we'll see good growth in the business that will allow us to de-lever back down and get back at levels where our target would be, so the headwinds will create some uplift around that leverage ratio and then we think over time we'll be able to bring it back down in line. The last part of your question around ways to manage the business and M&A and other things, I don't think there's anything specific that I would comment on. But just generally, the way we think about running our business is there are three ways that we view we can create long-term shareholder value.

00:24:48 The first way is to add additional revenue to the assets that we own; that organic growth comes at great incremental returns. And the second way is we can invest in more assets that we believe would extend the runway of growth into the future, and then the third way is to lower the cost of capital. We think all three of those are ways of driving long-term shareholder value and we are constantly working on all three of those. What's unique about the current environment that we're in is that oftentimes in periods of disruption, more opportunities arise. And I made reference to that in terms of the capital costs of our customers can create opportunities for us to invest capital that can drive returns over the long-term. That also happens sometimes around the way assets are priced.

00:25:42 And so us being really thoughtful about how we can create value on those three fronts and we are always looking at those opportunities. And I would say in periods of disruption, our experience has been that oftentimes, there are some pretty unique opportunities that arise. And so we'll continue to work on all three, growing the revenues on the existing assets, looking for opportunities for new assets, and then trying to find ways to lower our cost of capital.

00:26:12 **Question – Simon Flannery:** Great. Thanks a lot.

00:26:15 **Answer – Jay A. Brown:** You bet.

Operator

00:26:16 The next question is from Michael Rollins of Citi. Please go ahead.

Analyst: Michael I. Rollins

00:26:23 **Question – Michael I. Rollins:** Thanks and good morning. I also want to give my best wishes to Dan as well. Two questions if I could today. The first one as you're just describing returns, curious if you can give us an update on how the returns for small cells – as the growth is now accelerating, how those returns are pacing versus your expectation and if you're seeing difference in pricing on a per-node basis relative to the current portfolio? And then just drilling down into the earlier question on assets. Do you have a significant amount of non-core assets or non-core ground leases and can you possibly unpack the size if you have any of that given the recent press reports?

00:27:15 **Answer – Jay A. Brown:** Sure. On the first question around returns for small cells, we continue to see really attractive returns in our small cell business. And the amount of co-location that we're seeing both in 2023 and 2024 and the economics of those incremental adds well in excess of 20% is encouraging. As we have seen systems develop, we continue to be – initial returns going to that second tenant, we get into the low double-digit returns. And as we get to the third tenant, we're high teens, low 20% from a systems standpoint. Given the quantity of nodes that I talked about in my comments, both that we're seeing in 2023 as well as when we go into 2024, and half of those nodes being co-location, we're seeing the multi-tenant systems track those expected returns, and so feel really good about where those are going.

00:28:19 As we think about pricing, we have always priced the business based on, focused on returns, so there's not a – unlike towers where there's more of a national pricing across assets, small cells is different. Small cells is priced based on the required returns based on the cost to build systems and so in areas where the costs are higher, the pricing follows, and that has had some uplift in it as a result of some of the inflationary pressures that have been in the environment and so that does affect the pricing and we're able to lift pricing associated with that in order to maintain and grow the returns associated with the systems and so we've seen the business develop as we would have expected. On the second question around non-core assets and potential size there. I don't think we have a lot of non-core assets inside the portfolio of assets.

00:29:22 But one of the things that I would say is, the ground leases you specifically referenced, ground leases, we have over time brought a significant portion of ground leases on balance sheet by acquiring the ground leases. We also extend ground leases for very long periods of time. We're now north of 30 years of duration in our ground lease portfolio and so we have the opportunity, obviously, to go out and push ground leases in terms of duration for over very long periods of time, and we may choose to do that off balance sheet or on balance sheet, so I would put that in the category, that could be an opportunity for us to lower the cost of capital, depending on how we think about it. In order to run the business sufficiently, the key is, do we have control both in terms of the cost of that activity and then do we have control in terms of certainty of being able to maintain the assets and add additional revenue.

00:30:30 So the financing decision really just comes down to what's the lowest cost of capital and we're always looking for opportunities to try to figure out the way to achieve that lowest cost of capital across the assets.

00:30:44 **Question – Michael I. Rollins:** Thank you.

Operator

00:30:48 The next question is from Nick Del Deo of MoffettNathanson. Please go ahead.

Analyst: Nicholas Ralph Del Deo

00:30:58 **Question – Nicholas Ralph Del Deo:** Good morning. Thanks for taking my questions. First to continue on the capital allocation theme, in the past, generally the returns you see from small cells, I guess fiber more generally, were so far ahead of what you could get from repurchases. Repurchases really weren't in your consideration set. How would you describe that relationship today? Are repurchases starting to look more interesting versus fiber or other uses of capital?

00:31:21 **Answer – Jay A. Brown:** Good morning, Nick. Obviously, the move downward in the stock price and the yield associated with it, while we've maintained a long-term view that we'll return after we get through 2025, that we'll be able to return to growing organic growth in line with our targets, obviously, that becomes a more attractive investment at lower prices. As I mentioned in my comments, what's also true is there's a growing – we believe, growing demand and focus by our carrier customers for the assets around small cells and so it absolutely affects the way we think about the incremental projects that we take on, because we're always thinking about things, as what is the opportunity cost or the potential opportunity returns that we could pursue by choosing one path over another path.

00:32:17 And our consistent approach has been over a long period of time to compare things like repurchasing shares or investing in assets, so as the stock price has moved, it does adjust how we think about opportunities and it will continue to do so.

00:32:34 **Question – Nicholas Ralph Del Deo:** Okay. Maybe turning to the employee relocation plan that you disclosed last night. It seems to reflect a pretty meaningful philosophical change in how you manage this company, at least from an outsider's perspective. I guess, why do you think a more centralized approach is better now? Has something changed in terms of your ability to better manage the business in a more centralized way than you once were or am I kind of overthinking it?

00:33:03 **Answer – Jay A. Brown:** I don't think you're overthinking it. We are constantly looking at ways to run our business more efficiently, and so as we have come off of the peak of 5G activity, one of the things that we looked at as we were evaluating what's the rightsizing of the organization, one of the things that we thought was necessary was to reduce the number of employees in the business, which we did that in the July and completed that work over the last several months. The second part of it is, how can we run the business more efficiently in terms of our processes and business operations? And so the view that we took on that front is that by centralizing things, we can reduce long-term costs of operating our business and we can get to the place where we can deliver for our customers more quickly and more efficiently.

00:33:58 So improving the customer experience, which we believe will both reducing our long-term cost of operating the assets, but also give us an opportunity to potentially increase the revenue that we can deliver for customers by delivering for them more quickly. I think that's just the way you should always be running the business is looking for ways to reduce the costs, run it more efficiently and as we've looked at the activity that we believe will occur for the business over the long-term, we believe this reformatted business will be the best way to run the business both from a cost standpoint and then give us opportunity for additional revenues over time.

00:34:39 **Question – Nicholas Ralph Del Deo:** Okay. Just one quick follow-up. Any risk of an operational hiccup given all the changes taking place or do you feel like you have that pretty well buttoned down?

00:34:49 **Answer – Jay A. Brown:** I wouldn't say there's ever a place where there isn't the opportunity for a hiccup, so we've got to be disciplined operators of the assets and run the business thoughtfully and we intend to do that. I have a great deal of confidence in our team and our ability to do that. The restructuring plan that we announced in the press release yesterday affects about 25% of our employees and so I'm confident that the plans that we have in place to work through that, they'll do well. The 80% that are unaffected, I believe today are hard at work and doing what you would expect in terms of delivering on the business, so it's something we've got to watch and certainly manage and we have a plan internally to do that.

00:35:38 **Question – Nicholas Ralph Del Deo:** Okay. Thank you, Jay.

00:35:40 **Answer – Jay A. Brown:** You bet.

Operator

00:35:42 The next question is from Jonathan Atkin of RBC Capital Markets. Please go ahead.

Analyst: Jonathan Atkin

00:35:49 **Question – Jonathan Atkin:** Thanks. A couple of questions. When you say no equity issuance, does that include not drawing on the ATM and then more broadly, on the financial side, wondered what your updated thinking would be about the pace of dividend growth beyond 2025 from your vantage point right now.

00:36:09 **Answer – Daniel K. Schlanger:** Yeah, Jon, I'll take the first one on the ATM. Yeah, it means that we're not going to be issuing equity, even under the ATM.

00:36:18 **Answer – Jay A. Brown:** Beyond 2025, I would look at the business and say, based on the characteristics that we see for organic revenue growth and our long-term forecast for where we think the carriers are going to invest to continue to build-out 5G which is going to take the better part of the decade we expect, we see organic growth in AFFO returning to that targeted level of 7% to 8%, and so feel good about the underlying demand drivers of how we're going to get there, and then as we get closer to that date, we can talk more specifically about what we think the growth rate will be in 2026. But the underlying demand drivers, and as we look at it today, look to be healthy and intact and we think those are sustainable and as we get through these headwinds over 2024 and 2025 that we'll get back to a targeted level of growth in our AFFO.

00:37:21 **Question – Jonathan Atkin:** And lastly from my side, just on the core fiber business, ex-small cells, what are the types of trends you're seeing with demand, customer renewals, pricing and so forth?

00:37:34 **Answer – Jay A. Brown:** Sure. Two big trends that are affecting that, as we've gone through the calendar year and moved past the churn events that we've been talking about, we've seen the net growth come back in line with where we expected to get, we still think we're going to exit this year at about 3%. You could see in our guide for next year that we're on pace to get – we believe we'll be on pace to get to next year's level of growth by the time we exit this year. The two trends that we're seeing is both an uplift on the core leasing side, so we're seeing more activity from both new logos and an opportunity to continue to sell to the logos that we're already selling to. We also see a reduction in churn. Our team has undertaken a number of really thoughtful activities over the last couple of years that are starting to bear fruit and that results in a reduction in churn.

00:38:36 And so both on the top as well as the reduction in churn is leading to that 3% growth that we see next year. The more macro drivers of that business are healthy, as data demand not only for wireless which we've talked a lot about on this call, but also for connectivity on a wireline basis, those growth drivers continue to be healthy. The movement of enterprises towards moving data to the cloud and off-premises continues to create opportunities for that business. We think those trends are intact, especially for the customer base that we serve. Our fiber business primarily serves large enterprises. We have very little exposure to medium and small businesses, and we don't do anything direct-to-consumer. On the large enterprise side, we see those trends towards off premises and movement to the cloud to be sustainable drivers that are going to drive growth for a long period of time.

00:39:40 And we're continuing to be thoughtful about how can we make those revenue streams more sticky.

00:39:48 **Question – Jonathan Atkin:** Great. Thank you very much.

Operator

00:39:52 The next question is from Ric Prentiss of Raymond James. Please go ahead.

Analyst: Ric Prentiss

00:39:57 **Question – Ric Prentiss:** Good morning, everyone, and, Dan, enjoyed getting to know you over these last seven years.

00:40:03 **Answer – Daniel K. Schlanger:** Yeah. Thanks, Ric, me too.

00:40:09 **Question – Ric Prentiss:** I want to start on the dividend side. You all know I really like looking at cash more than the AFFO reported metric, but it looks like the midpoint of 2024 AFFO $3.005 billion and that amortization of prepaid rent to non-cash you talk about was $423 million. That kind of implies that a cash AFFO number would be more like ballpark $2.6 billion versus dividends might be like $2.7 billion. Am I thinking of that correctly and then what other ways are there to, kind of, bridge that working capital or other ways to get to that, kind of, how you pay the cash dividend?

00:40:49 **Answer – Daniel K. Schlanger:** So, Ric, I would say yes, you're thinking about that correctly. Looking at our AFFO, taking out the prepaid rent amortization to get to a cash level makes sense as a shorthand way to do so, and that number is going to be below our dividend at the midpoint when we look at 2024. And we believe, as Jay pointed out throughout his comments is that given that we think that we're going to be returning out to growth past 2025 that it made a lot of sense to keep the dividend where it is and we can fund that dividend in all sorts of different ways. We don't have a liquidity issue of trying to figure out where the cash comes from. What we have is – what we'll do is we'll continue to pay out the dividend. And then as organic growth in the business continues to increase over the course of the next several years, we feel really comfortable with the trajectory of that dividend over time.

00:41:41 **Question – Ric Prentiss:** Okay. And a couple times, I think, Jay, you mentioned maintain the dividend in 2024. Obviously, it's a board decision but should we assume the intent is to maintain the dividend in 2025 as well? And to Dan's point, there's other ways to pay it if cash is short?

00:41:58 **Answer – Jay A. Brown:** Yeah, Ric. Obviously, we're setting the dividend policy for 2024, so I don't want to get ahead of ourselves and start talking about 2025. But philosophically, the reason why we're referencing the low point is to help give you a view of this multi-year work-through that we've got with the consolidation of Sprint and some of the headwinds that we've been facing. As you kind of referenced and walked through the math there of the gap, in essence what we're saying is we expect that gap to be smaller in 2025 than it is in 2024. So historically, as we've looked at the business, what we've done is sized up the cash flow generation of the business and we've paid out to shareholders in the form of the dividend the cash generated by the business in any given year. That's how we've set our dividend.

00:42:50 As we got into this period of time, which we believe is an anomaly in the business, the consolidation of the carriers and worked through the headwinds associated with more of the macroeconomic changes, what we tried to do was look through those specific events that we were seeing on the horizon and look out beyond those events and try to figure out where do we think the cash flow generation of the business would be as the business normalized. As we looked through that, our view was it made sense to maintain the dividend in 2024. The gap will be the widest between that dividend payout and the generation of cash in the business in the first half of 2024, and then it will close as we go to the second half of 2024 and then into 2025 and get beyond that, and we believe we'll return to a growth period of time once we get past 2025.

00:43:47 So we're in essence looking through these movements in these events and trying to set the dividend at a level that we could maintain in 2024. The gap between the current level of dividend and the cash generation will be smaller in 2025, and then we'll return to growth, we believe, in 2026.

00:44:09 **Question – Ric Prentiss:** That's clear. Okay. Thanks. One other question on my side. On the small cells, I think you mentioned there were 5,000 nodes decommissioned in mid-2023 from Sprint. Was that within second quarter or there's more of those to be decommissioned, sorry, in third quarter? Assume you're done with it. And the 14,000 nodes in 2024, is that a gross or a net number or are they almost the same?

00:44:35 **Answer – Jay A. Brown:** On the 5,000, there's a little bit of movement. Most of those have come out at this point which is why you saw our total nodes and contracted nodes come down from 120,000 to 115,000. That's reflective of the churn, so most of those have worked their way through. The number for 2024 when we talk about 14,000 gross and net are the same, so we don't expect any meaningful churn in 2024 of small cells nodes. So there's no offset there that you need to be made aware of.

00:45:09 **Question – Ric Prentiss:** Good. And the $10 million Sprint churn in the 2024 guidance, is that basically in essence kind of a half year then of the $10 million reflective?

00:45:18 **Answer – Daniel K. Schlanger:** Yeah, it basically is, exactly, it's the rollout of this year's churn hitting 2024.

00:45:23 **Question – Ric Prentiss:** And that gets back to that first half versus second half kind of concept that's a contributing factor to second half being better then?

00:45:29 **Answer – Daniel K. Schlanger:** Yes.

00:45:31 **Question – Ric Prentiss:** Great. Thanks so much again. Best wishes.

00:45:35 **Answer – Jay A. Brown:** Thank you.

Operator

00:45:37 The next question is from David Barden of Bank of America. Please go ahead.

Analyst: David W. Barden

00:45:42 **Question – David W. Barden:** Hey, guys. Thanks for taking the questions. Just a couple on the small cell side. So Jay or Dan, with a 40% step-up in the rate of node deployment happening at a time when you're kind of shrinking the organization, what has to happen? How does that happen to kind of make that step-up because this is larger than we've kind of ever seen you guys do before? And then the second question related is should we assume that this is kind of the new normal both in terms of discretionary CapEx and in terms of kind of node deployments for the foreseeable future or is this more of an anomaly and kind of more like the 10,000 node, $1.2 billion discretionary CapEx is more the norm? Thanks.

00:46:18 **Answer – Jay A. Brown:** You bet. Good morning, Dave. On your first question, the changes that we made in terms of reduction of staffing happened almost exclusively on the tower side and what we were adjusting the internal costs related to were both in the services business on the tower side as well as on the tower operating side. And those were adjusted based on the volume of activity that we saw for tower leasing and the movement from those peaks of 5G down to the levels that we provided both – we think we're going to deliver both in the second half of 2023 and then as we go into 2024. As we think about resources on the small cell side, I believe in (00:47:10) our team and the growth in both use of technology and refining some of the processes and making ourselves more successful at navigating through municipalities which I talked about in some of my comments.

00:47:25 I don't see a significant need for us to add additional resources to our fiber segment as we tackle this significant increase in the amount of nodes. Our team has been preparing for this, and one of the benefits of the long lead time that we have in that business is we can be really thoughtful about making sure we plan the work and engage the work and as well as looking for ways to do it more efficiently. The team has done a really good job of that, so the job shrinkage and the reduction of costs has really not come from that segment of the business and I believe we're prepared to deliver the growth that we're talking about without material changes to the cost structure on the upward side. On your second question around the discretionary CapEx, it's hard to give you a really long-term forecast about that because we haven't paired that with what do we think the demand is going to be and the amount of activity.

00:48:26 At a given level of activity that's similar to what we're doing in 2024, I would say yes, we would expect the CapEx to be in and around that level if that's the level of activity that we're operating with. We're continuing to see the business move and navigate towards a greater percentage of co-location nodes. Those returns, as I mentioned to an earlier question, have come in at levels that we would expect – we expected them to come in at, so we're seeing the multi-tenant model, multi-tenant systems deliver returns that were in line with expectations. And then as we go out a long way, our view is generally that the carriers are going to need more small cells than what they're currently taking today as they densify the 5G network and we believe that densification will continue as consumers use the network to an even greater degree.

00:49:22 So, the total addressable market and the need for small cells, we believe, will have upward trends on it, and as those upward trends come, I think it creates the opportunity for us to put investment opportunities back through that rigorous process that I talked about in my comments around do these investments in those – in particular markets that may have opportunity in them, do they make sense for us relative to other alternatives, and we'll just have to see how that unfolds to see whether it makes sense for us to pursue those or not.

00:50:01 **Question – David W. Barden:** Got it. Thanks so much.

00:50:03 **Answer – Jay A. Brown:** You bet.

Operator

00:50:07 The next question is from Greg Williams with Cowen. Please go ahead.

Analyst: Gregory Williams

00:50:12 **Question – Gregory Williams:** Great. Thanks for taking my questions. Just echoing the comments for Dan. Wish you all the best and thank you for the support. The first question is on the higher costs for 2024. It looks like it's up $30 million to (00:50:22) $60 million even after the $35 million in cost savings. I'm just wondering if you can break out the piece parts there if it's ground lease escalation, etcetera. And then the second question is just on the comments around the small cell returns, you're saying it's just as good as towers on a multi-tenant basis, so is there any update to, kind of, lease-up rates in small cells as we think of that vis-à-vis towers? Thanks.

00:50:45 **Answer – Daniel K. Schlanger:** Yeah, thanks, Greg. Appreciate the comments and then I'll start with the first question on higher costs in 2024. You hit on a bunch of them, so the major cost increases that we experienced, we do have ground leases under our towers. It's a single large line item that we have in our P&L on the expense side, and those ground leases increase at about 3% per year in cost. That has to be baked in. Secondly, we, like every other company, are faced with increasing costs for labor for people who work here, people who are hiring because the cost of people is going up with inflation. And then lastly, we had some one-time savings in the back half of 2023 that won't occur going into 2024 which show a little bit more of an increase also. When you add those things up, you get to the type of cost increases you were just referencing.

00:51:43 **Answer – Jay A. Brown:** Greg, on your second question around the returns, small cells have been – historically continue to be in our view would be – will continue to be, initially and with the first co-located tenant and the second co-located tenant on a particular system, actually better than what we've seen historically from towers. When we put capital into the ground for small cells, we are at about double the initial yield on invested capital to what we are with towers, whether those towers were acquired historically or built, our initial returns are more than double what a tower is. When we get to the second tenant on a small cell system, we're in the low double-digit range. Generally with towers in order to get to those kind of yields as you can see in the supplement, we're well over two tenants in order to get to low double-digit yields on invested capital. And then when we get to a third tenant on a system, we're high-teens low-20% yields.

00:52:53 You could see some of that in the disclosure that we gave last quarter around some markets that we've been in for a long period of time and have a significant number of multi-tenant systems in some places where we've got the three tenants. We get the very attractive returns that would exceed those of even towers historically. So, we're at the early stages of co-location, so we're not multi-tenant across the entire system yet, but we do believe over time, like towers, over 25 years of adding tenants, we'll continue to see growth in those returns and yields. And we believe over time this business on the small cell side will continue to trend towards what we've seen in towers and will create a significant amount of shareholder value over time as we've been able to build assets in the best markets in the United States, those with dense populations and a lot of data demand.

00:53:50 And believe as the carriers densify the network, the assets that we have are going to result in a lot of co-location over many years and that'll consistently drive increases in yields and growth and value creation for equity holders.

00:54:07 **Question – Gregory Williams:** Great. Thank you.

Operator

00:54:11 The next question is from Matt Niknam of Deutsche Bank. Please go ahead.

Analyst: Matthew Niknam

00:54:18 **Question – Matthew Niknam:** Hey, guys. Thanks for taking the question. Just two quick ones. First, on AFFO per share growth, maybe if you can help us think through the moving parts driving the expectation for second half AFFO per share in 2024 to be better than the first half, is it improved leasing, is there anything on the cost side in terms of ramp-up of savings to be cognizant of? And then secondly on services. If you could just help us think through the progression from the, call it, 25-ish percent range in the third quarter to around the 50% exit rate by the end of next year. Is that linear, is that more of a stair-step higher, just how to think about the path there? Thanks.

00:54:57 **Answer – Daniel K. Schlanger:** Yeah, Matt, on the first question, on what's driving second half, is really a combination of just normal kind of seasonality in our business, which we didn't see in 2023 and called out in 2023. It's returned more to how that works in 2024 and our business typically works in the second half of the year and even better than the first. In addition to some of the churn events that Ric was mentioning, kind of, hit the first half of the year not the second, and so we think that all of that added up would lead to the low point in AFFO being in the first half of 2024.

00:55:32 **Answer – Jay A. Brown:** Matt, on your second question, I'm assuming you're referring to the margins in the business, is that the question that you're asking? The extraction of the margins.

00:55:41 **Question – Matthew Niknam:** Yes.

00:55:41 **Answer – Jay A. Brown:** Okay. The current margins, and there will be some bleed over of this into the beginning of 2024 and around the 25% range, has to do with our exit of the construction services. Those would be the project management services that historically we performed to help our customers install on the assets that we have. The margins in that business are much lower than the margins that we have on a go-forward basis, the services that we'll perform on a pre-installation, pre-construction for our customers, so what you're really seeing is a mix change over the course of the year, as the legacy business ramps down and goes away, and the business that we will continue to perform for the foreseeable future, the margins on that business are better, so you're seeing that in the guide.

00:56:36 And by the time we get to the second half of next year, virtually all of those legacy services that we'll no longer be performing will have been moved out of the results.

00:56:50 **Question – Matthew Niknam:** That's great. Thank you, both.

00:56:51 **Answer – Jay A. Brown:** You bet, Matt. Thanks. Operator, we can take one more question.

Operator

00:56:58 Okay. The final question is from Brandon Nispel of KeyBanc Capital Markets. Please go ahead.

Analyst: Brandon Nispel

00:57:06 **Question – Brandon Nispel:** Great. Thank you for taking the question, Dan. Thanks a lot for all your help over the last several years and best of luck. Hoping you guys could unpack the tower leasing, sort of, both for 3Q and 2024. You've always talked about, sort of, the contracted nature of this business, but on a year-over-year basis, leasing went down roughly 40%. So, I was hoping you could, sort of, unpack the drivers from like a sequential or year-over-year standpoint and then talk about your first half or second half expectations for tower leasing in 2024. And secondly, I was hoping you could unpack the churn that you've guided to, the $155 million just from a tower, fiber and small cell side and then the one-off churns from the remaining Sprint cancelations. Thanks.

00:57:58 **Answer – Jay A. Brown:** Sure. I'll take the first question, and Dan can walk through the numbers on the second question. Brandon, as we came to our tower leasing guide for 2024, we looked at the activity that we were seeing from the customers and embedded in that activity, about 85% of what's in the guide for 2024, at this point, is contracted, so there is some amount of roll over of activity that we'll see in this calendar year where the tenant goes on the tower this year and then shows up for a full 12-months in calendar year 2024. There is, by definition, about 15% that we still got to go get in calendar year 2024 that we don't have line of sight to, and our view has been, as we came off of the peak of 5G, that there is absolutely going to be a needed addition to tower sites of our carriers investing to add additional equipment to build-out 5G. We're not done with 5G and they're not done with macro sites.

00:59:04 So, that activity will continue, and it's – based on the conversations that we've had with them, the activity that we've seen, and the work that we see ahead, still believe that there's good activity on the macro tower side, feel good about where the guidance is, and feel good about where we'll be not only in 2024, but in the years beyond as the towers are still the most efficient way to deploy network capacity and so to the extent that macro tower sites can solve the need, the carriers, we believe, will continue to prioritize those assets in the portfolio, and we'll continue to see good growth in towers for a long period of time. So, we've reset our expectations from where we were at the peak of 5G, but feel good about where we are from this point forward.

00:59:58 **Answer – Daniel K. Schlanger:** Yeah. And the second question on the $155 million of churn. On the tower side, it's going to be very similar churn in 2024 to what we think we'll see in 2023 which is on the low-end of our 1% to 2%, on the $30 million range of churn on towers. On small cells similarly, very similar to 2023. We'll see about 1% of our small cells, so as long as you take out the Sprint cancelations and fiber solutions, as Jay mentioned, we believe the churn is coming down from closer to 10% in 2023 to around 9% in 2024, so in the neighborhood of $115 million, maybe $120 million, so when you add all those up you get to about $155 million total churn.

01:00:44 **Question – Brandon Nispel:** Great. Thank you for taking the questions.

01:00:46 You bet. Well, thanks everyone for joining the call this morning. Appreciate the continued support, and we look forward to seeing and talking with you soon, and just want to thank our team broadly for all the work that they have done to deliver the results for 2023 so far. We've got a good quarter ahead of us to finish up the year and then excited about the opportunity to continue to grow the business as we get into 2024 and beyond. Thanks for joining. We'll talk soon.

Operator

01:01:04 The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.