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EDITED TRANSCRIPT

T.N - Q1 2024 AT&T Inc Earnings Call

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OVERVIEW:

Company Summary

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PRESENTATION

Operator

(technical difficulty)

quarter 2024 earnings call. (Operator Instructions) As a reminder, this conference call is being recorded. I would like to turn the conference call over to your host, Brett Feldman, Senior Vice President, Finance and Investor Relations. Please go ahead.

Brett Feldman

Thank you, and good morning, everyone. Welcome to our first quarter call. I'm Brett Feldman, Head of Investor Relations for AT&T. Joining me on the call today are John Stankey, our CEO; and Pascal Desroches, our CFO.

Before we begin, I need to call your attention to our safe harbor statement. It says that some of our comments today may be forward-looking. As such, they are subject to risks and uncertainties described in AT&T's SEC filings. Results may differ materially. Additional information as well as our earnings materials are available on the Investor Relations website.

With that, I'll turn the call over to John Stankey. John?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Thanks, Brett. I appreciate you all joining us this morning. We started the year with a solid first quarter as we continue to make steady progress on our investment-led strategy of being the best connectivity provider through 5G and fiber. We're growing the right way by adding valuable long-term wireless and broadband subscribers. Since Pascal will cover first quarter results in detail, I'd like to spend some time highlighting how our strategic priorities are enabling us to deliver positive results and build a long runway for sustainable growth.

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When you look under the hood, it's clear that our largest and most powerful EBITDA growth engine, Mobility, is running well. Our strength in value proposition helped us deliver 349,000 postpaid phone net adds in the quarter. We now have about 71.6 million high-value postpaid phone subscribers, which is up 1.5 million from a year ago. And these aren't empty calorie additions. Our results reflect the quality of our customer growth with higher ARPU, higher adjusted operating income, improved margins and lower postpaid churn.

We're also growing efficiently, thanks to our consistent and simple go-to-market strategy. Our postpaid phone churn of 0.72% was our lowest first quarter churn ever on record. And once again, we expect to report the lowest postpaid phone churn among the major service providers this quarter. This highlights the value customers place on the wireless service we provide and the continued strength of our best deals for everyone's strategy.

Now let's move to fiber, which is our fastest-growing engine. The story here is familiar and one we like. Where we have fiber, we win. And we're bringing fiber to more Americans than anyone else. Since the first quarter of last year, we passed about 2.4 million locations with fiber and now pass more than 27 million consumer and business locations.

Over the last year, we grew our AT&T Fiber consumer subscriber base by about 1.1 million to nearly 8.6 million customers. This includes 252,000 AT&T Fiber net additions in the first quarter. As a result of our established fiber success and early AT&T Internet Air subscriber growth, we've grown our consumer broadband subscriber base for 3 consecutive quarters. And we expect this trend to continue.

We're even more excited about the converging power of 5G and fiber together. Where we have AT&T Fiber, our strong national 5G wireless brand provides us the opportunity to be customers' single converged provider, seamlessly connecting them both in the home and on the go.

We're able to deliver convergence at a level that none of our peers can match as we're the only provider that benefits from owners' economics and scale with both 5G and fiber. This all matters because convergence presents clear benefits. When a customer has both our wireless and fiber products, we see a meaningful improvement in churn and Net Promoter Scores. This ultimately translates to much higher lifetime values for converged customers.

We're also making great progress on ensuring more Americans have access to high-speed Internet. Just this month, we expanded our commitment to $5 billion over this decade to help bridge the digital divide in our country. We've already contributed to connecting approximately 5 million Americans. And our goal is to help connect 25 million people in total by 2030.

We believe that connecting changes everything, and that we must collectively address the communications capabilities of our country's needs for the next century, not the last one. To make this happen, we need sound policy that's done right. And our teams are working hard to make that happen. The future of connectivity is critical to advancing our society. That's why we're focused on growing and evolving our networks.

As a result of these efforts, the areas where we're investing most heavily through 5G and fiber are performing very well. For perspective, in 2023, Mobility and Consumer Wireline together represented more than 80% of revenue and about 85% of EBITDA in our Communications segment. This means we're growing the large majority of our business and driving improved operating leverage across it. We expect this to continue.

However, we still have legacy elements of our business that we're in the midst of transitioning, particularly in Business Wireline. In the quarter, Business Wireline EBITDA was down 16.5% as the industry-wide secular decline of legacy voice continues. While the wholesale market has stabilized, the reality is that businesses are transitioning to mobile and cloud-based services at an accelerated rate as post-pandemic workplace restructuring takes hold.

We see the benefits from this connectivity transition in Business Solutions, where wireless service revenues grew 4.6% in the first quarter, outpacing our overall Mobility services revenue growth. While we continue to actively work our legacy transition strategies to end-of-life products, reduce our operating footprint and eliminate fixed costs, we're advancing several cost savings and productivity initiatives to align with this reality such as vendor and management workforce rationalization.

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We also strongly believe that the future-focused area of Business Solutions aligns well with our core connectivity competencies. And we continue to build out a connectivity portfolio with real long-term growth opportunity. Take FirstNet, this prioritized service for first responders shows what we're able to accomplish when we focus on growing our business in areas where we have traditionally under-indexed.

Additionally, our continued 5G and fiber expansion will enable new growth when paired with broader distribution. We have relationships with nearly 2.5 million business customers today and an opportunity to win with more small- to medium-sized businesses.

One way we intend to meet small and medium businesses connectivity needs is with our new fixed wireless service, AT&T Internet Air for Business. We believe this is a durable national play with business because it's able to serve as a reliable 5G-powered primary Internet connection, where fiber is not available in remote locations, when temporary access is needed or with small and medium businesses that don't require always-on video streaming. While it's still early, we've been very pleased with the solid demand we're seeing from businesses.

Given our success growing core connectivity, we're focused on furthering the AT&T value proposition in ways that matter to our business customers. And security is at the top of the list. That's why we introduced AT&T Dynamic Defense, which provides built-in security controls on top of world-class access.

The takeaway is that we're well positioned to capitalize on urging connectivity opportunities with businesses, thanks to the strong relationships we have with almost all of the Fortune 1000 and our leading position in fiber and the fact we operate the largest wireless network in the U.S.

Our Business Wireline operations transformation will not be a linear process. And we're going through the heaviest lift right now. However, our strong momentum across our growth areas of Mobility and broadband is allowing us to outpace legacy declines and drive positive consolidated results. And we remain on track to deliver on all the consolidated financial guidance we shared in January.

Now let's spend a moment on our second priority of being effective and efficient in everything we do. Last year, we set a new target for an incremental $2 billion-plus in run rate cost savings by mid-2026. This came on top of the $6 billion-plus run rate cost savings target we achieved last year.

The continued adoption of AI is not only helping us make progress on this goal but also benefiting our employee and customer experiences. This focus on efficiency is translating into improved operating leverage despite continued elevated inflation. You can see this in our cash operating expenses, which were down year-over-year in the first quarter, contributing to adjusted EBITDA margin expansion of 170 basis points.

This brings me to our final priority, which is our deliberate and balanced approach to capital allocation. As we indicated would happen, our capital investment levels have come down year-over-year as we move past the peak of our 5G rollout. Still, we remain a top investor in America's connectivity and continue to expand fiber at a steady pace.

Even with this continued investment, we delivered first quarter free cash flow of $3.1 billion compared to $1 billion a year ago. This aligns with the expectations we shared for more ratable quarterly free cash flow, which we've accomplished by efficiently growing EBITDA, improving cash conversion and reducing our short-term financing balances.

Our strong free cash flow has also enabled us to pay down debt. We finished the first quarter with net debt to adjusted EBITDA of 2.9x and continue to expect to reach our target in the 2.5x range in the first half of 2025. So it's clear we're operating well against our business priorities. And as a result, we're growing share with 5G and fiber.

In Mobility, we've been increasing our share of wireless service revenue growth even without the benefit of fixed wireless, which is reported in Consumer Wireline. We also expect that this will be the 11th time in the last 13 quarters where we deliver the industry's lowest postpaid phone churn. In Consumer Wireline, we're outpacing cable as we add broadband customers. This is driven by AT&T Fiber, which has consistently captured over 1/3 of broadband net adds across major providers for the past 3 years.

So in summary, across the services and technologies most important to the future, 5G and fiber, we're performing well and growing our share in a healthy industry environment. This gives me confidence in our strategy and tells me our team is making solid progress on our priorities.

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With that, I'll turn it over to Pascal. Pascal?

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Thank you, John, and good morning, everyone. So let's start by reviewing our first quarter financial summary on Slide 7.

In the first quarter, revenues were down slightly as the decline in low-margin Mobility equipment revenues and Business Wireline revenues offset growth in high-margin wireless service revenues and fiber revenues. Adjusted EBITDA was up 4.3% for the quarter as growth in Mobility, Consumer Wireline and Mexico were partially offset by a continued decline in Business Wireline. For the full year, we still expect adjusted EBITDA growth in the 3% range.

Adjusted EPS was $0.55 compared to $0.60 in the year-ago quarter. In the quarter, there were about $0.11 of aggregated EPS headwinds from four items we discussed last quarter. These include higher depreciation, higher noncash postretirement benefit costs, lower capitalized interest and lower equity income from DIRECTV. For the full year, our expectations remain for adjusted EPS of $2.15 to $2.25.

First quarter free cash flow of $3.1 billion was up more than $2 billion compared to last year. The important takeaway is that improved conversion of EBITDA to free cash flow has allowed us to pay down short-term supplier obligations. The paydown of these facilities should allow us to continue to drive more ratable quarterly free cash flow.

Cash from operating activities came in at $7.5 billion versus $6.7 billion last year. As a reminder, the first quarter is typically the high-water mark for device payments. And we expect payments to get progressively lower throughout the year. Capital investment for the quarter was $4.6 billion, down about $1.8 billion compared to the prior year. Capital expenditures were $3.8 billion compared to $4.3 billion in the prior year.

Now let's look at our Mobility operating results on Slide 8. The wireless industry remains healthy, and our Mobility business continues to deliver strong results, driven by our consistent go-to-market strategy and solid execution. For the quarter, we reported 349,000 postpaid phone net adds. We grew service revenue by 3.3%, which included the impact of customer credits. This was offset by lower equipment revenues with postpaid upgrade rate of 3%, which was down from 3.7% last year. We continue to expect wireless service revenue growth in the 3% range for the full year.

Mobility EBITDA grew 7% or about $600 million year-over-year, which exceeded service revenue growth on a dollar basis. This demonstrates we're significantly improving operating leverage and highlights the efficiency of our consistent go-to-market strategy, which has enabled us to take cost out of the business. We now expect our Mobility EBITDA to grow in the higher end of the mid-single-digit range this year, driven by better-than-expected performance with Business Wireless customers and continued disciplined cost management.

Our postpaid phone ARPU was $55.57. This was up nearly 1% year-over-year, largely driven by higher ARPU and legacy plans. For the year, we continue to expect modest postpaid phone ARPU growth.

Now let's move to Consumer Wireline results on Slide 9. Our growth in Consumer Wireline was led once again by our fiber subscriber growth, which consistently yielded strong returns. In the quarter, we had 252,000 AT&T Fiber net adds, which is in line with the outlook we provided. This is the 17th consecutive quarter with AT&T Fiber net adds above 200,000. We now have fiber penetration of 40% with several markets well above that level.

Broadband revenues grew 7.7%, including strong fiber revenue growth of 19.5%. For the full year, we continue to expect broadband revenue growth of 7%-plus. Fiber ARPU of $68.61 was up more than 4% year-over-year with intake ARPU remaining above $70.

Consumer Wireline EBITDA grew 14.6% due to growth in broadband revenues and ongoing cost transformation. We now expect Consumer Wireline EBITDA to grow in the mid- to high single-digit range this year, driven by continued strong fiber revenue growth and disciplined cost management, partially offset by continued legacy copper declines.

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As our customer base continues to migrate to fiber from legacy services, our broadband support costs are decreasing, thanks to fiber's more efficient operating model, greater reliability and higher quality service. While fiber remains our focus and lead product, we continue to be encouraged by the early performance of AT&T Internet Air, our targeted fixed wireless service, which is available in parts of 95 locations. We now have more than 200,000 AT&T Internet Air consumer subscribers, having added 110,000 in the quarter.

Ultimately, we couldn't be more excited about the future of Consumer Wireline with AT&T Fiber well positioned to lead our growth and AT&T Internet Air helping us provide quality broadband service to customers where we don't offer fiber.

Now let's cover Business Wireline on Slide 10. Business Wireline EBITDA was down 16.5% due to faster-than-anticipated rate of decline for our legacy voice services. At the start of the year, we shared that we expected Business Wireline EBITDA trends to improve on a full year basis. However, due to faster-than-expected decline of legacy voice services, we now expect full year Business Wireline EBITDA declines in the mid-teens range versus our prior outlook of a decline of 10%, plus or minus.

As John mentioned, we're advancing several cost-saving and productivity initiatives. This should benefit results in the second half of the year, when we also have more favorable year-over-year comparison. As we transition this business, we believe our 5G and fiber expansion presents plenty of growth opportunities.

We're already seeing this in some of the parts of our broader Business Solutions results today. A great example is FirstNet, where wireless connections grew about 320,000 sequentially. We're also pleased with early demand for AT&T Internet Air for Business, which we expect to benefit results in the second half of the year.

Now let's move to Slide 11 for an update on our capital allocation strategy. Our approach to capital allocation remains deliberate. We're successfully balancing long-term network investment to fuel sustainable subscriber and service revenue growth, paying down debt and returning value to shareholders. We remain on track for full year capital investments in the $21 billion to $22 billion range versus approximately $24 billion in 2023.

While our overall capital investment will be lower in 2024 compared to recent years, we continue to invest in key growth areas, given the compelling returns on these investments. In Mobility, we are focused on modernizing our network through our Open RAN initiative. And with fiber, we remain on track to pass 30 million-plus consumer and business locations by the end of 2025.

As we've stated before, the better-than-expected returns we're seeing on our fiber investment potentially expands the opportunity to go beyond our initial target by roughly 10 million to 15 million additional locations. This also assumes similar build parameters and a regulatory environment that remains attractive to building infrastructure.

It's important to note that as we continue to build out our network this year, we expect to have lower vendor financing payments while increasing the total investment we make directly into our networks as we continue to invest in fiber expansion and wireless network transformation. In other words, we expect our total capital investment and capital intensity to decline this year even as we boost investments in our network.

We also remain laser-focused on deleveraging. Over the last 4 quarters, we reduced the debt by about $6 billion. At the end of March, net debt to adjusted EBITDA was 2.9x. And we're making steady progress on achieving our target in the 2.5x range in the first half of 2025.

As I mentioned last quarter, we expect to address near-term maturities with cash on hand. And this quarter, we repaid $4.7 billion of long-term debt maturities. Looking forward, our debt maturities are very manageable, and we are in a great position with more than 95% of our long-term debt fixed with an average rate of 4.2%.

In addition to paying down debt, we reduced vendor and direct supplier financing obligations by about $2.3 billion during the quarter. This was partially offset by $400 million in additional proceeds on our securitization facility. These efforts highlight the quality of the free cash flow we're delivering.

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DIRECTV distributions in the quarter were $500 million compared to $1.3 billion in the first quarter of 2023. For the year, and thereafter, we continue to exact DIRECTV cash distributions to decline at a similar rate to 2023 or by about 20% annually.

With $3.1 billion in first quarter free cash flow, we've dramatically improved our free cash flow ratability just as we committed we would last year. Looking forward, we still anticipate generating approximately 40% of our total 2024 free cash flow in the first half of the year and continue to expect full year free cash flow of $17 billion to $18 billion range.

To close, I'm really pleased with our team's overall performance in the quarter. Despite managing through legacy declines, our strength in Mobility and Consumer Wireline has us on pace to deliver on our full year consolidated financial guidance.

Brett, that's our presentation. We're now ready for the Q&A.

Brett Feldman

Thank you, Pascal. Operator, we're ready to take the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question will come from the line of Simon Flannery of Morgan Stanley.

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

Good to hear the reiteration of the 2.5 leverage target for early next year. It would be great if you could just go through how you're thinking about the various capital allocation alternatives, buybacks, dividend growth, deleveraging, the 10 million to 15 million fiber adds, BEAD investments. Any other considerations?

And how we should think about the profile? Presumably this time next year, we'll be having a more fulsome conversation. But anything more you could add around that would be great. And then just housekeeping on the outage, maybe you could just size the credit for us. And was there any impact on net adds in the quarter?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

So I don't know that I'm going to give you a whole lot more than what I've previously said. I mean, it's really good to have choices. And we clearly have choices coming up. And we've worked really hard to put ourselves in this position to do that. And I told you there would be a very deliberate process that the Board would go through to understand what they want to do as those choices start to materialize. And we're in the middle of doing that. We are working through a pretty systemic process. And at the top of that, as you can well imagine, is we're very cognizant of a desire to ensure that we're treating our shareholders well and returning capital where we can and doing it in a smart way.

And so as I've said before, we'll evaluate at that time where things like interest rates stand. We'll evaluate where we are on the dividend yield relative to the equity value and where we have opportunities for reinvestment in the business and kind of understand what we think the right combination of those are. And we have a pretty deliberate approach to making that happen. I would give you some characterization right now as we've worked really hard over the last couple of years to ensure we protect the dividend. I think you've seen that we've done that. And we've put ourselves in a really strong financial position. That's paramount and important to us as we move into this.

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You heard Pascal's comments that we feel pretty good about where the balance sheet sits today relative to what we're paying for the capital on the balance sheet and our abilities to manage that moving forward. I don't feel like we've got some immediate need to move differently than the trajectory we've been on. And so if I was awaiting, we'll be waiting against those other options that we think about and how we want to go and get the mix right. So I think you'll see more as we get to the end of the year. As I said, the Board is working really hard on this issue. And I don't want to take away any degrees of freedom and latitude they have to debate it and figure out what they want to do, given what's going on in the market at the time we arrive.

On the outage, look, I'm upset that we had it. It's unfortunate we had it. The entire team feels responsible for it. We know we can do better. We've put in place an awful lot of steps to ensure that we do better moving forward. I think I'm confident that we have done that. And I feel like we can operate better than what we exhibited on that particular morning. Now having said that, I'm really proud of the way they responded to the circumstances when they occurred. And they managed through the situation as well as could be expected. And in fact, I think you see that in the metrics. You see that we had a really, really good churn quarter. Obviously, that wouldn't happen if we didn't do the right things with the customer base.

I'm pleased relative to what I've seen reported so far in the industry of our customer growth. I'm sure there were a couple of days of maybe some suppressed activity as a result of the outage. I think it's probably something that's measured in days, it wasn't measured in weeks and months. But we feel pretty good about where we stand right now. Certainly, as you might guess, we have a variety of survey methodologies that we use in research with our customer base and prospective customers. Those indicators don't show me anything that causes me to be concerned about what transpired or what occurred.

I think some of our recovery methods that we use with our customer base was -- they were the right decisions. And you've seen most of that reflected in the first quarter financials. There's a little bit that will drag into the second quarter base on how bill rounds go. But you should expect that you've seen the bulk of that move through our numbers. And I'm satisfied that where we ended up on service revenue growth and margins that, that was a strong quarter in aggregate, inclusive of what we had to do in terms of the credits.

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

And on BEAD?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Nothing that I think -- as I said last quarter, Simon, I think BEAD is a 2025 issue, it's not a 2024 issue. It doesn't feel like it's moving in any particular way all that fast at the state level. And as I've also indicated, it's pretty clear to me that there's places where we're going to be more energized about playing and places where we're going to be less energized about playing based on how various states are approaching this.

And I don't think there's anything right now, I can tell you point blank, we won't be coming back in with any revisions to our guidance or anything like that, that is relevant to 2024. I think through this year, there may be some incremental things that we talk about in 2025 in terms of how we choose to reinvest capital and where we choose to go. But it's not anything that I see right now that's front and center.

Operator

Our next question will come from the line of John Hodulik of UBS.

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John Christopher Hodulik - *UBS Investment Bank, Research Division - MD, Sector Head of the United States Communications Group and Telco & Pay TV Analyst*

First, sort of a follow-up to Simon's question, on the data breach, that's a sort of a second quarter issue, but just want to make sure to see if there's any impact that you saw early in the quarter from the data breach.

And then certainly, one of the themes that we're seeing here in the first quarter is the low upgrades and low churn environment. Do you expect that to continue despite the fact that we may have a sort of AI device launch later this year? And does that low churn environment give the industry and AT&T, in particular, pricing power as you look into the rest of the year?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

I don't want to characterize this incorrectly, but there are a lot of things going on broadly beyond AT&T and the cyber environment. I'm sure you're all obviously consumers and are seeing the dynamics of what's happening. There's clearly -- the bad actors have stepped up a level in the last several months, I think. And if I were to broadly step back and say, are we going to see more activity and more problems partly because of just the activity level and how robust the business opportunities are for hackers and those that want to inflict bad acts on folks and partly, I think, because of reporting requirements, I expect you're probably going to see the noise level go up.

What we have seen from our notification is very similar to the outage. I don't see anything in the customer metrics or anything that's going on that suggests that it creates a long-term issue on sentiment. That doesn't mean we don't take it seriously. That doesn't mean that we're not examining what happened back in 2019 and trying to understand what root causes are around that. Those actions are all underway. But it doesn't appear to me that it's doing anything to impact our business as we stand here today in 2024. But we'll continue to evaluate that, and we'll continue to work through the dynamics that are occurring.

I would tell you that on the upgrade rates and churn, we've seen, as I've said last quarter, a little bit of tapering in the industry. We expected that to occur. We expected upgrade rates to be a little bit more tempered than what we had seen last year. I don't see anything going on right now that suggests we're out of pattern to what our expectations were as we set up a plan for 2024. We'll probably see a little bit of ebb and flow each quarter. I'm not sure that I'm of the mindset that there's going to be something that occurs in the device portfolio that dramatically changes things in the latter part of the year.

There will be the usual holiday promotions. There will be the usual devices and opportunities for individuals to create something that's special during the holidays. But that's a seasonal pattern we're accustomed to. And I think we'll be seeing things on the margin adjusting left and right. I just don't believe we're going to be into a cycle that's what I would consider to be an out-of-pattern cycle in any way, shape or form.

And I'm going to give you the same answer I always give on where we are in pricing power. Look, I think the industry is healthy. I think as I've indicated before, we're coming off of policies that drove record levels of investment in the industry. I think all players are mindful after record levels of investment to try to yield the appropriate returns that you would have to get after making those things. And I see that kind of dynamic occurring. I think I know we're mindful of it, and we want to make sure that we're getting reasonable returns off that level of capital.

And my observations of what I see being reported over the last couple of quarters is that others are doing the same. And we're providing tremendous amount more value to customers. They're using 30% more of our product, 35% more every year. The performance of these networks is increasingly better. There's choices that are coming in and how they apply the use of the technology for mobile to fix. So one would expect that maybe there's an opportunity to change the value equation and continue to take a little price in places. And we're going to continue to do that.

Where we think certain products have that kind of staying power, I think we've been pretty consistent over the last couple of years of saying there's opportunities to do that. I think we've tried to stress with you when we do it, we're very mindful of doing it intelligently. I believe our churn numbers reflect that we've executed pretty well on that front. And I feel good about the fact that we've been able to drive our ARPUs up, keep our margins in check, if not improve them, and continue to do some things that take some price in certain places where we think we can keep the value equation in check. And I expect we're going to continue to do that as we move through this year.

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Operator

Peter Supino of Wolfe Research.

Peter Lawler Supino - *Wolfe Research, LLC - MD & Senior Analyst*

A question about the Mobility side. Obviously, the consolidated or segment results were really good. In looking at the EBIT growth, it's similar to the rate of service revenue growth in a quarter when gross adds and churn were lower, a great thing, less cost. And I'm just wondering why -- what else is happening in the cost structure so that EBITDA wouldn't outgrow service revenue in a quarter like this?

And then a quick one on Internet Air for Business. Is your intent to distribute that nationally? Or will that be a more regional strategy in the way that IA has been so far in residential?

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Peter, Pascal. In terms of EBIT, and you're talking about operating income that's inclusive of the depreciation, correct?

Peter Lawler Supino - *Wolfe Research, LLC - MD & Senior Analyst*

Yes, I am.

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Remember, we guided that, as a result of the Ericsson Open RAN deal, we would have accelerated depreciation associated with some of the equipment that was previously in our network that we were going to depreciate over shorter lines. That's a dynamic you're seeing come through there. I feel really good about the overall expense management and overall cost profile. And you see that coming through in our EBITDA margin expansion in that business.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

And Peter, we broadly, as I indicated in my remarks, see Internet Air for Business being a national product. You probably maybe noticed that -- you may not be a golfer, but you noticed during the Masters, we kind of previewed some of our advertising that we'll be coming out on the product that's geared toward the business market segment. And it doesn't mean that it's a product for every business, but it certainly is a product for every state is what I would say.

We want to be mindful of making sure that we match the product to businesses that have the right usage characteristics that we think we can provide a quality level of service and right value. There are many businesses that match that. And there are many businesses that have usage characteristics and behaviors that are atypical to a typical single-family dwelling. And that's why we think it's a good place to invest time, energy, money. And I think that was consistent with what our expectations were from the founding of the product and where we thought we'd go to market with it.

Operator

Bryan Kraft of Deutsche Bank.

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Bryan D. Kraft - *Deutsche Bank AG, Research Division - Director & Lead Research Analyst*

John, can you talk about how you're balancing the marketing and sales budget today between customer acquisition and retention and how that's driving AT&T's performance relative to your competitors? One of the concerns we often hear from investors is that while churn has been great, gross adds have been down for several quarters. But I suspect this is at least partly a function of the strategy. So if you could shed some light there, that would be great.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

You've answered your question. It's intentional with the strategy. I'm more than happy to take gross in places where I think I can drive gross profitably. And I think in some cases, we have to think about how much people are paying for growth and then we also have to think about gross and we have to think about whether or not that gross really has yield on it if it's what the end user is paying ultimately when they come on a network.

And so I think some of the numbers ultimately are, what I referred to in my opening remarks, a bit low calorie. I don't really want to play in the low-calorie space. I want to make sure I'm getting my fair share of the high-calorie subscribers. And that's why we're focused on share of service revenues as maybe being a better benchmark of is the company balancing its growth in the right way.

And when you think about how we balance our budget and what we do internally is we're pretty rigorous around asking ourselves those questions and the segments we attack, how we go after them, the longevity. And look, churn is a key driver when you're investing for that growth. And I'll take lower churn all the time. I don't think that's a bad sign necessarily. I'm perfectly okay with where we stand on that front.

We've talked previously, Bryan, that one of the things I like about where we've been in the market and that I think is, frankly, sustainable probably 1.5 years ago or 2 years ago, most of the questions on this call was where's the growth coming from, and I kept saying the growth was balanced. It's coming from a lot of different segments. We're seeing it come from different parts of the business community. And we're giving you the fact that our business growth has been strong.

We like what we're picking up in the residential environment and the consumer environment and where we see our growth coming from there in terms of what we're taking. So we have a pretty balanced approach to our distribution right now that I think that diversity is helpful. It diversifies our portfolio. It diversifies the base. And that's one of the reasons why the churn numbers are as strong as they are.

Operator

David Barden of Bank of America.

David William Barden - *BofA Securities, Research Division - MD & Global Research US Telecom Services & Communications Infrastructure Senior Analyst*

I guess, first, a follow-up question if I could. John, thank you for your comments about kind of having digested the impact of the outage. But the postpaid phone ARPU was obviously down about a little over 1% in the quarter. And I'm assuming at least some, if not all, of that had to do with the credit and the GAAP accounting for that. And so I was wondering if we could get maybe, Pascal, a jumping-off point from where ARPU really is if we normalize for that credit.

And then second, another kind of housekeeping question is with the sale of Sky Mexico back to, I think, Televisa, what happens now? Like how does that affect the reporting as we think about the rest of the year?

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Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

All right. Dave, I can take both questions. First, on postpaid phone ARPU, I'm assuming you're citing the sequential trend as opposed to year-over-year because we [do] year-over-year. The sequential trend, a couple of things to keep in mind. Yes, the credit was a factor. But it's part of the mix. And we told you, at the time, it was not significant. But it was still a factor in sequential trends.

And the other thing to keep in mind, too, is there is seasonality associated with international roaming, that there are periods where international roaming is going to be higher than not. And that impacts ARPU as well. Overall, we feel really good about the guidance we gave for modest ARPU growth for the year, so nothing substantive there. And your second question was, remind me?

David William Barden - *BofA Securities, Research Division - MD & Global Research US Telecom Services & Communications Infrastructure Senior Analyst*

Sky Mexico.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Sky Mexico, it's a nonevent.

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

It really is a nonevent, Dave. We didn't consolidate. It was an equity method investee that it was, in the context of AT&T, not a significant item.

David William Barden - *BofA Securities, Research Division - MD & Global Research US Telecom Services & Communications Infrastructure Senior Analyst*

Great. And then just one follow-up if I could. Pascal, you said that we should expect a 20% rate of kind of run rate decline in DTV cash contributions on an annual basis, on a kind of go-forward basis? Is that the...

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Yes, that is our best judgment, yes. And that's the guidance we gave at the beginning of the year. And that hasn't changed. In Q1, there was some -- last year, there were some one-time items. And that's probably why you saw some of the decline year-over-year. But we feel good about the guidance we previously provided, which should put us at around -- Dave, are you still there?

David William Barden - *BofA Securities, Research Division - MD & Global Research US Telecom Services & Communications Infrastructure Senior Analyst*

I'm here, I'm listening, all of it.

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Yes. All right. So for the year, we expect to have overall $3 billion of cash distribution from DIRECTV.

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Operator

Michael Rollins of Citi.

Michael Ian Rollins - *Citigroup Inc., Research Division - MD & U.S. Telecoms Analyst*

When we look at the EBITDA growth for the first quarter of 4.3% year-over-year and compare that to the guidance of 3% range for the full year, can you just frame some of the elements that may be changing, whether it's by segment or between revenue and cash expenses, just to think about the differences there?

And then this could be a related question. Can you review your exposure to the ACP program, your expectations on the program possibly being discontinued and potential impact to AT&T's financial results?

Pascal Desroches - *AT&T Inc. - Senior EVP & CFO*

Mike, thank you for the question. So first, as it relates to our segment-level guidance, relative to the start of the year, as I noted in my comments, I anticipate Business Wireline will be a little bit worse than we thought principally because of an acceleration of the legacy voice decline, so putting that down in the mid-teens.

But look, you saw the strong start to both our Mobility business, including the record low churn. And Consumer Wireline, I mean, we delivered over 14% of EBITDA growth. And the dynamics for both, we would anticipate -- what you saw in Q1, we would anticipate being there for the balance of this year. Those businesses are operating really well. The transformation work we've done the last few years is really setting us up to have margin expansion in those businesses. And we feel really good about the trajectory of those two businesses.

Business Wireline is at an earlier point in the product transition. And while we are growing fiber revenues, and then John mentioned, AT&T Internet Air for Business, that's going to grow. And of course, the wireless business relationships will also grow. But those will be offset by legacy declines. And we're confident we can manage through that in the balance of the year and still deliver on or around 3%.

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Mike, I think we indicated last quarter and are still no different position that we could work through the ACP sunset if, in fact, that occurs. And I would say it's probably more likely than not that it does occur. And we could do so without any revisions or changes to what we guided you to. And we still feel that way. We've started the process, as you might guess, of notifying customers and working with them. And we're not just idly sitting by. I think we'll be successful, in many instances, finding ways to continue relationships with customers and ease them into different constructs that make sense for them.

But I feel good about how we went about using the program. I think we used it consistent with the way that policymakers probably would have liked to have seen it used, which is to over-index more than anything else on fixed broadband capabilities. And I think we had a quality customer base relative to how the program was set up. And that's going to allow us to probably transition some of them into other approaches for how to use the service and those that we ultimately do is because the subsidy sunsets. I don't think it's going to be anything that impacts ultimately what we're giving you in terms of our ability to operate the business and hit our financials.

Operator

Sebastiano Petti of JPMorgan.

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Sebastiano Carmine Petti - *JPMorgan Chase & Co, Research Division - Analyst*

A couple of quick housekeeping questions. John, I think you talked about the balanced growth on the Mobility side. You have cited though some underpenetrated segments. I was hoping you can give us an update on the opportunity there, I think SMB, value and fiber selling on the Mobility side. When do you expect to see some of the share gains, I guess, within some of these segments? Is that more of a -- is that -- could we see that within '24? Does that take some time to build on '25 and beyond?

And then on the Business Wireline side, I think, obviously, some focus there on the EBITDA trajectory. But you mentioned you are accelerating some cost-cutting initiatives. Would that be within the context of the $2 billion cost-cutting program? Or should we maybe think of these as additive to that program?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

I would tell you that as we indicated, we've accelerated some of the work that we're doing. So this is things that probably would have occurred later in the cycle that we're moving forward. So we'll get some incremental run rate benefit to that maybe and accelerating our forecast, not necessarily change the endpoint, I guess, is the way I would describe that.

And on our progress around where we're trying to make sure that we're operating more effectively and how our channel distribution works within distribution, I would say that we've made some reasonable progress and have things in place around what we're able to do to penetrate fiber, where we don't have fiber on a wireless subscriber that is eligible to get fiber and the reverse of that. I feel pretty good about what we have lined up around that front. I think we're going to see progress in that regard as we move through '24.

We expected in our business plan and how we've communicated to you our performance that we would have progress in that regard. And I do think I'm starting to see the machine work the right way. We're working hard in trying to position ourselves in the value segment. I would say that it's been a little bit slower ramping in that space and specifically getting the right lineup and the right products in the right place. I do expect as we move through this year, that we will make progress in that regard.

Again, we expected we would make progress in that regard in terms of how we guided our expectations around the performance of the business. And we'll keep pushing and working on it. And I would also say that it's probably the same statement and truth in where we see certain ethnic segments that maybe we could do a little bit better at than what we're doing right now. And we'll continue to work those as well.

Sebastiano Carmine Petti - *JPMorgan Chase & Co, Research Division - Analyst*

Following up quickly just on Mike's question about the ACP, obviously, access from AT&T program was a portion within the commitment that you made earlier in the month. Do you see this as an opportunity to leaning in perhaps on access from AT&T as an opportunity to gain some share from ACP subs that are maybe churning from peers? Or do you see this as an opportunity to lean in a little bit into the low-income segments to drive greater adoption of broadband over time?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

So we intend to continue to keep the access from AT&T in the market, and we'll continue to actively promote it and try to apply it where it makes sense. And I think we're going to continue to see the same segments we were attempting when ACP was live to find that an attractive place to go. I don't know exactly how some of our competitors have used the ACP subsidy. I know how I've used it. I think we've used it in a way where we believe we're catching the waterfront of what we think are the right customers to be putting the subsidy in front of, which are the right customers that should get access from AT&T.

Does that mean that incrementally we should see more coming back our way? I don't know. I would have intuitively hoped that in the form of the competitive markets in which we operate that our message is equally communicated to those who chose us and those who didn't choose us. So

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I don't know that just because ACP goes away that I'm going to dramatically see that equation change. And so I don't expect there's going to be a strong pivot over to AT&T. And I would hope or expect that our competitors might continue to leave some kind of a discounted offer in place for those that qualify for it. So I'm not expecting huge shifts as a result of that.

Sebastiano, I'm pretty proud actually and comfortable, given the overall state of what I'll call the fixed broadband market of our performance and how we've been growing in that space. It's a big deal. We just hit 40% -- about 40% penetration of our fiber base right now. And if you'd ask me 2 years ago that I think we'd arrive at that level, given the number of households we're adding and building to, I probably wouldn't have said that we'd arrive that quickly. So I think our goal is to just keep operating as effectively as we have been and taking the good growth that's coming our way. And I think you see that reflected in the overall performance of the numbers.

Operator

Frank Louthan of Raymond James.

Frank Garrett Louthan - *Raymond James & Associates, Inc., Research Division - MD of Equity Research*

I want to delve in on the business side. First, can you give us your overall read on the economy and your outlook there? And then secondly, what is sort of the endgame on the Business Wireline side? It continues to kind of decline. Is there a bottom there? And can you give us maybe a split between what's left in that revenue that's voice versus other data services to get an idea of where the weakness might be?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

Yes, Frank. So first of all, look, I don't -- I'm not going to sit here and tell you that I think the shifts in the business segment are economic-driven. I know there's been some discussion around what's happening in business investment and communication services. And I fully expect there are going to be businesses that look around and say, "Gosh, I need to find incremental money to invest in AI." And as we all know how corporations that we're part of work, sometimes it's -- you take from one to invest in another. And I expect we're going to see that happening.

But I think the fundamentals under what's occurring in the business segment are largely technology-driven. I think we've known for a long time that traditional voice had a shelf life. And ultimately, it was going to get replaced with integrated communication services and as-a-service capabilities that run over the top of IP. I think what we saw is, a bit during the pandemic, there was a suppression of change. For whatever reason, people were out of the office. It wasn't a priority. People didn't want to mess around with their communications infrastructure while they were working hard to accommodate a different hybrid work environment.

And now we're kind of seeing that evolution kind of pick up with a degree of steam. There's probably some good business reasons that's occurring, people are rationalizing office space. They're moving things around. They're working differently. They're evaluating the kind of technology they want in place as a result of that. And that's, from my point of view, why we're seeing a little bit of that step-up in that voice transition and what's occurring. I think we're going to try to do some work with you broadly, not just specific to business, but we'll give you some transparency and visibility of what's left in the legacy businesses and what's going on around those things.

As we move through this year, I think we're working on maybe some ways to schedule some of that for you, so you kind of get a sense of what's occurring there. I understand your desire to want to understand it. I think what I would balance that with is, as we stressed multiple times this morning, those things that we're investing in right now, we've got a really good, strong, solid growth business. And those growth businesses are built on 5G and fiber. And business' endgame is really no different. We're shifting to build a company that is good at selling 5G and fiber into business, and selling 5G and fiber in the business, not just at the top end of the market for the Fortune 1000 but across the continuum of the market.

And that's a bit of a transition for AT&T. Because I would say where we made our bread and butter over the last decade, rightly or wrongly, has been at the top end of the market. And so as we shift and generate more revenues and more share out of the mid-portion of the market, we're having to rebuild some muscle and some distribution and the right product mix to attack that. And we can do that. And the endgame is we will

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catch this decline and we'll ultimately catch the decline with connectivity-based services both in fiber and 5G. We're just going through that transition to make that happen. And unfortunately, as you know, some of the historic voice services are really high-margin services. They're being replaced with good margin services but not quite as high.

And it's going to be a little bit painful for a couple of quarters as we move through this transition. But I have ultimate confidence that the AT&T brand plays incredibly well in business. All of our research suggests that. I have very high confidence that when we walk in and we talk to businesses of any size about using AT&T for either their wireless or fixed connectivity, we're high in the consideration set and can win that business. And I have confidence that there is another generation of incremental services that go on top of that connectivity, as I alluded to in my opening remarks, and what we're doing with Dynamic Defense is a good example, which is overlay incremental service that comes on top of the base of transport that allows us to scrub traffic on behalf of the customer to improve their security posture.

I think there's a lot more of those things that can come on in the middle market, given the lack of sophistication, the lack of ability to have full-time staff dedicated to those things. And I think that's just natural for us to extend our capabilities into that space. And I'm long-term bullish that it's the right thing for us to be in both the fixed and the wireless market, given our brand presence, our distribution channel capabilities and how we build products.

Operator

Our last question in queue will come from the line of Walter Piecyk of LightShed.

Walter Paul Piecyk - *LightShed Partners, LLC - Partner & TMT Analyst*

John, I just want to get your kind of refreshed views on the fixed wireless market. If you look at Verizon, they've added 1 percentage point of overall wireless growth using fixed wireless. T-Mobile has added, I think, 160 basis points. We're seeing advertisements for, I guess, I think what you call free air or something like that.

What do you think in terms of the growth opportunity here? And if you were able to get some additional spectrum or maybe even with your existing spectrum, as you've seen the usage from some of your early learnings, can this be as broad of an opportunity for you as it's been for Verizon and T-Mobile?

John T. Stankey - *AT&T Inc. - CEO, President & Director*

I think the short answer to the last part of your question is I don't intend to promote it in the market in the manner that Verizon and T-Mobile are promoting it in the market. And I just -- I sit along the sideline and I observe, I also see them doing some things right now to try to manage the dynamics around those product sets that are reflective of what I believe the ultimate outcome was going to be and what I've been saying for a period of time, which is wireless networks aren't particularly the best place to take the single-family home that streams hours and hours of video a day and try to serve them with a kind of $50 a month product or service.

And I just don't see that as long-term sustainable or healthy growth of returns for the business. And I've been pretty consistent in saying that, and I'm still consistent in saying that. And that's why we're making a choice in our capital allocation to invest more heavily in fiber as the basis of which to make an investment that we think has long runway and a long annuity stream and is a technology that has flexibility to deal with what we know is going to be continuing calls and demands on growth for high-performance networking in homes and businesses.

Now having said that, I've also been very, very clear that there is a place for fixed wireless in our portfolio. And I don't believe my point of view on this has changed in any way, shape or form nor our execution is any different than that. I've said from the start that there are many businesses that do not have the characteristics of single-family homes. And as a result of that, fixed wireless can be a really effective way of meeting their needs and doing so at a value proposition, price and performance that makes sense for them, especially when you start to think about those companies that have a convergence of both fixed and mobility needs. It's a natural in those cases.

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And I'd like to participate in that market aggressively. And I will go after it as aggressively as my competitors and picking up any of those business customers that I can on a national basis. And I think that's a margin-accretive decision within the context of how we're allocating capital between spectrum investments and fiber investments.

I've also said that in the consumer space, there are places where I would apply the technology. I gave a couple of specific examples. We have some places where we have a good copper DSL base that we're in the process of deploying fiber. And in some cases, fixed wireless can give better performance than what our copper network can deliver. And we know that we'll be 12 months, 18 months from fiber deployment, and we may want to hold some customers, offering them a better service. And we'll use it as a bridging or hold strategy for customers that are high value to us. And we'll continue to use that technique where we can.

I've indicated that we will use it as an opportunity for us to turn down footprint. So where I've got small numbers of data customers in place, I need to get them off of fixed infrastructure that I ultimately want to shutter because that allows me to turn down a geography that is a low utilization geography and a low profitable geography on the fixed side. And I can turn out the lights, walk away, take cost out of business. I will do that. And I've also said we have some select markets where our penetration levels in Mobility are low and our spectrum position is high. And we may choose in those markets to do some incremental marketing to do, as you indicated, to buy some incremental growth that we believe has a longer runway.

So that's how the team is operationalizing around this. But in the end, when all those plays are put together, no, I don't think you're going to see us have the same posture that two of our competitors do because our posture is different. We're investing in fiber. And I don't see myself moving into the market just to buy spectrum so that I can change the operating posture I just described to you.

Brett Feldman

All right. Well, thank you, everyone, for joining us. Operator, you can go ahead and close out the call.

Operator

Ladies and gentlemen, that does conclude our conference call for today. On behalf of today's panel, we'd like to thank you for your participation in today's earnings call, and thank you for using our service. Have a wonderful day. You may now disconnect.

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