TITAN CAPITAL MANAGEMENT RESEARCH REPORT FOR: **TCM PRESIDENT'S SCHOLARS**

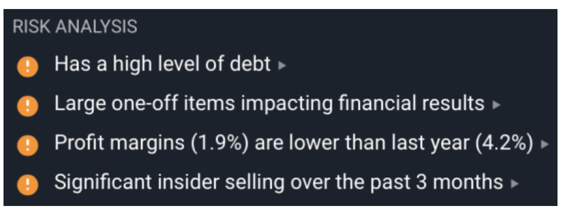
Analyst(s): German Romero | Date: November 12, 2022

COMPANY/TICKER: **T-MOBILE (TMUS)** **Stock** **SELL**

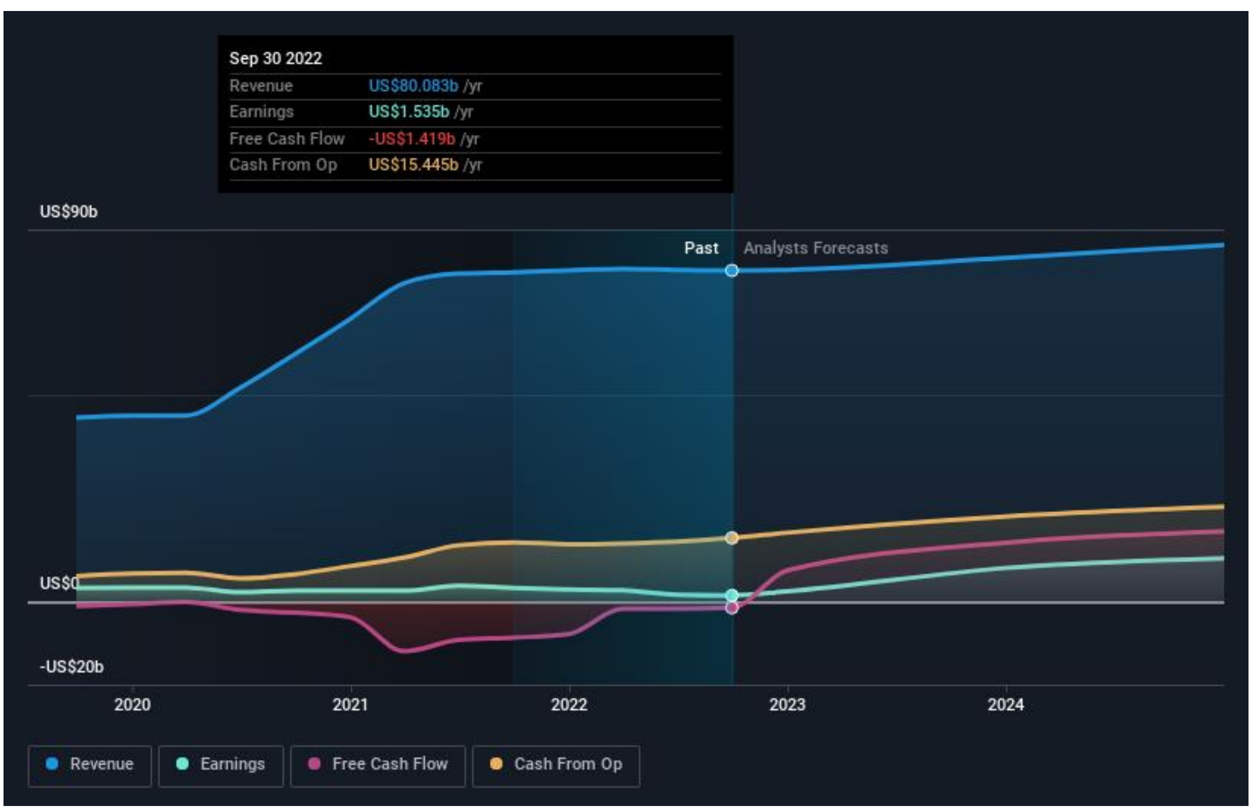
EXECUTIVE SUMMARY

We recommend a SELL rating for T-Mobile (TMUS) because the catalysts for the buy recommendation from April 2021 are played out and the current price is too high relative to its financial risk. T-Mobile has a P/E ratio of 106.2 (current) and 29 (NTM) which brings the President's Scholars portfolio out of compliance. (Currently 35.65 compared to our benchmark's P/E ratio of 20.) Moreover, the stock is trading near its 52-week high which may signal a favorable time to sell.

The company's lower profit margins in Q3 and Q2 of this year relative to last year, continuously increasing restructuring expenses, and nearly $48 million of insider selling since February may indicate growth has tapped out, at least for the intermediate term. T-Mobile also does not offer a dividend, while its two largest competitors offer attractive yields. This lack of dividend is undesirable given the President's Scholars investment objective to fund at least one scholarship each year.



Key uncertainties include earnings stabilizing in the first half of 2023 and the possibility of such post-synergy earnings rising substantially and quickly. This could open opportunities to increase shareholder benefits by starting to pay a dividend or buying back shares.



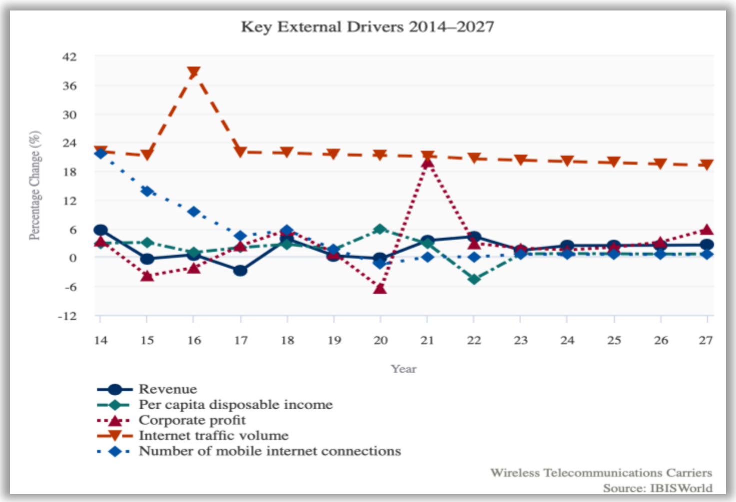
Source: Simply Wall St

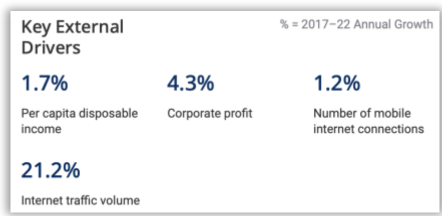
COMPANY OVERVIEW

T-Mobile is a subsidiary of Deutsche Telekom AG that provides wireless telecommunications services. It offers data, messaging, and voice services on a pre-paid, post-paid, and wholesale basis. The company also sells devices, such as cellphones, tablets, and other wireless devices, and their accessories. In 2020, T-Mobile acquired Sprint and subsequently became the second largest wireless carrier behind Verizon. T-Mobile is regarded as a growth company within the industry. This is congruent with its large P/E ratio and lack of dividend yield—characteristics that do not fall in line with President's Scholars compliance and investment objective.

INDUSTRY OVERVIEW *(IBISWorld 'Industry at a Glance' September 2022)*

IBISWorld characterizes the industry as mature, highly competitive, and requiring much capital. Households (66.2% of industry revenue) are disconnecting their landlines in lieu of mobile connectivity. Wireless data services have become essential. The shift to fifth generation (5G) allows mobile carriers to reposition themselves with their customers. Yet, there is no clearly observable upside to 5G connectivity without the proper bandwidth infrastructure. Verizon and AT&T have acquired such infrastructure via their acquisition of C-band spectrum waves. T-Mobile is not expected to reach C-band spectrum until 2024. They opted to acquire Sprint in 2020 to stay competitive.





IBIS World reports that the key drivers of the U.S. telecommunications industry will plateau in the next five years. Three out of the four key drivers will gradually decrease over the same period. Per capita disposable income growth will stay under 1%. This inevitably affects the growth of mobile internet connections, which will also stay under 1%. The growth of internet traffic will remain around 19%.

CATALYSTS

Played-Out Factors

The T-Mobile buy report from April 2021 included the following catalysts as benefits. We believe these no longer play a role as competitive advantages.

<u>T-Mobile's 5G "advantage"</u>

- In 2021, mid-band spectrum put T-Mobile ahead of the game in terms of 5G, but the forecasted two-year advantage stated in the buy report is no longer existent with Verizon's and AT&T's acquisition of C-Brand spectrum
- Verizon 5G speeds are on par with T-Mobile's in certain areas, which can be observed with the "UW" (ultra-wide) indicator next to service bars on phones
- T-Mobile may be on track to nationwide mid-band coverage by the end 2021, but competitors are keeping up closely

<u>Sprint acquisition creates threats too</u>

- T-Mobile not only acquired Sprint's infrastructure and customer base but also its debt
  - About 52% of T-Mobile's debt is inherited from Sprint
  - T-Mobile almost tripled its total debt after acquiring Sprint
- With $2.2 billion in debt maturing in November 2022 and a net loss of $108 million recorded in Q2 2022, T-Mobile presents potential credit risk
  - This loss may also play a big role in why P/E ratio spiked while its stock price fell recently
- A driver of the net loss is restructuring expenses derived from decommissioning Sprint operations

Sell Drivers

<u>T-Mobile's P/E ratio brings us out of compliance</u>

- Making up 4.1% of the equity segment of the President's Scholars portfolio, T-Mobile brings us out of compliance with its P/E ratio of 106.2
- We strive to keep our P/E ratio, currently around 35.65, at or below our benchmark, currently around 20.20

<u>Synergies with Sprint may have been reached</u>

- T-Mobile is expected to have finished decommissioning Sprint's legacy network by Q3 2022
  - Profit margin has fallen from 4.9 and 4.2 in Q2 and Q3 2021 to 2.1 and 1.9 in Q2 and Q3 2022
  - One major reason for this is the continuously increasing one-time expenses up 6.5% since last quarter and over 106% since Q3 2021
- Nearly $48 million have been sold since February and over $28 million since August by management
  - This demonstrates a lack of confidence from the leaders of T-Mobile in future growth

RELATIVE VALUATION

Unattractive Financial Comparison

1. VALUATION Factors (1- best, 6 - worst: low is better except for FCF/Share)

									---- RANK ----						
Company Name	P/E (NTM)	P/B (NTM)	EV/Sales (NTM)	EV/ EBITDA	BV/Share (NTM)	FCF/Share (NTM)	Price	Price Target	P/E Rank	P/B Rank	EV/Sales	EV/ EBITDA	FCF/Share (NTM)	Total	*Evaluation*
T-Mobile US	28.69	2.45	3.06	11.19	58.33	9.76	$143.02	$172.69	5	4	5	5	2	21	*High Price*
Verizon Communications	8.28	1.83	2.36	7.22	23.62	4.38	$43.25	$50.89	2	3	3	3	3	14	*Fair Price*
Comcast A	9.77	1.67	2.05	7.05	22.10	3.63	$36.80	$47.60	3	2	2	2	4	13	*Fair Price*
AT&T	7.11	0.95	2.03	6.51	18.79	2.20	$17.89	$21.39	1	1	1	1	5	9	*Low Price*
Charter Communications A	11.86	7.73	3.05	8.02	55.09	44.77	$425.77	$549.63	4	5	4	4	1	18	*High Price*
														0	*Low Price*
Average	*13.14*	*2.93*	*2.51*	*8.00*	*35.58*	*12.95*	*$ 133.35*	*$ 168.44*							

<u>Valuation</u>

- T-Mobile's P/E ratio of 106.2 is very much over our President's Scholars threshold of about 20. Ideally earnings should catch up to price to bring P/E into compliance, but IBIS World projects industry revenue growth of only 2.3% over the next five years
- There exists a large discrepancy between BV/Share (55.32) and current price ($136.77) which raises red flags regarding valuation

2. PROFITABILITY Factors (1 - best, 6 - worst: high is better except Total Debt)																
									RANK							
Company Name	Sales Growth (3 yr.)	Gross Margin (NTM)	EBIT Margin (NTM)	ROIC (NTM)	ROE (NTM)	Sales	EBITDA	Total Debt	Sales Growth	Gross Margin	EBIT Margin	ROIC	ROE	Total	Evaluation
T-Mobile US	81.22	56.47	14.18	1.01	8.55	$80,230	$25,764	$112,076	1	5	5	5	5	21	Less Profitable
Verizon Communications	2.47	64.30	22.94	8.55	22.13	$134,325	$49,239	$175,566	4	3	2	1	2	12	Profitable
Comcast A	17.32	68.80	19.25	7.32	17.04	$121,660	$36,282	$98,713	3	1	3	2	3	12	Profitable
AT&T	-19.03	67.41	18.22	6.65	13.39	$148,628	$46,022	$158,791	5	2	4	3	4	18	Less Profitable
Charter Communications A	18.98	64.04	23.37	5.19	65.17	$53,156	$20,940	$96,282	2	4	1	4	1	12	Profitable
														0	More Profitable
Average	*20.19*	*64.20*	*19.59*	*5.74*	*25.26*	*$107,600*	*$35,649*	*$128,286*	*All numbers shown in millions except per share items*						

Profitability

- T-Mobile has healthy NTM gross and EBIT margins, but they are significantly lower than its main competitors implying that competitors have more control over their expenses
- The company severely lacks in its NTM ROIC (1.01) and ROE (8.55) compared to its peers, which means investors can do better things with their money

3. LIQUIDITY, LEVERAGE, YIELD (1 - best, 6 - worst: high is better for current ratio, EBITDA/Int. Exp, and yield; low is better for debt ratios and beta)																
									RANK							
Company Name	Curr Ratio	EBITDA / Int. Exp	Net Debt / EBITDA	LT Debt/ Ttl Capital	Dividend Yield	FCF Yield	Beta (3 Year)	Diluted Shares	Curr Ratio	EBITDA / Int. Exp	Net Debt / EBITDA	LT Debt/ Capital	Dividend Yield	FCF Yield	Total	Evaluation
T-Mobile US	0.85	7.84	4.23	57.42	0.00	4.78	0.73	1,253.93	2	3	4	3	4	5	21	More Risk
Verizon Communications	0.71	15.83	3.50	60.70	4.88	8.93	0.32	4,202.00	3	1	3	4	2	2	15	Avg. Risk
Comcast A	0.88	9.06	2.53	50.82	1.99	8.53	0.74	4,482.00	1	2	1	1	3	3	11	Avg. Risk
AT&T	0.52	7.03	3.36	53.70	8.46	14.36	0.65	7,611.00	4	4	2	2	1	1	14	Avg. Risk
Charter Communications A	0.33	4.96	4.57	88.99	0.00	6.84	0.81	167.09	5	5	5	5	4	4	28	More Risk
															0	Less Risk
Average	*0.66*	*8.94*	*3.64*	*62.32*	*3.06*	*8.69*	*0.65*	*3543.20*	*All numbers shown in millions except per share items*							

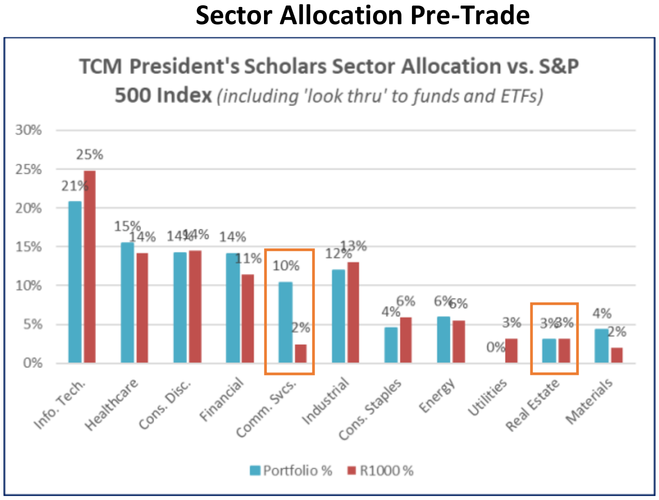
Liquidity

- Over a third of T-Mobile's debt matures in the next five years, so Net Debt/EBITDA ratio of 4.23 is a concern
- T-Mobile's FCF yield of 4.78 trails all its competitors, plus the stock does not pay a dividend

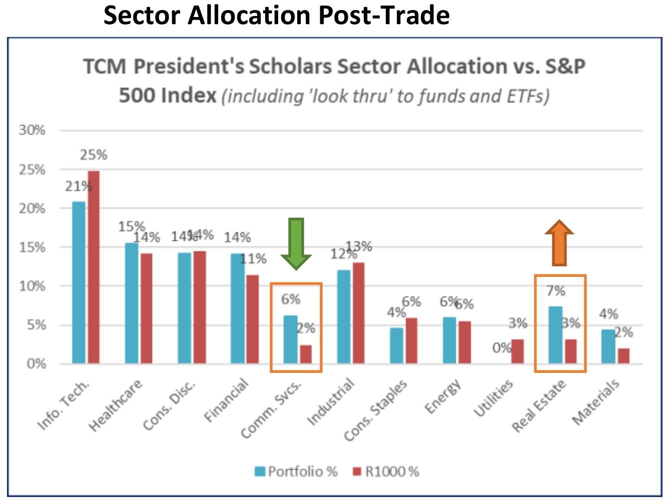
PORTFOLIO IMPACT AND SUMMARY

We recommend selling the entire 4% equity position in T-Mobile. T-Mobile is not a good fit for the President's Scholars portfolio because of its uncertain future growth, high valuation, and lack of dividend yield. Proceeds from the sale would be used to fund a proposed purchase of Public Storage (PSA). This trade would decrease our significant overweight to Communication Services to add to Real Estate at much more attractive valuations.

Sector Allocation Pre-Trade



Sector Allocation Post-Trade



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T-Mobile Coverage Map

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Verizon Coverage Map

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