

Lumen Technologies Inc.

4Q23 Wrap: Expecting to put balance sheet issues behind it and focus on operations

Reiterate Rating: UNDERPERFORM | PO: 1.00 USD | Price: 1.35 USD

TSA on track to close in 1Q and included in FY'24 guide

Lumen Technologies Inc.'s (LUMN) amended TSA with participating bondholders is on track to close in 1Q24. The amended TSA will address \$9.0bn of debt including ~\$7bn of debt maturing through 2027, while also providing \$1.3bn of new issue bonds and a \$1.0bn revolving credit facility. At a high level, LUMN will extend maturities to 2029 at the expense of higher interest payments, worsened FCF, and higher leverage. In all, it appears sufficient to address the looming 2027 debt wall but deepens the hole from which the company must climb to create equity value. Management confirmed that its FY24 interest expense (\$1.3bn at the mid-point) guide includes \$125mn-\$225mn incremental cash interest subsequent to closing the TSA net of using \$1.8bn in EMEA sale proceeds to pay down debt asap. In our view, management would need to revisit its financing arrangements following the close of this TSA and address the complaints of "non-participating" bondholders. Any future transactions will likely come at a similarly high cost that will further eat into the equity opportunity. We reiterate our Underperform rating and \$1.00 PO as LUMN restructures its balance sheet while facing steep cash flow costs and continued pressure on business operations.

2024 guidance in-line with expectations

LUMN guided to \$100-\$300mn of FCF in '24E. The company expects to offset declining EBITDA trends and higher interest expense with 1) lower fiber capex (\$2.7-\$2.9bn), 2) a full year impact of the headcount reduction (\$300mn/yr distributed evenly across quarters), and 3) \$700mn of cash tax refunds anticipated in 2024. We update our estimates following 4Q results: see [Exhibit 1](#).

Mixed but still net negative revenue trends

In Enterprise, the company expects continued revenue pressure on legacy wireline products and services. Management expects improving Public Sector segment sales to revenue conversion (excluding the relatively substantial 'other' revenue) will lead to sequential improvement this year making it the 'lead dog' in the return-to-growth narrative. In Mass Markets, LUMN is maintaining its 500k fiber enablement target for 2024 and the team is expected to focus on sales and marketing initiatives to grow its Quantum Fiber brand.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	(1.54)	(10.47)	(0.12)	(0.33)	(0.44)
EPS Change (YoY)	NM	-579.9%	98.9%	-175.0%	-33.3%
Consensus EPS (Bloomberg)			(0.05)	(0.03)	(0.07)
DPS	0.75	0	0	0	0
Valuation (Dec)					
Dividend Yield	55.6%	0%	0%	0%	0%
EV / EBITDA*	6.0x	NM	4.9x	5.2x	5.3x
Free Cash Flow Yield*	125.2%	-68.5%	7.9%	-29.9%	-34.9%

* For full definitions of *IQmethod*SM measures, see page 5.

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Refer to important disclosures on page 6 to 8. Analyst Certification on page 4. Price Objective Basis/Risk on page 4.

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Timestamp: 07 February 2024 11:04AM EST

07 February 2024

Equity

Key Changes

(US\$)	Previous	Current
2024E Rev (m)	13,276.7	13,091.2
2025E Rev (m)	13,301.7	12,490.6
2026E Rev (m)	NA	12,153.3
2024E EPS	-0.34	-0.12
2025E EPS	-0.39	-0.33
2026E EPS	NA	-0.44

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Stock Data

Price	1.35 USD
Price Objective	1.00 USD
Date Established	10-Oct-2023
Investment Opinion	C-3-9
52-Week Range	0.78 USD - 5.15 USD
Mrkt Val (mn) / Shares Out (mn)	1,373 USD / 1,017.0
Free Float	98.0%
Average Daily Value (mn)	20.23 USD
BofA Ticker / Exchange	LUMN / NYS
Bloomberg / Reuters	LUMN US / LUMN.N
ROE (2024E)	-52.9%
Net Dbt to Eqty (Dec-2023A)	NA
ESGMeter TM	High

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TSA = transaction support agreement

iQprofileSM Lumen Technologies Inc.

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	0.2%	-24.0%	3.0%	2.4%	2.1%
Return on Equity	-13.5%	-189.8%	-52.9%	NM	NM
Operating Margin	0.6%	8.4%	9.4%	8.0%	7.0%
Free Cash Flow	1,719	(940)	108	(410)	(479)

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	NM	NM	NM	NM	NM
Asset Replacement Ratio	0.9x	1.0x	1.0x	0.9x	0.9x
Tax Rate	NM	NM	26.0%	26.0%	26.0%
Net Debt-to-Equity Ratio	185.1%	NM	NM	NM	NM
Interest Cover	0.1x	-8.0x	0.9x	0.7x	0.6x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	17,484	14,557	13,091	12,491	12,153
% Change	-11.2%	-16.7%	-10.1%	-4.6%	-2.7%
Gross Profit	9,616	7,413	6,840	6,526	6,350
% Change	-14.1%	-22.9%	-7.7%	-4.6%	-2.7%
EBITDA	3,340	(17,413)	4,074	3,903	3,798
% Change	-59.8%	NM	NM	-4.2%	-2.7%
Net Interest & Other Income	(1,086)	(653)	(1,387)	(1,439)	(1,439)
Net Income (Adjusted)	(1,506)	(10,298)	(119)	(328)	(435)
% Change	NM	-583.6%	98.8%	-176.8%	-32.5%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	(1,542)	(10,298)	(119)	(328)	(435)
Depreciation & Amortization	3,239	2,985	2,847	2,908	2,947
Change in Working Capital	559	(1,498)	(117)	(196)	(206)
Deferred Taxation Charge	(1,230)	8	232	(226)	(300)
Other Adjustments, Net	3,709	10,963	79	118	128
Capital Expenditure	(3,016)	(3,100)	(2,815)	(2,685)	(2,613)
Free Cash Flow	1,719	-940	108	-410	-479
% Change	-52.3%	NM	NM	NM	-16.9%
Share / Issue Repurchase	(200)	0	0	0	0
Cost of Dividends Paid	(780)	(11)	0	0	0
Change in Debt	(8,293)	15	1,250	(468)	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	1,251	2,234	3,382	2,504	2,024
Trade Receivables	1,477	1,318	1,190	1,143	1,110
Other Current Assets	2,692	1,223	1,223	1,223	1,223
Property, Plant & Equipment	19,166	19,758	19,726	19,503	19,169
Other Non-Current Assets	20,995	9,485	9,485	9,485	9,485
Total Assets	45,581	34,018	35,006	33,858	33,012
Short-Term Debt	1,503	1,503	1,503	1,503	1,503
Other Current Liabilities	4,649	3,373	3,025	2,923	2,854
Long-Term Debt	19,069	18,485	18,959	18,491	18,491
Other Non-Current Liabilities	9,923	10,236	11,488	11,227	10,905
Total Liabilities	35,144	33,597	34,974	34,144	33,753
Total Equity	10,437	417	32	(286)	(741)
Total Equity & Liabilities	45,581	34,014	35,006	33,858	33,012

* For full definitions of iQmethodSM measures, see page 5.

Company Sector

Telecom Services-Wireline

Company Description

Lumen Technologies is the nation's third-largest telephone company and the largest rural exchange provider serving residential, enterprise, and wholesale customers. It is the product of the acquisition of Embarq by CenturyTel in 2008, Qwest Communications in 2011, and Level 3 Communications in 2017. Embarq is Sprint's former wireline unit. Lumen Technologies changed its name from CenturyLink in 2020.

Investment Rationale

We believe LUMN is structurally challenged with high capital intensity, few growth opportunities, and declining cash flow. While Lumen shifts focus to fiber investment and growth, the remaining pieces of the business have a weak outlook.

Stock Data

Average Daily Volume 14,986,407

Quarterly Earnings Estimates

	2023	2024
Q1	0.52A	0.01E
Q2	-8.88A	-0.04E
Q3	-0.08A	-0.04E
Q4	-2.03A	-0.06E

Estimate changes

Exhibit 1: Our new 1Q24 and FY-24 estimates table

We update our estimates following 4Q results

	New	Old	%	New	Old	
	1Q24	1Q24	change	2024E	2024E	% chg
Total Revenue	3,361	3,345	0.5%	13,091	13,277	-1.4%
Adj. EBITDA	1,039	1,085	-4.2%	4,126	4,311	-4.3%
EBITDA Margin	30.9%	32.4%	-4.6%	31.5%	32.5%	-2.9%
Capex	723	652	10.8%	2,815	2,589	8.7%
FCF (LUMN definition)	19	728	-97.4%	108	577	-81.3%
Large Enterprise	986	989	-0.3%	3,754	3,954	-5.1%
Mid-Market Enterprise	483	487	-0.7%	1,905	1,938	-1.7%
Public Sector	442	429	3.1%	1,742	1,755	-0.7%
Wholesale	736	726	1.3%	2,906	2,838	2.4%
Business Segment Total	2,647	2,631	0.6%	10,307	10,486	-1.7%
Mass Market Segment Total	714	714	-0.1%	2,784	2,791	-0.2%

Source: BofA Global Research

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Price objective basis & risk

Lumen Technologies Inc. (LUMN)

We believe LUMN should be trading at a discount to its peers. Our price objective is \$1.00/share based on a 4.7x 2024E EV/EBITDA multiple. We view 4.7x as appropriate given Lumen has high capital intensity, few growth opportunities, and declining cash flow.

Downside risks to our PO are increased competition from wireless, cable, and enterprise service providers and LVLT deal integration. Upside risks are faster-than-expected revenue, EBITDA, and free cash flow growth.

Analyst Certification

I, David W. Barden, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North America - Telecom Services Coverage Cluster

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	Verizon Communications Inc.	VZ	VZ US	David W. Barden, CFA
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	Lumen Technologies Inc.	LUMN	LUMN US	David W. Barden, CFA
	Uniti Group Inc	UNIT	UNIT US	David W. Barden, CFA

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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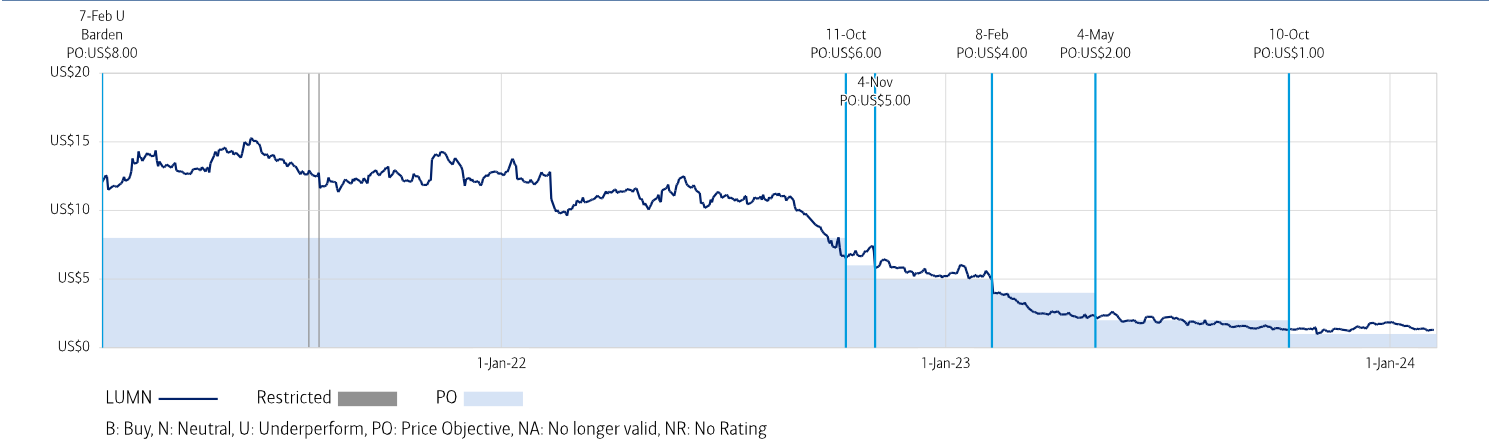
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Lumen Technologies (LUMN) Price Chart



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Equity Investment Rating Distribution: Telecommunications Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	57	51.82%	Buy	43	75.44%
Hold	27	24.55%	Hold	17	62.96%
Sell	26	23.64%	Sell	12	46.15%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
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Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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