The Sunday Brief: Choppy Waters? (3Q 2020 Earnings Review – Part 2)
November 1, 2020

November greetings from Davidson/ Lake Norman, where we endured the remnants of Hurricane Zeta this week. The picture summarizes the current political climate in the Tar Heel state as we are bombarded with calls, texts, and TV ads. Thankfully, calmer waters are ahead starting Wednesday as we return to "normalcy."

This week's Brief focuses on earnings, with Comcast and Charter providing an upbeat broadband, TV and wireless assessment. Prior to that, we'll quickly recap the Fab 5 earnings picture, discuss T-Mobile's un-carrier TV announcement and analyze backorder volumes for the iPhone 12 for each of the "Big 3" carriers.

Before diving into market cap changes, a note of thanks for each referral and comment. This has been the best month for website traffic and newsletter signups since 2016. We are contemplating a podcast (in 2021) and may ask a few of you to be guests. Despite the pandemic, this has been a banner year for the Sunday Brief – thanks again!

The Week That Was

	Ticker	Shares (millions)			Stock Price		Equity Value ($B)		Annual Change		2020 YTD PERFORMANCE		
Stock Name	**Symbol**	**Dec-18**	**Dec-19**	**Jun-20**	**Dec-18**	**Dec-19**	**Dec-18**	**Dec-19**	**Amount**	**Percent**	**30-Oct**	**% change**	**Value Gained/ Lost ($B)**
Apple	AAPL	18,861.1	17,493.9	17,419.2	$ 38.85	$ 73.41	$ 733	$ 1,284	$ 551	75%	$ 108.86	48%	$ 617
Alphabet (Google)	GOOG	695.2	689.7	687.0	$ 1,035.61	$ 1,337.62	$ 720	$ 923	$ 203	28%	$1,621.01	21%	$ 195
Microsoft	MSFT	7,672.2	7,665.0	7,650.0	$ 100.09	$ 157.70	$ 768	$ 1,209	$ 441	57%	$ 202.47	28%	$ 342
Amazon	AMZN	491.2	497.8	509.0	$ 1,501.97	$ 1,847.84	$ 738	$ 920	$ 182	25%	$3,036.15	64%	$ 605
Facebook	FB	2,854.0	2,850.5	2,879.0	$ 131.09	$ 205.25	$ 374	$ 585	$ 211	56%	$ 263.11	28%	$ 167
Totals	**Totals**						**$ 3,333**	**$ 4,921**	**$ 1,588**	**48%**			**$ 1,926**

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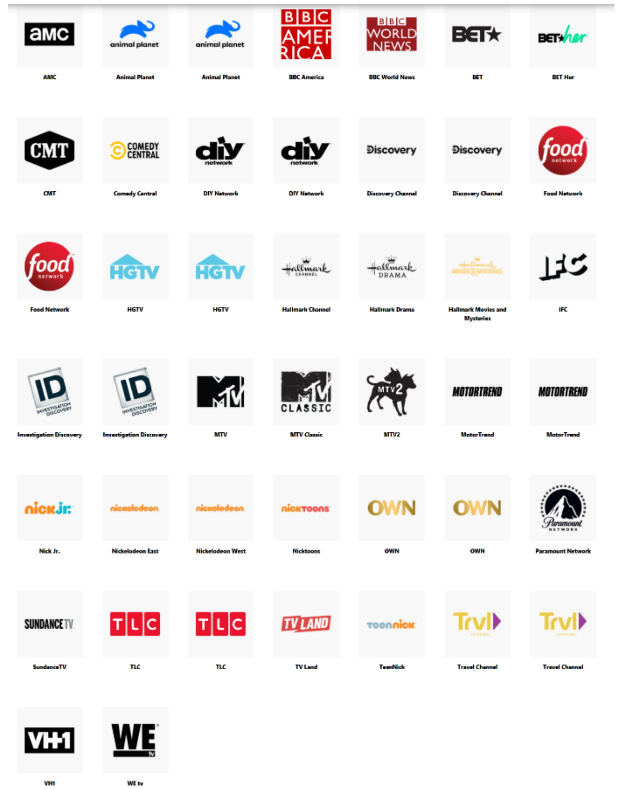
AT&T	T	7,285.0	7,170.0	7,125.0	$ 26.50	$ 38.56	$ 193	$ 276	$ 83	43%	$ 27.02	-30%	$ (82)
Verizon	VZ	4,130.0	4,140.0	4,141.0	$ 53.38	$ 60.77	$ 220	$ 252	$ 31	14%	$ 56.99	-6%	$ (16)
T-Mobile	TMUS	850.2	855.6	1,236.5	$ 63.61	$ 78.42	$ 54	$ 67	$ 13	24%	$ 109.57	40%	$ 39
Comcast	CMCSA	4,517.0	4,607.0	4,607.0	$ 33.39	$ 44.76	$ 151	$ 206	$ 55	37%	$ 42.24	-6%	$ (12)
Charter	CHTR	225.3	214.8	211.1	$ 284.97	$ 485.08	$ 64	$ 104	$ 40	62%	$ 603.82	24%	$ 25
Totals	**Totals**						**$ 683**	**$ 906**	**$ 223**	**33%**			**$ (46)**

"Fear, uncertainty and doubt against the backdrop of solid earnings" is a pretty good summary of the week for each of the seven stocks that announced quarterly earnings this week. High fliers like Amazon (-$85 billion weekly market cap loss), Microsoft (-$106 billion), and Apple (-$108 billion) had their year-to-date gains clipped (Amazon +64% YTD, Microsoft +28%, Apple +48%) but still are each valued well over $1 trillion. Overall, the Fab 5 lost $375 billion in market cap this past week but is still $338 billion ahead of last year's gains.



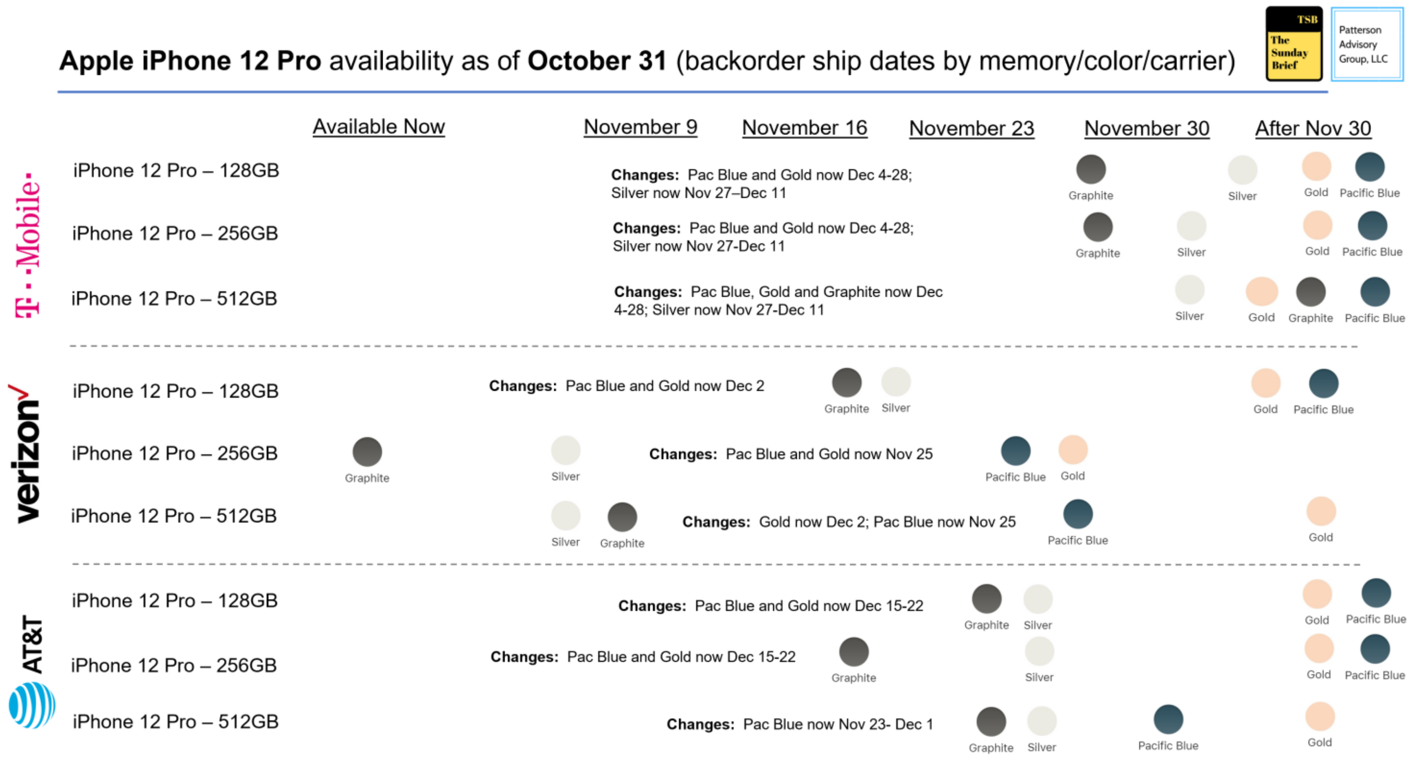
The Telco Top 5 also had a tough week, as a slight gain for Charter (+$2 billion) offset by losses in T-Mobile (-$3 billion), Verizon (-$4 billion), AT&T (-$5 billion), and Comcast (-$13 billion). The $24 billion in market cap losses was the largest weekly loss since June. T-Mobile announces earnings next Thursday and is expected to announce solid phone net additions even as they are transitioning the Sprint base.

Speaking of T-Mobile, they announced that their TVision TV product will be available for sale starting November 1 (announcement here). Our attention was immediately drawn to the $10/ mo. product called TVision Vibe. Nearby is a collection of the 44 channels included in this plan. TVision Vibe + local broadcast channels through a traditional TV antenna (see Walmart example here with a 55+ mile reach for under $30) will be an effective alternative to traditional cable TV to a certain subset of value-seeking customers. If the concept of setting up an indoor antenna is too daunting, T-Mobile's $40 TVision Live has a decent array of channels (although it omits a lot of channels included in the VIBE lineup). There is a great lineup comparison from CNET here - embedded in that article is an informative 9+ minute interview of T-Mobile's CEO, Mike Sievert.

In addition to the channel lineups, T-Mobile's partnership with Apple TV and Apple+ throws a wrench into the Verizon bundling strategy (six months of Apple Music is included for free with all Verizon plans but Big Red partnered with YouTube TV for their over-the-top offering). Customers who sign up for TVision Live TV+ or Live Zone packages by December 31 will get Apple TV+ free for a year and have the option to add Apple TV 4K for just $99. Apple rarely if ever allows a third party (let alone a wireless carrier) to sell hardware at a discount. For Apple TV+ fans (or owners of earlier versions of the Apple TV product), this promotion could drive switching to or adoption of Apple TV (although new iPhone 12 purchasers will already get a year of Apple TV+ included with their purchase).

Not surprisingly, T-Mobile is only making this product available to T-Mobile postpaid customers at the $10 and $40 price point. Our guess is that this has a marginal/ modest impact on 4Q 2020 switching decisions (perhaps from cable). What will be most interesting is when T-Mobile bundles their Home Internet product, wireless, and TVision on a single bill. Our understanding is that's a few quarters away. **Bottom line:** Watch for management's comments on the sale of the $10/ month product through the end of the year. Vibe is highly attractive as a stand-alone product, and LIVE might result in some downgrades from YouTube TV and Hulu Live.

This week was active for T-Mobile on another front: iPhone 12 Pro sales. For those of you who have not been following the story closely, Apple released two of four total products in October (iPhone 12 and iPhone 12 Pro), with the remaining two (iPhone Mini and iPhone 12 Pro Max) to be available for pre-order starting next Friday (Nov 7). While there has been a lot of handwringing over Apple's earnings call, our channel checks (and those of Wave7) have indicated that the iPhone 12 Pro is selling quite well. Here's the backlog chart for the iPhone 12 Pro:



As a reminder, the Verizon and T-Mobile dates are "ship by" while AT&T is "delivery by." We saw this same backlog last year by T-Mobile with the iPhone 11 and iPhone Pro sales (and last year's figures did not include Sprint). T-Mobile is sold out of the iPhone 12 Pro for at least the next two weeks and perhaps longer. Either their supply chain miscalculated demand (highly unlikely), or Apple had to ration initial supplies of the iPhone 12 Pro (probable), or T-Mobile, with their standard trade-in promotion, is using the iPhone 12 Pro as a share-taking event (highly probable). It's likely a combination of all three, but Apple's iPhone Pro sales are not due to lack of demand, at least from T-Mobile's and AT&T's perspectives (note the availability of certain colors at AT&T – a seven week backlog).

It's important to note that this is all occurring prior to the launch of the iPhone 12 Pro Max next week (we think the Mini will compete more heavily with the iPhone 12 and iPhone SE). If the analysts are correct, that demand wave will be more significant for Verizon and AT&T.

Bottom line: If the holiday spending forecasts are to be believed (Visa forecasting 7.8% annual increase – best since 1999), there is going to be robust consumer spending over the next 90 days. That is very good news for all wireless carriers, and, from initial iPhone 12 Pro demand, especially good for AT&T and T-Mobile. (Note: PDFs of both iPhone 12 Pro and iPhone 12 backlog are available on the Sunday Brief website here. Just click on this article and PDF downloads are at the beginning of the article).

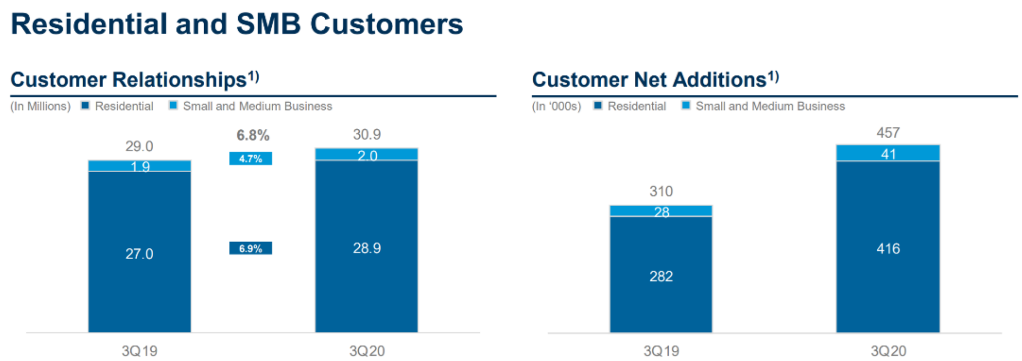
Choppy Waters? (3Q 2020 Earnings Review – Part 2)

We have listened to both the Comcast and Charter conference calls, digested each operating and financial metric, and reviewed others' analyses of their earnings. Our conclusion is that cable remains the dominant provider of broadband service, and, despite potential threats from Verizon (Ultra Wideband 5G), T-Mobile (4G LTE Home Internet), and AT&T (promised acceleration of home fiber deployments), the cable HSI moat is very deep.

The question in our minds is whether a single play is sufficient to produce sustainable residential profits. If the answer to that question is "no" (jury is out in our view), then what's the next Revenue Generating Unit (RGU) to produce incremental profitability? Is it aggregation (Comcast Flex), mobile, or something completely different (e.g., a cable-led broadband gaming effort, perhaps with Sony or Microsoft)? For the reminder of this Brief, we'll look at Comcast and Charter results through this lens of new growth.

Broadband results were outstanding for each of the cable leaders. Comcast (full results here) added 633K net new High Speed Internet customers in 3Q (97%+ of net new adds were residential), reaching a penetration of 50.6%. This is the first time that Comcast has passed the 50% mark in their history. In the first nine months of 2019, Comcast added a respectable 963K customers; that figure is 1.43 million for the first nine months of 2020 (49% higher).

Charter had similarly strong results (here and in nearby chart), adding 537K High Speed Internet RGUs in the quarter (92% residential). Penetration is now approximately 55% (28.633 million RGUs/ 53.022 million passings). Over the last nine months, Charter has added more than 1.96 million net new HSI RGUs, more than 80% higher than the same period in 2019. For context, Verizon added 144K FiOS residential and small business customers in 3Q and 214K in the first nine months of the year. AT&T grew a more respectable 357K fiber subscribers, although their total broadband net additions for the year is negative (translation: AT&T did a good job of migrating current customers, but not so well enticing current cable customers to switch, even with aggressive first year pricing of a fiber+TV bundle).



Residential Net Additions / (Losses)

(In '000s)

	3Q19	3Q20	Y/Y Change
Internet	351	**494**	143
Video	(77)	**53**	130
Voice	(213)	**(63)**	150
Mobile Lines	275	**348**	73

SMB Net Additions

(In '000s)

	3Q19	3Q20	Y/Y Change
Internet	29	**43**	14
Video	2	**14**	12
Voice	23	**38**	15
Mobile Lines	1	**15**	14

As we have stated in many Briefs, Verizon and AT&T are much better at defending an incumbent position than challenging other incumbents. Both have had the potential to bundle wireless with broadband to grow market share, largely to no avail. When cable begins to bundle wireless with broadband (an inevitability in our view, perhaps as early as 2021), won't that dampen Verizon and AT&T's addressable market? **Bottom line:** Charter and Comcast have a dominant position in one of the most important residential revenue streams – home and small business broadband.

Within this growth, however, is a troubling trend – single play exposure. Nearly 40% of Comcast's base is Internet only; the corresponding figure is worse at Charter – 45.7% of their residential total customer relationships exclude video (up from 41.8% in 3Q 2019 and 45.1% in 2Q 2020).

What reduces that exposure? According to Charter, it's likely their mobile product. Here's CFO Chris Winfrey's response to a question on mobile from Jonathan Chaplin at New Street:

> **Chaplin:** On EBITDA growth, the contribution from wireless this quarter was awesome. And I assume that just continues …the losses continue to recede and that will be a propellant for EBITDA next year as well. Do you have a sense of what that could contribute to year-over-year growth for EBITDA next year?
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> **Winfrey:** …You can look at it a few different ways. You can take a look at our losses per mobile line, which is doing very well. You can think about it in terms of what I said before: once we got to 2 million lines, which we crossed over inside this quarter, that it's now an incrementally positive business, but for the subscriber acquisition cost. So, it's already EBITDA positive if we decided to stop growing, which of course, we won't do.
>
> …it's going to continue to get better. But, the amount that it continues to get better in terms of its contribution to our EBITDA performance really depends on the growth rate of wireless and that subscriber acquisition cost.

> The faster you grow, the more you're going to spend. And we're going to try to grow as fast as we can. So, it depends on growth.
>
> **Tom Rutledge (Charter's CEO):** The other quick way to think about mobile is, yes, it's EBITDA positive going forward, and as it's currently priced. But, if you grow mobile rapidly as we are, you'll grow your broadband rapidly too.

Today, Charter has about 2% market share in wireless, and they have 55% penetration in High Speed Internet. The opportunity clearly appears to be on the shoulders of the mobile unit.

Comcast takes a different approach to growth, opting for a broader-based set of aggregation and platform streaming options. Their Flex (or Sky Q) aggregation solution is great for Xfinity Internet subscribers, but legacy users of certain subscription services (e.g., YouTube TV, Sling, others) will be disappointed. The Flex service is included in the Xfinity Internet monthly recurring charge, although specific additional subscriptions could carry a monthly fee. We clearly understand the need for tightly coupled content relationships and Comcast has a very strong product.

On top of providing Flex to Xfinity customers in their service area, Comcast is aggressively marketing a white-labeled version of Flex for wholesale consumption. Comcast's CEO mentioned this initiative on the earnings call (transcript here):

> "The goal of our common tech stack is to build once and deploy as many times in as many markets and in as many ways as possible on our network or through wholesale distribution. We've already experienced great success with our current X1 syndication model. White labeling our software and technology gives us a significant revenue stream that boasts healthy margins and even more important, more scale for our platform. We look forward to expanding this expertise to other distributors and believe that an even larger nationwide and potentially international syndication model will create new opportunities in this rapidly changing ecosystem that will create value for our company and our shareholders."

We think that Comcast's approach to be one of a few global streaming platforms is an extremely good way to create shareholder value (as evidenced by Roku's $25 billion market cap). Cable companies who currently license the X1 platform (Rogers, Shaw, Cox and others) are either currently using the Flex platform or have shown interest. Wide syndication of the platform would then allow it to be included in smart TVs (something we discussed in conjunction with Comcast 2Q 2020 earnings).

Then there is Peacock with 22 million new subscribers in less than three months. We don't have enough time to discuss the value of Peacock (probably will require an entire Brief), but a deep library coupled with the 2021 Olympics and time-shifted "recent" NBC programming sets up Peacock as a potential winner in the streaming wars. Peacock's success will depend on its ability to reach a critical mass of 50 million+ monthly active streamers and to grow time on platform. Comcast's executives indicated that they had work to do in this area, but acknowledged that their fast start would not have been possible without Flex.

Bottom line: Comcast and Charter face many of the same headwinds: Video cord-cutting, slower (if not negative) high-margin home phone disconnections, small business pressure across all products (but especially voice and video) as the economy recovers, and retransmission/ programming negotiation challenges. Under these choppy waters, however, there are additional sources of growth, including mobile and advertising, as economic conditions improve (we will review more about cable's mobile opportunity with T-Mobile earnings next Sunday). Despite current headwinds with theme parks and content development, Comcast has an additional buffer of developing a world-class aggregation platform and broadly launching a very robust streaming product in NBC Universal.

There'll be more earnings discussion next week, which will focus on wireless (including Altice's strong results). Until then, if you have friends who would like to be on the email distribution, please have them send an email to sundaybrief@gmail.com and we will include them on the list (or they can sign up directly through the new website).

Stay safe, keep your social distance, and Go Chiefs!