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LMRK - Q2 2019 Landmark Infrastructure Partners LP Earnings Call

EVENT DATE/TIME: AUGUST 07, 2019 / 4:00PM GMT

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Landmark Infrastructure Partners' Second Quarter Earnings call. (Operator Instructions) As a reminder, this conference call may be recorded. I would now like to introduce your host for today's conference, Mr. Marcelo Choi, VP Investor Relations.

Marcelo Choi - *Landmark Infrastructure Partners LP - VP, IR*

Thank you, and good morning. We like to welcome you to Landmark Infrastructure Partners' Second Quarter Earnings Call. Today, we will share an operating and financial overview of the business, and we'll also take your questions following our presentation. Presenting on the call today are; Tim Brazy, Chief Executive Officer; and George Doyle, Chief Financial Officer.

I would like to remind all participants that our comments today will include forward-looking statements, which are subject to certain risks and uncertainties. A number of factors and uncertainties could cause actual results in future periods to differ materially from our current expectations. For a complete discussion of these risks, we encourage you to read the Partnership's earnings release and documents on file with the SEC. Additionally, we may refer to non-GAAP measures such as FFO, AFFO, EBITDA and adjusted EBITDA during the call. Please refer to the earnings release and our public filings for definitions and reconciliations of these non-GAAP measures to their most comparable GAAP measures. And with that, I'll turn the call over to Tim.

Arthur P. Brazy - *Landmark Infrastructure Partners LP - CEO & Director of Landmark Infrastructure Partners GP LLC*

Marcelo, thanks very much. Good morning, everyone. Today we're going to discuss our financial and operating results for the second quarter and provide you with an update on our activities and more recent developments and strategic initiatives, including our FlexGrid program.

However, before we talk about our quarterly results, I'd like to take a few minutes to discuss the T-Mobile-Sprint transaction.

As you know, this merger transaction was announced over a year ago.

After months of review, Justice Department just recently settled with T-Mobile and Sprint regarding the proposed transaction, requiring a divestiture of assets to Dish and access for Dish and T-Mobile's network for an extended period of time, so that Dish can position itself as a viable fourth facilities-based wireless competitor. Under the terms of the proposed settlement, T-Mobile and Sprint must divest Sprint's prepaid business to Dish including Boost Mobile, Virgin Mobile and Sprint Prepaid. In addition, the proposal also provides for the sale of certain spectrums to Dish. The 800 megahertz spectrum licenses along with access rights to T-Mobile's network, a minimum number of 20,000 cell sites and hundreds of retail locations for Dish for a period of 7 years. This arrangement is designed to assist Dish while it builds out its own 5G network and facilitate further 5G deployment across the industry. Now although the official closing still faces a number of hurdles including various state challenges, the current structure incorporates several elements that make the transaction much more likely to happen than in the past. And as we've previously said, we don't think a transaction would have much of an impact on our business.

In fact, based on the information we have today regarding the merger, we view the recent developments as very positive for us. When the original merger announcement was made in April 2018, we were anticipating going from 4 major carriers to 3 major carriers with more significant potential site decommissionings as the 2 carriers rationalized their combined network. Today, under the proposed terms of the transaction, we view Dish as a practical alternative, a fourth major carrier with a better credit profile than the old Sprint. And we anticipate lower decommissionings as Dish builds out and expands its network footprint across the country. So we end up with more carriers, better credit, fewer potential site decommissionings and the opportunity for incremental benefits as the industry deploys additional capital at a faster pace for the next generation of wireless infrastructure. How would the contemplated T-Mobile-Sprint merger potentially effect LMRK? It's still too early to fully analyze the specific implications of this particular transaction, but we'd like to call attention to a couple of important points. First of all, our current portfolio exposure to T-Mobile and Sprint is relatively modest. As of the second quarter 2019, T-Mobile and Sprint accounted for approximately 8% and 6%, respectively, of the Partnership's quarterly rental revenue.

As of June 30 of this year, less than 5% of the Partnership's rental revenue was from Sprint sites where those sites had direct overlap with T-Mobile leases. And even with this overlap, it doesn't necessarily mean that the Partnership would lose 5% of its revenues in the worst-case scenario.

Assuming the transaction does eventually satisfy all remaining objections and closes, we expect the full combination of the 2 companies and technologies would take several years to complete. For example, it took years for MetroPCS to be fully integrated when T-Mobile bought out Metro, and that was a much, much smaller transaction. Given the size and complexity of the proposed merger between T-Mobile and Sprint, we expect the rationalization of these networks will take much longer and be far more complicated.

Given the time frames here, we believe that effects from any specific site decommissionings or portfolio reconfigurations would be significantly mitigated for a number of reasons.

First, LMRK's portfolio itself is expected to continue to grow and become more diversified during that time, lessening the impact of any site-specific changes.

Second, the rationalization of the 2 different networks into one common technology platform would create significant modification income and additional revenue opportunities as the network is reconfigured, upgraded and expanded. In addition, the organic growth from our contractual escalators and ongoing asset acquisitions will also help offset any effects from a potential merger. Perhaps, most importantly, the sale of certain spectrum licenses to Dish with ongoing service arrangements would further position Dish as an effective fourth carrier and that may have positive effects, including a lower potential likelihood for decommission sites, given that Dish will be offered access to a significant number of cell sites from the new T-Mobile. With Dish expected to ramp up its network coverage across the country, including the build-out of its own 5G network, we also expect additional lease modifications and higher demand for our FlexGrid offering. All in all, we do not expect the Sprint-T-Mobile merger to have a material negative impact on our business.

In fact, it may result in a fewer potential site decommissionings, as well as additional revenue opportunities.

Turning now to our second quarter, we delivered another strong quarter of operating and financial results as our portfolio continues to generate stable and consistent cash flows.

Occupancy rates remain high at 95%. And contractual rent escalators and the accretive acquisitions that we've made in the past 12 months continue to contribute to portfolio growth. Regarding our acquisitions year-to-date through June 30, we have acquired 119 assets for total consideration of approximately $13 million. Those assets are expected to contribute approximately $1.1 million in annual rents and were comprised primarily of U.K. outdoor advertising assets.

As we've discussed on prior calls, we're committed to executing our shift in strategy, which is focused primarily on our higher return development initiatives including FlexGrid and are also selectively acquiring higher cap rate ground lease assets on a direct basis. Our existing portfolio of over 2,000 assets, which provides growing and stable cash flows for the partnership, affords us the ability to target the higher growth, higher return development projects.

These projects are more complex in nature and involve a number of participants, including strategic property owners and potential tenants.

We are in various stages of deployment across all of our initiatives and continue to make significant progress on a number of projects.

We expect 2019 will continue to be a transitional year for FlexGrid, as we make further progress and expect revenue to commence towards the end of this year. We are confident that as we scale these deployments, they will contribute more meaningfully to our operating results and further strengthen our foundation for significantly greater deployments.

Right now, we're in discussions with the number of other potential real estate partners and tenants regarding various projects. And we expect to build them in a number of our current deployments, and we'll share further details with you on our third quarter conference call.

Looking ahead to the remainder of this year, we're very encouraged by the favorable wireless industry fundamentals to support our efforts with FlexGrid and order development projects.

Landmark continues to deliver stable and consistent results from our ground lease portfolio. And when that's combined with the higher returns and growth profile of our development activities, we believe that we're very well positioned to drive further value for our unitholders.

And with that, I'll turn the call over to George, who will provide us with a more detailed financial review of the quarter. George?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Thank you, Tim. As Tim outlined in his remarks, the assets in our portfolio continue to perform well, generating stable and predictable cash flows. In the second quarter, rental revenue was $15 million, which was 10.5% lower year-over-year and an increase of 4.4% from the first quarter. As we have outlined on prior calls, the JV established with Brookfield in the third quarter of 2018 is accounted for as an equity method investment. And the results of those properties are no longer consolidated into our revenue and operating expenses, but rather, we pick up our share of net income of the JV through equity income in the unconsolidated JV.

The assets that were contributed to the Landmark/Brookfield JV generated rental revenue of approximately $3.6 million in the second quarter.

Turning to FFO and AFFO. FFO per diluted unit was $0.07 this quarter compared to $0.30 in the second quarter of last year.

As we have discussed on past calls, FFO can fluctuate quarter to quarter depending on the change in the fair value of our interest rate hedges. AFFO, which excludes these unrealized gains and losses on our interest rate hedges along with other various items was $0.33 per diluted unit this quarter compared to $0.32 in the second quarter of last year.

Now turning to our balance sheet. We finished the second quarter with approximately $167 million of outstanding borrowings under our revolving credit facility. In secured notes, we're at approximately $221 million at the end of the quarter.

We ended the second quarter with 100% of our outstanding debt, either being fixed-rate debt or borrowings that have been fixed through interest rates swaps.

At the end of the second quarter, the Partnership completed the sale of 38 assets for total consideration of approximately $31.8 million.

The annual rents associated with these assets totaled approximately $1.7 million.

These assets were sold from our taxable REIT subsidiary and generated income taxes on the sale of $3.1 million.

As it relates to our distribution coverage ratio, in the second quarter of 2019, the distribution coverage ratio was 0.89x. We continue to expect our distribution coverage ratio to improve as we execute on our acquisition in development strategy. On our first quarter conference call, we stated that we expected to fully cover our distribution in the third quarter. We currently expect the distribution coverage ratio to improve in Q3, but due to the timing of certain acquisitions in development activity, the full coverage of our distribution has shifted to the fourth quarter. AFFO growth to cover the current distribution is anticipated to be driven by growth in revenue from our portfolio, the full quarter impact from recent acquisitions and anticipated acquisitions and developments over the remainder of 2019, and lower financing rates on our line of credit borrowings.

Regarding the growth in revenue from our portfolio, we are seeing strong renewal in leasing activity. Based on recent leasing activity, we are expecting higher organic revenue growth in the fourth quarter of this year and the first quarter of next year.

In summary, the portfolio continues to perform well, generating stable and predictable income. We continue to make progress with our development projects with assets expected to be placed in service in the second half of the year. And we are well positioned both from a capital availability and growth perspective. We will now take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from Ric Prentiss from Raymond James.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

A couple of questions. I appreciate the update on the distribution coverage including third quarter, but not to gain full coverage until fourth quarter '19. How do you think about how it plays out in 2020? Which -- and does full coverage mean 1.0x, 1.01x. What does full coverage mean when you think 2020 holds for us given the timing of acquisitions and development?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Sure. Once we get to full coverage from that point on, it will fluctuate a little bit depending on which quarter we get the final coverage in place. And then, I expect it to generally grow thereafter. So little over 1x initially from a coverage perspective. And then, I would expect that to get to kind of our normalized level at a minimum of 1.05x. But it will take a kind of few quarters to get there and it's a function of the developments coming online and completing some of the acquisitions that we have got on our pipeline.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

Okay. And speaking of development pipeline, the $13 million that you spent in the quarter, I think that was all for acquisitions? Or was there some FlexGrid CapEx in there? And what was the FlexGrid CapEx?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

The $13 million is year-to-date number, and those are all acquisitions. As Tim mentioned, they are mostly U.K. foreign acquisitions. We did spend approximately $15 million on the different development projects. And some of that is going to be outdoor advertising such as the kiosks, and some of it will be some of the FlexGrid infrastructure as well.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

And is that $15 million, is that a year-to-date number as well for first half?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

No, that's just for the quarter.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

Okay. And can you go back and -- you talked about at least some asset sales and some of the numbers on that. How many assets did you sell? And what was the price you got for them?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

It's a little under $32 million, and it was -- I think, it was approximately 28 assets.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

Okay. And then $1.7 million in revenue annually for that?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

That's correct.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

So kind of like a 6% cap rate?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

A little bit lower than that.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

And when -- I think, Tim, you mentioned, you'll start seeing some revenues from the development projects kind of by the end of '19. How much revenue should we -- is it like a rounding point? Does it actually noticeable by the fourth quarter? And how do you think what percent of revenues could the development projects represent may be in '20?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

That's a good question. As far as Q4, we expect to see a number of sites come online. But it's hard to say how many will exactly come online in Q4 versus fourth quarter, and when exactly they will come on in the fourth quarter. So we're expecting a small amount of revenue in the fourth quarter, and then it should pick up starting in the first quarter of next year. From a total revenue perspective, we've invested roughly, call it, $60 million in projects. And based on the minimum return levels, call it, 7 cap would be the minimum and we'll be looking at generating $4 million, maybe $5 million in revenue of those projects, based on what we spend today.

Operator

And our next question comes from Dave Rodgers from Baird.

David Bryan Rodgers - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

I just wanted to go back to the dividend coverage, George, if I could. And I understand you're saying full coverage in the fourth quarter and it'll bounce around, I guess, moving into '20. But can you give us a little more color on just kind of the delay in timing and what gives you the confidence then in the fourth quarter, it's going to be there. Is there a big incremental spend? Is it some approvals you're waiting on? What gives us the confidence that you're going to get there this year?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Sure. There's couple of things. One, as I mentioned, we're seeing fairly strong leasing activity.

So based on some of the recent leases that we've executed and some of the leases that are in the pipeline for renewal, we anticipate higher revenue in the fourth quarter.

We also have visibility on some of the developments that we're pursuing. We can see that some of those will be coming online in the fourth quarter. And then also, our borrowing costs have dropped a bit. We did implement U.K. LIBOR borrowing, which has about 125, 150 basis points lower costs than a U.S. LIBOR borrowing would. We're also seeing the Fed drop rates a bit. So when you kind of put all the factors together plus a small amount of acquisitions that we're targeting in the third and fourth quarter. And that would give us to coverage in the fourth quarter.

David Bryan Rodgers - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

And then to follow up on the acquisitions. I think in the last couple of quarters, you really targeted development that was going to be the primary method of deploying capital. And so as you kind of introduced the concept that I guess reintroduced more acquisitions, and you said it's a small amount, so I get that, but you mentioned a quite a few times in the call, how do we think about that relative to the development projects or the developments just coming along more slowly? Did some of those not materialize? Do you feel like you've got the CapEx that you can go out and deploy more? Can you kind of dive down that road a little bit further?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Sure. On the acquisition side, we're being selective on what we pursue versus the strategy.

We had -- going back a couple of years ago where we were doing more of the drop-down acquisition approach, where we're targeting larger portfolios. These are for the most part very selective, very accretive transactions. So we're not deploying a lot of capital, but the acquisitions that we are completing are very accretive. So depending on what opportunities surface over the next couple of months -- or sorry, next couple of quarters, that's -- those are the acquisitions that we'd anticipate closing.

On the development side, the development as we've mentioned before, it's a little tricky to forecast for a number of reasons. The -- just working through the whole planning process, leasing process, it takes time and things do shift around. But we've made a lot of traction, and we've got a number of sites that are going to be coming online in the fourth quarter. So we're getting very close to transitioning that in a position where sites are going to regularly come online and come out of development stage.

Operator

(Operator Instructions) And our next question comes from Liam Burke from B. Riley.

Liam Dalton Burke - *B. Riley FBR, Inc., Research Division - Analyst*

Tim, in the last call you mentioned that there's been a lot of interest over and above your current projects with people developing FlexGrid. How do you look at balancing developing existing projects with attracting new opportunities with other partners?

Arthur P. Brazy - *Landmark Infrastructure Partners LP - CEO & Director of Landmark Infrastructure Partners GP LLC*

Well, we are active in both, right? So as George mentioned, these projects are in various stages of deployment.

So when you think about what development or construction project or program might entail, there's identifying the opportunity, having the discussion with the strategic counterparty and the parties include not only the real estate owners, the fee owners, but the tenants.

These are larger, more complex deployment opportunities that means if there are a fair number of detail discussions about the customize solution that we're designing for the Partnership, for the opportunities. So at any one point in time, we have a number of projects and discussions in the early phases. We have others that are in process where we've agreed on the scope and the scale of what we are going to be doing over the next 12 to 24 months.

And we have others where equipment has been ordered. There is permitting involved. We have a very specific deployment calendar related to individual sites. So it continues to grow and advance quarter by quarter. The more we do, the more visibility we get, the more opportunity we have. And we see this as a very significant part of what we'll be doing over the next several years.

Liam Dalton Burke - *B. Riley FBR, Inc., Research Division - Analyst*

Okay. And just looking at your core portfolio, again, if I net out the JV contribution plus the sale of assets, did it -- did the rental revenue grow year-over-year on an organic basis similar to historic rates?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Yes, it did. Yes, we've generally been running at 2%, 2.5% kind of organic growth rate on assets that we've owned for a period of time.

Operator

Our next question comes from Ric Prentiss from Raymond James.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

I appreciate couple of follow-up questions. On the $1.7 million revenue that you sold, who is the buyer? What type of buyer? Who are they? And when did that close?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

We generally don't give the name of the counterparty. But it's the large institution that bought the portfolio from us. There's a lots of institutional interest in our asset classes. We've talked about that a bit in the past. There's certainly a lot of infrastructure money that's in the market at this point in time. And what was the last part of the question, Ric, I'm sorry.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

When did it close, specifically, like what day?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Pretty close to the end of the quarter. It was in the last week of June.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

Okay. All right. So didn't really have an effect on the 2Q numbers, say, in its annual meaningful size?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

That's correct. Yes.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

Okay. And then as we think on your balance sheet going forward, how should we think about just a ballpark sizing of what kind of development CapEx should like to put to work in 2020 and beyond?

Just kind of thinking of pacing of that with the outdoor kiosks and the FlexGrid, just even order of magnitude?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Yes, we haven't come out with our -- any sort of 2020 guidance. But I would say that the -- some of the projects that we have going on this year will continue to roll into 2020.

So I would say, it's going to be a similar level of spend as to what we're incurring at the moment, absent new projects coming -- or getting to the point where we're actually going to be spending money on new projects.

Richard Hamilton Prentiss - *Raymond James & Associates, Inc., Research Division - Head of Telecommunication Services Equity Research*

And given the time line, you're getting these things from signing to actually building that might not have as much. Are you still thinking kind of 12, 18, 24 months for some of these projects?

George P. Doyle - *Landmark Infrastructure Partners LP - CFO & Treasurer of Landmark Infrastructure Partners GP LLC*

Yes. Varies on the project, but yes, from start to finish, I would say, you're in that 12 to 24 months range.

Operator

Thank you. And that does conclude the question-and-answer session for today's conference. I'd now like to turn the conference back over to Tim Brazy for any closing remarks.

Arthur P. Brazy - *Landmark Infrastructure Partners LP - CEO & Director of Landmark Infrastructure Partners GP LLC*

Great. Thanks very much. And thanks everybody for joining us this morning. As you can tell, we're -- we continue to be excited about the opportunities we have in front of us. Things are taking somewhat longer and in some cases, for some of our development initiatives to get the traction that we're seeing now. But we are very confident that this will have a meaningful impact on the company as we work to continue to deliver growth at the Partnership. And we will share more details with you on the third quarter conference call. And look forward to speaking with you then. Have a great day everybody.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program. You may all disconnect. Everyone, have a wonderful day.