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Exchange Income CEO fires back at critics over WesTower unit

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The chief executive officer of Exchange Income Corp. says the company's second-quarter results – which include a surprising jump in profits – refute critics who question the company's earnings power and its viability.

Late Tuesday, Exchange Income reported flat revenue but EBITDA, or earnings before interest, taxes, depreciation and amortization, of \$28.4-million – a 14-per-cent increase over the prior year.

The company's WesTower subsidiary reported \$8.8-million of EBITDA, a 169-per-cent increase from 2013's second quarter. The EBITDA margin was 4.9 per cent, versus 1.6 per cent in the prior-year period. (All figures exclude a \$600,000 loss on a building destroyed by a tornado.)

The future of WesTower, which builds cellphone towers for wireless companies, is central to a thesis by **Veritas Investment Research** that Exchange Income's shares have a fair value of \$8.50. AT&T, WesTower's primary customer, seems to be scaling back its capital expenditures this year, based on its own disclosures and guidance of double-digit revenue declines provided by MasTec, a WesTower competitor.

Veritas said it believed that WesTower, which reported EBITDA margins between 2 per cent and 3 per cent in the four quarters prior to Tuesday's results, would not meet earnings expectations in 2015 because of the AT&T spending cut and financial disclosures that suggested it wouldn't be able to collect from AT&T.

Rather than the \$130-million in 2015 EBITDA some analysts were forecasting, **Veritas** said, Exchange Income was more likely to post \$95-million. And a greater deterioration in the business could challenge its ability to pay off debt, making the stock potentially worthless.

When the **Veritas** analysts issued their report on July 9, Exchange Income traded at \$21.48 a share; it quickly fell below \$20. The shares recovered from a July 31 low of \$17.16, but following a Globe and Mail column about the **Veritas** report on Aug. 7, the shares fell as low as \$14.30.

In an interview on Wednesday, CEO Mike Pyle said that while the company doesn't provide 2015 guidance, the second-quarter profits put Exchange Income on a path higher, and sooner, than the **Veritas** numbers. And the remainder of Bay Street analysts covering the company, who typically have "buy" ratings and target prices in the \$20-plus range, essentially reject the **Veritas** critique, he said.

"They predicted we couldn't fix WesTower," Mr. Pyle said. "I suggest to you our Q2 results say that's not true."

“Their [2015 EBITDA] assessment is clearly not looking particularly good when we made \$28-million in the last quarter,” he said. “The balance of opinion in the marketplace is that [**Veritas’s** forecast] is wrong.”

The key will be in 2014’s second half. Mr. Pyle said the company expects a revenue decline for WesTower of up to 10 per cent, with capital expenditure issues in the wireless industry offset by the ability to win business, including a new contract with another company that could be worth “up to \$100-million [U.S.] over multiple years.”

Margins “may be smaller” in the next two quarters, he says, “but we’re not going back to zero-per-cent margins.”

WesTower has “not been good enough” in its billing practices and will do a better job of collecting from AT&T, Mr. Pyle said in a conference call, addressing the numbers that suggested a collections issue.

Michael Yerashotis, the **Veritas** analyst who was the lead analyst producing the report, says the firm stands by its research.