

## Strategic Capital Fund Management

## The case for investing in cell towers

**Brooke Heffington**, managing director of *Real Assets Adviser*, recently spoke with **Jerry Sullivan**, CEO and managing director of Strategic Wireless Infrastructure Funds Management (Strategic Wireless), about the investment opportunity found in cell towers. Strategic Wireless is the wireless infrastructure division of Strategic Capital Fund Management. Following is an excerpt of that conversation.

**I doubt there is anyone out there who doesn't know that the U.S. cellular infrastructure is being upgraded to support 5G networking. You can't turn on your TV without seeing a provider's commercial touting its 5G network. Why is this such a big deal?**

I know some people look at the drive to upgrade the country's telecommunications infrastructure and the benefits it will bring as overblown hype. They are happy with their cell service and really don't understand why they should care whether they are receiving 4G or 5G service. And if all we were talking about was voice phone service, they would probably be right; however, the cellular networks today are more than just phones. The wireless networks today provide both audio and visual streaming services for phones, tablets, computers and smart TVs, as well as for autonomous cars, delivery drones, package tracking systems and smart homes. Add in the massive amounts of data transferred daily to and from hospitals, government and military installations, research facilities, universities, manufacturing, and other major data users, and it is obvious that the current systems in place today have reached their limits. If carriers don't upgrade to 5G, we are going to see consumers' ability to continue to progress and grow stymied. A network too slow for today's data demands is likely to have a real impact on economic growth and sustainability.

**How is 5G better than 4G?**

5G is an exponential jump in capacity and speed as compared to earlier networks. If you go back to the beginning, the 1G network was simply an analog phone system. 2G brought consumers SMS text messaging; 3G saw the introduction of alphanumeric paging and email capacities; and 4G supported the introduction of the iPhone and apps. If you envision each of those steps as moving an inch or two up a yardstick, 5G will take us all the way to the end of the stick in terms of adding capabilities. Looking at



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it another way, the 4G network is beginning to look like the Los Angeles freeway, with cars bumper to bumper 24 hours a day. 5G will add lanes, or frequency bands, that will not only allow more cars to enter the system — i.e., traffic — but also enable those cars to go faster.

**What does this mean for investors?**

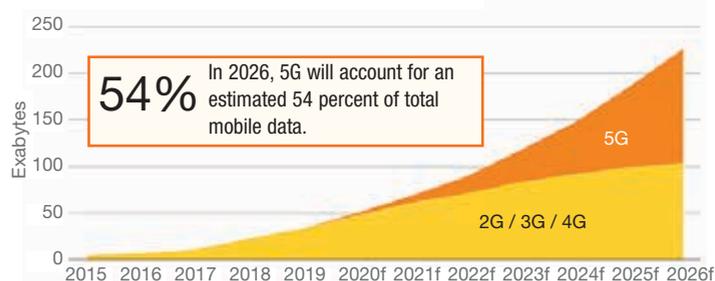
Everything always comes back to supply and demand. The demand for more and better telecommunications infrastructure is growing by the day, and there is no reason to think it is anywhere near slowing down. 5G networks provide more bandwidth and greater speed to move all the data that is being generated by the consumer. However, depending on operating frequencies, 5G's RF signal doesn't travel as far. That means carriers not only need to upgrade radio transceiver equipment on the towers currently in place, we need to build many more towers, and therein lies the investment opportunity. Whenever demand outpaces supply, investor capital soon follows. This additional infrastructure won't necessarily focus on your standard 150- to 300-foot tower. It will also consist of a variety of other types of distribution infrastructure, including micro towers, small cells or distributed antenna systems in discrete areas, such as healthcare facilities, coliseums, shopping malls and stadiums. These smaller distribution assets will help 5G signals connect consumers in areas that would normally experience network congestion. There are a lot of components that are being introduced with 5G, so there are lots of ways investors can be part of the telecommunications-asset growth story.

**What part of this growth story is Strategic Capital Fund Management involved with?**

Through Strategic Wireless, we primarily acquire and provide the vertical asset, the tower with its ability to support network components to the various service providers, who are, in essence, our tenants. It is

very similar to a small office building with multiple tenants but without the operating and capital expenses associated with owning office real estate. We typically have an anchor tenant plus two to three additional lessees. Once we have the initial lease in place, there are rarely any additional capital expenses or tenant improvement costs to us when adding a tenant. The principal cost is already covered, so anything that we derive from that second, third or fourth tenant on our tower — which most towers are capable of handling these days — typically drops directly to the bottom line. That is a very appealing business case. We also seek to acquire some of the infrastructure subsectors, such as ground and rooftop rights, fiber networks, small cells, and distributed antenna systems.

### Global Mobile Data Traffic (EB per month)



Source: Ericsson Mobility Report November 2020

Note: This graph does not include traffic generated by fixed wireless access (FWA) services.

### What makes one tower portfolio better than another one?

A better-than-average portfolio is usually diversified by geography and asset type, as well as managed appropriately for above-market returns. Our portfolio covers sites from Oregon all the way to the East Coast. We target five primary subsectors covering towers, ground and rooftop easements, fiber networks, small cells, and distributed antenna systems. When looking at performance, we run a very disciplined model that looks at how we can improve the cash flow of the towers we manage, as well as how we can acquire them at a below-market rates. We also pay attention to the length of lease terms, try to extend them wherever possible, and incorporate annual rent escalators to provide consistent growth in rental income over time. The goal of a good management team is to maximize the value of its assets, and that is something we strive toward with each acquisition.

### What makes a good management team?

Nothing beats experience. The top three executives on our wireless infrastructure team have about 85 years of collective experience in wireless and fiber network telecommunications, and about \$135-plus billion of transactions under our belts. Another important factor is that we all come from the carrier side of the business. That means we understand our customers' needs and wants better than most of the operators out there. It also allows us to access the financial markets at very attractive rates and gives us the ability to leverage our equity dollars in the marketplace, which is very accretive to overall returns in our portfolio.

### What makes cell towers a particularly attractive investment?

This asset class exhibits many utility-like characteristics. It is necessary for the efficient functioning of the U.S. economy, it has high barriers to entry, and it generates predictable, stable income streams with inflation-based escalators. Because of its indispensable nature and high-creditworthy tenants (e.g., AT&T, Verizon, T-Mobile, etc.), these assets have historically performed well in a variety of economic cycles, including recessions, elections, administration changes and now a pandemic. Cell towers also have a couple of added benefits. Each tower and each subsector (ground rights, small cells, etc.) tend to be stand-alone revenue drivers, so one is not necessarily dependent on the success of the other, making for non-correlated assets. In addition, tenants are extremely sticky and tend to stay in place for very long periods, if not indefinitely. Leases are long-term, typically starting out with an initial 10-year period and often including multiple five-year renewal periods. It's not uncommon to see a new lease that goes out 30 years when you factor in the renewal periods. It is very expensive for a carrier to move from one tower to another. It involves all kinds of network reconfigurations and disruptions in service. So, once you have a tenant, there's a relatively high degree of probability and predictability on that income stream. 5G upgrades are also helping to increase income and returns. When tenants upgrade their existing network equipment on towers with new 5G equipment, it is usually done in conjunction with lease extensions and an increase in rent, due to the added load on the tower.

### Bottom line, why are you so enthused about this asset class?

We think there is a long growth runway ahead given ongoing consumer demand expectations and the utility-like nature of connectivity. On top of that, 5G and new data-driven technologies like autonomous cars, artificial intelligence and virtual reality are in their infancy and are likely to rely on sophisticated wireless networks as they grow and become part of our daily norms. We believe providing the underlying infrastructure that supports wireless carriers' networks should remain a good investment for the foreseeable future.



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**Strategic Capital Fund Management** develops unique alternative investment solutions that provide attractive risk-adjusted returns while protecting investor capital. The company strives to create investment opportunities with superior management teams, cutting-edge asset classes and distinct product structures that can provide durable income, growth potential, reduced volatility and low correlation to traditional markets. Strategic Wireless Infrastructure Funds Management is the wireless infrastructure division of Strategic Capital Fund Management.

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