BEHIND
THE NUMBERS
Quality of Earnings Analysis
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Iron Mountain Incorporated (IRM)
Earnings Quality Update- 6/21 Qtr.

6- Exceptionally Strong
5- Strong
4- Acceptable
3- Minor Concern
2- Weak
1- Strong Concern
+ quality improving
- quality deteriorating

We are maintaining our earnings quality rating of IRM of 1+ (Strong Concern) and maintain our Top Sell rating.

For an explanation of the EQ Review Rating scale, please refer to the end of this report.

Summary

IRM's adjusted FFO of 69-cents beat forecasts by 5-cents. It is worth noting that IRM pulled in 3.9 cents from using financing leases and ignoring the principal payment. It also saw stock compensation more than double from 1Q21 from $10.7 million to $22.5 million. This was another 7.7 cents that IRM added back to FFO. Another 1.6 cents of FFO came from adding back FX losses. IRM sold its Intellectual Property Management business in early June, but did not classify it as a discontinued operation in May. It reported the results of the business as normal operating income for another month. This may have added another 0.5 cents to FFO. The company also touted that it grew storage volume by 4.5 million cubic feet – but they acquired 5.0 million cubic feet in the quarter – it wasn't organic growth.

We still see evidence of ongoing operating cash costs starting to increase again coming out of Covid, which IRM ignores in its REIT stats. As more business resumes, we expect these costs to rise much higher and more records to be destroyed and need to be replaced. Rent expense should also rise faster than revenues as IRM has expanded its sale-leaseback program for assets.

- After guiding to sale lease-backs of $125 million for 2021 as part of the capital recycling, IRM sold $197 million in 2Q21 and boosted guidance to $250 million for the year. This is effectively adding to the cost structure as IRM has rising operating leases and that expense is growing faster than the business. The discount rate for leases was 6.9% at the end of 2020.

	2Q21	2Q20	1Q21	1Q20	2020	2019
Oper. Lease Cost	$135.1	$119.2	$132.7	$123.3	$499.5	$439.6
Growth	13.3%		7.6%		13.6%	
Organic Storage Rev Growth	2.5%		1.7%		1.7%	

- The recurring costs that IRM faces from buying out new customer's existing contracts at competitors, picking up and delivering files, and other incentives and payments made to acquire new storage volumes are returning. IRM benefited during Covid as many customers weren't as focused on moving their stored documents and many of these costs fell noticeably:

2Q figures	Acq. Cust. Relations	Customer Inducemt	Fulfillmt Commiss.	Stock Comp.	NonCash Rent	Withdraw < Mk Rnt	Finance Leases
2021	$2.8	$2.4	$12.3	$22.5	$4.0	$2.1	$11.2
2020	$1.2	$2.6	$7.6	$18.9	$3.0	$2.6	$11.2
2019	$9.4	$3.0	$10.2	$12.5	$2.6	$3.5	$14.5

Many of these items show up on the cash flow statement, but as expenses, many are capitalized. That allows IRM to ignore the initial cash outlay and the amortization of the capitalized amount is added back as a non-cash item when it reports AFFO. We believed that during Covid, the cash situation would look better as many customers had employees furloughed or working from home and therefore were not adding or destroying stored documents. As some normalcy returns, we believe these costs will continue to rise. We noted that IRM's own employees were furloughed and it enjoyed a $14.5 million decline in labor costs y/y in 1Q21. In 2Q, labor jumped by $34.4 million y/y.

- The basic story is still AFFO was 85-cents and the dividend is 61.85 cents so IRM says there's great coverage. AFFO added back 1.6 cents from FX and the items listed above are 19.7 cents of AFFO. We expect to see those cash costs increase going forward and there were many quarters in 2019 where those cash outlays were much higher than 1Q21 and 2Q21. Also as noted above, IRM bought more records storage with $35.7 million in acquisitions. In terms of cash per share for AFFO – that was another 12-cents. We still believe AFFO often understates recurring maintenance. That spending was up to $35.9

million in 2Q21 but even the company says that is because it delayed many projects last year when spending was below that figure. Another sign that cash spending is higher than IRM shows on its REIT stats – Net Debt is up $179 million YTD (plus operating lease liabilities are up too). That is despite selling IPM for $214 million and selling $210 million of sale-leaseback assets YTD against initial guidance of $125 million for all of 2021.

- IRM announced that Project Summit has reached 95% of its intended workforce reduction. We are still surprised to see that was one of the largest expected cost savings – yet severance is only 24% of all spending on this project and only 10% for 2Q21. The huge focus on professional and other fees still makes us skeptical that some normal and ongoing expenses made it into these "one-time" charges. The focus of the $322 million spent so far has been one-third on streamlining the records storage business and two-thirds on cutting corporate overhead. They intend to cut 45% of senior staff ranked VP and above as a key part of the plan. Why do you need so many third-party professional consultants involved to rework the corporate staff or a cash cow business you've been operating for over 70 years?

Explanation of EQ Rating Scale

6- (Exceptionally Strong)- Indicates uncommonly conservative accounting policies to the point that revenue and earnings are essentially understated relative to the company's peers. Higher possibility of reporting positive earnings surprises

5 (Strong)- Indicates the company has no areas of concern with its reported results and we see very little risk of the company disappointing due to recent results being overstated from aggressive reporting in recent periods.

4 (Acceptable)- Indicates the company may have exhibited a minor "red flag", but the severity of the issue is not yet a concern. Minimal risk of an earnings disappointment resulting from previous earnings or cash flow overstatement

3 (Minor Concern)- Indicates the company has exhibited either a larger number of or more serious warning signs than companies receiving a 4. The likelihood of an immediate earnings or cash flow disappointment is not considered to be high, but the signs mentioned deserve a higher degree of attention in the future.

2 (Weak) Indicates the company's recently reported results have benefitted materially from aggressive accounting. Follow up work should be performed to determine the nature and extent of the problem. There is a possibility that upcoming results could disappoint as the impact of unsustainable benefits disappears.

1 (Strong Concern)- Indicates that the company's recent results are significantly overstated and that we view a disappointment in upcoming quarters is highly likely

In addition to the numerical rating, the EQ Review Rating also include either a minus or plus sign. A minus sign indicates that our analysis shows the overall earnings quality of the company has worsened since the last review and there is a possibility the numerical rating will fall should the problem continue into upcoming quarters. Likewise, a positive sign indicates that the overall earnings quality is improving, and the company may see an upgrade in its numerical rating should the trend continue.

Key Points to Understand About the EQ Score

The EQ Review Rating is much more than a blind, quantitative scoring method. While we utilize proprietary adjustments, ratios, and methods developed over decades of earnings quality analysis, the foundation of all of our analysis is reading recent SEC filings, press releases, conference call transcripts and in some cases, conversations with managements.

The EQ Review Rating is not comparable to a traditional buy/sell rating. The Rating is intended to specifically convey the extent to which reported earnings may be over/understated. Fundamental factors such as forecasts for future growth, increasing competition, and valuation are not reflected in the rating. Therefore, a high score does not in itself indicate a company is a buy but rather indicates that recent results are a good indication of the underlying earnings and cash generation capacity of the company. A low score (1-2) will likely result in us performing a more thorough review of fundamental factors to determine if the company warrants a full-blown sell recommendation.

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