A Closer Look at Shaw Communications

Description

by Gaurav Seetharam

Three minutes after the opening bell on Oct. 24, 40 million shares changed hands, and **Shaw Communications** (TSX: SJR, NYSE: SJR) lost nearly $2.5 billion of its market capitalization. The share price would recover slightly, ending the day at $24.48 in Toronto and USD$23.47 in New York, but investors had expressed clear disappointment with the company's fourth-quarter earnings.

Net income dropped 12% to $117 million from $133 million in the same quarter a year ago, yet somehow, revenue bumped up slightly in all three segments. Compared to last year, cable, satellite, and media brought in an additional $15 million, $6 million, and $14 million, respectively.

Revenue up, net income down. Huh?
It's true that Shaw has outpaced the field with its average revenue growth (3 year) of 13.8% to the industry's 11.3%, but its net income growth lags far behind the pack (10.7% to 47.8%). Things get even more muddled when you notice that Shaw actually has a higher-than-normal operating margin (27.1% to 18.9%). I pulled some data to make sense of it, and here's what I found:

While **BCE** and **Rogers** have seen steady improvement in their net income margins, Shaw (yellow line below) appears to have plateaued around 14.5%.

image 1 Image not found or type unknown

Source: Data from S&P Capital IQ

Part of the problem is their Earnings from Continuing Operations Margin dropped to 15.2% from 21.7% five years ago. Companies that rely on one-time events for revenue, such as selling a subsidiary, building, or equipment, are unable to streamline their expenses.

Another important metric to consider is the Return on Common Equity. Subtracting out preferred dividends makes it a better measure of shareholder return than the simple Return on Equity ratio.

image 2

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Source: Data from S&P Capital IQ

It's the clearest indication of a firm's profitability and this graph speaks for itself.

Foolish Bottom Line

Shaw's feeling the impact of its participation in a mature market. And its quarterly results did nothing to quell investor's fear that growth from here will be a challenge. Although the company's cable network acts as a sturdy piece of infrastructure, how the company plans to leverage this asset to grow the business from here remains somewhat of a mystery.

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Disclosure: Gaurav Seetharam does not own shares of any companies mentioned.

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Date
2025/06/30

Date Created
2013/10/28
Author
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