What to Expect From BCE Inc's Acquisition of Bell Aliant Inc

Description

Just recently, **BCE Inc** (TSX: BCE)(NYSE: BCE) announced its acquisition of **Bell Aliant Inc** (TSX: BA) by offering existing public minority shareholders a choice of cash, BCE shares, or a combination of both.

What is BCE getting by acquiring Bell Aliant?

Lower capital expenditure

Excluding a one-time pension funding outlay in 2011, Bell Aliant has consistently generated over $1 billion in cash from operations over the past few years.

BCE has stated that it plans to spend $2.1 billion on capital expenditures, or capex, across Atlantic Canada over the next five years, averaging $420 million per year.

As a stand-alone company, Bell Aliant has invested $578 million in capex over the past three years.

Quick math shows that about $160 million — that is, $578 million minus $420 million — in cash would be freed up in the form of less spending in capital expenditure.

Dividend savings

Currently, BCE's equity interest in Bell Aliant is 44%, as it owns 100.4 million out of a total of 227.9 million shares.

Bell Aliant has been consistently paying $0.475 per share in dividends every quarter, for a total of about $108.25 million per quarter, or $433 million per year.

Quick math again shows that about $242 million in dividend cash — that is, $433 million minus BCE's existing annual dividend of $191 million — would be freed up as result of this acquisition.

Cash accretion

As of May 2014, BCE was paying a dividend of $0.6175 per quarter with common shares outstanding of 777.3 million, for a quarterly dividend payout of about $480 million per quarter, or $1.92 billion per year.

Assuming all of Bell Aliant's 127.5 million public minority shares elect to convert to BCE common shares, using a conversion rate of 0.6371 from Bell Aliant to BCE shares, this would result in an additional 81.23 million shares. This would cause an incremental payment of $50.16 million per quarter in extra dividend spending, or about $200 million per year.

Taking into account the $160 million in capex and the $242 million in dividend savings, and then subtracting the $200 million in newly issued shares, the deal looks to be a $200 million cash accretive merger for BCE annually.

The big picture

This figure of $200 million is about 10.4% of BCE's entire annual dividend outlay. Its current dividend growth rate is between 5% and 6% annually, slightly below the 10-year average of 6.9% as of 2013.

Assuming the entire $200 million is not distributed to shareholders all at once, this acquisition could add up to 2% annually to its existing dividend growth run rate over the next five years, resulting in a respectable dividend growth rate of 7% to 8%.

Don't expect too much synergy

Currently, Bell Aliant's EBITDA margin is a healthy 53%, higher than both BCE's home phone, internet, and TV services' one of 38% and its wireless service's one of 40%. While there may be some operating synergies, investors should not expect significant savings here.

Ultimately, with BCE's dividend growth slowing in recent years, it looks like this acquisition may provide BCE with the possibility to boost its dividend, which otherwise would not have been possible had the two companies remained separate entities.

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patrickli