



Is Manitoba Telecom Services Inc. a Better Bet Than Telus Corporation?

Description

Back on March 16th I wrote [an article](#) where I stated my bullishness for **Manitoba Telecom Services Inc.** (TSX:MBT).

My bullish thesis had three major tenets. Firstly, the stock was trading at a much cheaper valuation compared with peers. Manitoba Telecom had a P/E ratio of approximately 14, while its competitors were closer to 18. I figured that gap would close over time.

There was also the company's underrated moat. Many investors view Manitoba Telecom as a bit player on the cusp of being beaten on its home turf by better competition. But the company owns a market share of approximately 60% in Manitoba, and Manitobans continue to support the company. In fact, its market share in both wireless and television services has actually gone up lately.

Finally, there was the potential for the company to erase an overhanging issue: its pension shortfall. At the time analysts were speculating that the generous 7% dividend would be cut, with proceeds going towards paying back the pension. That's exactly what ended up happening, much to the market's delight.

Three months later it appears my prediction has come true. Shares of Manitoba Telecom are up more than 15% since I wrote the original article, while shares of its major competitors are only up some 2%. With this in mind, is the stock still a good buy? Or should investors switch out of it for **Telus Corporation** ([TSX:T](#))([NYSE:TU](#))? Let's take a closer look.

Valuation

Because of the run-up in shares, Manitoba Telecom isn't quite as cheap as it used to be. Shares are currently trading at 18.6 times trailing earnings. And they get less attractive if you believe analysts estimates for 2016, which puts them at more than 19 times earnings.

Telus, meanwhile, currently trades at 18.1 times earnings, with earnings projected to grow to \$2.79 per share in 2016. That puts shares at just 15.4 times 2016's estimated earnings. Advantage, Telus.

Balance sheet

For telecoms, both Telus and Manitoba Telecom have decent balance sheets.

Let's start with Telus. The company currently owes \$11.5 billion in total debt compared to \$7.7 billion in equity. This has been creeping up lately, with the company taking out more than \$2 billion in debt in the last quarter alone.

Manitoba Telecom, meanwhile, looks to have the more attractive balance sheet. It owes just \$898 million compared to \$1.07 billion in equity. It has also been borrowing lately, but only to the tune of \$50 million over the past year.

With a debt-to-equity ratio of just 0.84, Manitoba Telecom is by far the least leveraged telecom in Canada. Advantage, Manitoba Telecom.

Dividend

Figuring out which of these companies has the better dividend isn't as simple as just looking at the yield. We also have to look at the sustainability of the payout.

Telus currently pays out \$0.42 per share quarterly, good enough for a 3.9% yield. Free cash flow for 2014 was slightly negative, but that was fueled by investments in the business. A more typical year sees \$2 billion in capital expenditures, giving it \$1.5 billion available to pay approximately \$1 billion in annual dividends.

Manitoba Telecom recently cut its dividend, dropping its payout from \$0.425 per share to \$0.325 per share quarterly. This new dividend will set the company back approximately \$100 million per year, which looks to be sustainable based on 2014's free cash flow, but without a whole lot of room to spare. Advantage, Telus.

Operations

As mentioned, Manitoba Telecom has done a nice job competing against its nationwide competition. It has maintained its market share and posted a 2% revenue increase in the latest quarter.

But Telus is perhaps the best operator in Canada. It continues to post record low wireless churn, and is making nice gains in its television business. It also has done a terrific job revamping its customer service, giving front-line employees the freedom to make decisions without having to transfer to a manager. This is a smart move. Once again, advantage Telus.

Three months ago, Manitoba Telecom was the cheapest telecom in Canada. But now that shares are up 15%, they're not a great value any longer. For the same valuation, I think investors are better off choosing Telus over Manitoba Telecom, even with the latter's 4.7% yield and better balance sheet.

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