It's Not the Best Time to Buy BCE Inc.

Description

BCE Inc. (TSX:BCE)(NYSE:BCE) is a quality business. However, against common belief, just because it's a quality stock doesn't mean you should buy it anytime at any price.

A quality business

BCE is Canada's largest communications company with a market cap of over $48 billion. It has an investable-grade S&P credit rating of BBB+ and manageable debt/cap levels of 38%.

The big business continues to grow steadily. Compared with the third quarter of last year, its operating revenues increased by 2.9%, its adjusted earnings per share (EPS) increased by 12%, and free cash flow grew by 10.4%

What BCE offers

BCE offers services to Bell Canada and Bell Aliant customers. Services include Bell Mobility and Virgin Mobile wireless, high-speed Internet, IPTV and Satellite TV, Home Phone, IP-broadband and information, and communications technology services.

Then there's Bell Media, which is Canada's premier multimedia company with leading assets in television, radio, and digital media, including CTV, Canada's top television network and the country's most-watched specialty channel.

Segment-wise, Bell Wireline makes up 56% of revenue, Bell Wireless makes up 32%, and Bell Media contributes 12%. Product-wise, Wireline Broadband & TV makes up 37% of revenue, Wireless makes up 32%, Wireline Voice makes up 19%, and Media contributes 12%.

Valuation

With a price of $57.40 per share, BCE is trading roughly at a price-to-earnings ratio (P/E) of 17. However, the telecom has normally traded at a P/E of about 15 in the past 12 years.

The business gives a EPS guidance of $3.28-3.38 per share. This range implies a fair price range of $49.20-50.70 per share at a P/E of 15, which is a potential downside of 11.6-14.3%.

The business is moderately expensive today.

Yield

In the past five years, BCE has hit yields as high as 5.4% and is commonly above 5.1%. That's because during most of that period it was trading at a P/E of about 15.

Today, BCE only yields 4.5%, which is 11.8% lower than the minimum ideal yield of 5.1%. With its quarterly dividend of 65 cents per share, a 5.1% yield equates to just under $51 a share, which would be closer to the high end of the fair price range.

Additionally, BCE's payout ratio of about 80% is on the high end compared with its competitors. **Telus Corporation** (TSX:T)(NYSE:TU) and **Rogers** have payout ratios under 65%. In other words, BCE's dividend growth is highly dependent on earnings growth versus payout ratio expansion.

In conclusion

Perhaps you're a retiree and you don't mind if BCE trades downwards of 11-4% in the near term. You only care about the safety of its 4.5% yield and that it remains sustainable.

If you care more about total returns and whether or not you're paying a fair price for a quality company, I think you should wait until it gets to at least 5.1%, which will probably occur due to a price decline and a dividend hike, which are expected in the second quarter of 2016.

I like Telus better for its 4.2% yield. It has better growth potential.

CATEGORY

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