Income on Steroids: Get a 10.6% Yield From Shaw Communications Inc.

Description

Companies like **Shaw Communications Inc.** (TSX:SJR.B)(NYSE:SJR) make up the bedrock of thousands of portfolios across Canada.

There's a lot to like about Shaw as an investment. Shaw has morphed from a growth story a decade ago to a steady dividend payer today. It has three basic services it offers to consumers–cable television, Internet access, and home phone services. The company also has a media division, but that is slated to be sold to **Corus Entertainment** to help Shaw pay for its much-anticipated entry into the wireless space through the planned acquisition of Wind Mobile.

Shaw seems to be the whipping boy of investors who are concerned the cable TV business is irreparably damaged. These investors might be onto something–after all, Shaw did lose approximately 3% of its cable and satellite television subscribers in 2015. But at the same time, it managed to push through a price increase to most of its remaining customers.

For most people, cable is still a reasonable expense for the value provided. Where else can you get hours of entertainment for $2 or $3 per day without leaving your home? For every millennial who thinks cable is a rip off, there are two baby boomers who can't envision watching their favourite shows any other way.

Besides, I like to look at it another way. If someone cuts cable, they can likely be talked into purchasing an upgraded Internet plan. If you've just cut a $60 per month cable bill, paying $20 per month extra for ultra-fast Internet isn't a big deal. If you're a **Netflix** addict, you'll gladly pay a little extra.

I like Shaw's Internet offerings for one simple reason: the company has a network of more than 45,000 locations in western Canada which offer free WiFi to existing customers. I don't have to do anything; my phone or laptop just automatically connects.

Get huge dividends

Shaw has one of Canada's most attractive dividends. The current yield is 5.1%, and the payout ratio is approximately 67%. There's a chance the payout ratio could go up a bit once the company ditches the media assets, but the purchase of Wind should help offset that. Besides, the growth potential for Wind is much higher than owning television channels, even if they are some of Canada's most popular.

That's a nice yield, but there's an opportunity for income investors to increase it substantially using the option market.

The strategy is called writing covered calls, and it's not nearly as complex as it sounds. Essentially, a Shaw shareholder would use call options to generate their own additional income stream.

Investors can take both sides of a call option, which enables you to buy a stock at a certain price on a particular day. Buying the call option gives the investor the right to buy on the date. Selling the call option means the investor is forced to sell at that price on that date.

Let's use a real-life option to illustrate. The March 18th $25 call last traded for $0.11 per share. An investor who already owns Shaw shares can sell that call option, pocketing the $0.11 per share premium today. If shares rose above $25 by March 18, this investor would be forced to sell their shares at that price. If shares are below $25, the options expire worthless.

This can be done 12 times a year, generating some very decent income in the process. An investor in Shaw could collect an additional $1.32 per share in option premiums over the course of a year. Add that to the $1.19 in annual dividends, and this investor would enjoy a yield of 10.6%.

There's one major risk, and that's the limitation of upside. If Shaw shares shoot up to $26 the week of March 18, an investor would be out $1 per share in profit. But they'd still make money, and the covered call writer would still have the option premium.

Assuming an investment of just 400 Shaw shares–which would set you back $9,400 today, less any commissions–an investor could generate $996 in annual income. Which is just about right amount needed for the average Canadian to pay their cable bill.

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2. Investing

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