



3 Reasons to Buy Telus Corporation Over Manitoba Telecom Services Inc.

Description

About a year ago, I [pounded the table](#) on **Manitoba Telecom Services Inc.** (TSX:MBT).

The company had plenty of things going for it.

It traded at a price-to-earnings ratio of approximately 14 times trailing earnings, while its larger competitors traded at a P/E between 16 and 19. It had a good balance sheet, a dominant position in Manitoba, and a couple of potential catalysts that could have potentially unlocked value. The company ended up selling its Allstream division for \$465 million, removing a part of the company most analysts thought was a dud.

Shares have done well in the last year, even after the company cut its dividend from \$0.425 per quarter to \$0.325. They've soared nearly 34%, easily outpacing all of the company's Canadian peers. If you include dividends, shares are up nearly 40%.

Now that Manitoba Telecom has done so well, I think it's time for investors to consider selling if they're sitting on nice gains and redirect that capital to **Telus Corporation** ([TSX:T](#))([NYSE:TU](#)). Here are three reasons why.

Valuation

The last year hasn't been nearly as good for Telus's shares as it has been for Manitoba Telecom. Telus is down approximately 11%.

This decline has brought Telus to a more reasonable valuation. When looking at trailing earnings, the company trades at a P/E of approximately 17. Manitoba Telecom has a trailing P/E of 42.5, but that number has been skewed by one-time charges.

Looking forward, Telus appears to be even cheaper. Analysts estimate the company will earn \$2.70 per share in 2016, giving it a forward price-to-earnings ratio of just 14.5. Manitoba Telecom is projected by analysts to earn \$1.30 in 2016, putting it at 25.7 times forward earnings.

Dividend

There were a couple of reasons why Manitoba Telecom decided to slash its dividend in 2015. It was dealing with a pension shortfall, and the company's shares were so depressed that the yield had popped up to 7%. With everyone else in the sector paying approximately 4%, management made the prudent decision to cut the payout, freeing up cash which could be redirected to the pension problems.

It's obvious Manitoba Telecom isn't going to raise its dividend, at least in 2016. It's silly to hike a dividend just a year after it was cut. Besides, the company is projected to have a 100% payout for 2016, paying a \$1.30 per share dividend while earning \$1.30 per share.

Telus has a much more attractive dividend profile. It has raised its payout twice per year since 2010 and looks poised to do so again in 2016. Thanks to the sell-off in shares, the stock yields 4.5%—a full 15% more than Manitoba Telecom.

Telus also has a better payout ratio. If the company raises its quarterly dividend to \$0.46 per share this year, it has a payout ratio of 68% based on analyst earnings projections.

Will Manitoba Telecom get acquired?

I believe part of the reason why investors have bid up Manitoba Telecom shares over the last year is because they're speculating it is the next acquisition target.

I'm not sure how realistic that is. A company looking to acquire Manitoba Telecom would likely have to pay a premium of 25-30% over the current share price, which works out to approximately \$40 per share. Would you pay \$40 per share for a company that's projected to earn \$1.30 per share this year? There have to be a lot of synergies to make that deal attractive.

Canadian telecoms don't really have great balance sheets anyway. Investors tolerate the large amounts of debt and preferred shares issued by the sector because cash flows are so predictable. Swallowing a transaction worth upwards of \$3 billion is no small feat.

Manitoba Telecom could very well get acquired. There's plenty of speculation that Telus could be the company that buys it. The geography makes sense, and Telus has been notably absent while the other big players have been spending.

But just because you think something could happen doesn't make it a compelling reason to invest.

A year ago, I urged investors to buy the cheap telecom over the more expensive one. It worked out well. Now that their roles are reversed, I think the decision to buy Telus over Manitoba Telecom today is pretty obvious.

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