Shaw Communications Inc.: Expect Lower Dividend Growth in the Future

Description

Dividend-growth investors who owned **Shaw Communications Inc.** (TSX:SJR.B)(NYSE:SJR) have done pretty well in the last decade.

Back in 2006, the company was paying a paltry $0.02 per share monthly dividend–good enough for a yield of approximately 1%. The company was still in growth mode back then, and the lack of dividend yield reflected that reality.

The dividend shot up, increasing to $0.06 per share each month in 2008, $0.0767 in 2011, and then $0.09875 in the early part of 2015. That's growth of 400% or so in just a decade.

Much has changed in the last 18 months. Shaw sold its mature media assets, using the proceeds to buy Wind Mobile, its first foray into the wireless sector.

Wind represents a good opportunity for Shaw. It gives it a significant growth market, which is especially important as the cable business begins to shrink. Wind also gives Shaw the ability to bundle wireless subscriptions with other services, which is an enticing perk for some customers.

But while the acquisition of Wind was a good long-term move for Shaw, there is one group of investors who likely won't be happy with the result. It's likely that Shaw's days of being a dividend-growth superstar are largely behind it.

Big investments upcoming

Wind's strategy has traditionally been a pretty simple one. The company focused on some of Canada's largest metro areas, gaining market share by undercutting competitors.

This strategy was necessary because of Wind's capital restrictions. It didn't have the money to roll out a true nationwide network, so it just bought spectrum in a few local markets and let customers roam when they left town.

Wind currently operates in southern Ontario, Calgary, Edmonton, and Vancouver.

After acquiring Wind, Shaw identified a number of upgrades that would have to be made to its network, including upgrading it to 4G LTE speeds. When announcing the acquisition, Shaw estimated these upgrades would cost at least $250 million.

In total, Shaw is on pace to spend $1.2 billion in capital expenditures in 2016. That number will increase to $1.3 billion in 2017 with much of the increase from the announced spending on Wind's network. This will depress free cash flow, which is where dividends come from.

Just can't afford it

In its fiscal 2015, Shaw generated $1.54 billion in cash flow. It's on pace to generate a little more than that in fiscal 2016–about $1.6 billion. That number will likely decrease a little in 2017 because the recently sold media division generated more cash than Wind will, even accounting for the latter's growth rate.

Say Shaw can generate $1.6 billion again in cash flow in 2017. After accounting for the $1.3 billion in planned capital expenditures, that leaves the company with $300 million to pay dividends. But dividends currently come in at close to $400 million.

Since many capital expenditures are optional, this shortfall isn't that big of a deal over the short term. Shaw can afford it, in other words. But can it really afford to increase the dividend in such a scenario? Would that be something a prudent management team would do?

Ultimately, until Wind really starts contributing to Shaw's bottom line, Shaw will, at best, only give investors token dividend increases. It just can't afford to increase the payout much. And with Wind only contributing $65 million in EBITDA–versus approximately $2 billion for the other parts of Shaw–it's going to be a long time before the new prize really makes a dent in the bottom line.

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