Shaw Communications Inc.: Don’t Expect Much Dividend Growth

Description

Shaw Communications Inc. (TSX:SJR.B)(NYSE:SJR) has been a dividend-gr0wth stud over the last decade.

It paid just $0.02 per share each month back in 2006 to shareholders. It then hiked the payout to more than $0.04 per month in 2007 and has raised it every year since, although it has yet to announce a higher dividend for 2016. Shares currently pay owners 9.875 cents per month, which is good enough for a 4.5% yield.

Many investors have held Shaw shares for years, happy to collect the rapidly increasing dividend. As the company has matured, it has morphed from a growth story to an income stock with most of its value from paying a steady dividend.

This is the reality investors should expect going forward. I think we all know Shaw’s days of growing the dividend 10% or 15% annually are behind it. But many investors still expect a raise in the 5-8% range.

I think those investors are aiming too high. I believe Shaw will only keep its dividend steady over the next few years, or, if it does hike it, it will only give investors token raises designed to keep it on certain dividend-growth lists.

Here’s why Shaw’s days of being a true dividend-growth stock are behind it.

Wind Mobile

After years of thinking about getting into the wireless market, Shaw finally bit the bullet in December 2015 and announced it was going to acquire Wind Mobile. Shares promptly tanked on the news, although they have slowly recovered.

At first glance, the bearishness seemed somewhat unwarranted. Wind is doing a nice job growing wireless subscribers in a crowded market, and the company is in the process of upgrading its network to handle faster data speeds. It also had big plans to expand from its current operating areas, which include Vancouver, Calgary, Edmonton, and the Toronto area.

There’s just one problem. Because Wind is a low-cost carrier, it doesn’t enjoy the kind of margins other wireless providers have. It turns out that the rest of Shaw’s divisions are much more profitable on a per-dollar-of-revenue basis.

In its most recent quarter, Shaw posted a 42% operating margin. Its three other divisions–customer, business network services, and business infrastructure services–all had operating margins above 35%.

Wind Mobile’s operating margins were 19.6%.

It gets worse. Shaw sold off its media business to pay for the Wind acquisition. In the first quarter of 2016, that part of the company reported an operating margin of more than 40%.

In short, Shaw traded profits today for higher growth. There’s nothing wrong with that per se, but investors have to realize that if there’s fewer profits right now, that means less money available to pay to shareholders.

High payout ratio

Shaw just released full-year 2016 numbers. They were a little disappointing versus last year.

The company earned $2.51 per share–a nice result. But that was buoyed by the sale of the media division, which boosted profits.

Free cash flow was considerably worse. It came in at $482 million, or just over $1 per share. Shaw currently pays a dividend of $1.185 per share. That gives it a payout ratio comfortably over 100% of free cash flow.

Shaw should post higher free cash flows in 2017. It won’t have any acquisition or sale-related expenses. Wind should continue to grow. And it can likely push through rate increases to many of its existing cable and internet subscribers. This is all good news.

I’m not suggesting Shaw is anywhere close to cutting its dividend, because the company is still in fine shape. But I also think it just can’t afford to hike the payout, possibly for a number of years. Any available cash should be spent trying to grow Wind Mobile. It’s the better long-term move.

The bottom line

Shaw is still a decent dividend choice, but investors looking for a similar yield with better growth potential would be wise to avoid Shaw and check out one of its competitors instead.

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