Why BCE Inc. Could Be Your Biggest Loser in 2017

Description

BCE Inc. (TSX:BCE)(NYSE:BCE) has been a favourite for Canadian dividend investors for some time, and the company has done a good job in the last quarter by obtaining 107,000 new subscribers to its wireless business, but growth opportunities from here look slim, and with valuations stretched, we may see the stock pull back next year.

Billionaire Canadian investor Prem Watsa recently dumped his stake in BCE earlier this year because the stock has become expensive, and growth expectations are likely to lag going forward. Should you join Prem Watsa and dump your shares for the competition, or does BCE still have gas in the tank to keep moving higher?

Growth opportunities may come up short going forward

BCE has been a terrific grower of revenues for many years. The business has a fantastic return on equity of 16.6% and a return on invested capital of 8.1%, which is quite outstanding. The free cash flow margin is at a healthy 17.6%, which supports its fat 4.7% dividend yield.

While these numbers sound promising, the long-term revenue growth of -2% has been disappointing over the last five years. While in the last quarter BCE crushed analyst expectations for wireless customer growth, there's only so much growth that the company can have; competitors steal market share, like **Shaw Communications Inc.** (TSX:SJR.B)(NYSE:SJR), which acquired WIND mobile last year and is looking to upgrade its wireless network to compete with the likes of BCE as well as the other telecoms in the Big Three.

BCE has one of the largest holds on wireless Canadian customers, and as Shaw continues to improve its wireless segment, we may see it eat into BCE's market share over the next few years, while introducing pricing pressure; Shaw made it clear that it wishes to make WIND mobile a discount carrier for the time being.

BCE is Canada's largest telecom company, so it's a given that it will be hard to grow, but the company has been making acquisitions to sustain its revenue growth rate. While such acquisitions will help, I do not believe they will be able to offset the threat of new competitors that are jumping into the telecom scene and are determined to steal market share; this is what the CRTC wanted and is what will benefit Canadian consumers.

Canadian wireless rates are ridiculously expensive, and Shaw will hurt the bottom line of BCE the most of the other Big Three Canadian telecoms because of BCE's size, its limited ability to grow, and the fact that it's fighting against the CRTC. While Shaw doesn't have a wireless network as strong as BCE's, we could see Shaw catch up over the next few years, and this is bad news for BCE.

Great dividend, but the stock is very expensive considering low growth expectations

BCE has a fantastic dividend, and it's safe, but I would be cautious holding on to shares of BCE at current levels, as the stock is overvalued and could decline in 2017.

The stock trades at a 18.2 P/E and a four P/B, both of which are more expensive than their five-year historical average values of 15.6 and 3.3, respectively. This makes BCE considerably more expensive than it was over the last five years, and, given recent headwinds, BCE is a stock I would avoid, even if the yield goes above 5%.

Prem Watsa is a smart investor, and this "safe" stock is no longer safe at current levels. It may be time to rethink this investment if you hold shares.

CATEGORY

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joefrenette