Integrated Telecommunication Services

3Q23 Canadian telecom preview – Price rationality and wireless growth persist

Earnings Preview

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Equity
Canada
Telecommunications

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Cogeco kicks off 3Q reporting Nov 1, BMO

Reporting season begins 11/1 when Cogeco reports its fiscal 4Q23 and shares fiscal 2024 guidance. We believe the industry remains healthy with stable pricing, growing subscribers, falling capex, and rising free cash flow. Current valuations, however, suggest deep problems exist. We believe the Street is worried about 1) competitive intensity, 2) regulatory events (wireless MVNOs & wholesale broadband rates), and 3) rising interest rates. We expect 3Q results to generally soothe investor concerns and have a positive impact on sector stocks.

Competition remains, and is rational

Back-to-school season and the iPhone15 launch led to the typical elevated competitive intensity in late 3Q. While promotions increased and discounting occurred, it was not measurably greater than in prior years. Encouragingly, promotional pricing reverted to regular pricing as back-to-school ended. The iPhone15 launched in September and once again proved more evolutionary than revolutionary. Given the large price tag against an inflationary backdrop, its presence did not lead to new competitive pressures.

Regulatory concerns are a weight on the sector

The market awaits a CRTC decision on wholesale broadband rates. In an October 1, 2023 speech, CRTC Chair Vicky Eatrides suggested we should see a decision soon. Mandated wholesale broadband rates are not new but there is concern that the CRTC's new rates may, again, be set too low for the market's comfort. Returns on invested capital have declined as the industry has invested heavily in wireless networks, spectrum, and fiber. We believe the regulator is aware of the math and understands that ROI informs future capital investment. Management teams will likely use their conference calls to comment on the regulatory environment. We expect the CRTC's ultimate decision will mirror its past decisions which have regularly balanced the twin interests of consumer affordability and carrier investment.

Rising stock yields are out of sync with rate history

Over the past year dividend yields and rates have moved meaningfully higher. There has been a strong positive correlation between the two in the past year. Over a longer timeframe, the data does not support the lockstep movement observed over the past 12 months. We take a closer look at this relationship here, and show that the recent increase in dividend yields of BCE and TELUS actually deviate materially from long term averages. Dividend payouts as a percent of free cash flow are currently above company target ranges. We expect coverage ratios to improve as capex moderates after a period of accelerated spending (eg. 5G, fiber). Organic growth within core connectivity businesses will also support improved coverage. Longer term, cost cutting should contribute to higher margins as fiber cost benefits are realized and copper is decommissioned. We expect the companies to field dividend coverage/comfort questions this quarter.

Exhibit 1: Reporting timings
CCA to report first (FY-4Q)

	Date	Release
Cogeco	1-Nov-23	AMC
BCE	2-Nov-23	BMO
TELUS	3-Nov-23	BMO
Rogers	9-Nov-23	BMO
Quebecor	TBA	TBA

Source: BofA Global Research
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Refer to important disclosures on page 9 to 12. Analyst Certification on page 8. Price Objective Basis/Risk on page 7. 12612410

Summary of reporting times

Exhibit 2: 2Q23 Reporting times
Cogeco kicks off reporting Nov 1

	Date	Release	Call	Time	Dian-in
Cogeco	1-Nov-23	AMC	2-Nov-23	11:00AM	1-888-886-7786
BCE	2-Nov-23	BMO	2-Nov-23	8:00AM	1-800-806-5484
TELUS	3-Nov-23	BMO	3-Aug-23	TBA	TBA
Rogers	9-Nov-23	BMO	9-Nov-23	11:00AM	1-800-319-4610
Quebecor	TBA	TBA	TBA	TBA	TBA

Source: Company report

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Key Metrics

Exhibit 3: Consolidated Estimates summary
Revenue, EBITDA and EPS for the group

	BofA estimates			Consensus estimates		
Consolidated	BCE	Rogers	TELUS	BCE	Rogers	TELUS
Revenue	6,085	5,015	5,035	6,168	5,058	5,116
Growth (% y/y)	*1.0%*	*34.0%*	*7.8%*	*2.4%*	*35.1%*	*9.5%*
EBITDA	2,658	2,355	1,811	2,680	2,364	1,831
Growth (% y/y)	*2.7%*	*48.8%*	*5.0%*	*3.6%*	*49.3%*	*6.2%*
EPS	0.78	1.09	0.31	0.82	1.10	0.26
Growth (% y/y)	*-11.4%*	*29.7%*	*-8.9%*	*-6.6%*	*30.4%*	*-23.8%*

Source: BofA Global Research estimates, Visible Alpha

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Exhibit 4: Wireless estimate summary
Subscriber additions will drive industry service revenue growth

	BofA estimates			Consensus estimates		
	BCE	Rogers	TELUS	BCE	Rogers	TELUS
Wireless						
Wireless service revenue ($mn)	1,839	1,970	1,761	1,836	1,973	1,777
growth (% y/y)	*4.5%*	*11.9%*	*3.8%*	*4.4%*	*12.0%*	*4.8%*
Wireless ARPU ($/mth)	60.51	57.30	59.48	60.35	57.47	59.98
growth (% y/y)	*-0.4%*	*0.8%*	*0.0%*	*-0.7%*	*1.1%*	*0.8%*
Wireless net additions (k)	160	187	143	168	181	146
growth (% y/y)	*-4.6%*	*13.9%*	*-5.0%*	*-0.1%*	*10.4%*	*-2.5%*
Postpaid churn (%)	1.05	1.10	1.00	1.02	1.07	1.03
growth (% y/y)	*16.7%*	*13.4%*	*5.3%*	*12.9%*	*10.2%*	*8.7%*

Source: BofA Global Research estimates, Visible Alpha

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Exhibit 5: Telecom segment estimate summary
Wireless business will drive telecom growth

	BofA estimates			Consensus estimates		
Telecom	BCE	Rogers	TELUS	BCE	Rogers	TELUS
Telecom revenue ($mn)	5,475	4,539	4,328	5,552	4,556	4,374
growth (% y/y)	*1.4%*	*40.0%*	*8.0%*	*0.7%*	*40.5%*	*9.1%*
Telecom EBITDA ($mn)	2,469	2,323	1,632	2,498	2,328	1,643
growth (% y/y)	*2.6%*	*49.1%*	*7.1%*	*3.8%*	*49.4%*	*7.8%*
Telecom EBITDA margin (%)	45.1%	51.2%	37.7%	45.0%	51.1%	37.6%
Broadband net additions (k)	83	15	34	82	20	33
growth (% y/y)	*-7.4%*	*150.0%*	*-5.0%*	*-8.1%*	*232.6%*	*-7.0%*

Source: BofA Global Research estimates, Visible Alpha

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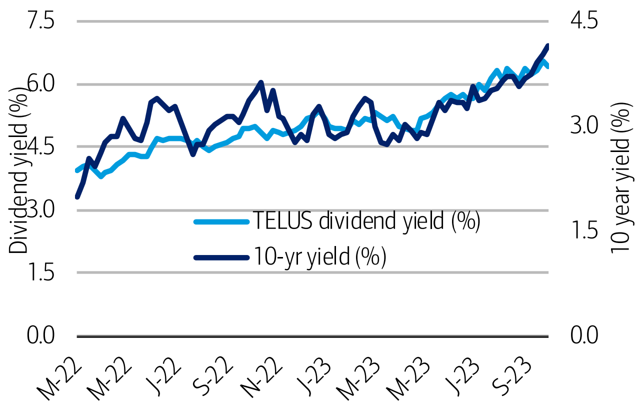
Rates are driving yields up, but shouldn't

Telecom stock dividend yields are at historical highs. This is happening as rates rise to multi-year highs as central banks move to fight inflation and credit spreads widen. Looking at the data from this past year, the relationship between rates and dividend yields is very strong. As rates have increased, so to have dividend yields. The historical relationship, however, has not always been so in lockstep.

Exhibit 6: TELUS dividend yield and 10-year rate (March '22 - present)
Both rates and dividend yields moved higher this past year



Source: BofA Global Research, Bloomberg

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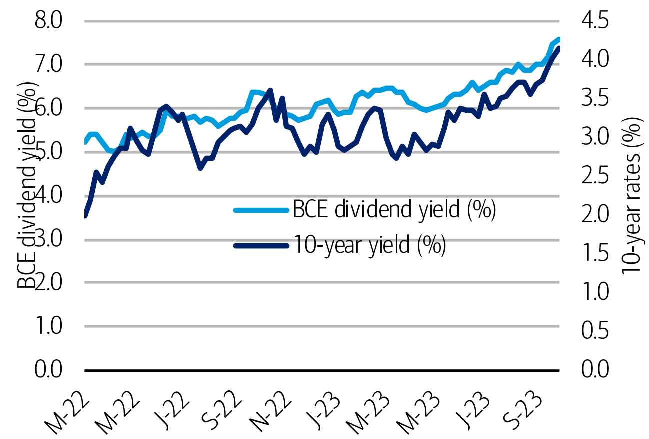
Exhibit 7: BCE dividend yield and 10-year rate (March '22 - present)
Both rates and dividend yields moved higher this past year



Source: BofA Global Research, Bloomberg

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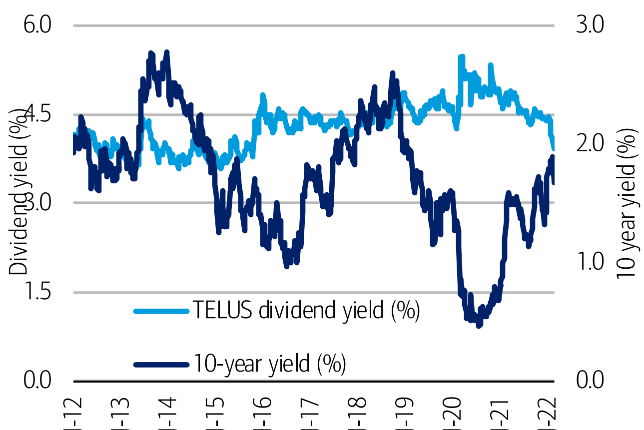
If we step back and examine a longer time horizon, the relationship is much less straight forward. As 'rates' moved from near 3% to below 1% dividend yield fluctuated around a narrow range. Historically, we do not observe the lockstep movement observed over the past year.

Exhibit 8: TELUS div yield and rates (Jan'12 – March '22)
Dividend yield hovered around 4.5% as rates fluctuated



Source: BofA Global Research, Bloomberg

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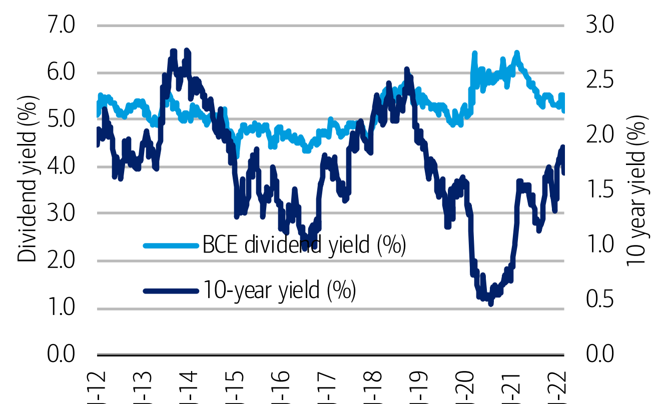
Exhibit 9: BCE div yield and rates (Jan'12 – March '22)
Dividend yield hovered around 5.2% as rates fluctuated



Source: BofA Global Research, Bloomberg

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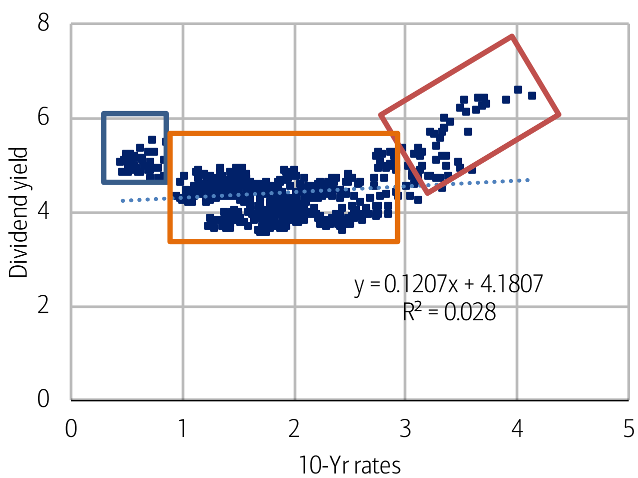
We have plotted the government 10-year bond yield and the dividend yields of TELUS and BCE since Jan 2012 below. The slope of the trend line is positive which indicates some positive relationship between higher rates and higher dividend yields. On the left of each graph, when rates fall below 1%, this coincides with the COVID pandemic. On the right-hand side when rates are above 3%, this is the most recent time period.
For both TELUS and BCE, the dividend yields in the most recent period (right hand side) materially differ from the historical relationship outside of the COVID pandemic. The recent increase in rates accompanies rising dividend yields at an increasingly large gap beyond the historical trend line. History does not support recent stock moves in relation to the move in rates, in our view.

Exhibit 10: TELUS dividend yield and 10-yr rates
Current dividend yield materially above historical trendline



Source: BofA Global Research, Bloomberg

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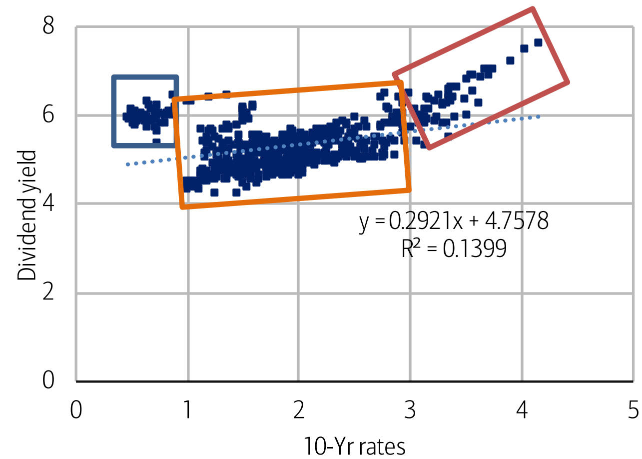
Exhibit 11: BCE dividend yield and 10-yr rates
Current dividend yield materially above historical trendline



Source: BofA Global Research, Bloomberg

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3Q expectations

Largest variances vs. consensus

We highlight noteworthy variances between our estimates and the Street here. We have the Street low estimate for BCE's consolidated revenue mainly due to our Street low equipment revenue forecast. We are the Street low for TELUS's consolidated revenue due to below-Street forecasts for equipment revenue and wireless service revenue.

Exhibit 12: Notable variances
We are below the Street on consolidated revenue for BCE and TELUS and the low estimate for BCE equipment revenue

	BofA	Consensus	vs. Consensus	Low	High	Range
BCE Consolidated Revenue	6,085	6,168	(83)	6,085	6,245	2.6%
TELUS Consolidated Revenue	5,035	5,116	(81)	5,035	5,182	2.9%
BCE Wireless equipment	675	733	(58)	675	761.20	11.7%

Source: BofA Global Research estimates, Visible Alpha

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Consolidated revenue and adj. EBITDA

We forecast both revenue and adjusted EBITDA growth for the incumbents in 3Q23. Our growth rate forecast is slightly below consensus. We have lower equipment revenue estimates than the Street and we forecast slightly lower EBITDA margins in 3Q than consensus but we are not the Street low estimate for any of the incumbents and the estimate ranges are fairly narrow. On a consolidated basis, we are not expecting surprise results this quarter.

Exhibit 13: BofA consolidated revenue and EBITDA vs. consensus
BofA is below the Street estimates for EBITDA in 3Q

	BofA	Consensus	vs. Consensus	Low	High	Range
Consolidated Revenue						
Rogers	5,015	5,058	(43)	5,012	5,099	1.7%
BCE	6,085	6,168	(83)	6,085	6,245	2.6%
TELUS	5,035	5,116	(81)	5,035	5,182	2.9%
Consolidated EBITDA						
Rogers	2,355	2,364	(8)	2,281	2,396	4.9%
BCE	2,658	2,680	(22)	2,655	2,748	3.5%
TELUS	1,811	1,831	(20)	1,790	1,873	4.5%

Source: BofA Global Research estimates, Visible Alpha

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Wireless

Rogers and Quebecor should lead year-over-year wireless service revenue growth due to the inclusion of Shaw Mobile and Freedom subscribers, respectively. The main underlying driver of service revenue growth will be net adds which we believe will remain robust in 3Q. ARPU growth in recent quarters was primarily driven by a return of high margin roaming revenue. Roaming revenue has leveled off and will not likely contribute to overall ARPU growth. We expect Rogers will report the highest ARPU increase at approximately 0.8% y/y while we expect BCE to report a slight contraction, in part due to lower overage revenue caused by higher data plans.

Exhibit 14: BofA wireless estimates vs. consensus
BofA is the low estimate for TELUS wireless ARPU in 3Q

	BofA	Consensus	vs. Consensus	Low	High	Range
Wireless service revenue						
Rogers	1,970	1,973	(3)	1,933	2,007	3.7%
BCE	1,839	1,836	3	1,806	1,852	2.5%
TELUS	1,761	1,777	(16)	1,761	1,796	1.9%
Wireless EBITDA						
Rogers	1,271	1,260	11	1,204	1,294	-7.2%
Postpaid net additions						
Rogers	187	181	6	150	200	27.6%
BCE	160	168	(8)	155	181	15.4%
TELUS	143	146	(4)	130	155	17.1%
Wireless equipment	BofA	Consensus	vs. Consensus	Low	High	Range
Rogers	578	562	15	506	609	18.3%
BCE	675	733	(58)	675	761	11.7%
TELUS	561	583	(21)	540	627	14.8%
Wireless ARPU	BofA	Consensus	vs. Consensus	Low	High	Range
Rogers	57.30	57.47	(0.17)	56.31	58.43	3.7%
BCE	60.51	60.35	0.16	59.85	60.94	1.8%
TELUS	59.48	59.98	(0.50)	59.48	60.37	1.5%

Source: BofA Global Research estimates, Visible Alpha

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Combined wireless and wireline comparison

We aggregate the wireless and cable estimates for Rogers to compare against the CTS segment at BCE and the Ttech segment at TELUS. Our 3Q estimates are slightly below consensus. The largest variance to consensus is BCE. We believe BCE's 3Q results will reflect some pressure from falling high margin overage revenue as wireless data buckets increase and broadband promotions remain elevated. Across the incumbents the variance to consensus EBITDA is relatively small and continues to reflect y/y growth.

Exhibit 15: Telecom segment estimates
We have below consensus EBITDA estimates

	BofA	Consensus	vs. Consensus	Low	High	Range
Telecom revenue						
BCE	5,475	5,552	(77)	5,475	5,607	2.4%
TELUS	4,328	4,374	(46)	4,328	4,432	2.4%
Rogers	4,539	4,556	(17)	na	na	na
Telecom EBITDA						
BCE	2,469	2,498	(29)	2,469	2,551	3.3%
TELUS	1,632	1,643	(11)	1,608	1,669	3.7%
Rogers	2,323	2,328	(6)	na	na	na

Source: BofA Global Research estimates, Visible Alpha

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Media

Advertising weakness will continue to impact Media in 3Q. While there is little variance between our estimates and consensus, the range of estimates is relatively wide.

Exhibit 16: Media segment estimates
Advertising market weakness will impact 3Q profitability

	BofA	Consensus	vs. Consensus	Low	High	Range

Exhibit 16: Media segment estimates

Advertising market weakness will impact 3Q profitability

Media Revenue						
Rogers	557	550	6	530	583	9.6%
BCE	705	711	(7)	705	733	4.0%
Media EBITDA						
Rogers	83	82	1	74	88	17.0%
BCE	189	185	4	176	196	10.9%

Source: BofA Global Research estimates, Visible Alpha

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3Q expectations by company

Rogers: Buy rated; C$75 price objective

The integration of Shaw and related synergy realization are running on schedule to slightly ahead of schedule based on our conversations with the company. RCI continues to target $200mn in synergies in calendar 2023E and an annual run rate of $600mn by 1Q24 or earlier. We expect management to update investors on its progress when it reports 3Q results. We do not expect RCI to deviate from its existing synergy realization or its deleveraging timeline.

We expect RCI to once again lead the market in wireless net additions in the context of overall strong wireless subscriber growth. Robust growth is driven in part by large numbers of new Canadians among which Rogers captures a disproportionate share. RCI also has a new western-Canada wireline base into which it can sell wireless service which is also helping.

Wireless service revenue growth will be driven by RCI's leading subscriber growth and the inclusion of the Shaw mobile subscribers. Wireless pricing was a key focus during the busy back to school quarter and we will look for RCI to comment on the competitive intensity and the level of discounting in the market. We believe the market was competitive but showed healthy signs as promotional offers were short lived and pricing reverted back to regular levels when the back-to-school season ended. We expect a similar focus on pricing and promotions to re-emerge in 4Q over the holiday season.

The cable segment will see improved y/y performance against easy comps last year when it dealt with a network outage. We forecast improvements in both broadband net additions and customer relationship net additions.

We maintain our Buy rating and C$75 price objective. We expect RCI to deliver on its merger synergy targets and delever at 0.5x per year before factoring in any potential improvements in the western cable footprint. RCI has the potential to improve legacy Shaw's cable performance through increased investment in the network, bundling with a superior wireless product, and leveraging its existing distribution scale to drive sales of both wireless and cable services.

TELUS: Buy rated; C$30 price objective

Since the close of the Rogers/Shaw merger, the market has wondered how Rogers's presence in the western wireline market (in place of Shaw) would change the competitive landscape. To-date, we do not believe it has had a material impact. We continue to expect TELUS to generate a similar number of broadband and wireless net adds as it did last year thanks to its consistent go-to-market strategy and focus on high value customers and fostering a subscriber base with lower churn. We do not believe 3Q will show any signs of a price war or uneconomic escalations to competitive intensity.

Heading into 3Q we lowered our margin expectations for the Ttech segment to reflect a slower pace of realizing the cost benefits from the LifeWorks integration/synergies and the slower than initially modeled pace of achieving the cost savings from the cost efficiency program. While we have modeled a longer time to achieve the savings we remain confident TELUS will achieve them. We will listen for an update on how the

Health and Agriculture businesses are performing into the 4Q when TELUS reports 3Q results.

The segment of the business most exposed to the current macro headwinds is TELUS International (TIXT). Technology sector cost cutting in one of its largest verticals is impacting top-line growth. The headwinds are partially offset by growth in other verticals (e.g. banking, financial services, and insurance). Current guidance assumes improving trends in the second half of 2023. TIXT management is guiding to y/y declines in EBITDA in 3Q followed by a return to y/y growth in 4Q. We expect TELUS to update investors on these expectations during 3Q results.

We maintain our Buy rating and C$30 price objective. Underlying demand for its core telecom services remains strong and is the main driver of wireless service revenue growth. TELUS is executing on multiple initiatives to improve the performance, including the LifeWorks integration and synergies as well as the cost efficiency program. While the LifeWorks integration is already beginning to contribute to results it will not be until 2Q24 that the cost efficiency program adds material benefits to the bottom line. We also expect DLCX to begin to show improving results by year end and will look to management for an update on its outlook.

BCE: Neutral rated; C$62 price objective

BCE has invested heavily to increase its fibre footprint, acquire wireless spectrum and roll out 5G service. While these investments will generate growth over the long term, its high dividend payout ratio is getting more attention from investors. In a high rate environment, investors wonder if BCE can sustain its dividend growth model. We believe subscriber growth, falling capex, lower cost networks, and lower customer service costs will sustain the current growth model. We expect BCE to update investors on its long-term plans to return to its target dividend payout range and share a timeframe to achieve its targets.

The Street and our estimates both forecast strong wireless subscriber growth and wireless service revenue growth between 4-5% y/y. Wireless service revenue growth will be entirely driven by subscriber growth as ARPU is forecast to decline y/y in 3Q. Recovery of international roaming revenue has plateaued and BCE is experiencing a decline in data overage revenue as more subscribers adopt larger data plans and go into overage less frequently.

We maintain our Neutral rating and C$62 price objective. We believe the current valuation fairly reflects BCE's steady wireless and consumer broadband subscriber growth offset by headwinds in Business Wireline and Media.

Stocks mentioned

Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BCE	BCE US	BCE Inc.	US$ 38.58	A-2-7
YBCE	BCE CN	BCE Inc.	C$ 52.53	A-2-7
RCI	RCI US	Rogers	US$ 39.41	A-1-7
YRCIB	RCI/B CN	Rogers	C$ 53.62	A-1-7
TU	TU US	TELUS Corp	US$ 16.91	A-1-7
YT	T CN	TELUS Corp	C$ 23.01	B-1-7

Source: BofA Global Research

Price objective basis & risk

BCE Inc. (YBCE / BCE)

Our $62 (US$46) price objective is based on an 8.5x forward (2024E) EV/EBITDA multiple. Over the last 5-years, BCE has traded at an average multiple of 8.3x. We think that the small 0.2x multiple premium us justified by BCE's solid execution, wireless growth, expanding FTTP footprint and strong FCF growth, partially offset by headwinds in Business Wireline and Media.

Downside (upside) risks to our price objective are multiple contraction (expansion) related to competitive and regulatory concerns in wireless, weaker (stronger)-than expected revenue growth due to economic and competitive pressures and accelerating wireless/wireline substitution, slower (faster)-than expected progress in cost reduction and a reversal (continuation) of the continuing P/E multiple expansion.

Rogers Communications (YRCIB / RCI)

Our C$75 (US$60) price objective is based on a forward (2024E) EV/EBITDA multiple of 8.1x. This is above RCI 5-year average multiple of 7.8x but within the range of 6.8x to 9.0x. We believe a multiple near the upper end of its historical range is justified after its merger with Shaw due to 1) synergy realization, 2) ample FCF to delever the balance sheet, and 3) expanded growth opportunities. .

Downside risks to our PO are the inability to reach cost synergy targets, merger integration issues, and higher than expected costs required to realize targeted synergies.

TELUS Corporation (YT / TU)

Our C$30 (US$22) price objective is based on a forward EV/EBITDA of 9.3x, which is a premium to TELUS's historical average of 8.2x but within its range of 6.9x - 9.8x. We believe the premium is justified by its higher growth, more attractive business mix, and solid execution.

Downside risks to our PO are a decline in historically high sector multiples, an acceleration of wireless margin/average revenue per user (ARPU) compression in a maturing and competitive market, ARPU pressure from more aggressive regulation and competition from Freedom Mobile, further economic slowdown in Western Canada, and, in the wireline segment, and failure to show progress in expanding cash flow margins.

Upside risks are better-than-expected revenue growth driven by strong execution, with the key drivers being continuing investments in fibre-to-the-premise (FTTP) and increasing wireless data consumption, and better-than-expected improvement in wireline cash flow margins.

Analyst Certification

I, David W. Barden, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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North America - Telecom Services Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	American Tower Corp.	AMT	AMT US	David W. Barden, CFA
	AT&T Inc.	T	T US	David W. Barden, CFA
	Cogent	CCOI	CCOI US	David W. Barden, CFA
	Digital Realty Trust Inc	DLR	DLR US	David W. Barden, CFA
	Dycom Industries, Inc.	DY	DY US	Alexander Waters
	Equinix, Inc.	EQIX	EQIX US	David W. Barden, CFA
	Quebecor Inc.	YQBRB	QBR/B CN	Matthew Griffiths, CFA
	Rogers Communications	RCI	RCI US	David W. Barden, CFA
	Rogers Communications	YRCIB	RCI/B CN	David W. Barden, CFA
	TELUS Corporation	YT	T CN	David W. Barden, CFA
	TELUS Corporation	TU	TU US	David W. Barden, CFA
	T-Mobile US	TMUS	TMUS US	David W. Barden, CFA
NEUTRAL				
	BCE Inc.	YBCE	BCE CN	David W. Barden, CFA
	BCE Inc.	BCE	BCE US	David W. Barden, CFA
	Crown Castle Inc	CCI	CCI US	David W. Barden, CFA
	SBA Communications Corporation	SBAC	SBAC US	David W. Barden, CFA
	Uniti Group Inc	UNIT	UNIT US	David W. Barden, CFA
	Verizon Communications Inc.	VZ	VZ US	David W. Barden, CFA
UNDERPERFORM				
	Cogeco Communications Inc.	YCCA	CCA CN	Matthew Griffiths, CFA
	Dish Network Corporation	DISH	DISH US	David W. Barden, CFA
	Lumen Technologies Inc.	LUMN	LUMN US	David W. Barden, CFA

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Telecommunications Group (as of 30 Sep 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	53	49.07%	Buy	38	71.70%
Hold	30	27.78%	Hold	20	66.67%
Sell	25	23.15%	Sell	13	52.00%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1869	53.48%	Buy	1046	55.97%
Hold	828	23.69%	Hold	461	55.68%
Sell	798	22.83%	Sell	370	46.37%

[R1] Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
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Underperform	N/A	≥ 20%

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