

Why a Rogers-Shaw merger is unlikely to happen

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March 25, 2013

Veritas analyst **Neeraj Monga** says the children of the late Ted Rogers are not of the gambling type to take on an acquisition that could cost up to \$13.6-billion

Investors betting that Rogers Communications Inc. will eventually acquire Shaw Communications Inc. could be in for disappointment.

That's the view of **Veritas Investment Research** analyst **Neeraj Monga**, who rates the possibility of such a blockbuster merger as remote, given his belief that the Rogers family would be unwilling to launch such a risky and transformative acquisition.

"I do believe a deal is highly unlikely," **Mr. Monga** said in an interview.

He questioned the idea in a recent note to clients that dwelled on one of the most popular guessing games on the Canadian stock market: Selecting which of the dwindling number of names in the media and communications sector will be next to be swept up in an acquisition.

Given the tangled nature of investment banking relationships on the Street, it isn't often that a report analyzes the prospects for such takeovers, but **Veritas** is an independent research advisory firm and doesn't face such conflicts.

Speculation about the fate of Shaw often makes the rounds because it is the last big-name communications and media company remaining in the country that would make a nice fit with an existing industry leader like Rogers.

Interest in a possible hookup involving Shaw has risen since BCE's bid for Astral Media has eliminated the other remaining large-sized company with attractive assets in the broadcasting end of the communications business.

There are other potential deals that are sometimes bandied about, but they either face incredibly long odds, such as a tie-up between industry behemoths BCE and Telus that would be unlikely to pass regulatory scrutiny on competition grounds, or would involve the Lilliputians in the industry.

Among these small fry are East Coast phone and communications company Bell Aliant, which is often touted as an acquisition for corporate parent and 44-per-cent owner BCE; a possible tie-up between Shaw and Corus Entertainment, which are both controlled by the Shaw family; or Quebec broadcaster TVA Group being swallowed up by its major owner Quebecor Media.

Another possible acquisition target is Asian Television Network; with its stable of foreign-language specialty channels, it might be of interest to one of the larger broadcasters.

One alternative to an outright Shaw-Rogers tie-up might be a scenario where Shaw spins its media assets into Corus and then sells its cable operation to Rogers.

Shaw is a prized asset because of its big base of cable operations in Western Canada, a natural complement for Toronto-based Rogers. Shaw is such a choice asset that it will likely be sold only once and would therefore be expected to receive a rich control premium.

Mr. Monga estimates the two companies, if combined, have a substantial scope to attain synergies, allowing a cut in capital and operating costs by about \$500-million annually, before tax.

That's an enticing number offering a decent economic rationale for a deal going forward.

But **Mr. Monga** believes the main reason against a tie-up is that the Rogers family is taking a conservative stance with their namesake company and aren't willing to make a bet-the-ranch-sized acquisition. A deal for Shaw shares at even a relatively slim 25-per-cent premium to the current market price – probably the lowest amount that would get bidding going – would make the company worth more than \$13.6-billion, compared to Rogers' market capitalization of around \$26-billion.

It's a gamble that patriarch Ted Rogers, who died in 2008, might have contemplated because he built the firm through daring acquisitions, but not his children, Edward and Melinda, who are now calling the shots on the strategic direction for the company.

Looking at both companies on their own investment merits, **Mr. Monga** prefers Rogers.

Although Shaw and Rogers have similar valuations based on EBITDA (earnings before interest, taxes, depreciation and amortization), **Mr. Monga** says the prospects for higher dividends are better at Rogers.

He estimates that Rogers will be paying out about 65 per cent of its free cash flow this fiscal year in dividends, compared to 86 per cent for Shaw.

At a time when many investors are interested in the possibility of dividend growth, that would give the nod to Rogers as having more flexibility to return money to shareholders.