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RCI.B.TO - Q4 2014 Rogers Communications Inc Earnings Call

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OVERVIEW:

Reported 2014 consolidated adjusted operating profit of just over $5B. 4Q14 YoY consolidated revenue growth was 4% and consolidated adjusted operating profit was $1.2B.

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PRESENTATION

Operator

Good morning, ladies and gentlemen. Thank you for standing by. Welcome to the Rogers Communications Q4 2014 results analyst conference. (Operator Instructions). I would like to remind everyone that this conference call is being recorded today, Thursday, January 29, 2015 at 8 AM Eastern time. I'll now turn the conference over to Bruce Mann with the Rogers Communications management team. Please go ahead, sir.

Bruce Mann - ***Rogers Communications Inc. - IR***

Thank you very much. Good morning, everyone. We appreciate you joining us. Here with me in Toronto this morning are Rogers President and CEO, Guy Laurence and our Chief Financial Officer, Tony Staffieri. We released our Q4 results about an hour ago. If you don't have them, they are available on the newswire or the Rogers.com website and the purpose of the call is to crisply provide you with a bit of additional color upfront and then we will answer as many of your questions as time permits. The remarks and discussion will undoubtedly touch on estimates and other forward-looking types of information, which ultimately could differ from our actuals. So with that, the cautionary language included in the earnings report and also in our annual report apply equally to the discussion on the call and are both available on the Rogers.com website. So with that, I'll turn it over to Guy and then to Tony both for a bit of additional perspective on the quarter and then we'd be pleased to take your questions.

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

Well, good morning everyone and thank you for joining us today. Let me say I'm pleased that we've made our overall guidance for 2014 and that we now have a shift in the trajectory of Wireless ARPU and network revenue growth, which is in line with the plans that we've set. However, before talking through the results in detail, given I've been here a year, I thought it would be useful to recap the overall scope of what was accomplished during 2014 so you can get a sense of where we are.

A year ago, I said that I viewed this as a multiyear journey to restore our performance back to an industry-leading profile. We have now completed the foundation year of that journey. During the first quarter of 2014, I undertook what was dubbed the listening tour, crisscrossing Canada, meeting stakeholders both internally and externally. In addition and importantly, we secured the beachfront spectrum in the 700 megahertz auction, which we are well along in the deployment of.

In late May, I shared with you that I would spend the latter part of Q2 and most of Q3 putting in place a more customer-focused structure. We created a separate customer experience function, a new enterprise business unit and reduced the number of senior management positions by 15%. Whilst we generated cost savings in the short term, I said we would reinvest those savings in key customer-focused areas and those investments are also well underway.

We strengthened our senior management team with key hires from Google in the US and Cisco in Canada and we announced just last week the new President of our consumer unit who will be joining us from Deutsche Telekom in early Q2. These are experienced proven leaders who bring global best practices, a customer-centric mindset and experience of dealing with complex regulatory frameworks.

In the fourth quarter, we turned our attention to executing on our 3.0 plan and introduced the first of the new commercial propositions focused on our customer base. NHL, Roam Like Home and shomi all launched in Q4. Although in fairness, most of them came in the second half of the quarter and will take time to feed into the financials.

During the past several quarters, as I disclosed to you before, we've moved away from using heavy discount price offers in order to attract and retain customers. We called this initiative a shift from volume to value. I said that these would cause vibrations in our figures, particularly in the customer metrics, but that we needed to go through this period and it would take some time.

So turning to this quarter, how should you interpret these figures? First of all, overall revenue growth was solid at 4%, which Tony will go into in more detail in a minute. Of particular note is Wireless network revenue and postpaid ARPU growth of 2%, which has come directly from our move from volume to value. Media revenue has also benefited this quarter from our investments in sports.

I'm sure you'll want me to comment on the customer metrics, which appear at first glance to be at odds with our financial success. During Q4, we stepped up our discipline in removing short-term pricing practices from our Wireless and Cable subscriber bases. We started tackling the practice of rolling forward various promotional and retention offers that portions of our existing base were put on in past years as band-aid solutions to more systemic issues, which we are now addressing.

In addition, our subsidy policies were adjusted to be in line with the economics of our customer lifetime value objectives. The strict and disciplined application of these commercial policies to new and existing customers impacted the subscriber numbers in the quarter, but this was expected and it was in line with our internal forecast. It's one of the vibrations that I told you you should expect.

To reiterate, you should continue to expect some degrees of vibrations on volume metrics in coming quarters, but also note that as we experimented with several of the changes during Q4, the subscriber metrics were actually improving on a year-on-year basis as we exited the quarter.

In summarizing the whole of 2014, we delivered what I said we would. We actually delivered quite a lot in one year. We have a new plan, we've reorganized the Company, we've infused new management where required, as well as empowered existing management with a more agile structure. We started the long journey to fix some of our fundamental execution issues and importantly we delivered on our financial guidance that we set out at the beginning of the year. That is a considerable achievement given the degree of change and the investment we undertook.

So where does that leave us? Well, let me remind you that Rogers 3.0 is a plan to reaccelerate our growth relative to our peers and progress will be measured over a series of quarters rather than overnight. The bottom line is we have put a lot of important change behind us, but we still have a lot of execution in front of us.

Looking forward to 2015, I fully expect that we will continue to see some good momentum on the key financial drivers and the resulting figures. The plan shows a gradual and planned improvement as the year progresses and Tony will talk to more of that in a minute. I would describe our 2015 plan as ambitious given the double cohort, but achievable. I don't want to share too much granularity of our plans publicly with our competitors, but I can tell you that you will see some meaningful progress in terms of revenue, brand, customer experience and how we go to market.

At the industry level, we have two spectrum auctions. I can't really comment on these given the industry Canada rules. There are also some key regulatory decisions in both Wireless and the Cable space that will provide clarity as to whether pro-investment facilities-based competition is still a priority in Canada. However, we are waiting for those decisions and our focus remains on execution. So I hope that brings you up-to-date and let me turn it over to Tony who will speak in more detail regarding the financials. Tony?

Tony Staffieri - *Rogers Communications Inc. - EVP & CFO*

Thank you, Guy and good morning, everyone. Let me quickly provide a bit more detail and color around the fourth-quarter results, as well as our 2015 guidance and then we can get to your specific questions. In Q4, we showed progress from a financial perspective when we finished the full-year 2014 in line with our guidance. Adjusted operating profit came in at just over $5 billion, Capex is slightly under $2.4 billion and after-tax free cash flow at just over $1.4 billion.

During the fourth quarter, we continued to generate solid cash flow and strong operating margins, building on the year-over-year trends you saw in Q3. Those trends showed continued positive movement in ARPU, revenue and cash flow reflecting our shift in focus from subscriber volumes towards subscriber lifetime values and bringing additional value to our customers in unique ways other than simply price-related.

In looking at our trajectory over the year, you'll see our consolidated revenue grew 4% in Q4, up from 1% growth in Q3 and from flat in the first half of the year. Overall growth was led by Wireless, which was up 3% and Media, which was up 20%. Adjusted operating profit was strong at the consolidated level, up 6% year-over-year driven by Wireless, which was up 4%, Business Solutions up 17% and Media up 59% offset by a modest decline at Cable where we ramped up service and customer value-related investments. And we accelerated the top-line growth at the same time as we delivered additional operating leverage with consolidated margins up 60 basis points to almost 37% reflecting productivity improvements we've put in place across the business.

At Wireless, Q4 network revenue was up 2% and improved year-over-year for the third straight quarter. In terms of postpaid ARPU, we saw the first year-over-year increase in seven quarters with a 2% increase versus a decline of 0.7% last quarter, a decline of 1.4% in Q2 and a decline of 4.9% in the first quarter. The reversal of that decline reflects our focus on lifetime value and discipline around pricing and promotions.

As I've described in previous quarters, our new roaming constructs have had and continue to have an impact on our Wireless revenue and ARPU profiles, but we believe we're headed towards the right value propositions for our customers in the long term. For this quarter, postpaid network revenue, excluding changes in roaming, would have been up 4% and postpaid ARPU, excluding roaming, would have been up over 3%. Total roaming revenues, both inbound and outbound, were down about 15% year-over-year and are now less than 7% of our Wireless network revenues.

This quarter, we launched our Roam Like Home value proposition for customers traveling to the US and it has shown some good elasticity in terms of customer adoption. I expect we will see this trend continue as we shift an increasing proportion of the subscriber base to Share Everything plans where customers are most able to take advantage of these value enhancements. We now have about 30% of the Rogers brand postpaid base on these Share Everything plans, which are increasingly accretive to our overall ARPU.

While there was an uptick in Wireless postpaid churn, which led to the reported negative postpaid nets in Q4, we can, as Guy outlined, attribute much of this to our increasingly disciplined execution around pricing, promotions and subsidies, not just in the market, but increasingly around how we manage our base with an eye towards overall customer lifetime value. And this is apparent when we look at the improving profile of ARPU and adjusted operating profit.

We're pleased with the trending we see when we compare the profile of new customers' ARPU compared to that of exiting customers' ARPUs in the quarter where the difference continues to widen. To be clear, we continue to expect to gain our fair revenue share of the market, but will do it in a very disciplined way. We also continue to manage the migration of consumer customers from three-year contracts to two-year contracts. As we exited 2014, only about 21% of our total postpaid base remained on expiring three-year contracts, which gives us an increasing degree of confidence that the double cohort impact coming up in mid-2015 will be a manageable transition.

In terms of higher value customer upgrades and additions, smartphone demand has remained strong as we activated 836,000 in the quarter, which is the highest number in two years and a 6% increase over Q4 of last year. And approximately a third of those activations were new subscribers to Rogers. I also want to quickly point out that our reported postpaid subscriber metrics do not currently include subscribers to our Wireless home phone product, which had a cumulative base of approximately

92,000 subscribers of which approximately 9,000 net new subscribers came in the fourth quarter. I point this out as effective with our reporting of results for the first quarter. We'll begin including these subscribers in our postpaid base consistent with our Wireless counterparts in the US.

In the quarter, we continued to demonstrate success around our cost management and efficiency initiatives in Wireless, which provided the operating leverage to drive adjusted operating profit growth of 4% with solid margin expansion of 90 basis points to 42.6% despite higher equipment sales relative to last year.

Turning to Cable, revenue was essentially flat this quarter balanced by higher Internet revenue, a bit of additional revenue associated with Source Cable, which was acquired in November and modestly lower TV and home phone revenues. Cable adjusted operating profit was down year-over-year on a 2% increase in certain programming costs and quarter-specific customer value enhancement investments combined with the impact of the year-over-year change in subscriber levels, partially offset by productivity initiatives.

The subscriber metrics were also somewhat softer in Q4 in part due to our pricing discipline that we began to implement in the Cable segment similar to what we've described for our Wireless business, but a lot of it is also due to the incremental loss of multiproduct customers, particularly as our main video competitor continues the expansion of their telco TV footprint with the associated competitive pressure on household bundles.

At our Business Solutions segment, the shift to and growth of on-net next-gen revenues continues to drive improvements in the financial profile. Next-gen revenue now represents 75% of total service revenues and grew 13% year-over-year. These were, however, more than offset by planned ongoing migrations away from legacy off-net revenues and you see this shine through in the 17% growth of adjusted operating profit in the quarter as the mix continues to shift to higher margin on-net business.

In our Media segment, you can see revenue increased 20% year-over-year largely from incremental NHL revenues. Excluding the incremental NHL impacts, the underlying Media segment on an organic basis would have been down about 2%. While we see solid growth in our Sportsnet and Radio divisions, these are more than offset by continued softness and structural shifts in conventional TV and print advertising.

We're off to a good start with our landmark 12-year NHL deal, which is performing pretty much bang on to our internal expectations. We added almost $100 million of revenue in the quarter and we'll break even from an adjusted operating profit perspective, but this was expected in the first portion of the season in our first year. We continue to expect the contract to be operating profit accretive for the full season with much of the margin being generated during the playoff period in the second quarter. Overall, Media's $19 million increase year-on-year in adjusted operating profit was the result of some solid cost-saving initiatives particularly in the television and publishing divisions.

So overall, on a consolidated basis, we reported adjusted operating profit of $1.2 billion, or a 37% margin overall. However, I think it's important to also highlight that these are extremely capital-intensive industries and while our operating margins are healthy, there is a significant amount of fixed investment that they need to cover. Our margin after depreciation and amortization landed at 20% in the fourth quarter and this doesn't include spectrum costs, which are not amortized for accounting purposes.

Turning to our consolidated results below the operating profit line, you'll see that adjusted EPS was unchanged year-on-year with a higher adjusted operating profit growth offset by higher depreciation and amortization expense combined with smaller increases in interest and income taxes, but clearly a good improvement from the trajectory we saw earlier in the year. Our free cash flow for the quarter of $275 million was up $166 million year-on-year, the result of higher adjusted operating profit, lower cash taxes and a more focused deployment of our Capex in a way that better spreads the work more efficiently across the full year.

Looking at the balance sheet, we ended the quarter with $200 million in cash and $2.6 billion in additional available liquidity consisting of $2.5 billion available under our bank facility and approximately $100 million under our accounts receivable securitization program. Leverage is at 2.9 times debt to EBITDA and down at 2.7 times when you give effect to the approximately $1.1 billion value of marketable equity securities we hold. We continue to focus on managing our leverage back down to within our target range below 2.5 times.

I'd also like to point out that Rogers continues to have a relatively low pension obligation deficit. The entirety of the deficit is relatively minimal in the $300 million range, which represents approximately 1% of our equity market cap and our expected incremental funding for 2015 is expected to be less than 1% of our free cash flow.

Turning to our 2015 guidance, we're expecting continued growth in adjusted operating profit. In the range we provided, we gave ourselves some room to manage around the double cohort effect later in the year and on Capex, the range we provided implies some potential incremental investments that could marginally take up our full-year Capex year-over-year. Overall, after-tax free cash flow is expected to be relatively consistent year-over-year at a substantial level of over $1.4 billion. Also, for 2015, we announced this morning a 5% dividend increase effective immediately to $1.92 per share on an annualized basis.

To sum up, I would say that Q4 was solid from a financial perspective with some good progress on the revenue line, combined with continued good operating leverage and discipline around capital spend together with driving operating profit, margin and free cash flow growth all at the same time. With that, let's use the remaining time to get into whatever questions you have.

Bruce Mann - ***Rogers Communications Inc. - IR***

Guy and Tony, thank you and operator, just quickly before we jump into the questions people might have, we will request to those on the call, as we do on each of these, that for the people asking questions if you could limit them to one question and one topic and then that way as we have a chance to have everyone participate, we can circle back to the extent you have additional questions and if not, we'll get them answered separately after the call, but that will give everyone a chance to participate in the limited time we have on what we know is a busy morning for everyone. So operator, if you wouldn't mind explaining quickly how you want people to organize the Q&A polling process and we will be ready to dive in.

QUESTION AND ANSWER

Operator

(Operator Instructions). Simon Flannery, Morgan Stanley.

Daniel Rodriguez - ***Morgan Stanley - Analyst***

Thank you and good morning. This is Daniel Rodriguez for Simon. A quick question on Capex. Can you outline the key Wireless and Cable drivers behind the Capex guidance for 2015? And quickly on the churn front, can you just outline the churn trajectory in 2015 in light of the more disciplined approach you're taking in the marketplace? Thanks.

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

Daniel, thanks for your question. In terms of Capex as we look to 2015 in both Wireless and Cable, as you would expect, it's largely going to be focused on network and in particular capacity and bandwidth capacity. For Wireless, the focus will continue to be on LTE. When you look at our LTE footprint today, population covered is now at 84%, which is up from 79% back in the third quarter. So good investment going on there.

When you turn to the Cable side of it, it will continue to be on a couple of things. Certainly on Internet capacity and as we bring our homes covered per node, we'll continue to bring that down to provide the bandwidth that we need, but also in customer premise equipment and in particular set-top boxes. Our NextBox 3.0 continues to be deployed aggressively and you ought to expect to see continued investment in that in 2015.

With respect to the churn profile, as we've talked about in our comments, what you're starting to see is the application of commercial policy and discipline in our base and that will continue into Q1. And some of the following quarters, but you ought to expect the impact to erode as we progress into 2015.

Daniel Rodriguez - ***Morgan Stanley - Analyst***

Great, thank you.

Operator

John Hodulik, UBS.

John Hodulik - ***UBS - Analyst***

Hey, thanks. Good morning, guys. A question on roaming. Obviously, it was down 15%. A lot had to do with the Roam Like Home promotion. Could you just give us a sense of how you see those trends playing out? I think it was a partial quarter of that offer. Does that get worse from here or as we go through the year, should you start to see improvement there? Thanks.

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

John, thanks for the question. A couple of comments in terms of roaming. It's important to keep in mind there are two dynamics that are going on. There's roaming that's happening with respect to the US and we're really pleased with the way the penetration or user adoption is working out for us, particularly with the new Roam Like Home plan; although it is early days. So I would say that piece of it is proceeding and we're probably close to the bottom of the U curve on that.

But the other dynamic is the international roaming side of it and we launched in the second quarter of last year our new construct for that. So we're only a couple of quarters into the international side of it and so it will continue to have an impact we expect for several quarters as we work our way through that. But as I said in my comments, the overall roaming revenue is now at a point where it's only 7% of total network revenue. So the impact on postpaid ARPU in particular has also come down to about 4% in total.

John Hodulik - ***UBS - Analyst***

Okay, thanks, Tony.

Operator

Richard Choe, JPMorgan.

Richard Choe - ***JPMorgan Chase - Analyst***

Great, thank you. Given your guidance and related assumptions, should we be looking for postpaid subscribers to be flat or down this year? As we work through some of the issues and focus on value, could Rogers get more aggressive maybe later in the year to reverse that trend?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

It's Guy here. What I would say is we don't give guidance on subscribers and you can't put subscribers in the bank; you can only put cash in the bank. Therefore, we're not going to lead the witness on that one, if you like. In terms of aggressiveness or not aggressiveness, again, we're not going to signal to the market. We believe in a disciplined pricing regime. Obviously, we have to be competitive; therefore, if competitors want to take actions, we may decide to follow them rather than lead them, but our focus is on disciplined top-line and ARPU growth that translates into respectable profitability.

Richard Choe - ***JPMorgan Chase - Analyst***

Great, thank you.

Operator

Adam Shine, National Bank Financial.

Adam Shine - ***National Bank Financial - Analyst***

Thanks a lot. Maybe one for you, Tony. We've talked very clearly about the discipline in terms of how the subscriber numbers evolve. Can you talk a little bit more about some of the moving pieces in the quarter in terms of the iPhone receptivity, any supply constraints you might have had and obviously acknowledging the bigger than usual spike in smartphone penetration up almost 7 points in the period and then I'll have one quick follow-up.

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

Sure, Adam. So I think a couple of things. As we look to the dynamics, I would say we're pleased with the way it's played out in terms of our focus on Share Everything Plans. So your question was with respect to smartphone, but it dovetails with our smartphone and much of what we've said around disciplined pricing. So I've talked about the smartphone metrics. As I said, we activated 836,000 in the quarter. Almost 80% of our gross adds came in on smartphones. So a good increase in penetration of smartphones. 84% of our cumulative postpaid base is now on smartphones. When you look at our customer upgrades in the quarter, almost all of it, 98% of the upgrades came in on smartphones. So that piece of it is working well.

When you turn to our Share Everything plans, which is another piece of it, again, over 60% of our gross adds on Rogers postpaid came in on Share Everything and so we're already at a point where 20% of our total base is now on Share Everything plans and that translates to about 30% of the Rogers postpaid base.

Adam Shine - ***National Bank Financial - Analyst***

Okay, great. And were there any iPhone-related supply issues at all to speak of and any momentum into the Q1?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So what I would say is the iPhone is obviously very popular and they had a lot of demand and therefore, you've got some spotty weeks where expected shipments got delayed and then turned up. You got two trucks the following day and all the rest of it, but I wouldn't describe it is a major factor in the quarter or in Q1.

Adam Shine - ***National Bank Financial - Analyst***

Okay, I appreciate it. And just lastly, Tony, in terms of the last quarter, you gave a split in regards to HSPA versus LTE dynamics or usage. Can you just update us on that if possible?

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

Yes. So as you would expect, we've seen good trajectory shift in that split. For the fourth quarter, roughly 60% of our data usage came in on LTE compared to about 40% on HSPA. Again, that's looking at volume of data usage. While in the past quarters, we've seen that sequential shift quarter-on-quarter be in the 5% range roughly, what we saw in the fourth quarter is that sequential shift jumped to 10 points. So good adoption on the LTE and data usage ramp up dovetailing with the increase in POPs covered that I talked about a moment ago.

Bruce Mann - ***Rogers Communications Inc. - IR***

Adam, it's Bruce Mann. Let me just add something really quickly to what Tony said. Two things. One is with respect to the penetration of smartphones this quarter and we do mention it in the MD&A, we began including what we call grey market phones or phones that weren't initially sold by Rogers, which historically we didn't. The trend doesn't change; it was just a little bit of a bump in the numbers in terms of why you saw that unusually high level of step-up. Then secondarily, to add to Tony's point on LTE versus HSPA, we're seeing the LTE base using almost 90% more data on a monthly basis than the HSPA subs and they are giving us around 30% more ARPU as well. So to support what Tony's saying, it's going in the right direction.

Operator

Bob Bek, CIBC World Markets.

Bob Bek - ***CIBC World Markets - Analyst***

Thanks, good morning. I just wanted to get some clarification on the Cable growth targets out there, low end sort of plus 1.5%, higher end more like 4% plus. Assuming the vibrations on the subscriber side, we're still going to see negative RGU for this area. Can you talk a bit about what's driving that confidence in the numbers? Is it pricing? Is it pricing discipline as you focus on value? Is it usage? Any clarification on -- I suspect Source Cable gives a little bit of a positive, but anything else you can add to here as far as what's driving the growth? Thank you.

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

To be honest, it's all of the above. You kind of answered your own question.

Bob Bek - ***CIBC World Markets - Analyst***

I love when I do that.

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

I think that part of the problem when you're looking in on companies like ours is you tend to assume all the base is the same, but actually you've got multiple cohorts within the base that behave different ways and there are opportunities to trade some of those cohorts up to larger packages. You see opportunities for other cohorts that maybe have lower speed band wanting to move to higher speed band. You have customers who have been used to entertaining a series of promotions over years that when they find out they are no longer available, they leave you and the art is in managing that mix. But I think where we're focused is very much on shaping is being disciplined in our execution and shaping our propositions in such a way that people feel confident in the product and willing to trade up over the long term. And that's where our efforts are going and it takes time to address the different cohorts with different offers.

Bob Bek - ***CIBC World Markets - Analyst***

Thank you, Guy.

Operator

Glen Campbell, Bank of America Merrill Lynch.

Glen Campbell - ***Bank of America Merrill Lynch - Analyst***

Yes, thanks very much. Guy, I wanted to follow up on your last answer there. I'm seeing there is a trade-off you're making on customer retention between principal and pragmatism where you're wanting to stick to your guns on pricing. It makes a lot of sense, but if you're facing competitors who are willing to do two-year deals to attract customers on the Cable side, is the view that you're going to stick to your guns on retail pricing and not do the retention discounting thing or would you describe your approach as being more pragmatic? Can you give us a little help on that?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

I would describe it as being more pragmatic. So of course, you set out with a set of principles on a Monday morning, but you also have to look at what's happening in the high street and if you see activity that takes you beyond your level of confidence then you react to it. But all the while, my belief is that you should continue to innovate and develop your products to get to a point where the necessity to intervene because of that activity is reduced. And since I have a long-term perspective, that's where I'm focused, but if I need to, I'll react. It's as simple as that.

Glen Campbell - ***Bank of America Merrill Lynch - Analyst***

Thanks. And a follow-up on that, on the Wireless side, one could make the argument that Q4 is actually a bad quarter to try to grow because the level of subsidies and devices spikes up and that maybe we should see your results in that context. Is that a fair observation that there are better quarters to try to grow or not?

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

No, I think that's a good characterization, Glen. With the higher volumes that happen in Q4, I think what you see when you look at our subscriber metrics is a magnification of the principles that we're trying to apply both in our base, as well as on the acquisition side.

Glen Campbell - ***Bank of America Merrill Lynch - Analyst***

Okay, thanks very much.

Operator

Greg MacDonald, Macquarie.

Greg MacDonald - ***Macquarie Capital Markets - Analyst***

Thanks, good morning, guys. Guy, I think nobody's going to argue with the focus on profit, but the questions that I get from investors are the risk of sustainability on growth of ARPU alone. So when I look at the market potentially -- well, fully funded WIND, potentially very spectrum rich WIND seems to me like there's a very real scenario where we inevitably go to a pricing environment in Canada, kind of $50, 5 gig, similar to what we've seen in the US and that's a market I'd point out that both AT&T and Verizon have responded to on price.

I wonder if you might comment on the strategy overall on a couple things. Number one, do you assume that WIND is dead on arrival, first of all, that I'm wrong in my assumption that the market could go to $50, 5 gig? And then second, what does the negative 17% gross add result tell us about whether Rogers is losing share to Bell and Telus or this is an overall industry decline? What is the bigger impact there? Is this a share loss issue or is the overall industry declining on gross adds?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So it's not for me to comment on WIND. You probably need to ask their CEO what his strategy is. With respect to the US market, what I think you see is a substantial lack of innovation and propositions. So when you have -- when customers can't see the difference between brands then they resort to comparing via only price and at that point, it's a bit of a downward spiral. What the US carriers have been focused on is extension of their coverage in their network and also their distribution and in the market for smartphones and ensuring penetration of that. When you're in that kind of gold rush, you don't tend to focus on differentiation, you tend to focus on execution of those metrics.

So as the market matures, what happens is there is a need to -- in a market where there's not differentiation created by the operators, you'll always default to price. My philosophy is we can create differentiation and therefore, I don't see us going down the route or certainly from my perspective down the route of where the US market is going. So I probably have a far more optimistic view of the world than you do.

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

And add to that the 17% decline in gross adds that you see in the fourth quarter. I wouldn't read any long-term trends into that. If you were to go back and look at the course of the last several quarters, while we had less of a decline in Q3, we were at a 17% decline in the second quarter. So I think it's more a function of the specific pricing and promotions that are put out there and how we've approached it this quarter.

Greg MacDonald - ***Macquarie Capital Markets - Analyst***

And Tony, just to be clear, is this quarter where you lost share? Is that reflected in the 17% or do you think this is an industry thing because of the increase in prices in late 2013?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So I think no one should judge what happens in one quarter and since neither of our competitors have released their results yet, I don't think we should comment further on it.

Greg MacDonald - ***Macquarie Capital Markets - Analyst***

That's fair.

Operator

Jeff Fan, Scotiabank.

Jeff Fan - ***Scotiabank - Analyst***

Thanks and good morning. I want to follow up on the last question and, Guy, your comment regarding innovation and differentiation. Since you joined, there's been a number of new products that have been launched -- the NHL, shomi -- as you talked about. Can you talk about -- are those the products and services that we expect to see that will differentiate Rogers? Can you just elaborate a little bit on perhaps areas that we should be looking at to assess how Rogers or whether Rogers can differentiate against your competitors so that we can have some sense as to the pricing scenario that Greg mentioned is not something that we're probably going to head to?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

Yes, that's a good question. So let me just take a bit of time to go through this one. So first of all, you create propositions, let's take shomi or NHL or Roam Like Home, and if you take those three examples, the first one launched on October 8, the second two were in November as I remember -- so actually they've been in the market very little time. So what happens, you have a proposition, you put it into the marketplace and you start advertising it and over time, the awareness of the product builds up.

The next thing you get is adoption of the product, which then leads to penetration providing it's something that the customer values and then they've got the product, they are using it. Then it has to feed into their view of whether affects their overall -- their total value for money of what they are getting from a provider and then it has to influence their behavior.

So back to your question, what I would say is the kind of innovation I'm talking about is certainly in the style of the things that we launched in Q4 and you would expect to see more of that kind of thing coming out across the course of 2015. The thing you have to work out in your own mind is the rate at which you'll get penetration. You get penetration on multiple products, so one customer might take two or three of the different propositions and at what point that affects their behavior in relation to their propensity to churn. At the same time, however, those products and propositions are actually positioned towards the higher end of our pricing matrix and therefore, as customers do adopt them, what the earliest indicator you start to see is ARPU.

So depending on whether we position the kind of proposition to be attractive, the number of propositions we have and the pickup in penetration rate, that will affect the rate of ARPU increase and then, secondly, it will ultimately affect the basis on which they stay with us or go to another operator. So I hope that kind of puts a bit of color around it.

Jeff Fan - ***Scotiabank - Analyst***

And just a quick follow-up, is it fair to assume that it's going to be a culmination of a number of things and we're not looking for you guys to come up with the magic bullet with one big product? It's going to be a combination of various things?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

That's absolutely right. Having said that, if you do have the magic bullet, if you could just email it to me, I'd be very grateful. I'll take that as you don't. Okay. No, no, seriously. Think about your own behavior as a consumer in this regard. Think about the fact that if you're working with -- if you're using a particular company's brand and over time you start to see more and more benefits of using that brand because they are adding value into what you're receiving then what you see is a subtle shift in your own relationship with that brand and your behavior to that brand and your willingness to spend more with that brand. So actually what I'm suggesting here is nothing more than what you yourselves as individuals experience in using products in different sectors.

Operator

Phil Huang, Barclays Capital.

Phil Huang - ***Barclays Capital - Analyst***

Maybe a question for Guy. Just wanted to dig a little deeper on how you expect your volume to value strategy to play out this year. The Q4 financial metrics and 2015 guidance are quite encouraging. Obviously, the subscriber decline was the compromise. If competitors begin to take advantage of your strategy shift to accelerate their marketshare gain, at what point do you say we need to fight back a little harder even if that means some sacrifice on margins? And in terms of your Wireless subscriber volumes, are you seeing bigger marketshare movement in one region versus another or pretty evenly spread across the regions? Thanks.

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

To be honest, I'd have to go back to the answer I gave to Glen. So rather than repeat it, I think I should stick with that answer. With respect to regions, you always see shifts in regions because you have other operators -- not all the competition is consistent in every province and therefore as different operators dial up and down their activity, so you see variations in subscriber metrics, for instance. Less so on ARPU, I would say. ARPU does vary by province obviously, but in terms of our trajectory and growth aspirations, they're proportionate to whatever is in the region. So there's nothing in Q4 that I would highlight as being particularly material in that respect.

Phil Huang - ***Barclays Capital - Analyst***

And maybe just a follow up on the first part of my question, on the Cable side, subscribers similarly saw the vibrations as Wireless, but I guess unlike Wireless, Cable revenues and EBITDA didn't see as much support from the strategy shift. Maybe can you talk about how your strategy may be different here?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

That's a good point. That's a good question. So to be honest, just from being honest about the realism of changing a company this size is you start where the need is greatest and then you move onto the next greatest need and so the work on the Cable side was not as far progressed as Wireless up until quite recently, but interestingly I would say our focus right now is as much, if not higher, on Cable than Wireless in relation to creating propositions and dealing with some of the underlying issues. That doesn't mean to say, by the way, that somehow there's going to be some magic shift in trajectory. You should view the evolution of Cable probably as not dissimilar to Wireless, although there are some differences.

Operator

Vince Valentini, TD Securities.

Vince Valentini - ***TD Securities - Analyst***

Yes, thanks very much. Maybe a good segue from that is Business Solutions and where that fits in the focus list versus Wireless and Cable. The revenues were down 1% in the quarter. I know the next-gen revenues are up 13%, but are you seeing as much of the momentum that you had hoped to see in that area, Guy, seeing a market that's somewhat underserved where you could take marketshare or is there still a lot more to come and maybe you can talk about some expansion plans for 2015?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So when we created the enterprise business unit, we announced it at the end of May. We actually had a number of different groups working on enterprise scattered across the business and we had to bring them together and create one unit. The leader of that unit, Nitin, only joined us in December and only completed induction at the end of December. So what I would say is a little bit tying back to the previous question is that we focused on getting a good grip on Wireless and we see that feeding through to the financial metrics this quarter. We are well underway with our planning work and strategy on Cable and with a high degree of focus on Cable and probably I'd put business or enterprise the last of that list in terms of the fact that -- we're doing that work now.

So you really shouldn't see or expect some fireworks in the enterprise side immediately and even when we do engage with the market and start our work, it's more of a steady progression that is solid rather than just trying to get fireworks for the sake of one quarter.

Vince Valentini - ***TD Securities - Analyst***

Thank you.

Operator

Dvai Ghose, Genuity Capital Markets.

Dvai Ghose - ***Genuity Capital Markets - Analyst***

Yes, thanks very much. Guy, when I look at the 5% increase in the dividend, I'm sure everyone's very happy to see that, it's a very healthy yield, but, as you know, since 2010, free cash flow has fallen every year at RCI, albeit in part due to cash taxes and other extraneous events, but nonetheless they are cash items. Your guidance is flat in terms of free cash flow essentially for 2015, which would be a good achievement, but nonetheless do you find this obsession in the market with dividends and dividend growth to be healthy or a major constraint when it comes to trying to do what you want with the business? And with the changes that you expect in 2015, do you think we will be in a position for free cash flow growth from beyond this year?

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

Dvai, it's Tony. I'll capture most of it. When you look at our dividend growth -- well, let me start with our capital allocation. We've been very consistent and what we said is job one is to grow cash flow, free cash flow on a consistent, sustainable basis and this year has been a transition year in a number of respects. So what you see, particularly in our Capex line as it increased slightly year-on-year, is that focused investment. We'll continue to make the right acquisitions and for the most part, they've been tuck-in and our largest capital expenditure has been on spectrum, which is critical as we look at it over the long term.

So nothing there has changed and then to the extent there is cash left over from that, we will then have a very balanced view of return of cash to shareholders. The last little while, we've steered away from share buybacks as we're focused on reducing our leverage on the balance sheet from where we are today and to focus it to get it back down to under 2.5 times. We will augment that with dividends.

In looking at dividends, we're looking at two things in our view. One is what does it look like in terms of our long-term outlook and to the extent that we long term have a view that cash flow will increase then it makes sense to increase dividends. And two, and it really gets at the sustainability, what does our payout ratio on free cash flow look like? And when you look at our free cash flow for 2014 payout ratio, we came in at about 65%. When you exclude the one-time cash tax items that aren't representative of long-term cash taxes, we come in at under 60%.

As we model it out for 2015, again, as we adjust for cash taxes, which really is the only single biggest item besides Capex that's increased significantly over the last few years and that's just as a result of our operating loss carryforwards for tax purposes having been used up. So when you take into account recurring cash taxes, our payout ratio for 2015 continues to be at a relatively conservative number and in line with what you saw in 2014. So I would say the dividend is really part of our strategy and not necessarily as a result of any type of pressure that we see out there for a dividend increase.

Dvai Ghose - ***Genuity Capital Markets - Analyst***

Yes and just as a quick response, Tony. I believe 2015 is the last year of unusually high cash taxes and we normalize in 2016. I just wanted to confirm that's still the case because that by itself should obviously help in terms of free cash flow growth on a post-tax basis.

Tony Staffieri - ***Rogers Communications Inc. - EVP & CFO***

No 2016 is the last year. To be helpful, as I said in the past, our cash taxes as a percentage of adjusted operating profit has been sitting at about 12% and we've been doing a fairly good job of bringing that down. And so as you look at it long term, we see cash tax as a percentage of adjusted operating profit as we exit the one-time items to be in the 10% range.

Operator

Maher Yaghi, Desjardins Securities.

Maher Yaghi - ***Desjardins Securities - Analyst***

Yes, good morning. Thanks for taking my question. Guy, could you give us your view as to how much of the effort to reprice or shed low profit customers in the Wireless business has been made so far? And would it be fair to say that you might have pulled back maybe too much in the second and third quarter and that had a disproportionate impact on Q4? As you mentioned before, you're going to test the market and is it fair to say that maybe you pulled too much? And in terms of Rogers 3.0, you made the significant proposition that you wanted to grow revenue for Rogers over the long term. Could you share with us your views as to revenue growth potential for 2015, which was not provided in your guidance today?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So I'm not sure how many questions there were underneath that. So on the first part though with respect to pulling back, did we pull back too much in Q2, Q3? No, I don't believe we did. So we have a long-term strategy. We've been very clear about what our long-term strategy is. We've said that there will be vibrations in a number of metrics, but we said we're focused on revenue growth and that's what you see. So I'm very comfortable with the way that we've performed within the market during last year. We'll continue to experiment, which is why we said there will be vibrations in the subscriber metrics. What you see is a better trajectory on the revenue and AOP metrics and that's our strategy.

In terms of your second part of your question, which was how long will it take to play through, well, as you know, customers come up for contract renewal -- if they're in a two or three-year contract, it takes two or three years for them to come up and we have to make sure that we are presenting compelling propositions in front of them at the point that they do, but it will take at least another year to play through completely through the base just by virtue of the length of the contracts.

Operator

Drew McReynolds, RBC.

Drew McReynolds - ***RBC Capital Markets - Analyst***

Yes, thanks for taking my question. Most of mine have actually been answered. Just maybe a follow-up on data growth. And Tony, I think you gave some good statistics around LTE and the increase in data consumption on LTE. Just wondering, just tying this into shomi and NHL GameCentre LIVE, I know it's still early days, but to what extent are you seeing an uptick in your data growth on the LTE network related to that increased video streaming? And with respect to what you've seen to date, are you comfortable with your network performance supporting that type of data growth as we look forward?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So if I might pick that up, so we're not going to reveal exact figures on that, but I would describe myself as extremely satisfied in terms of the data consumption associated with the propositions we're putting in the marketplace.

The second thing is I have a small paranoia over making sure there is sufficient network capacity there when we introduce these things because there's no point in putting a huge amount of work into creating a proposition only to find out that your customer can't benefit from it. So way before we had solidified the proposition such as NHL, which launched October 8, we actually put in place plans to increase our network capacity and they continue apace so that we stay ahead of the curve.

Drew McReynolds - ***RBC Capital Markets - Analyst***

Thanks, Guy.

Operator

Robert Peters, Credit Suisse.

Robert Peters - ***Credit Suisse - Analyst***

Hi, thank you for taking my question. Just actually kind of circle back in terms of building out capacity, but talk maybe more on the Cable side of things. We saw earlier this month at CES the debut of a number of affordable 4K TV sets and some services in the US have announced plans to explore broadcasting 4K content and streaming 4K content. I was just wondering if you could talk in terms of how you see your network in relation to having the capacity to handle 4K or if there's any more additional investment needed?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

Good point again. I would say the evolution of 4K is one of the contributors that goes into our capacity planning models and I was at CES as well. There's nothing that I saw that would take me beyond the assumptions that we've already got in our plans for 2015. I do think the evolution of 4K and things like this will drive demand and then, of course, it becomes our job to monetize that, but I do believe that we've anticipated that in our capacity planning and there is no change of course I need to make as a consequence of what was at CES.

Operator

Tim Casey, BMO Capital Markets.

Tim Casey - ***BMO Capital Markets - Analyst***

Thanks for taking the question, Guy. I want to push back a bit on your contention that you can compete against the rollout of Fibe by just -- by not having to rely on price. The innovations you've introduced, I think one could argue that they are also innovating and some of their products are priced lower than yours and whatnot. How confident are you that you can still maintain your share of the traditional cable market given that they are not standing still as well?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

Well, you have seen that what we've introduced in terms of innovation thus far are not the only things we're going to introduce and that wouldn't be a fair assumption. By the way, I'm not saying that the competitors aren't innovating. When I was talking about innovation earlier, I was talking more in answer to the question about whether we are likely to see the commoditization that you're seeing in the US as the result of a lack of innovation. So there is innovation in the Canadian marketplace and it's our job to be more relevant and more attractive than others. Thus far, in terms of what we've launched, we're talking about a small number of propositions that launched in the middle of Q4. We have a full roadmap for 2015, so we'll have to see how this plays out, but I wouldn't -- I understand why you're saying should you be pushing back, but I think you've got to again look at this in light of where we are in the process right now and we have a lot to unveil yet.

Tim Casey - ***BMO Capital Markets - Analyst***

As a follow-up, is there any more light you could shed on the path to IPTV at Rogers?

Guy Laurence - ***Rogers Communications Inc. - President & CEO***

So as I said in the previous quarter, we are targeting to have a beta product ready for the end of the year. IPTV as a roadmap is a difficult technology to introduce and get the user experience right, but there is considerable focus on that as there is on cable in general. And therefore, I have nothing more to update you on other than it's still very much in the labs and it still very much has a large team dedicated to it.

Tim Casey - ***BMO Capital Markets - Analyst***

Thank you.

Bruce Mann - ***Rogers Communications Inc. - IR***

All right, well, this is Bruce Mann. I just wanted to, first of all, say thanks, operator and more importantly to the management team at Rogers wants to thank everyone for joining us on the call this morning and investing a bit of your time during what we know is a busy morning. If you've got questions that weren't answered on the call, please feel free to follow up with myself or my colleague, Dan or Bruce. Our contact info is at the end of the earnings release and we will get your questions answered for you. So thank you very much. This concludes today's call.

Operator

Ladies and gentlemen, this does conclude the conference for today. Thank you for participating. You may now disconnect your lines.