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Rogers Communications, Inc. (RCI)

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CORPORATE PARTICIPANTS

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

MANAGEMENT DISCUSSION SECTION

Unverified Participant

I think everybody knows Tony Staffieri, the CFO of Rogers. Welcome, Tony. Thanks for coming.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

Thank you for having me and us.

QUESTION AND ANSWER SECTION

Q

Tony, let's get right into it. What's your assessment of the wireless market these days? We're in another seasonally busy period, back-to-school quarter. What's happening up there in wireless?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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I'd say generally, it's been a good gradual progression to – of increasing growth. We started off, I would say, the first half of the year, what we saw is a continual increase in the rate of growth. And as we look to the activity in Q3, particularly around back-to-school, I would say the growth rates seem, our read on it, flattish to the rate of growth we saw last year which was a pretty good rate of growth, maybe slightly down but a continuation of the progression that we saw throughout the year.

So, it's a good backdrop, and I think it really speaks to the fundamentals that have driven growth in the past that continue to be there, first and foremost, the penetration rates in Canada still sitting at, we estimate now, 88%-89%, but still well below where other countries are at. In the U.S., for example, at over 120% rate of immigration, the backdrop of GDP. All those things that have contributed to subscriber growth continue to be there. And it's sort of lending itself to good growth in the industry, notwithstanding what I would call a period in Q3 where we've gone through a change in pricing strategies. We launched the unlimited Infinite plans towards the end of the second quarter. And I would say, the adoption of our plans in the industry still have vibrations in them in terms of subsidy or no subsidy and all the way through. And so, it's a bit of a noisy quarter. But I think as we continue to work our way through that, I think all the ingredients are there to look to continued growth in the rest of the third quarter and fourth quarter.

Q

You led the way in the new pricing plans. They were still fairly fresh the last time you guys made public comments, right after the second quarter release. And at that time, you said you had more people trading up and down essentially. What's happened [ph] over in the three months (00:02:26) here?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

We're really pleased with the success we've seen to-date. Today, we're now approaching almost 750,000 of our subscribers on the new plans. So, the rate of migration and acquisition on the new plans has exceeded our expectations. So, it's been very good. We had talked about earlier, at the right time, we may do things to incent set the market to try to migrate. And that's been happening on its own. So, we're really pleased with the way that's been going.

In terms of upgrader versus downgraders, I think we're getting what you would expect that even more are upgraders than downgraders. I quoted before, two-thirds of our customers were upgraders. And that's really what we wanted to have happened was those customers in the CAD 45 to CAD 65 price point would migrate up to CAD 75 entry point on unlimited for the sake of certainty, etcetera. And that's actually even increasing beyond that. So, it's still roughly a two-thirds/one-third. So, one-third, downgrade; two-thirds, upgrade. But even more so on the upgrade side.

And so, what we really like in terms of what we're seeing when you look at the underlying MRC, so put aside overage revenue for a moment and I'll come back to that. But what's the true underlying MRC that we're seeing net of those two aspects. And we continue to see really good MRC growth in the 1% to 2% range. So, that's a really good fundamental that we like.

And then, as we look to the metrics that ultimately get a churn in usage, very good there. If we look at likelihood to recommend on the new plan including, in particular, value for money, the metrics are up over 50%. So, really good customer acceptance and satisfaction with them. If you're to look at our operating metrics and, in particular, the call center, what we see is much fewer calls. So, in the past, once customers made a price plan change, it wasn't uncommon for customers to call back and tweak the change to the plan. What we're seeing is those follow-up calls for further changes to the plan are way down, significantly down. What we're finding is calls to the call center in general are way down. The length of time on the call is much shorter. And so, that's coming in better than expected. And importantly, what we measure as first call resolution, so getting it right the first time, is way up. So, when we look at those types of metrics, we're really pleased with what we see.

The faster adoption than we expected, what it does mean is that that overage revenue that we knew was going to go away. That decline is happening faster than we thought. So, the total quantum is still the same, but we're moving customers on to Infinite a lot faster, which is a good thing. So, previously talked about our anticipation would be that we were through a period of six to eight quarters of migration. Our thinking now is, probably in about four quarters and maybe five quarters, we'll be through this. And so, in the very short-term, what you'll see is overage revenue decline faster than we thought. But those underlying fundamentals are improving faster than we thought as well. And so, if you sort of think a year out from now, the majority of the Rogers base will be on Infinite plans which have a starting point at CAD 75. And that compares very favorably to our average ARPU today of, as you know, CAD 55. So, all the metrics and indices are indicating very good success with it.

The one piece of that we're still hoping settles out is really the hardware subsidy piece of it. If you look to competitive intensity this quarter, I would say some par to last year when it comes to hardware subsidies and promotional things like gift cards. But what we don't have is MSF or recurring revenue discounting through data bonuses and that type of thing. So, in that way, the market, I would say, is less competitive on that side of it in terms of connectivity revenue, but we see about the same level of hardware discounting.

So, the strategy when we launched Infinite was to really balance the economics of good value on the connectivity side, and balance that with lower hardware subsidies. And I would say, we're disappointed that that piece of it hasn't come in as quickly as we expected. A couple of our competitors have really stuck to the subsidy model. And so, we're disappointed with that. One of our competitors, so much so, that they've given away CAD 1,000 phone. And so, when you subtract that from the MSF, you're left with ARPU's that we just don't get in terms of lifetime values, and maybe those aren't sustainable and they aren't long-term anyway.

So, and as I said at the outset, we're optimistic that as we work through the busy period and towards the end of the year that you'll see a migration out of reliance on the subsidy model and more indexing to equipment installment plans, which we think fundamentally are just a better balance of economic for us and for the industry.

Q

One of the nuances of the EIPs, equipment installment plans, was the 24 and 36-month. And you had initially said customers were very responsive to the 36-month. It saves them a little money every month. And then, CRTC has kind of pushed back on that. They're reviewing it. But how are you thinking about EIPs, notwithstanding the competitive pressures from the subsidy model?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

The appeal of it, if you focus on the premise of customer affordability, the subsidy model and we've talked about this before was really something that was invented when hardware costs were CAD 200 to CAD 300. And as they've now escalated now well beyond CAD 1,000 or I'd say an average of about CAD 1,500 per device, the subsidy model sort of breaking down and it makes it confusing for consumers and small businesses. And the affordability piece starts to fall apart.

And so, we thought 36-month was a good clever solution aimed at customer affordability. While it was in market, the majority of customers were moving to that. So, we're disappointed that the government put a halt on it until they review it. Nonetheless, we stay focused on that customer affordability metric we just introduced over the last two days. It now includes upfront taxes. So, we'll amortize that over 24 months. Again, aimed at customer affordability and penetration of smartphones. And we think it's good for that.

We don't think that removal of 36-month has had a big impact on volumes in the sense that the hardware subsidy is still a market that sort of compensated for that, we think. But we are hopeful that as the government looks at this, it really is a win-win for consumers and small businesses.

Q

Do you think it will get, you think, pushed into the overall wireless review or you're expecting clarity on this prior to that?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

We don't know. They've asked for comments for the month of October. And so, we perhaps aspirationally read into that they're going to look at this a bit quicker than the full review. And as I said it's something that is in to the benefit of customers. And so, we're hopeful but we really don't know.

Q

Okay. And maybe just sticking on the regulatory side for a moment. And what are your thoughts on the wireless review and the analysis of MVNOs? And what's going to shake out of the hearing next January?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

I think it's important to always remind ourselves, this was really part of a regular five-year review. That was slated in this five-year review includes a look at MVNOs. I think we take comfort in the fact that this government, for a very long time, has been very focused on facilities base competition. And we think, it's important we think they will take a look at that investment cycle. I think numbers are out there that, over the last 10 years, the industry invested almost CAD 70 billion in infrastructure. Collectively, we employ 120,000 across the country, and probably double that indirectly through various suppliers. So, a big part of the economy, and it's been privately funded infrastructure investments. And I think that's healthy for the country, and healthy for the industry, particularly as we embark on the eve of 5G investments. So, we're optimistic that that all gets factored in.

In terms of specifically on the MVNOs, we still sort of scratch our heads as to the problem it would solve. We think we have – we see very healthy competition. We have four well-capitalized players in each of the markets, and over 10 brands in each of the markets. And so, we continue to see healthy competition, if you are to look at pricing. On a per gig basis, it's come down considerably over the last several years. We look to our neighbors in the U.S. and they've moved to three facilities base competitors with no mandated MVNO, and seems to be a healthy market there and healthier with industry consolidation.

So, I'm not sure the problem they're trying to solve. At the same time, the government's done a lot to subsidize the fourth player in the country, whether through set aside non-spectrum, mandated roaming. And so, they enter to contemplate MVNOs that are really going to impact those players the most sort of seems contradictory. And so, we hope all of that is factored into the mix. And as I said, the importance of facility base seems to be a mainstream, and we'll see how it plays out.

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And maybe, let's touch on 5G, it's a segue out of the regulatory. Because obviously, there's going to such profound changes to the industry. Your national competitors really highlight their fiber footprint. [indiscernible] (00:13:28) 5G. How is Rogers conditioned for 5G and [indiscernible] (00:13:32)?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

We're extremely positive on where we sit network-wise. I'll start with our investment into 4.5G on an all-Ericsson network, where we ended up being well timed both in terms of selecting Ericsson a few years ago before these issues sort of emerged. Then, we went with Ericsson for a number of reasons. But we invested in 4.5G equipment

that's upgradable to 5G. And so, the timing and the investment worked out well. We just went through the 600 MHz spectrum auction, which is foundational spectrum for 5G. And we're extremely pleased being the only national carrier to get 600 MHz spectrum in every province and territory, including some additional spectrum in southern Ontario. And so, that foundational spectrum position, extremely pleased with.

Now, as we look to auctions coming up and spectrum that's needed for 5G, 3,500 next year. We already sit with 30 MHz. And most technical folks would tell you, you need 50 MHz to operate a 5G network. And so, we're entering the auction from a position of solid strength. So, from a spectrum perspective, we see that as a big positive.

We continue to believe that having a national network is going to be a competitive advantage as we go through 5G. Certainly, there will be, as you're starting to see in the U.S., a pick-up of the consumer upside. And we think there is a place where consumers will pay a premium to move to 5G. But I think most would agree that the upside is really going to sit on the enterprise side. And so, our ability to have a national solution and target investments across the country for a particular enterprise solution is going to be a competitive advantage. And keep in mind, it's not just towers. But as we move to edge computing, owning the real estate at the base of the towers are going to become increasingly part of the solution for 5G. And so, having that complete ecosystem is important. And it's really – I often get asked about how we think about selling towers. It really does point to 5G, owning towers is a big competitive advantage. And so, we continue to focus on that.

In terms of fiber footprint to support that, we've always had a healthy position and continue to make the investments needed. But that's working really well and just working through it. I think one of the things to keep in mind is the technology around small cells continues to evolve. We were just – when you look at the thought not too long ago was every small cell would have fiber fed to it. Well, the new technology is not necessarily cell. It might have the first one that then repeats off the other small cells. So, it's more about power necessarily than fiber. So – and, of course, microwave will continue to be a good solution, cost-effective solution. So, I think all that put together, very optimistic about our roadmap for 5G.

Q

In terms of networks and spectrum, you generally go it alone. You do have a network sharing arrangement in the province of Quebec. How are you thinking about that as we move into 5G?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

I think not dissimilar from what you heard before. We think – and the comments I just made. Owning a national network, we think, is important in a 5G world. I think the complexity of tower ownership combined with the spectrum, because it's more than just broad-based distance spectrum, you're into short wave 3500, 2800 the year after that, and then 3800 after that.

So, having a partner that brings in the right amount of spectrum is important. And I don't know that we just don't see us having to rely on a partner's investments in spectrum and a partner's balance sheet as the right approach to something like networks, which are so fundamental to this industry. So, we'll always look at potential network sharing arrangements, but we just don't see the economics making sense, particularly in a 5G world.

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Did we infer from that that you're willing to go it alone in Quebec then?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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I think there are things between us and Vidéotron that are mutually beneficial. And out of respect for our partner, I wouldn't say much more than that. And I think they probably see it the same way. And so, as we look to our respective agreement, I think we'll move to something that ends up being a win-win for both of us.

Q

All right. Let's move over to wireline now. Ignite has been in the market for around a year, maybe a little more commercially. It was initially launched with a very hands-on sort of premium focus. How is that go-to-market strategy evolving now that you're down the road a year?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

Extremely well is the summary. As you said, we launched it carefully. We wanted to toggle demand and deployment of it to make sure we got the product right. And we're now sort of at full scale. And it's coming in nicely. The customer response has been terrific.

Strategically, still has a lot of upside for us. It's a product [indiscernible] (00:19:47) familiar with it. It's the Comcast X1 platform, but the IP-based version of it. And so, it's a terrific transitional product from what we would describe as conventional TV linear streaming to something that integrates OTT solutions very ratably. And so today, we have, as you know, Netflix and YouTube. Very soon, we'll have Amazon Prime. And the roadmap for product integration picks up from there. And so, as other OTT players enter Canada, it'll be integrated into the product with the voice search metadata, etcetera.

And so, the product response has been very good. If we were to look at all the metrics in terms of what it does for our food and ARPU and ARPA for our Cable business, we continue to see good upside on that. We expanded it, specifically to your question, you can now get the product with those tiers of internet speeds. And so, it is moving into volume very quickly.

We had talked about stop selling legacy towards the end of the year. I think we may have moved that up because of the success we've been having with it. And I've touched on the revenue side of it. But the cost piece of it is also coming in extremely well. We see churn down on the new product, which is what we hoped and are seeing that come in. On-demand purchases for video are up, and so that's a good sign. But importantly, CPE and install times have come way down relative to our legacy product, and relative to this product when we first launched it a year ago.

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Yeah.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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And so, all those metrics are coming in nicely. But again, it's important to reiterate that this product was always about supporting the whole Connected Home strategy, which is really centered around Internet.

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Yeah.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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And the Internet is really the driver of the Cable business. And so, overall, exceeding expectations.

Q

One of the metrics the Street will look to for progress on this – on Ignite this capital intensity on the wireline side. What's the messaging there?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

Capital intensity on wireline is coming in better than we expected. You saw in the first half of this year, we brought capital intensity down 29%. And you ought to expect capital intensity for the back-half of the year to be about the same. We had communicated previously that, by the time we exited 2021, so into 2022, our capital intensity would be in the 20% to 22%. And Cable cash margins would be in excess of 25%. If you look at the first half of this year, our Cable cash margins were at 19%; and capital intensity, as I said, down to 29%. And as we look to next year, we see further good declines. And so, relative to that benchmark we have put out there, we're tracking ahead. And so, the prospects for continued Cable cash margin growth continues to track even slightly ahead of what we initially indicated.

Q

Before we leave wireline, we should touch on the wholesale Internet decision. You've articulated the impact already. What messaging do you want to provide to investors with respect to that file, and how the whole regulatory process is going to play out?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

Well, we're obviously disappointed in it. As I go back to my comments on facilities base, we've had a long track record of fully costed models. We're disappointed that, on a number of fronts, that the rates that were proposed are below cost. And we've been fairly transparent. And you can see it from our P&L what costs are based on our margins. And so, to introduce something at this level is disappointing and a change in direction, we think, from what we previously saw in their cost models and cost studies. The fact that it's retroactive is similarly disappointing, and maybe even more so.

Now, since the interim rates were announced back in 2016, we made investments of CAD 4.4 billion in our Wireless wireline network on that basis. And so, for the CRTC to make a retroactive change, just from a policy

standpoint, just can't be good for the industry, and frankly can't be good for foreign investment in Canada. I think anything that gets back to predictability and transparency, I think, is a better alternative.

So, the retroactive impact we've disclosed is, as you said, [ph] Tim (00:24:49), up to the date of the announcement mid-August, the cumulative impact retroactive is CAD 140 million. It's not significant on a go-forward basis. And the wholesale piece of it overall is not a big part of it. But putting aside what I would call the rational economics of it, for the CRTC to issue the decision a week after the Competition Bureau, another branch of the government, talk to the Internet market as being healthy is kind of counterintuitive and inconsistent. And so, there are the – we're all going through the process. And there are appeal provisions that will work through. And of course, depending on where it ends up, we'll look to our capital allocation model accordingly.

Q

Any questions in the room for Tony? No? Okay.

Maybe, just to touch on a few more smaller businesses, Tony. Maybe on the SME initiative, you've – you don't disclose that. We don't see that directly anymore. But I know a lot of work has been going on there. What's happening with the small and medium enterprise side?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

Good progress on that front. We've always talked about us being under-indexed in the wireline SME side of the business. And that's still the case today. So, the opportunity for growth continues to be large for us, and the rate of increased penetration is coming in nicely. It's included as part of our Cable results, so you don't get complete visibility to it. But what I can tell you is we're focused on penetration on that with continued fiber investments where the payback is very good. And so, the model continues to hunt well.

Q

And you are seeing growth on that side?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

We continue to see growth...

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Yeah.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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...absolutely, on that side of it as I said. Small businesses, in particular, are looking for alternatives. Particularly, alternatives that are IP-based, which is our focus in that space.

Q

Okay. And how about on Media? It's granted a small business, but you've got some interesting assets there, and I know you've done a lot of work on that side as well. What's the outlook on Media?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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One of the things we focused on Media was having that business with good consistent growth on the 2% to 3% range, with good solid margin expansion. That was our focus. And when you look at the pieces that make that up, it's coming in nicely. Particularly now as we have sold off the publishing business, what would you see in our Media business is sports. That continues to have very good top line growth. The ebbs and flows of championships of the various teams sort of offset each other nicely. And so, you get a good balance of sports viewership and sports revenue modified [indiscernible] (00:27:59)...

Q

Weird to say that in Toronto, isn't it?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

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It is. And so, that piece is working well. The other big part of it – of our Media business is the radio side of it, and that continues to have very good solid growth and cash flow. And so, those are really the anchors for our Media business and continue to, as I said, good stable solid growth.

Q

Okay. Anything to call out on the asset monetization front? I know, I think one of your buildings is being – is up for sale. Anything you're doing with the broader portfolio there?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

I would say, on the broader portfolio, nothing to report at the moment. The building for sale that you're talking about is a particular property in Toronto, that's become somewhat high profile on Bloor Street there. And I would say, that's really reflective of our cost efficiency and space consolidation strategy. And so, you'll continue to see there's another one on – in Toronto last year that you saw us dispose of. And so, as we continue to improve our space efficiency, excess assets we'll put on the market. And it's a terrific market to monetize those types of assets. And so, you'll continue to see some of that happening. But on the broader, what I would call, balance sheet, nothing new at this stage.

Q

Okay. Tony, just to wrap up, I'll leave the last word to you. What message do you want to leave with investors as we go into the back half of this year?

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

I'll kind of wrap up on the parts of the business that I touched on.

In Wireless, I think we're going through a terrific shift then against a healthy backdrop. We're making a good transition and improving the fundamentals of our Wireless business. And although the overage revenue will mask some of that in the very short-term, we intend to be very transparent with our revenue trajectory based on overages and in our underlying MRC. But a good healthy business with solid margins. And then, as we flip to Cable, I think the upshot there is we've got a business with top line that continues to improve in growth rates, and expanding margins and expanding cash flow margins. And on the Media side, entering a phase of stable meaningful cash flow growth.

So, just emphasizing that we are executing on the things we said we would, and continue to be transparent on the moving pieces of it.

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Super. I think we'll leave it there. Thank you, Tony.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

Thank you.

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