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MANAGEMENT DISCUSSION SECTION

Bob Bek
Analyst, CIBC World Markets, Inc.

Good. All right. Good morning. Welcome back. Once again, my name is Bob Bek. I'm the cable, telecom and media analyst at CIBC. Welcome. Quite pleased to have with us today Rogers Communications. I'm sure many of you or all of you would know it is a leading communications company in Canada. And we have two very senior executives here to take us through the story which is opportune.

So, to my right, Tony Staffieri is the Chief Financial Officer; and to Tony's right is Jorge Fernandes, who is the Chief Technology and Information Officer.

So, before we dig in and also talk about on Wireless and 5G, but maybe I'll turn it over to you, Tony, for a little introduction.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

Yeah. Thanks for the introduction, Bob, and thanks for having us here. We thought before we get started, as we were going through our archives for one of our employee events, we're celebrating 60 years as a company, 35 years in Wireless, we came across a video that was kind of interesting and it's really short. So, we thought we'd play it up. It's sort of ironic when you see it and our founder is the host in it. And it really was the beginning of Wireless. And we thought it was – we're on the cusp of 5G. It'd be a nice little setup for that conversation.

So, let's go ahead and roll it.

[Video Presentation] (00:01:26-00:02:34)

We also found the business case that went with it. You'd get a kick out of this. The business plan was we would have 87,000 Wireless customers across the country, paying an average of CAD 1,000 a month. That was the business case. And the average count to the phone was going to be CAD 3,000. I think that one we got right. But as we think about the models for 5G, it is kind of a bit humorous to whatever we forecast, it will be different for sure.

Bob Bek

Analyst, CIBC World Markets, Inc.

No doubt. No doubt.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

Yeah.

QUESTION AND ANSWER SECTION

Bob Bek

Analyst, CIBC World Markets, Inc.

Q

Well, that's great. Thank you, Tony. Before we kind of launch into the 5G, maybe we'll sort of set the base on the Wireless environment as it currently stands, Rogers's playing a big role in kind of resetting the formula. We launched Rogers Infinite seven months ago. So maybe if you could recap the rationale for the move to unlimited and the timing and then we can kind of get into the early successes which are quite material.

Anthony Staffieri

Chief Financial Officer, Rogers Communications, Inc.

A

Yeah. Back in mid-June when we launched unlimited plans, it was really three objectives we were after, one was fundamentally get usage up in Canada. Average usage sat at around 2.5 gigs per month. If you're to compare it to the US, it'd be somewhere around 8 gigs; and for some carriers, even as high as 10 gigs per month.

So we really – for a company that deals in transporting data, it was fundamental that we had to get those growth rates moving up. Growth rates had stalled to double digit of 17%, 18% growth year-on-year. And so, we needed to get that moving back up.

The second thing we wanted to do is really uncouple the rate plans with the handset costs. Handset costs continue to escalate. And some of the latest devices are now pushing above CAD 2,500. And so, we really needed a model. The subsidy model had run its course. It was really based on phones being way back CAD 200. And we're one of the last countries to continue on with a subsidy model. And so we needed something that was more simple and fair and transparent for the consumers.

And the last piece was we really wanted to get at simplicity for the customer. Overage fees were the number one call – number one reasons for calls into our call centers, number one reason for customers leaving. They were just upset with the latest overage bills and wanted to deal with it. So it was all three of those that we were focused on as an objective. And I would say to move on to what we've seen so far in the seven months, we're thrilled with what we're seeing.

A couple of data points for you, average usage for customers on our Infinite unlimited plans, 7.5 gigs per month and growing at a rate of over 50%. If you're to look at metrics like churn for customers who move on to these plans, early days but way down. If you're to look at number of calls into the call center for customers on these plans, well below 50% of what it used to be.

And then, finally, how do the customers like it? I think two things as proof points; one is likelihood to recommend scores, also way up by 50%. And then the second piece of it is the appeal that we're seeing in the market. And I think our postpaid net subscriber loadings in Q4 really speak to the popularity of the plans.

So, from that perspective, we like what we see. I would say on the installment plan front, that's been a little slower. We thought it would get more traction in the market. Just this week and into next week, we are moving to all installment plans. So we – we'll retire all our subsidy plans and continue to try to reduce the promotional discounts that are inherent in some of the plans. And so, we'll see how that plays out in the market, but we continue to see it as a big opportunity not only for us but for the industry.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Just to follow on that thought. So how has the competitor response been relative to your expectations? Again, pushing subsidies has been kind of the early response from some of them. What are your thoughts on the dynamic and how it's changed?

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

It's kind of gone up and down. Since we launched it back in early July when we launched the installment plans, we had taken the subsidies way back. The marketplace didn't necessarily follow, and so we sort of by mid-Q3 had jumped back in the market with subsidies. As we then entered the fourth quarter, subsidies in the marketplace pulled back. And as we got into the busy period, the marketplace kind of went back up.

And then finally, in January, it was a pullback of subsidies to very low levels. And when I say subsidies, the promotional discounts on hardware. And January typically is slow, but if you were to compare it to the prior-year January, it's down year-on-year. So the initial read is it seems to be getting traction place in the market. Time will tell.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

So a couple of the positives that you touched on, if we can kind of poke it out a bit. So there's the overage melt you have to kind of work through, and that's – obviously, we've got seven months into that at this point, so your thoughts on how that plays out.

And you talked about some of the advantages, whether it's call center activity in that. So how long can we expect before we see some of the OpEx benefits of unlimited flow through into the numbers?

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

Yeah. Two things, so the – when we started this, the overage revenue for us was – and we had quoted a number of under 5%, just under 5% for us. That's been melting. And that's what's been dampening our profile of revenue and ARPU growth, and we continue to see that. And in a lot of ways, we're incenting the market to do that. We really want our base to continue to move on to these unlimited plans, over 1.4 million customers today on the plans. And as I said, we like what we see.

We think by the end of Q2, so as we get into Q3, overage revenue will be less than 1% of our total service revenue for Wireless. And you'll see a profile throughout the year of continued dampness or muted top line growth as a result of this overage melt continuing. But once we get into Q3, we expect to report return to growth, not only in revenue but in ARPU.

Throughout this period through to takeout of the overage melt, ARPU continues to increase. And so, that's the profile we wanted going into this. So, we're pleased with the underlying economics that we're seeing.

And then on the costs side, for this year, we're going to accelerate some of the things we had in our cost playbook. And if you're to look at, our focus has been continues to be on margin expansion. So, from – in 2017, 2018, in each of our businesses, we saw 200 basis points of margin expansion, slowed down a little bit in 2019 on the Wireless side. Cable still had good margin expansion of 100 basis points in the year, but it's slowed down as we made this change to Infinite.

And so, as we resume that playbook into 2020, our expectation and our guidance is on the basis that we will resume margin expansion in that business...

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Okay.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

...with a fairly stable CapEx profile and continue to grow free cash flow.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Excellent. And I want to make sure we have lots of time for Jorge here. It's a pleasure to have him on stage. 5G is another big topic for the industry and in particular for Rogers, launching the start of this transition in Canada.

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

A

Yeah.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

So maybe, Jorge, give us a bit of an overview on your thoughts on the giant opportunity in 5G, and then we can kind of poke away at some of the specifics, if we can.

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

A

Okay. Good morning, everyone. We're really at the early stages of 5G and, obviously, a lot has been said about 5G both in terms of what it is, what it isn't, so a lot of hype. And we've been really trying to focus on what are the key enablers of 5G and how will 5G essentially evolve over the next three to five years as it matures. And so, obviously, that has been very important to also inform our investment.

We're at the beginning, the first phase starting this year with the first devices that will become available. We'll essentially deliver what we see as more speed and more capacity. The speed will be a function of the spectrum that will be available. And so, again, as more spectrum becomes available, we will see that speed increase.

We could see some initial consumer applications such as cloud gaming become more pervasive. Cloud gaming, as you know, is one of those technologies that requires a certainty of latency. And whilst it's not yet the low-latency applications and the real-time critical applications that 5G will deliver later on, we do expect it to be a lot more consistent than the 4G latency. So that could be one of the sort of earlier applications that we see.

Over time, as I've said, as more spectrum becomes available, but more importantly, as we see the 5G stand-alone core becoming available and deployed on our networks, then we will start seeing capabilities such as the low-latency application, the availability and capacity for millions of IoT devices. We should also see an evolution of the devices becoming available. So, the first generation of 5G devices will be smartphones, no different from 4G. But over time, we will see 5G modems making their way into connected devices – small connected devices, sensors, essentially anything that can be connected into anything.

And that's where we will see an evolution, and I would say even a revolution of the digitalization of, frankly, any industry. And this is where we start seeing that sort of convergence of the new capabilities of the network, these new connected devices and then the developer community that will use a combination of the applications and also AI technology to start delivering new currencies and enabling new businesses.

So, we believe that this evolution will happen over the next sort of three to five years. We expect to see 5G hitting maturity sort of at the five-year mark which is, frankly, not too different from what we would have seen in previous generations.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

So, as far as that opportunity for 5G, it seems – again, 4G brought a lot that – obviously, a huge leap-up from 3G. How do you – having lived through that, how do you see the 5G to 4G sort of opportunity? I mean, it feels massively larger than what 4G was?

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

A

Yeah. 4G was interesting. Well, in fact, if you look at every generation, there's always sort of an evolution phase which is that the new generation did everything that the previous one did, slightly better on one or another aspect. And 5G initially is not that different. The data will be better than 4G data. The coverage will be there. But the new – the two new things that 5G brings that 4G did not have, as I said, was the ultralow-latency capabilities of 5G on a new architecture and the ability to serve and connect millions of devices, which 4G does not handle. This is due to the nature of the core.

And so what we will see is the edge of the network will become a lot more important to deliver low latency. If you think about – and I'll give you an example. An emergency vehicle connected into a smart city grid running an application at the edge of the network, you want to take a smart – you want to take an emergency vehicle from point A to point B. Your traffic light systems are connected, the traffic systems are connected into an application running at the edge of the network. You can use AI to analyze the information that it's receiving in real time and make real-time decisions on how it manages the traffic light systems and how it routes that emergency vehicle safely to its destination.

We really see this new software-enabled world bringing about, frankly, unlimited capabilities very much in the same way that 4G did when you combined the network, the smartphone that wasn't there before really add capacity, and then the developer community with apps brought about new industries, brought about the Ubers and the Airbnbs of this world. And so, we can expect new use cases and new businesses to come about as a result of 5G.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

So, how do you view Rogers' positioning, network positioning to kind of be early in 5G as you are and what spending requirements are going to be there? I mean, that's the question we get a lot from investors on the CapEx...

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

A

Yeah.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

...sort of behind the rollout of 5G. So, what are your thoughts on that?

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

A

We have – I would say, we have a number of advantages right now over our competitors. I think the first one is that we have equipment certainty. We've been partnering with Ericsson from day one on the first generation, in fact, the call that you just saw. And so, we've always enjoyed a very good relationship with Ericsson all through 1G through to 5G. And in a country where we don't have the economies of scale, for instance, that the US has, it was a very natural alignment for us to align with what the US is doing because it gives us access to the broader economies of devices and spectrum capabilities as well. So, that was, I think, a very important point for us.

The second one I would say is the spectrum assets that we own and the ones that we've acquired. Most recently, acquiring the 600-megahertz spectrum was incredibly important for us. Not only do we have 20 megahertz of low-band spectrum across the whole country in the most densely populated areas of the country, we have 40 megahertz.

When you take a combination of the 600 megahertz, plus the existing assets that we have on 700 megahertz and 850 megahertz, essentially, we have 80 megahertz of low-band spectrum that will allow us to provide not only a contiguous coverage across the whole country using the current site footprint that we have, very efficient way of delivering, but it also gives us a significant amount of capacity.

As we move forward and as we access the mid-band, [ph] 305 megahertz (00:17:43), we can leverage our – again, the Ericsson technology called dynamic spectrum sharing to leverage that spectrum that we have for both 5G and 4G. And over time, with millimeter wave, we can use that spectrum to deploy in very high-demand areas such as stadia and other areas where you have large congregations of people.

So as you think about a world of these new critical applications with a 5G stand-alone core, you now can imagine a situation where we're able to provide at a national level real-time, low-latency applications for our customers.

The third one, I would say, is the fact that we essentially are the only national network. We have the only national network today which allows us to have a conversation with the web-scale providers that potentially our competition can't do. So when you combine the spectrum and the fact that we have this national network, we have the ability to negotiate edge computing deployments for the likes of AWS or Google or Azure that will be enablers for some of these new use cases.

The partnerships that we've been signing are important as well. We've recently announced the 5G Future Forum. 5G Future Forum is a consortium of six telcos around the world providing sort of this global coverage; it's us, Verizon, Vodafone, KT, Telstra, and América Móvil. This partnership essentially is trying to address three things. The first one is interoperability on the standards of edge compute at the global level so that you can guarantee roaming of other edge computing applications.

The second one is enabling a platform not too different from what you would have seen in the app development for 4G, providing a platform for developers to build edge computing capabilities.

And the third one, and an important one, is to ensure that we are able to leverage each other's capabilities in negotiating agreements with the web-scale providers so that we are not just sort of limited to becoming these glorified real estate players where we give them access to edge space and power but where we start identifying what are the currencies, what are the values that 5G will enable, and how do we partake in that value.

And also, the last one is the fact that we are already today, in terms of machine-to-machine connectivity, the leaders in Canada. And so, that's – gives us a very important setting and footprint from which to start and build that capability.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

That's a great overview. Thank you. Maybe, Tony, on the CapEx side. I mean, how much spending – specific spending is behind it, or how should we look at that spending?

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

You should think about it as – capital intensity for us, we've said through the next three- to five-year period, will stay for Wireless in the 12% to 14%. And so against the backdrop of a top line that ought to resume growth this year and continue to grow, I think the prospects for a continued stable and growing ROI for us is there. And so, while the business case for a lot of the stuff that Jorge talked about and the monetization of that is still not finite and defined yet, I think you should take comfort in the fact that we'll continue to see solid ROIs throughout the period as we make the migration.

Unless there's a specific use case where we enter into an agreement with an enterprise customer that has defined benefits for us, we'll otherwise stick to our 12% to 14%...

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Okay.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.
A

...to maintain that rationality.

Bob Bek
Analyst, CIBC World Markets, Inc.
Q

Okay. Just looking at the CapEx picture overall. Obviously, the wireline side has much higher capital intensity, but that's a focus for Rogers to kind of bring that down. So maybe that's a decent segue to kind of talk about how – I mean, like you're close to 30%, 29% on the wireline side, you're targeting low-20s. Maybe just kind of tie that into the bigger CapEx discussion.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.
A

Yeah, absolutely. So we've – on the Cable side, we've said that we wanted to focus on cash margin expansion. By the end of 2021, we want to exit Cable cash margins with at least 25%, and that's on the back of a capital intensity ratio in the 20% to 22% range. More beyond that, but as an interim goal, that's what we've stated. We said that a year ago when our Cable cash margins were sitting at 8%, and capital intensity was sitting at about 38%.

Bob Bek
Analyst, CIBC World Markets, Inc.
Q

Right.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.
A

Few reasons for that is we migrated to the new platform, and everything that that entailed in terms of integration, as well as some CPE uplift as well. And so this – in 2019, we brought that down to 29% and Cable cash margins for the year ended at almost 20%. So, a good improvement. And this year, you ought to expect to see continued declines in our Cable capital intensity while, at the same time, continuing to expand EBITDA margins. And that should put us – continue to put us in a very good path to achieving the 25% target we have for Cable.

Bob Bek
Analyst, CIBC World Markets, Inc.
Q

So, all of this flows through to a continued really strong profile and free cash flow. You're looking – targeting somewhere CAD 2.3 billion, CAD 2.4 billion for this year again, which is a step-up from 2019.

Uses of cash, you bought back almost CAD 700 million worth of stock in 2019. So, how should we view the potential return of capital from that material cash flow?

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.
A

Yeah. We continue to be committed to a capital cash return model to shareholders. We think we have what we need for the business. And as you said, in 2019, on top of the CAD 1 billion of dividends, we bought back CAD 655 million of shares.

As we go through 2020, I guess, three things that we're looking at; one is making sure that we have the resumption to growth. I talked about the first half being pressured with the overage declines, and we need a bit of time for some of the cost productivity to start to come through in the second half. And so, we'll be keenly focused on resuming free cash flow growth. The second piece of it is getting clarity around spectrum...

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Right.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

...auction and whether that, in fact, is going to happen at the end of this year or is it pushed out into early next year. And then, the final piece we look at is debt leverage. And I would say, while we sit at CAD 2.9 million, I'll remind you that CAD 0.2 billion of that is really the lease accounting piece of it.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Yes.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

So, in substance, we're sitting at CAD 2.7 billion. Nonetheless, we do see ourselves just generally moving to CAD 2.5 billion as kind of a good beacon for us to move to. But given where interest rates are, it isn't something that we see as something that we need to panic about. Our natural burn rate is about 2% a year, and we'll slowly get to – that to about 0.3% a year. So, even with the upcoming spectrum auctions, I think we see a relatively good path over several years to move towards the CAD 2.5 billion.

So, those are the three factors we look at...

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Yeah.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

...in terms of thinking about continued share buybacks in the near term.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Okay. I want to make sure to leave time for some regulatory, obviously, a hot topic again for the space. You got Wireless hearings starting up next month, some big discussions and whatever. So, maybe just your big-picture views on the regulatory risk from a Wireless perspective and then any update you might have on timing from the wholesale appeal process on the TPIA and...

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

Sure.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

...Rogers' positioning.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

Yeah. As you said, the hearings start in a few weeks.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Yeah.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

In past conferences, we've stated kind of the main points. And it's kind of interesting to see a lot of the studies and data points that are starting to come out that we think are very relevant. And we're hopeful and, frankly, optimistic that the CRTC will go through these hearings in a very measured and thoughtful way, paying attention to some of the key facts. Ultimately, that's what got the industry to where it is today. We have some of the best networks in the world and we got here through very balanced, measured policies for the industry. And so, we think that's important.

If we then come back to what is it that the government's trying to achieve if they do seriously consider the path of MVNOs, a couple of data points, and the CRTC hearings have been sort of layered with some of the political comments on top of that. One of the interesting reports that I saw recently, and I'll just quote a few numbers from that, if you were to look at Wireless pricing in the country, 2016 to – I'm going to pick midyear last year when we first introduced unlimited, prices came down 50%. If you're to look at pricing per gig from July 1 to end of year, they came down 25%. By the time we hit July 1 of this year, we think we'll probably achieve another 25% decline based on effective pricing.

Another interesting stat is if you're to look at what consumers pay in Canada, our blended ARPU sits at about – so the average bill per month, CAD 55; US would be at about $50. So factoring in exchange, we're not that different, if you're to divide that by how many gigs consumers use. I've talked about – for us, it's 2.5 gigs previously. For customers on the new unlimited plans, it's spiked to 7.5 gigs per month. The US would sit at about 8 gigs. So if you think about price declines, price competitiveness and look at a benchmark that's close to home for a market that's 10 times our size, I think the data is very compelling.

And then the final point is, the government's gone through a period of subsidizing what we still call the new entrants. And one thing that's clear that we've seen in other places around the world, MVNOs depending on what rate they come in at in terms of wholesale rates, what we have seen is they moved to the bottom end as an entry point.

Bob Bek
Analyst, CIBC World Markets, Inc.

Q

Yeah.

And so, it is going to have a very big impact on some of the new entrants.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

A

And so, you sort of piece that all together, and we're having a hard time sort of seeing what the positive outcome is. Ultimately, as we're on the verge of 5G investment, we think it's critical that we keep going. Jorge talked about our alliance. The world's moving forward and we don't want to get left behind. And any regulatory outcomes that impact that is just going to be too bad for the nation in a lot of ways.

Bob Bek
Analyst, CIBC World Markets, Inc.

Well, that's great. We're out of time. I could probably do another two or three of these sessions still with the questions. But thanks very much, Tony, for joining us; Jorge, for joining us and...

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

Thank you.

Bob Bek
Analyst, CIBC World Markets, Inc.

...appreciate your interest, everyone.

Anthony Staffieri
Chief Financial Officer, Rogers Communications, Inc.

Thanks for having us.

Jorge Capelas Fernandes
Chief Technology Officer, Rogers Communications, Inc.

Thank you.