TELUS

Telecommunications
TSX: T | NYSE: TU
Market Underperform | Hold

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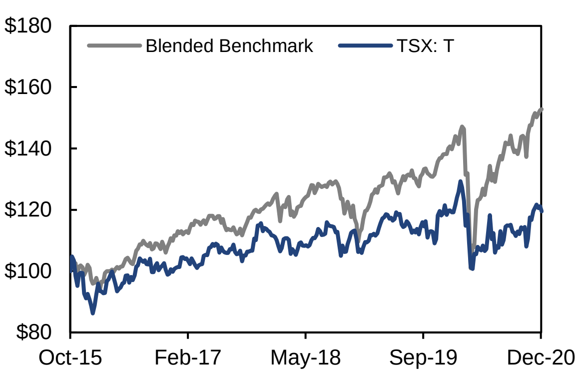
Return on Investment	
Current Share Price	$25.21
Target Price	$25.00
Dividend Yield	4.94%
Implied Return	4%
Conviction Rating	2

Market Profile	
52-Week Range	$18.54 - $27.74
Market Capitalization (US$mm)	$32,539
Net Debt (US$mm)	$18,268
Enterprise Value (US$mm)	$50,807
Beta (5-Year Monthly)	0.56

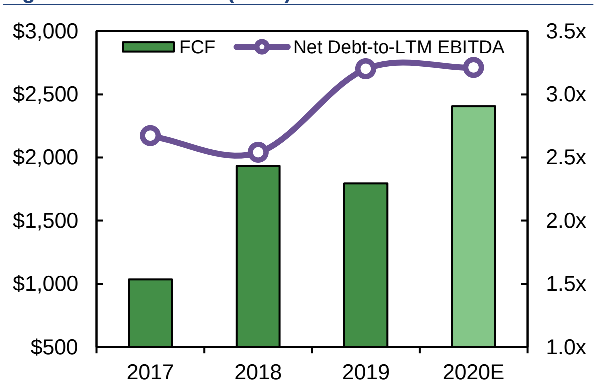
Metrics	2020E	2021E	2022E
Revenue (US$mm)	$15,359	$16,382	$17,307
EBITDA (US$mm)	$5,581	$5,936	$6,334
EPS	$1.10	$1.36	$1.42
EV/EBITDA	9.1x	8.6x	8.0x

Holding Period Trading Performance (Indexed to $100)



Source: Thomson Reuters Eikon

Figure 1: FCF Growth ($mm) & Net Debt-to-LTM EBITDA



Source: Company Filings, CPMT Estimates

Investment Thesis Summary

- The CPMT expects T to have strong wireless subscriber growth, low churn rates, high ARPUs, and stable margins
- T is a strong operator, however, growing competition in the wireless segment from RCI and BCE could pressure T's market positioning
- T has underperformed the benchmark over the last five years

Business Description

TELUS (TSX: T) is a telecommunications Company offering wireless, data, IP, voice, television, entertainment, video, and security services to over 15mm customers globally. T also operates in three niche business units: TELUS Health, TELUS International, and TELUS Agriculture. TELUS Health is Canada's largest healthcare IT provider, and TELUS International delivers innovative business process solutions to corporations globally. TELUS Agriculture was launched in November 2020 and provides data analytics and connectivity through the agriculture value chain.

Industry 5G Outlook

During the last decade, mass smartphone adoption and related data consumption have provided Canadian telecommunication companies with steady earnings growth. The driver for greater data consumption has been underpinned by the deployment of 4G LTE networks. In the upcoming decade, the Canadian telecommunications sector is expected to experience fundamental changes with advances in 5G technology. Operators are expected to provide this technology for internet connectivity to consumers, and internet of things (IoT) enhancements for businesses. Therefore, regulation is expected to lower the prices of 5G connectivity for consumers, making IoT 5G enhancements the growth driver for Canadian operators. As a result, national operators such as T, who have an established network of business relations, are expected to secure more business IoT contracts than regional operators. T's 5G network expansion across Canada remains on schedule and is estimated to create ~250k jobs and contribute $40B annually to the Canadian economy.

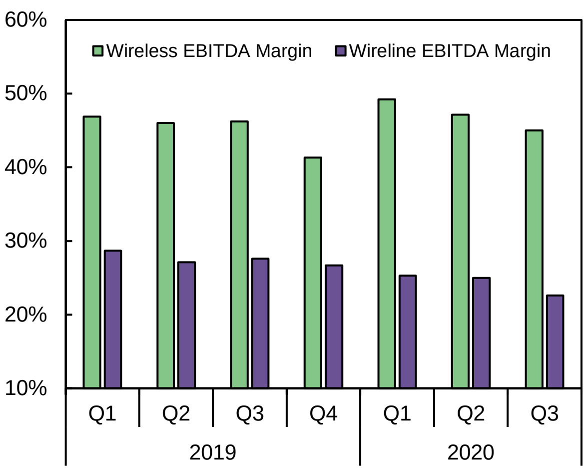
Mandate Fit

Growing Free Cash Flows: T has been able to grow FCFs at a CAGR of 7.0% during the past five years. As a result, the Company continues to develop its network's infrastructure by raising its capex at a CAGR of 1.9% during the same time frame.

Strong Balance Sheet: In past years, T's interest coverage ratio was ~8.0x. However, in recent quarters this ratio has fallen to ~7.0x. Similarly, the Company's Net Debt-to-LTM EBITDA has risen from 2.5x to 3.5x in recent years. The weakening of these metrics is attributed to the COVID-19 pandemic's adverse effects on T's EBITDA generation, which is discussed in more detail below. Nonetheless, T is in compliance with its debt covenants, preserving its investment-grade credit rating. However, the CPMT will monitor any material changes to these factors.

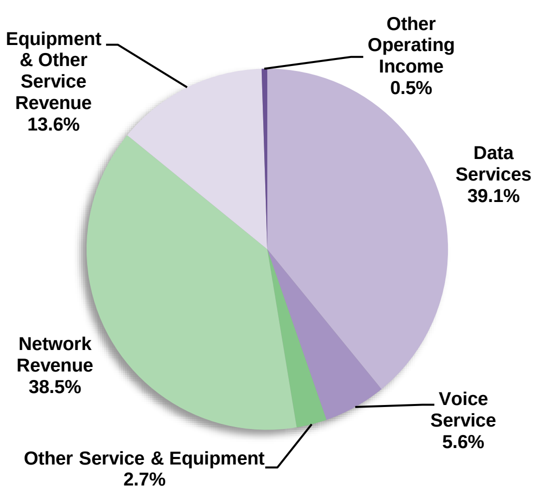
Competitive Advantage: The CPMT believes that T's competitive advantage stems from its diverse revenue streams as it expands into new industries. T has pursued new ventures without any (cont'd)

Figure 2: Historical EBITDA Margin by Revenue Segment



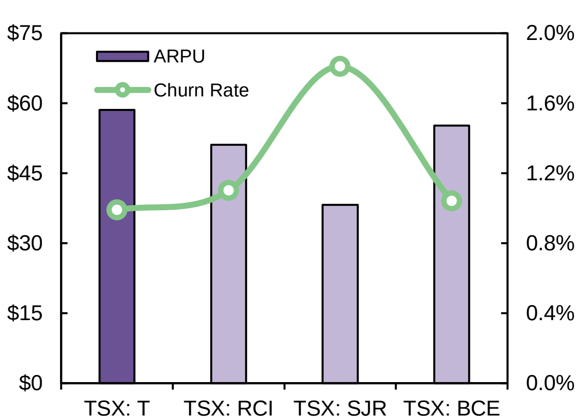
Source: Company Filings

Figure 3: Q3 2020 Revenue Breakdown



Source: Company Filings

Figure 4: Latest Competitor APRUs & Churn Rates



Source: Company Filings

damage to its current operations; for instance, T's total customers have increased at a CAGR of 1.4% since 2018, while its EBITDA margins have remained stable. T's strength can be further exemplified by its competitively low churn rate and high ARPU, when compared to its Canadian peers.

Quality Management: T has been led by current President and CEO, Darren Entwistle, for the past two decades. T's management team has been instrumental in growing the Company's geographical presence from Western Canada to international markets. Additionally, incentive plans and share-based rewards have constituted ~80% of executive compensation over the past three years. The CPMT views such compensation structures in a positive light, as they ensure that management's incentives are aligned with that of the Company's and its shareholders.

COVID-19 Impacts

T experienced adverse impacts on its top and bottom line from the pandemic-induced stay at home orders. For instance, the Company received traffic increases of over 25% of its normal internet usage. As a result, T waived much of its internet overage charge fees, with the belief that it was important for customers to be connected regardless of their financial situation. Additionally, T collected less roaming and wireless data fees due to travel restrictions, which was an integral growth driver in its Wireless segment. Accordingly, these factors reduced the Company's earnings and its dividend growth for FY2020's Q1 and Q2. Nonetheless, the CPMT stands by T's response, as it enabled the Company to keep its customers by entering flexible payment options.

ESG Initiatives

Recently, investors have placed a greater emphasis on companies' ESG mandates. T has historically had a strong focus on ESG initiatives. For instance, the Company aims to make its operations 100% net carbon neutral by 2030 and receive 100% of its electricity from renewable energy sources by 2025. T is also in the Dow Jones Sustainability Index, which tracks the performance of the world's leading ESG Companies. Moreover, 45% of T's Board of Directors are female, exceeding its 30% minimum requirement. This comes alongside its numerous awards for being a top Company in North America for workplace health and equality.

Investment Thesis and Valuation

A 50/50 blend of a five-year DCF, with a WACC of 6.36%, and a comparable EV/EBITDA multiple (8.1x) of T's main competitors Shaw Communications (TSX: SJR), Roger's Communications (TSX: RCI), and BCE Inc. (TSX: BCE), was used to value T. The results yielded a target price of $25, which corresponds to an implied total return of 4.2%.

T is an incumbent telecommunications operator in Canada, which has enabled it to build strong wireless and wireline franchises. The CPMT expects T to have strong wireless subscriber growth, low churn rates, high ARPUs, and stable margins in coming years.

While the overall telecommunications sector has been stable, it has not had attractive historical returns. Since entering the position, T has significantly underperformed relative to the Fund's Blended Benchmark. The CPMT sees T as a strong operator; however, growing competition in the wireless segment from RCI and BCE could pressure its market positioning. Therefore, the CPMT will continue to seek and analyze other names in the sector that provide desirable exposure and returns.