Seeking Alpha α

AT&T-Time Warner Merger: Bad Deal For Investors In Both

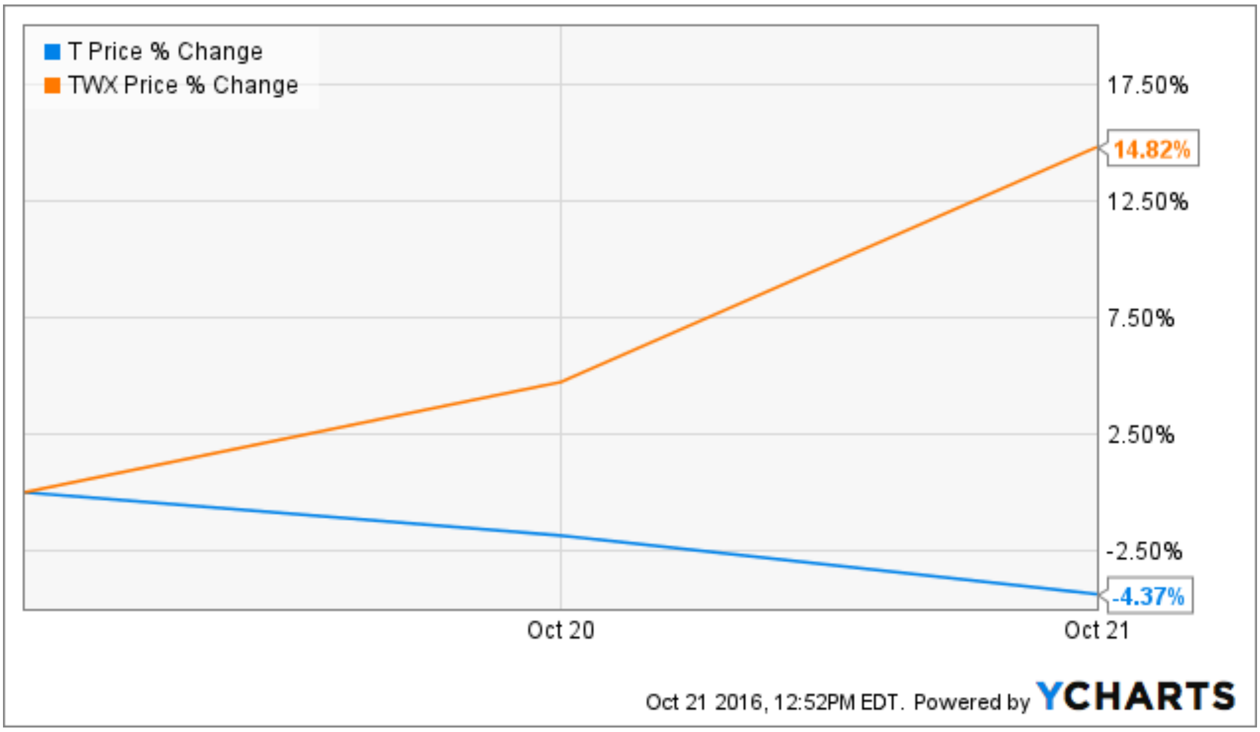
Oct. 21, 2016 3:50 PM ET202 comments
by: Dividend Sensei

Summary

- Bloomberg is reporting that AT&T is potentially in late stage negotiations to buy Time Warner.
- The news has sent shares of Time Warner soaring 7%, while AT&T crashes 3%.for two days in a row.
- BUT thanks to its large debt load from acquiring DirecTV, such a deal would likely have to be a stock funded deal..
- This would result in so much shareholder dilution that the deal would be minimally accretive to AT&T's EPS, and actually result in lower FCF/share.
- Which would end up hurting both current Time Warner, and AT&T shareholders due to slower dividend growth going forward.

at&t
Your world. Delivered.

On October 20th, Bloomberg reported on rumors that AT&T (NYSE:T) was looking to buy Time Warner (NYSE:TWX). The news sent Time Warner soaring, while AT&T shares reacted with far less enthusiasm.

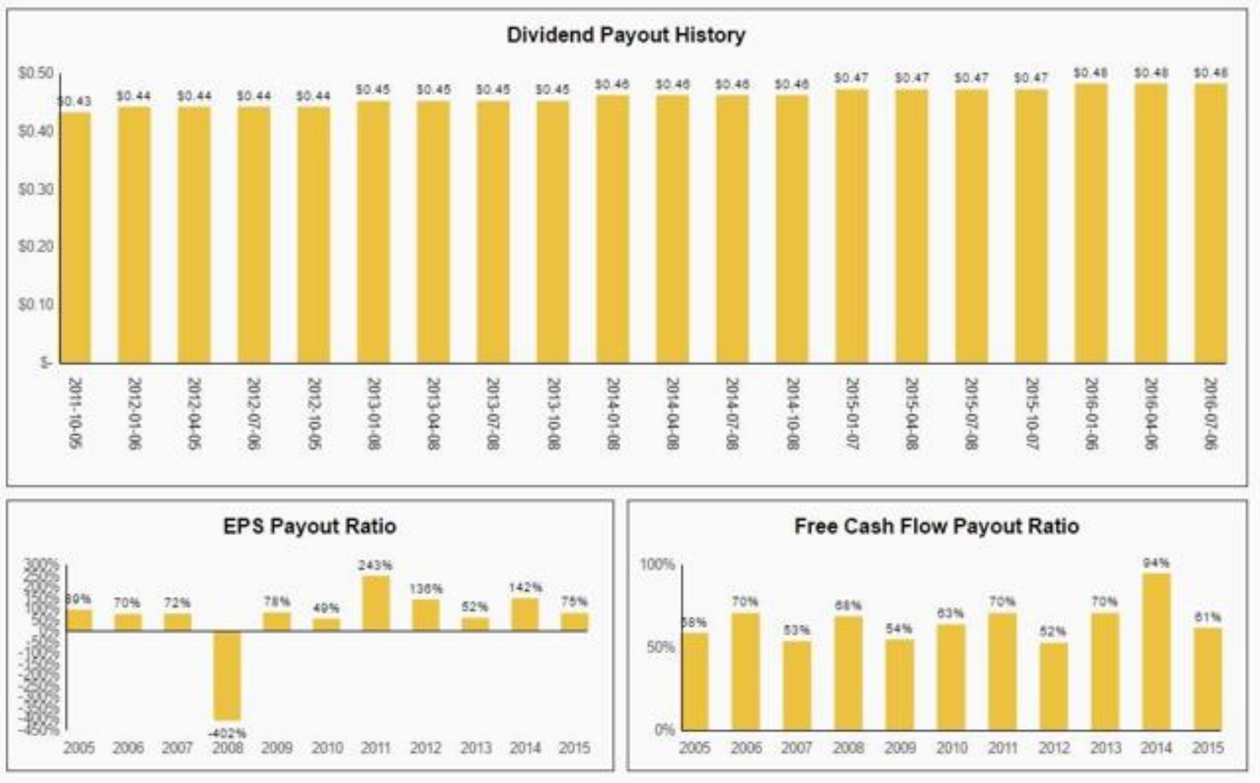


T data by YCharts

Let's take a look at why AT&T might be interested in acquiring Time Warner, but most importantly why such a deal isn't likely to benefit investors in either company.

In theory the deal makes sense

AT&T has long been a high-yield dividend growth favorite thanks to the utility like rock steady cash flow provided by its telecom business. And with management's bold acquisition of DirecTV, as well as its push into the faster growing Mexican wireless market, the company has the potential to accelerate its dividend growth rate from the anemic 2% it's been delivering over the last few years.



Source: Simply Safe Dividends

By acquiring Time Warner AT&T would be doubling down on its plans to become a global media giant, thanks to Time Warner's rich content, and intellectual property.

For example, purchasing Time Warner would bring the following under AT&T's tent, and turn it into a potential rival for Disney (NYSE:DIS):

- HBO and Cinemax
- Turner broadcasting, including CNN, TBS, TNT, Cartoon Network, AdultSwim
- Broadcast channel the CW
- DC Comics
- Warner Studios and its growing DC cinematic universe, as well as the Harry Potter franchise

In a fast changing media landscape, where cord cutting is a major concern for cable providers such as AT&T, the ability to acquire content, (and thus boost pay TV margins by cutting content costs), is potentially very valuable.

Which is why Bloomberg is reporting that AT&T CEO Randall Stephenson "is looking to add more content and original programming." Specifically, over the next three to five years, the company is planning on acquiring media companies, with a targeted market cap range of $2 billion to $50 billion.

...but the math just doesn't work out favorably for shareholders

However, as much sense as it makes for AT&T to continue to diversify its cash flows, and build a vast, globe spanning media empire, we can't forget that its recent acquisition spree. This included $49 billion for DirectTV, and $18 billion in wireless spectrum, has left its balance sheet with far more debt than management is comfortable with.

That's understandable since the DirecTV deal wound up resulting in a total of $126.8 billion in total debt, and a credit downgrade from S&P.

Sources: Morningstar, Gurufocus

Company	Debt	EBITDA	Interest	Debt/EBITDA	EBITDA/Interest

AT&T	$126.8 billion	$53.1 billion	$4.754 billion	2.39	11.17
Time Warner	$24.5 billion	$7.8 billion	$1.388 billion	3.14	5.61
AT&T + Time Warner	**$151.3 billion**	**$60.9 billion**	**$6.142 billion**	**2.48**	**9.91**

AT&T currently has only $7.2 billion in cash and cash equivalents on its balance sheet. And given its high debt load it's highly likely that any acquisition of Time Warner would have to be an almost entirely stock based deal.

But even then, Time Warner's $24.5 billion in debt would be added to AT&T's, which would create one of the largest debt levels in corporate America.

Now, that isn't to say that it would necessarily be a dangerous level of debt. After all, the average telecom's leverage ratio (Debt/EBITDA) is 2.59, and even before any synergies the larger AT&T would have a lower ratio than that.

However, the fact that AT&T would be reversing its recent deleveraging efforts could result in another credit downgrade, potentially leaving the company open to higher refinancing costs as interest rates gradually rise.

That's especially true given that AT&T has $5.77 billion, $6.5 billion, and $7.4 billion in debt coming due in 2017, 2018, and 2019 respectively.

However, I will admit that the combined AT&T and Time Warner would make for an attractive group of assets, with some of the highest sales, earnings, and free cash flow, or FCF in the world.

Company	Sales	Earnings	Free Cash Flow
AT&T	$162.3 billion	$14.2 billion	$16.7 billion
Time Warner	$27.9 billion	$4.1 billion	$3.6 billion
AT&T + Time Warner	**$190.2 billion**	**$18.3 billion**	**$20.3 billion**

Of course the real issue with a potential buyout of Time Warner is whether or not the deal can be structured in such a way to benefit shareholders in both companies.

Company	Shares Outstanding	EPS (Post 10% Synergy)	FCF/Share (Post 10% Synergy)
AT&T	6.195 billion	$2.29	$2.70
Time Warner	808 million	$5.02	$4.44
AT&T + Time Warner	**8.552 billion**	**$2.35**	**$2.61**

So let's take Time Warner's current market cap of $70 billion, add a 25% premium, and then figure out what an all stock deal would mean in terms of EPS, and FCF/share accretion.

As you can see, the large amount of shareholder dilution needed to acquire Time Warner actually results in minimal EPS accretion, and a small decrease in AT&T's FCF/share.

The reason that matters is because FCF/share is what secures, and funds the dividend and its growth; the primary concern of AT&T investors.

In other words, without first deleveraging its balance sheet, which would allow AT&T to borrow heavily to buy Time Warner, the dilutive nature of such a deal means there really is not benefit to AT&T shareholders.

As for Time Warner investors, they might also end up feeling screwed.

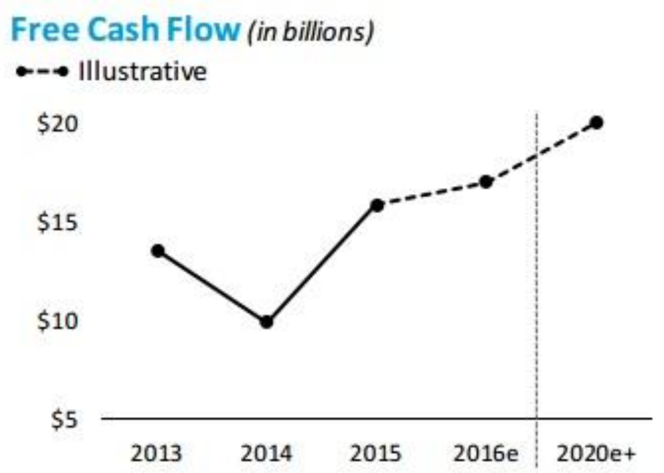
Sources: Yahoo Finance, Fastgraphs, Factset Research, Multpl.com, Moneychimp.com

Company	Yield	TTM FCF Payout Ratio	Projected 10 Year Dividend Growth	Projected 10 Year Total Return
AT&T	5.0%	67.2%	4.0%	9.0%
Time Warner	2.0%	33.6%	9.2%	11.2%
S&P 500	**2.1%**	**39.1%**	**6.2%**	**9.1%**

Academic studies show that a good rule of thumb for long-term total returns is yield + dividend growth. And while long-term analyst growth forecasts always need to be taken with a grain of salt, as you can see Time Warner is a much faster growing company.

So in a mega-merger its shareholders would end up with a much higher-yield BUT lower total return potential.

BUT WAIT! Maybe AT&T buying Time Warner could boost its own dividend growth rate and make up for the slower payout growth rate. After all, AT&T is still working on cost cutting in order to achieve synergies from its DirecTV acquisition and management expects its free cash flow to hit $20 billion in 2020.



Source: AT&T investor presentation.

In other words, over the next four years AT&T thinks it can squeeze another $3.3 billion in costs out of its assets. And assuming a conservative 10% synergy cost savings from eliminating redundant positions, and inefficiencies at Time Warner, by the end of 2020 the new, larger, AT&T could be looking at free cash flow of $25.6 billion per year.

Sources: Morningstar, AT&T management guidance

Scenario	Projected 2020 FCF	Share Count	2020 FCF/Share	2020 Dividend	4 Year Dividend CAGR	4 Year Projected Total Return
No Merger	$20 billion	5.77 billion	$3.47	$2.43	6.1%	11.1%
Time Warner Merger	$25.6 billion	7.96 billion	$3.22	$2.25	4.0%	9.0%

From 2007, right after AT&T restructured, to 2014, just before it acquired DirecTV, AT&T's net buyback rate was 2.36% CAGR.

Using this as a likely ongoing buyback rate, we can determine the likely number of shares outstanding at the end of 2020, and thus the ultimate FCF/share if AT&T does, and doesn't buy Time Warner.

Then using a 70% FCF payout ratio, which still leaves $7.7 billion a year in excess FCF to fund buybacks, pay down debt, or just build up a war chest of cash, we can predict a likely dividend in both scenarios.

As you can see, a Time Warner merger, because of the high shareholder dilution it would require, would in fact result in the far slower payout growth rate, and thus the worse long-term total return.

Bottom line: AT&T buying Time Warner would likely end up hurting investors in both companies

Don't get me wrong, as an AT&T shareholder I'm not entirely against the idea of adding Time Warner's strong brands, content, and cash flow to our own. At the right price, and after AT&T has de-levered its balance sheet enough to regain its previous credit rating, such a deal might make sense due to less shareholder dilution and greater FCF/share accretion.

BUT so soon after AT&T's most recent mega deals, the likely economics of this acquisition simply don't seem to make sense; for investors in either company.

For Time Warner shareholders they would end up owning a higher-yielding, but far slower growing company. Meanwhile AT&T dividend lovers would end up suffering from slower dividend growth for many more years due to the large dilution, and debt this deal would add to our balance sheet.

Disclosure: I am/we are long T, DIS.

I wrote this article myself, and it expresses my own opinions. I am not receiving compensation for it (other than from Seeking Alpha). I have no business relationship with any company whose stock is mentioned in this article.

Comments (202)

zack54
While their at it they should also pick up Lionsgate. In the long run this deal to me makes sense but will take a few years to see the benefits.

21 Oct 2016, 03:31 PM

Basman
They own 10% or minor ownership of Lionsgate already since september.

21 Oct 2016, 04:01 PM

Dividend Sensei, Contributor
Author's reply » LGF, sure, that makes sense. $5 billion or less, we could do that with cash on hand.

21 Oct 2016, 04:21 PM

thorgood4
are you investment bi-polar? your headline says it's a bad deal but you are saying you will buy T with both fists to capture the dividend?

21 Oct 2016, 10:33 PM

Dividend Sensei, Contributor
Author's reply » AT&T is a great company, and a solid core holding.

I'm saying that, at this time, with the balance sheet as it is, the deal will likely result in a ton of dilution that means it will take years to become accretive.

3-5 years by my math, depending on the synergies management can achieve.

In addition, if you compare the alternative, of not doing this merger, through a pretty much all stock deal (which is what I think is likely) then the break even point, in terms of when the dividend growth will become faster with this deal than without it, is even longer.

I love AT&T for its high-yield. I'm less thrilled with it's 2% payout growth rate.

The reason I chose AT&T over Verizon is because management's plan, of diversifying into cash rich businesses makes more sense than Verizon's strategy of trying to recreate Facebook's success in advertising.

My investment thesis was that AT&T would de-lever and then increase the rate of dividend growth.

That has just been pushed back a good long ways. Not forever mind you just back.

In the long-run TWX's content, and growing FCF will be great for us.

In the short-term not so much. Top line growth sure, net income growth, absolutely. EPS and FCF/share? No, not for awhile.

Does that mean I'm now bearish AT&T? No, because I did the math and even in a worst case scenario, 100% all stock deal at $110/share for TWX the dilution won't put the current payout at risk.

And if the stock ends up selling off to $37 or $36 then the yield gets high enough to make it worth buying more of, (per my planned strategy) and holding on long enough for the deal to finally come through in the end.

I'm trusting management that this is part of a bigger vision, and that eventually the FCF/share growth will result in that faster dividend growth.

So in the meantime I grab every opportunity I can to lower my basis and raise my YOIC.

21 Oct 2016, 11:15 PM

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thorgood4
It's deja vu Ma Bell all over again...or like in 1949 when $T took antitrust fire for first time.... their never ending quest for world domination rocks on...

22 Oct 2016, 12:26 AM

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thorgood4
if T is stupid enough to pay 110, she kisses 35 on Monday I betcha.

22 Oct 2016, 12:27 AM

Beet Farmer
Great synopsis.

22 Oct 2016, 04:46 AM

Dividend Sensei, Contributor
Author's reply » I wouldn't go that far. AT&T had a literal monopoly on land line phone service. Now they are branching out into media.

Now if they tried to buy Comcast? That would make for some major antitrust concerns.

22 Oct 2016, 11:02 AM

Dividend Sensei, Contributor
Author's reply » Depends on how they structure the deal. All stock? Maybe $36, because the stock has fallen so much already.

$35 is steep, but I wouldn't be opposed to picking up more shares at that price.

22 Oct 2016, 11:03 AM

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stockchump
AT&T wants TW for its content/show producing abilities. Streaming content via the Internet to a variety of devices is the move beyond cable and satellite. But, AT&T management's ability to properly manage content makers, producers, creative people and out of the box guys is questionable. AT&T is stuck in the 1980s copper wire and barely does cellular/wireless well, will it fail at managing the content it wants at such a high price. I see debt, stock dilution and then 5

years down the road a big bust up with the content folks running away.

22 Oct 2016, 12:06 PM

Dividend Sensei, Contributor
Author's reply » I don't know. They are number 2 in wireless and still growing subs, so they are doing something right.

As for content? Well all they have to do is leave current management in place for that.

I'm more optimistic. Not saying that $110 isn't a high price to pay for TWX, but in the end it will work out. Just means more token dividend growth for now.

But if you can buy them for $35 in the next few months? That's still more than ok with me.

22 Oct 2016, 12:47 PM

Croswell
Chernen will be making sure the content makers, producers, etc. are on the ball.

22 Oct 2016, 04:23 PM

Dividend Sensei, Contributor
Author's reply » I have to say I'm getting more and more excited for tomorrow's big announcement! And for Monday's open.

Now if the AH drop of JUST 0.8% is any indication I'm going to be disappointed. I am looking to buy under $37.

Here's hoping to not being disappointed on Monday.

22 Oct 2016, 09:08 PM

Outafter20
3rd Quarter Earnings Released:

http://tinyurl.com/gns...

22 Oct 2016, 09:10 PM

Dividend Sensei, Contributor
Author's reply » I know I'm excited. We get out token penny!

22 Oct 2016, 09:37 PM

as10675
"AT&T also announced that its board of directors has approved a 2.1% increase in the company's quarterly dividend. AT&T's quarterly dividend will increase from $0.48 to $0.49 per

share."

WOW!!, consistent 2% dividend increase. Get your penny here, get your penny.

There goes my far, far superior TWX investment out the window.

as10675

23 Oct 2016, 12:57 AM

Dividend Sensei, Contributor
Author’s reply » Well you're free to join us in our ongoing vigil, yearning and holding out hope for the dividend growth to increase...to a whole 2 pennies, one glorious day;)

23 Oct 2016, 01:12 AM

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as10675
>>>Well you're free to join us in our ongoing vigil, yearning and holding out hope for the dividend growth to increase...to a whole 2 pennies, one glorious day;)<<<

When that happens we can suck down two beers, followed by two shots and then dance to the 2-penny poka!! I may have to poka with my walker or do it in my wheel chair by then.

as10675

23 Oct 2016, 01:19 AM

Larry Fuller@fullerassetmanagement.com
Given the steadily improving net profit margins and productivity over recent quarters at AT&T as well as the growth in business in the commercial wireless and Mexican and Latin American markets, AT&T should be able to easily do a leveraged buyout of TWX and continue to increase the absolute cash dividend for their shareholders.

21 Oct 2016, 03:35 PM

Basman
👍

21 Oct 2016, 04:00 PM

Dividend Sensei, Contributor
Author’s reply » Borrow $80 billion to buy TWX? Now that would take our leverage ratio over 4, and guarantee some downgrades. Can't see management doing that.

21 Oct 2016, 04:23 PM

Croswell

Yep, this deal STRENGTHENS the Dividend longterm. People way-overthink things sometimes. This is a GREAT company they are buying. Not some crappy company that will be gone tomorrow.

21 Oct 2016, 08:54 PM

Dividend Sensei, Contributor
Author’s reply » I agree, TWX has great brands, and great content. It's a smart strategic move, but investors need to realize what the ramifications are.

Management had previously said big deals were done because the balance sheet was the priority. This deal pretty much blows that guidance out of the water.

Perhaps it was an opportunistic buy, I don't know. But as far as the next few years? Unless management can squeeze 20% to 30% synergies out of TWX it won't be that great.

We'll see what the details are. I look forward to crunching more numbers to see what the future of AT&T's dividend growth rate will be after this.

21 Oct 2016, 11:19 PM

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thorgood4
Mexico and Latin America- two stable economies with stable governments- bet T get s some pretty sweet deals down there. think like a criminal:)

22 Oct 2016, 12:30 AM

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thorgood4
"I agree, TWX has great brands, and great content."

yikes honey you don't set the bar very high do ya? you need to get out more:)

22 Oct 2016, 12:37 AM

Dividend Sensei, Contributor
Author’s reply » Well its all a matter of taste I suppose. BUT their brands are popular with enough people to make for some nice growing FCF. That's mainly what I meant.

22 Oct 2016, 11:04 AM

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dunnhaupt
Bad for investors? I can't complain. Made 8% profit.

21 Oct 2016, 03:36 PM

Dividend Sensei, Contributor
Author’s reply » I'm talking about long-term dividend investors.

21 Oct 2016, 04:23 PM

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thorgood4
if you just made 8% you're a trader not an investor.

22 Oct 2016, 12:38 AM

YoungGeezer
Appreciate the analysis.

I don't like the deal just from a customer standpoint: Take two companies with marginal customer service, squeeze some more "synergy savings" out, and you've just made a couple of icky companies even less customer-friendly. The only thing this has going for it is reducing competition, which means their rents are secure but us miserable consumers will be stuck.

Long T (but thankfully not a customer anymore), and not a happy TW customer.

21 Oct 2016, 03:41 PM

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richieri1318483
What customer service are you asking out of a content provider

21 Oct 2016, 03:53 PM

Dividend Sensei, Contributor
Author’s reply » Not sure what you mean by customer service for TWX. HBO?

If you mean Time Warner Cable, that was bought by Charter Communications and isn't involved with this potential deal.

21 Oct 2016, 04:24 PM

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yellow ledbetter
Haha. I was thinking the same thing. Dude doesn't even know what he is investing in!

21 Oct 2016, 06:02 PM

User 10342501
YoungGeezer -

I've been an ATT wireless customer for many years. Nothing but good experiences. That doesn't mean I like this deal as a stockholder, though.

21 Oct 2016, 06:04 PM

Dividend Sensei, Contributor

Author’s reply » Reuters is reporting deal is struck! $110/share, or 23% premium to today's close.

So my 25% premium pretty much called it. Now all that's left is to know...how much is stock, and how much is debt (ie cash).

I'm against the deal if its 100% stock, but if it must be done, then make it as non-dilutionary as possible. So ideally all debt, despite what that would mean for the balance sheet.

21 Oct 2016, 06:29 PM

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nickeld
I think the best part of this deal is that once Time Warner comes under the AT&T umbrella, people might stop confusing it with Time Warner Cable

21 Oct 2016, 08:26 PM

Dividend Sensei, Contributor
Author’s reply » Personally, I like the boost in FCF more. Also like that now I'll be able to go to the theater to see a DC movie and know that I'm supporting my company.

21 Oct 2016, 11:21 PM

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thorgood4
how about serving up shitty content?

22 Oct 2016, 12:39 AM

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thorgood4
Nothing but good experiences.

please tell us what alternate universe you live on.

22 Oct 2016, 12:40 AM

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thorgood4
hold your horses- ever hear of the DoJ? senior shareholder approval? not a done deal. they could get blocked as this puts a lockhold on the NYC market.

22 Oct 2016, 12:45 AM

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thorgood4
NYC=MONOPOLY

22 Oct 2016, 12:47 AM

YoungGeezer

Indeed, I haven't been keeping up. But gimme a bit of a break; I've gotten exactly one Spectrum bill, which looked exactly like my previous TWC bill save a couple of logos. From what I gather, Charter (Spectrum) has already killed TWC's plans for faster internet plans... not pertinent to this mess, though. So I'm back to your main point: Depending on how structured, probably bad for investors.

22 Oct 2016, 08:52 AM

Dividend Sensei, Contributor
Author's reply » Well that's a subjective opinion. Personally I enjoy the Arrowverse shows, as well as Jane the Virgin, and Izombie. Oh and supernatural is just pure fun.

The DC cinematic universe? Dawn of Justice was disappointing but Suicide Squad was pretty fun.

It may not be MCU but it should do pretty well.

And let's not forget HBO, our new crown jewel.

22 Oct 2016, 11:06 AM

Dividend Sensei, Contributor
Author's reply » Nope, no cable included in this deal. You're probably thinking of TWC which is now owned by CHTR.

22 Oct 2016, 11:07 AM

Dividend Sensei, Contributor
Author's reply » Well yes and no. It depends on 3 things.

1. Structure of the buy out, ie how much is stock and how much is debt/cash.

2. Synergies, 10% is bad, 20% is good, 30% is excellent.

3. Time horizon: if you're like me and were expecting a 3-5 year deleveraging period followed by faster dividend growth then you are disappointed.

BUT the assets are solid, FCF is good, and EVENTUALLY the deal will make for higher FCF/share and faster dividend growth.

Now that could be as long as 10 years which is an eternity in the stock market. It also assumes that management doesn't keep doing mega deals every 2-3 years, which based on track record they might.

AT&T tried to buy Tmo and that failed, so did DirecTV, then this.

And based on what insiders are saying is management's plan, we might end up going after LGF within 1-2 years for $5 billion or so.

Plenty of smaller content providers and strategically it's a smart move.

My follow on article will cover the pro and cons of such a strategy, especially the potential/risk of the upcoming 5G war with Verizon.

Telecom and media creates the opening for Bezos style "pour all cash flow into growth" mode.

Trouble is that AT&T isn't a growth stock, it's a high-yield dividend growth stock. So the shareholders aren't likely to be as forgiving if management decides to keep finding new worlds to conquer.

22 Oct 2016, 11:13 AM

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misscbd
Geezer, etc -- TIME WARNER cable/SPECTRUM is NOT part of Time Warner and the recent deal with T does not include the cable company -- it couldn't because it does not own it.

The cable company was spun off about 7 years ago but continues to use the Time Warner name (until now - Spectrum)...

Time Warner owns CNN, HBO and Warner Bros studios (films), etc.....

22 Oct 2016, 11:48 AM

Dividend Sensei, Contributor
Author's reply » Actually 2015, but I get your point. No cable in this deal.

22 Oct 2016, 12:47 PM

Basman
AT&T/Time Warner will be AOL-Time Warner done perfectly. The deal will cost $100 billion plus but it makes AT&T the largest broadband, mobile, media & entertainment company on the planet. I think for this deal to be approved by the government, they will have to shed away some assets and then theirs is the lobbying. Great article BTW.

Note: Disney being the only content company on par with Time Warner (excluding games business, and dominant tv distribution business) it tradinv high today plus it also does not have a majority shareholder.

21 Oct 2016, 03:59 PM

NickWNOLA
I could see them unload the old pots/dsl network get some cash and drop some dead weight. It's not like they would need to shed anything for regulatory reasons. This doesn't include any cable networks. That's been gone for a while from twx

21 Oct 2016, 04:06 PM

Basman
TWX own Turner the #1 cable networks group on the planet with TNT, TBS, CNN, Cartoon Network. What you talking about? I guess you did not read the article, right?

21 Oct 2016, 04:20 PM

Dividend Sensei, Contributor
Author’s reply » I doubt there would be any need for asset sales. Time Warner Cable isn't involved with this because TWX sold it to Charter in 2015.

21 Oct 2016, 04:26 PM

Basman
I guess that what Nick means, that for making it clearer Div-Sensei :D

21 Oct 2016, 04:27 PM

Basman
Thanks*

21 Oct 2016, 04:27 PM

ferjen
LOL. I remember the AOL Time Warner merger well. And IIRC, the word 'synergy' was used a lot back then, too. I've grown to hate that word. :-)

And BTW, didn't T make a foray into buying cable companies before? How'd that work out for them?

21 Oct 2016, 08:51 PM

Dividend Sensei, Contributor
Author’s reply » Well synergies are real. BUT studies show that about 85% of the time management can't get to their stated goal.

So when I do a follow up and re-run my models I'll use a range of synergies based on management guidance to make sure to factor that in.

As for cable, well it hasn't gone so well. They have a decent number of customers, so that's stable cash flow. But Comcast, Verizon and Charter are always keeping the heat on and so it's nowhere near as profitable as wireless.

Just more capital intensive. I'm really hoping 5G allows AT&T to take some market share from Charter and Comcast. Project AirGig has the potential to be a game changer.

No cord cutting potential there.

21 Oct 2016, 11:24 PM

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ijeff
What cable company has T bought? Is there one they attempted to buy where the deal fell through? My memory is hazy (to say the least).

22 Oct 2016, 10:19 AM

Dividend Sensei, Contributor
Author’s reply » People are getting confused with Time Warner Cable.

In 2014 Comcast, the nation's largest cable company tried buying Time Warner which still owned Time Warner Cable. That fell through due to antitrust issues. So in 2015 TWX sold TWX to Charter Communications.

Today TWX is pure content company. That's what we're buying.

22 Oct 2016, 11:14 AM

Retired (and tired) Dave
You are confusing content assets with cable assets. Time Warner had gotten rid of it's cable assets, and the content assets should not be a problem with the DoJ, except to the extent that they will want their pound of flesh to approve the deal. Our Government has become the largest blackmailer in the world in the last few years.

22 Oct 2016, 01:48 PM

Dividend Sensei, Contributor
Author’s reply » Indeed! Donald Trump just said he would try to block the deal if he's elected!

Why? On what grounds? Just because? Or maybe you don't like AT&T wireless service, or thought the last DC comics movie sucked.

22 Oct 2016, 03:59 PM

JR2251
Lot of analysts in CNBC were positive on the deal in view of the shrinking wireless business. I think this fits in their long term strategy after Direct TV acquisition.

21 Oct 2016, 04:08 PM

Dividend Sensei, Contributor
Author’s reply » Keep in mind that CNBC needs stuff to talk about. So they are more prone to be in favor of M&A activity.

In addition, I'm pretty sure they didn't run the numbers, nor do they care about what it would mean for the dividend.

21 Oct 2016, 04:29 PM

JR2251
Fair points. Dividend would be at risk of being cut.

21 Oct 2016, 04:50 PM

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gs3
Have a long enough memory to remember All the analyst were Positive on AOL / Time Warner merger also. We all know how that turned out.

I thought deal like this could happen in future , only after T reduced its debt level and fully integrated DirecTV acquisition .

Will follow this closely as debt level and dilution are now a major concern for me.
A very bold move that could be a game changer though...still long T will have to wait for complete details on price and how they will finance.

D.S. , thanks for your thoughts.

21 Oct 2016, 05:02 PM

Dividend Sensei, Contributor
Author's reply » Woah there friend, let's not go crazy!;) I didn't say it was at risk. Merely that the extra debt would mean that we get stuck with $0.01/year quarterly increases as we've seen since 2009.

Token amounts that don't keep up with inflation.

My concern is with how AT&T can get back to its glory days of 4% dividend growth.

This isn't it, at least not if they do an all stock buyout.

All debt? Doable but not wise. Not going to sink the dividend either, but over $200 billion in debt for a non-bank? That's going to take a long time to pay off.

So payout ratio would end up having to fall, thus the continued token dividend hikes to keep the streak going.

In other words, growth is great, BUT not just for its own sake. Growth, like money, must serve a purpose.

For most of us AT&T owners, that is dividends.

21 Oct 2016, 05:28 PM

Dividend Sensei, Contributor

Author’s reply » Don't forget the investment banks make a killing in advisory fees when this kind of mega deals goes down.

Asking an investment banker if a deal is worth doing is like asking a barber if you need a haircut.

Studies show that 56% of M&A destroy shareholder value, while 87% don't add any value.

It can be done, but must be done carefully.

Always ask, "How will this benefit FCF/share?"

If it doesn't then it isn't a good idea. At least if your goal is growing dividends.

21 Oct 2016, 05:30 PM

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mikeyji
These were telecom analysts who explained the Comcast and NBC correalations as a possible example considering that more people are using their devices to watch content these days. TWX throws off a lot of cash. I added to my T position as it closes in on 5 % yield. I bought TWX for a pairs trade with a tight stop if the deal does not pan out. A possible 20 up and 3 down scenario with my tight stop on Times Warner.

21 Oct 2016, 08:17 PM

Croswell
NO! This strengthens the dividend !

21 Oct 2016, 08:57 PM

Dividend Sensei, Contributor
Author’s reply » Personally I'm planning on owning AT&T forever, but I also added on the dip today.

It was in the morning when TWX halted trading because it was up so much. Saw the Bloomberg news that the deal might be announced over the weekend and I figured it would be proven false.

So now I have a 225% position in AT&T and will be adding another 150% on Monday on the dip. If it keeps falling, low enough for my cost basis to hit -10% I'll add another 175%, and then another 200%.

Will just keep going as long as the stock gets cheaper. Nothing short of the dividend being in danger would make me stop, and nothing short of a cut would get me to sell.

This is just one of those buy and hold forever stocks.

21 Oct 2016, 11:27 PM

Dividend Sensei, Contributor
Author’s reply » In the long-term yes. But it won't help the dividend growth any, at least not

without some major breakthrough in cost cutting by management.

21 Oct 2016, 11:28 PM

Moderation
If that happens, the sky will have fallen and all life on earth will immediately cease.

Okay, maybe a little dramatic-but really, if it happens there would be a LOT of drama in the market.

21 Oct 2016, 11:44 PM

Dividend Sensei, Contributor
Author's reply » Oh I agree. AT&T may not be like JNJ with its AAA credit rating better than the US Treasury, but I still consider its dividend, and token growth as safe as T-bills.

If AT&T can't afford to raise the dividend by $0.01/quarter per year? Then we are in another depression and we will have much bigger things to worry about.

22 Oct 2016, 11:16 AM

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pscalare
As I constantly point out, AOL/Time Warner merger turned out well for AOL (the acquiring company). For Time Warner - not so much.

22 Oct 2016, 12:51 PM

Dividend Sensei, Contributor
Author's reply » Not sure about that. Last time I checked AOL fell off a cliff and ended up being bought by Verizon for $4.4 billion.

22 Oct 2016, 04:00 PM

The Rebel
IMO, in the end this deal will not pass muster with the regulatory agencies, especially since AT&T acquired DirectTV. Why should they approve this deal when they already rejected Comcast-TWC? It may not be apples to apples, but it's pretty close. This deal will linger for two years while the stocks go nowhere during that time.

21 Oct 2016, 04:11 PM

NickWNOLA
Please read up on this. This isn't a purchase of a cable company. This is a content deal. $TWX not $TWC

21 Oct 2016, 04:14 PM

JR2251
One former FCC regulator appearing on CNBC thought due to lot of existing competition in terms of entertainment this would not be an issue.

21 Oct 2016, 04:25 PM

Dividend Sensei, Contributor
Author's reply » Comcast-Time Warner was way different. That was in 2014, back when TWC still owned Time Warner Cable. It would have meant creating a practical monopoly in cable/internet in most of the country.

That's what killed that. TWX sold Time Warner to Charter in 2015. This is just for content.

21 Oct 2016, 04:30 PM

Dividend Sensei, Contributor
Author's reply » TWC, although an acronym for Time Warner Cable, isn't the ticker that trades under. That would be CHTR.

21 Oct 2016, 04:31 PM

Dividend Sensei, Contributor
Author's reply » Yeah, I agree. Regulatory approval isn't the issue. It's how much to pay for TWX, how to structure the deal, and how to pay for it.

Now if you assume they do go crazy and borrow the money for it, then you're looking at $4.44 per share in FCF in 2020. That could allow a $3.11 per share dividend, representing 12.8% CAGR growth over the next 4 years.

In reality they wouldn't push it that far, but maybe half that would still be a win for DGI investors.

It would certainly send the stock to record highs.

21 Oct 2016, 04:34 PM

pscalare
TWX did not own Time Warner Cable in 2015. Time Warner spun off TWC in 2009 and was an an independent company in 2015 when it was bought out by Charter Communications.

22 Oct 2016, 12:57 PM

Retired (and tired) Dave
Adding a fair amount of debt might not be the worst thing in the world. I haven't looked at everything included in TWX, but I would be surprised if, with a company that large and varied, there isn't some portions that might not fit well with T, and can be sold off to reduce some of the debt load.

22 Oct 2016, 02:22 PM

Dividend Sensei, Contributor
Author’s reply » Thanks for the correction.

22 Oct 2016, 04:01 PM

Dividend Sensei, Contributor
Author’s reply » No there isn't. It's pretty much all content.

HBO and Cinemax
Turner Broadcasting (all the internet channels AT&T wants to put on DirecTV without paying for them)
Warner Brothers: including the CW, DC Comics, the studio, and its backlog of movies.

They are all valuable cash producers. Sure you could spend $85 billion to buy TWX, take on $25 billion in their debt, but then sell off 25-50% of the cash flow stream to pay down the debt?

If debt is the concern then don't do the deal. Management is basically saying, "forget what we said about being too leveraged, we want content, and cash flow".

22 Oct 2016, 04:04 PM

Busterzzz
AT&T still relies on leeching off the American Taxpayers. They cant even pay for their own IT-enabled employees in India and the Philippines. This acquisition proposal should make the American taxpayer question how long they want to continue to let AT&T steal from them.

21 Oct 2016, 04:45 PM

bluepup
Don't understand the leach off the taxpayer comment. How ? Long T , will buy a little more if much lower.

21 Oct 2016, 04:57 PM

Dividend Sensei, Contributor
Author’s reply » I too would like to know what you mean.

21 Oct 2016, 05:31 PM

jbc123
He doesn't know what he means, that would make it hard to explain to you!

21 Oct 2016, 05:48 PM

achilleus
TWX showing an annual dividend of $1.61

21 Oct 2016, 04:47 PM

Dividend Sensei, Contributor
Author’s reply » That's right, 2% yield.

21 Oct 2016, 05:32 PM

otistcampbell
Good article and thank you. If AT&T wasn't simultaneously creating new global markets, I would be greatly concerned but it appears as though they are ramping up their strength and market position to take advantage of a much broader marketplace. I am a babyboomer long on T who is very grateful for solid, stable and reliable divi's.

21 Oct 2016, 04:50 PM

whattruckamion
Ok, let me get this right. AT&T with arguably the worst customer service of any company around, buys direcTV, which absolutely hands down has the worst customer service I have ever seen in my lifetime and is a DYING company due to cord cutting, which is never going away and gaining momentum at a phenomenal rate....... is going to buy another dying company who happens to have horrific customer service and has even had to advertise extensively that their customer service has changed, because they lost so many customers. OMG. This will be fun to watch!!!

21 Oct 2016, 04:55 PM

Dividend Sensei, Contributor
Author’s reply » Time Warner Cable is not being acquired, that was sold to Charter Communications in 2015.

I should note, that I bought more after these 2 sells offs.

If a deal is announced, then I expect AT&T to fall another 3-4% on Monday. I shall be standing buy ready to add another 150% position.

Can't say no to a 5.3% yield.

21 Oct 2016, 05:34 PM

jbc123
If you see a clue, wave to it as it passes.

21 Oct 2016, 05:50 PM

bishop01

whattruckamion - please research the topic/companies before you comment.

21 Oct 2016, 06:00 PM

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ke8336
This is TWX the content company not the cable company which recently merged with Charter.

21 Oct 2016, 06:13 PM

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whiteowl
"Can't say no to a 5.3% yield."

Sounds pretty good until it is offset by a 9% decline in the value of my current position.

21 Oct 2016, 07:09 PM

13mike
whattruckamion, did you read any of the comments? At&t is not considering the purchase of a cable company. They are considering the purchase of a content provider.

whattruckamion, arguably customer service is a silly reason on which to base a stock purchase.

Mike

21 Oct 2016, 07:21 PM

Dividend Sensei, Contributor
Author’s reply » I can understand how that might make you upset, especially if you're retired and have to sell 3-5% of your portfolio each year to pay living expenses.

In that case you count on price appreciation.

But consider this. It seems current management is pursuing a Bezos like strategy of forgoing short-term dividend growth in favor of long-term FCF channels.

This means that the only real way we can make really good returns is if AT&T pulls back, and we buy on sharp dips, picking up shares at a 5% to 6% yield.

Then the price will rebound and we can all be rich AND have our rock solid dividend income.

Remember the more the dividend grows, the less shares you have to sell to pay the bills.

Being able to live completely off SS and dividends? Now THAT is the American dream. True financial independence.

21 Oct 2016, 07:50 PM

Dividend Sensei, Contributor
Author’s reply » Well in fairness to whattruckamion poor customer service isn't necessarily a

reason to stay away from a company.

After all, it hurts brand equity, and can lead to customer flight and falling sales.

It's a big concern for CMCSA shareholders but management is really making a concerted effort to improve service and customer satisfaction.

We can thank AT&T and Verizon for that. The competition they are providing is putting the fear of god into Comcast and reminding it that you can't treat customers like crap.

21 Oct 2016, 07:52 PM

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left_coaster
Good lord. Not a clue.

21 Oct 2016, 08:03 PM

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left_coaster
This. I'm looking for low 30's to add.

21 Oct 2016, 08:04 PM

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thorgood4
actually it's just a rolling scale of crap service-but who's splitting hairs? they all suck.cheers!

21 Oct 2016, 10:20 PM

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thorgood4
totally agree mate

21 Oct 2016, 10:21 PM

Dividend Sensei, Contributor
Author’s reply » Well this news won't likely get us there, but we can always hope.

21 Oct 2016, 11:28 PM

Dividend Sensei, Contributor
Author’s reply » I don't know. I've only heard good things about Google Fiber.

21 Oct 2016, 11:29 PM

RAchip
Its hard for me to imagine how T could do this acquisition without issuing a ton of new shares. Id they massively increase their outstanding shares, how are they going to pay the existing dividend on all those new shares? I dont see how the TWX cash flow could support the existing dividend on the new stock.

21 Oct 2016, 05:05 PM

Dividend Sensei, Contributor
Author's reply » No worries on that. FCF/share would decline a bit but the dividend would remain safe and continue growing at its annual token amount.

TWX is producing over $3 billion in FCF per year, so that will help.

Synergies from DirectTV are still coming, and other cost cutting endeavors are also planned.

The deal will lead to $26-$27 billion in FCF by 2020 but we can't forget that we would have more debt to pay off, and we have to fight a 5G war with Verizon.

21 Oct 2016, 05:37 PM

Basman
$12 billion in FCF alone this year, DC Comics alone is going to do must of that for Time Warner.

21 Oct 2016, 05:41 PM

Dividend Sensei, Contributor
Author's reply » ? TTM FCF is $3.586 billion. Where are you getting $12 billion from?

21 Oct 2016, 06:31 PM

Basman
the old yahoo finance? but maybe that the new update. thanks :)

21 Oct 2016, 06:40 PM

Dividend Sensei, Contributor
Author's reply » No, Morningstar, financial tap, cash flow, TTM

21 Oct 2016, 06:58 PM

Basman
alright... anyway i am reading that Peter Chernin was involved in the discussion between AT&T and Time Warner.

21 Oct 2016, 07:00 PM

Dividend Sensei, Contributor
Author's reply » Thanks for the info. This makes me feel better. The man has an impressive resume.

21 Oct 2016, 07:55 PM

Basman
Your welcome bro :)

21 Oct 2016, 07:58 PM

Croswell
Chernin said was a good deal for AT&T on CNBC yesterday.

21 Oct 2016, 09:09 PM

Dividend Sensei, Contributor
Author's reply » I'm assuming he has better synergy data so this is a hopeful sign. Then again, "trust but verify".

21 Oct 2016, 11:29 PM

User 10342501
Excellent analysis, Dividend Sensei. My guess is the dividend is not first-priority for AT&T executives.

21 Oct 2016, 05:26 PM

Dividend Sensei, Contributor
Author's reply » Bite your tongue sir!;) It sure had better be! It's the #1 priority of us owners.

Luckily I predicted the final price of $110 (within 3%) and so we can at least not lose sleep over worries that the dilution will kill the dividend.

It is safe, but not likely to grow, not unless we lever ourselves up to the eyeballs in debt.

21 Oct 2016, 06:33 PM

GoatLbk
I wholeheartedly agree. If the suits mess with the dividend you can current investors flee by the millions of shares.
If the deal goes through, which I hope it does not, they may want to look at selling off some of the newly acquired parts to raise cash and pay off debt.

21 Oct 2016, 08:39 PM

G. Blair Bauer
DS,I'd like your full name and address just in case the dividend isn't safe-I do believe in Kill the Messenger-lol. I truly hope you are right on this one. I am semi-retired and using the dividends to further build security for me when I have to draw upon my 2 portfolios. BUT I am VERY ALARMED at the buying sprees that both T & VZ have been on. They have become 2 mega-monopolies that are truly scaring me. VZ has repeatly scammed me and I have heard complaints from others about T. They get big and they get impersonal. And they get

egotistical...and I get scared. Do these big deals and all this debt make sense?

21 Oct 2016, 09:08 PM

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thorgood4
Not to me. I am steering clear of this lunacy. T has the WORST customer service on the planet. And these media mergers just keep dumbing down the content which is why there is nothing by GARBAGE left to watch anywhere. Personally I am building my own library to I can tell all these so-called content providers to choke on the feces they call entertainment.

21 Oct 2016, 10:17 PM

Dividend Sensei, Contributor
Author's reply » While I agree with the underlying sentiment, I am opposed to constant portfolio churn, by investors, and by companies.

Acquiring other sources of FCF, which this, and DirecTV were, is great. Later selling them off? Well that's just poor management, unless the assets are no longer cash cows, (and then why did you buy them in the first place?).

It's why I'm glad PFE is staying together.

Never listen to investment banks, because it's in their interest to make deals sound great, both buying, and selling.

21 Oct 2016, 11:32 PM

Dividend Sensei, Contributor
Author's reply » 1. If there is one thing I'm confident about its that management is committed to the company's dividend aristocrat status. Why else would they keep the token payout increases when they obviously want to be growing an empire?

2. The dividend is almost certainly safe. I showed you my math in the article. FCF/share will drop by $0.10 at first, assuming a 25% premium, and the latest reports says 16%.

That's also assuming an all stock deal, and it's likely it won't be, there will be some debt used, meaning the dilution will be less.

In other words, EPS will instantly go up by more than a nickel a share, and FCF/share should remain at least flat. Thus the payout ratio will be unaffected.

I'll have more specifics once we know more and I can update my models.

21 Oct 2016, 11:36 PM

Dividend Sensei, Contributor
Author's reply » HBO has some great shows, and personally I love all the superhero shows on

the CW.

Arrowverse for the win.

21 Oct 2016, 11:38 PM

PayneOrtlieb
DIS should have bought HBO

21 Oct 2016, 05:35 PM

Basman
DIS should have bought Turner, heck all the greatness of companies and brands owned Time Warner.

21 Oct 2016, 06:32 PM

Dividend Sensei, Contributor
Author's reply » I agree. But now AT&T will. I am REALLY looking forward to:

1. Buying a third position on Monday when AT&T tanks.
2. Reading the transcript of the conference call on this (and studying the presentation on it). Management better be able to squeeze out 20-30% synergies out of this thing, or we are all in trouble.

21 Oct 2016, 06:35 PM

Dividend Sensei, Contributor
Author's reply » It will be ok. As a shareholder in both AT&T and Disney I'll profit either way;)

Interesting side note. Perhaps one day AT&T will buy Disney. Seems that management has got itself a hankering for mega-deals now.

Last deal: $49 billion
New deal: $85 billion = 73% bigger
Next deal: $147 billion?

Disney is at $150 billion market cap. So obviously it would probably take $200 billion to make that happen.

Not that I endorse it of course. The amount of dilution THAT would take would be insane.

21 Oct 2016, 07:02 PM

Basman
If Peter Chernin get Bewkes blessing post-merger, there is going to be fantastic synergy. and i guess AT&T will just sell it stake in Otter (laughs).

21 Oct 2016, 07:06 PM

Dividend Sensei, Contributor
Author’s reply » Why sell Otter Media? Through them we have a stake in Fullscreen and its 450+ million subscribers.

From what I hear, that kind of user base is highly monetizable, at least if you know what you are doing. And with Churnin involved, I believe that to be the case.

Not that we're talking game changing sales figures just yet. Not when we are soon to be a company bringing in close to $200 billion in annual sales.

21 Oct 2016, 07:59 PM

Basman
Time Warner already buying Machinima, but yeah it could come in good use in future.

21 Oct 2016, 08:04 PM

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thorgood4
Jobs should have bought DIS

21 Oct 2016, 10:13 PM

Dividend Sensei, Contributor
Author’s reply » How the heck could he have done that? Apple was never big enough to do that.

It's cash pile didn't get until $200 billion until just recently, 93% of that is overseas and subject to 35% repatriation tax.

He died in 2011. So it was never an option for him.

Now Apple buying Disney? Well I love both companies but it would mostly need to be done in stock. Thus diluting and undoing much of the last few years of buybacks.

DIS has $7.8 billion in FCF, so a 15% increase for Apple. If they could do it all in debt or cash? Then sure it makes sense.

BUT Apple wouldn't do that since buybacks are a big piece of the plan Cook likes.

So it would need to be mainly debt. In order to keep the FCF/share growing.

Well that would mean Apple would have $300 billion in debt on its balance sheet. That's a lot, even for a cash cow like them.

Wouldn't be easy to get that much debt all at once either. Right now they are raising debt about $5-$10 billion at a time.

$200 billion all at once? Tough ask, this isn't a Treasury auction, and even those don't usually go THAT high.

21 Oct 2016, 11:44 PM

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mkemac
T will do a bankruptcy reorganization soon after they overpay for time w.

21 Oct 2016, 05:53 PM

Dividend Sensei, Contributor
Author's reply » Not unless its $85 billion in debt. That would put AT&T total debt at about $237 billion.

Might be hard to hold onto investment grade credit rating with that.

21 Oct 2016, 06:36 PM

Basman
$401 billion in total assets, after this deal that will balloon to $470 billion plus the new debts of $130 billion a fraction of that, add the combined FCF, and the annual revenue, heck Time Warner with HBO, Turner, and Warner Bros does $7 billion in revenue now that will increase AT&T's quarterly revenue. The debts will be paid off in a decade. The question should be synergy.

21 Oct 2016, 06:36 PM

Dividend Sensei, Contributor
Author's reply » Of course. We just can't forget that the capital expenditures we might face fighting with VZ could get a bit out of control.

BUT I'm not necessarily opposed to building a media empire.

At the very least we should see a nice crash on Monday, perhaps as much as 5%. A great chance to buy the dip.

Then, perhaps the market pulls back a bit, and we pull back another 5%. So buy more.

Then the Fed raises rates and we fall another 5%, so buy a 5th position.

Next thing you know AT&T is my biggest position, which I'm totally OK with.

21 Oct 2016, 07:04 PM

Tradestar
I'm mad as a hornet over this nonsense of a deal. You haven't considered shareholders who, like myself, have invested way too much of their portfolio in AT&T. I felt cornered into doubling and

then tripling down when the share price started to fall, which was a very big mistake. Because after this, what I planned to be a temporary increase in my shares until I could get back to break even and sell the excess shares, never came to fruition. The shares continued to languish or go down, so I was/are TRAPPED in a money pit. I don't even want to tell you how much money I lost on Friday with the $2 dollar drop. Now, the dividend probably dropping, and for certain its expected increase per year dwindling to almost nothing, coupled with a huge share dilution through the TWX deal, and taking on TWX debt, and having to pay dividend on the TWX portion, this deal all around has got to be the worst deal they could have decided to do.

Couple all the above with the fact that they are WAY overpaying for TWX, rumored to be perhaps $110 a share on a stock that was in the $80's until the potential deal was plastered all over every financial site and CNBC, CNN, Bloomberg & FOX -- could there be a bigger horror story for AT&T shareholders.

This smacks of complete shareholder violation of fiduciary responsibility. It is clear that AT&T could care less about the effects on its shareholders, and this is beyond disgusting.

There is all talk here about the EVENTUAL (& still questionable) increase in the overall value of AT&T, but this is years down the line. And, in the meantime, I will have a majority of my money tied up in this company. I feel like I have been put in straight jacket by AT&T. I have basically been screwed by AT&T to the max.

And, it has been said here, and is almost inevitably the case, that the share price will drop more, and perhaps it will continue to drop and drop. That alone is indicative of a reckless deal by a CEO and board that have the business saavy of a wet noodle.

So, Dividend Sensei, what have you to say about the position that AT&T has placed people in my position? I say, basically a screw job to the max.

22 Oct 2016, 09:09 AM

Dividend Sensei, Contributor
Author’s reply » Thanks for your questions.

1. Dividend will not be threatened. My numbers in the article assumes a 25% premium which is $87.5 billion buyout, and we're doing $85 billion.

2. Even if its all stock (not likely but close) then EPS would increase by $0.05. The slightly lower dilution should make it immediately accretive.

3. FCF/share would drop $0.10, but will likely be even, due to slightly less shareholder dilution than what I modeled.

4. So bottom line on dividend is FCF payout ratio, on day 1, will stay the same.

The synergies I modeled of 10%? That's a VERY conservative scenario. 20% to 30% are likely, and best case scenarios, but we'll have to see what management says on Sunday or Monday (CC on Monday I'm sure).

5. Long-term this is good, BUT short-term it means the "pay off debt before raising dividend more than 1 penny per year" is going to stretch longer. That is my big disappointment.

6. As for the price getting whacked over the past few days. Use it as a buying opportunity.

Case in point, like you I bought AT&T much higher, $40.74. That was small initial position.

Yesterday, back before the deal was announced and was just a rumor, I figured the 5% 2 day drop was overblown and added 125% more at $37.83.

Deal is being announced Sunday night most likely, so Monday we'll likely drop to $37 at the open, maybe lower. I'll add another 150% position then.

Now some have predicted we will REALLY get hammered all the way to $36 to $35 as Monday goes on. Potentially based on CC if Wall Street decides management is full of it.

If that happens I'm ready to buy another 175% position, making AT&T my biggest holding.

If next week turns out to be a bad week for the market and AT&T continues to get hammered by this? We could drop to $34 and I'd add another 200% (got to take advantage of market freak outs after all).

And if we see rates increase in December? Well then potentially down to $33, so another 225% position (relative to my initial position).

AT&T is a great core holding, BUT the issue is that from a DGI perspective the payout growth, while assured, is disappointing until they can pay down debt.

Which means that buying on dips becomes the best way to ensure good long-term returns out of this stock.

Get your cost basis as low as possible, get the YOIC (based on average cost basis) as high as possible, and then wait for management's strategy and growing FCF + buybacks to allow dividend growth to double.

Heck, the rising sales from TWX may allow the stock to eventually hit $45 by late 2017, who knows.

I'm focused on long-term growth, ie yield + dividend growth.

Wall Street isn't. They don't so much care about dividends as EPS and sales so they might like the higher top line boost.

7. Don't panic. A bad deal (from my DGI perspective) doesn't mean AT&T is a bad stock worth selling. If it keeps dropping keep adding.

Greedy when others are fearful and all that. Easy to say when the stock is rocketing up 30% in a year, much less easy to do when it's then falling from $42 high to $37. For a stock with a very low beta, that is an extreme drop, a practical bear market.

22 Oct 2016, 11:30 AM

Wilbodave
Tradestar,

I'm not trying to be nasty, but you have no one to blame but yourself. Chasing a declining price, and then becoming upset with management because their timing for a deal just happens to upset your trading has nothing to do with fiduciary responsibility.

T is the largest position in my portfolio, around 11.5%, and my cost basis is $24.88. A drop of 3% or 5% or even 10% doesn't concern me as I'm not trading it.

Unless the CEO and board of T somehow forced you to buy shares, you have no one to blame but yourself.

22 Oct 2016, 01:47 PM

Tradestar
Wilbodave,

I totally disagree with you. It's easy for you, with a cost basis of $24.88, & with only 11.5% of your portfolio in T. I have every right to blame T for doing nothing to stop their share price from falling from $45 to $37. A drop of over 18%? Even the author here calls this an "extreme drop" for a stock with a low beta.

If T, as a company, did nothing to intervene and figure out why they are dropping extremely, that IS a lack of fiduciary responsibility, no matter your assertions it is not. And, this stock will continue to drop, many saying expect even 5% on Monday, which is a little less than half the drop it has already experienced over a period of months, but in perhaps ONE day, and perhaps only to be followed by more and more drops. This has fallen through so many support levels, and there are levels all the way back to Sept. 2002 of as low as the mid 19's. Unless one wants to go back to 10/1/1991 when it was at a low of 13.44. My broker's charts don't go back any further, and I really don't need or care to see any more than this.

Charting has its ardent & pedantic suppporters; it also has its critics. However, I'm looking at what I consider a more reasonable and applicable time range and stock movement pattern, and I don't like what I see. That IS the responsibility of the company not to figure out what they are doing wrong or not doing what they need to to avoid this type of stock movement; especially in what is considered a "safety stock" with a dependable dividend. Now that dividend is threatened by this reckless buyout merger they have embarked on, with huge share dilution, taking on added debt of TWX, overpaying for it, and then having to take further debt to accomplish the buyout. Does any of that make any sense? Many think not, and actually list the reasons that this is a senseless and reckless decision, and I couldn't agree with them more.

22 Oct 2016, 05:48 PM

Dividend Sensei, Contributor
Author’s reply » 1. Support and resistance levels are meaningless when news breaks.

2. Fiduciary duty of management to shareholders only applies to maximizing long-term shareholder value. It doesn't entail preventing shares from dropping over short periods of time.

3. AT&T isn't a "widows and orphans" stock because it never goes down a lot, but because of A. High, secure yield, and B. Amazing track record of slow but steady payout growth, no matter what the economy/market/interest rates may bring.

4. While a drop from $45 to $37 in about a month is significant in terms of relative volatility, the reason for the drop is quite clear. Telcos, Utilities, Consumer Staples, and REITs, all the interest rate sensitive bond alternatives that did great this year, are pulling back pricing in the Dec rate hike.

Management was, and is powerless to stop this. In fact, I would be shocked and horrified if AT&T were to publish a press release over the share price decline. That would only worry people unnecessarily.

5. Dividend is not in danger by this deal, not even if its 100% stock and massively dilutionary. I ran the numbers for you in the article.

$1.96 2017 dividend/$2.60 FCF/share = 75.4% FCF payout ratio.

Stay Calm, Carry On, Buy the Dips

6. Stock price falling has no effect on the dividend. It helps us to reinvest at a better price and higher yield. Embrace the drops like a lover and you too will wind up rich and happy.

22 Oct 2016, 09:18 PM

Outafter20
"Stock price falling has no effect on the dividend. It helps us to reinvest at a better price and higher yield. Embrace the drops like a lover and you too will wind up rich and happy."

They just raised the dividend again tonight for the 33rd consecutive year.

"Fiduciary duty of management to shareholders only applies to maximizing long-term shareholder value. It doesn't entail preventing shares from dropping over short periods of time."

People complain when stock prices decline over a relatively short period of time (12-18 months). AAPL, and more recently GILD are perfect examples. People have been complaining about GILD and how they should make an acquisition. Any Acquisition. These would be the same people to complain if they made a crappy acquisition.

I never understood why people tend to complain about fiduciary duty when the stock price declines over a short period of time.

22 Oct 2016, 09:26 PM

Dividend Sensei, Contributor
Author’s reply » No, rather than just run out and light money on fire, buy back your super cheap shares while you wait to find something worth buying.

People are impatient, it costs them the chance to get rich.

22 Oct 2016, 09:38 PM

1504661
can you hear yourself? maybe its your own fault for putting too many eggs in one basket. relax, and just don't sell.

22 Oct 2016, 11:52 PM

GoatLbk
They recently announced they were looking in the $5-50B area and then a short time later go after a ~$90+B deal. It's too big of a deal which would require too much debt and it's too soon after the DirecTV purchase.
I was glad the T Mobile deal fell through but pissed at Stephenson for wasting $6B on it failing(he should have been fired then). I agreed and still like the DirecTV buy but I just can't see where this makes good financial sense.

21 Oct 2016, 06:32 PM

Dividend Sensei, Contributor
Author’s reply » I'll certainly be scrutinizing the CC transcript closely and adjusting my models.

Should make for an excellent follow up article, once we have the specifics and allow the dust to settle.

Who knows, maybe the market will freak out and overreact to this by taking us down another 10%, 15%, or even 20%. Who wouldn't want to buy AT&T at a 6.2% yield?

21 Oct 2016, 07:06 PM

mkemac
That's because it does not make sense.

21 Oct 2016, 08:51 PM

Dividend Sensei, Contributor
Author’s reply » Well it's too early to say without hearing the details.

Low enough dilution and high enough potential synergies could make it smart.

21 Oct 2016, 11:45 PM

Buyandhold 2012
"As for Time Warner investors, they might also end up feeling screwed."

DS, I have been an AT&T shareholder since Richard Nixon was president. And, believe me, I do not feel screwed.

Please remember that AT&T is famous for splitting up and then slowly coming back together. I have owned so many stocks as a result of buying AT&T that I can't even remember them all. At one time AT&T broke up into 8 companies. Bell Atlantic, Bell South, Nynex, Pacific Telesis were a few of them. Now I have three or four companies as a result of my investment in AT&T. Frontier, Nokia and another whose name escapes me. One of the companies went bankrupt. I think it was called Idearc. Great company. They printed the Yellow Pages. I am the only person left in the United States who still uses the Yellow Pages.

Trust me, Time Warner is a much better company than Idearc. Over the long term, the merger should be a benefit to AT&T shareholders.

21 Oct 2016, 06:53 PM

Dividend Sensei, Contributor
Author’s reply » I'm not saying that it won't. Believe me I love the idea that we will soon own all those properties and content. I'm a big fan of HBO, DC, and the CW.

Just saying that it will likely take 3-5 years for it to become accretive to us. Until then? Well I guess we'll have to be happy with annual penny per share increases and buy on dips.

Not complaining, got in at 5% yield today, and hoping to grab more on Monday at 5.3%.

21 Oct 2016, 07:09 PM

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thorgood4
As a young fogie myself, I must say you make Buffet look like reckless lunatic.

I bet you still use netscape on your commodore and drive your '47 LaSalle? (if true on the latter I am jealous!)

.By the way, I would't exactly be enthralled myself owning those other four companies.

I have no position in TWX (sold it a long time ago or T)

21 Oct 2016, 10:05 PM

Fi-Slut
yes, buy & hold; idearc. I got it too.....thanks for your comments. I may also buy more T

B&H, DS: at what price would you add?

Buy & Hold: you & I have a low cash basis..

best,

Fi

22 Oct 2016, 12:01 AM

Buyandhold 2012
Netscape? What's netscape?

No 47 LaSalle.

67 Ford Galaxy 500.

06 Toyota Camry.

I still have phone books and the yellow pages.

Never got over the trauma of giving up my rotary phone.

Still use a clothesline instead of a dryer. My lawnmower was passed down from 1920. Never pay bills online. Rarely buy anything online. Never do any investing online.

Dislike 90% of the changes that I see in the world.

22 Oct 2016, 09:40 AM

Buyandhold 2012
AT&T is now a hold.

It's a buy at 32.

22 Oct 2016, 09:41 AM

Dividend Sensei, Contributor
Author's reply » So my standard default is wait until stock is -10% for average cost basis, then add a 125% second position, then if -10% again, 150% third position, then 175%, 200%, ect.

For opportunistic flukes like this? I picked up 125% secondary at $37.83 on Friday morning thinking this rumor was false.

My plan as I wrote this article was to buy 150% third position at $37 or below on Monday open if the deal was true.

If the stock drops even lower? Like $36 $35? Then add a fourth position of 175%.

The cheaper AT&T gets the more I'm willing to add, at higher, and higher yields.

This is definitely one stock I don't mind getting to be a big part of my portfolio.

22 Oct 2016, 11:34 AM

Dividend Sensei, Contributor
Author's reply » Well as least you own AT&T. So there is some hope for you yet;)

22 Oct 2016, 11:34 AM

Dividend Sensei, Contributor
Author’s reply » Yes and no.

In my opinion, it's a stronger buy then it was before the deal, if only because the share price is lower.

But certainly don't sell because the dividend remains safe.

If the price hits $32? 6% yield? Oh definitely, back up the truck. Heck I'll probably be on my 5th position by then.

22 Oct 2016, 11:36 AM

Anasazi101
Yes AT&T of yesterday had done many things, besides break-up and then later other spin-offs after making different investments, they started breaking off more parts or discarding what they had bought or invested monies in, to capture Market shares or compete in different fields.

Then many of the parts started reforming back together again with latest being what had been South West Bell, becoming SBC communications, with other combinations of a few other old Bells and then finally re-united with "Old Mama Bell"...Much of Ma Bell rides again under the banner of AT&T or (T).

Much has been learned over the last 30 years or so, and I think good old T, is going to be a nice ride again..
After being away from her for a few years, once again we have been building a new core, to probably end up, passing unto our heirs.
Long T and a couple other Telcoms..
22oct11:40a

22 Oct 2016, 12:05 PM

as10675
>>>Trust me, Time Warner is a much better company than Idearc. Over the long term, the merger should be a benefit to AT&T shareholders.<<<

According FastGraphs $10K invested on 12/31/2011.

T yield 5.1%
Total compounded dividends paid $3,110
Total profit $5,663
9.8% average annual return
Estimated future earnings growth 5.4%

SPY yield 1.9%

Total compounded dividends paid $1,240
Total profit $8,518
13.7% average annual return

TWX yield 1.8%
Total compounded dividends paid $1,653
Total profit $17,091
23.0% average annual return
Estimated future earnings growth 13.4%

TWX returned to the investor $11,428 more over T for the last 5 years or $2,285 more per year. I own both TWX and T. I really don't want more slow growing T. This T buy out of TWX kills yet another "Golden Goose" in my opinion.

>>>"As for Time Warner investors, they might also end up feeling screwed."<<<

That about sums it up alright!

as10675

22 Oct 2016, 12:10 PM

Dividend Sensei, Contributor
Author's reply » I'm really surprised that VZ is trading at such a premium to AT&T, in terms of yield. Not sure why the market thinks that VZ is going to grow faster; its latest moves don't seem to point to that.

22 Oct 2016, 12:49 PM

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ecoman12453
I appreciate the information provides by the calculations are misleading.

first 10% assumed synergies is very low. It will probably be much higher.

more importantly..the new company's leverage ratio will be much lower than T has now.

There's no way they do a deal that would make T delever that much. If it went through like that and T reduced it's leverage 25%...like your numbers indicate they'd get a couple notches or more credit upgrade.

I would expect the deal to be credit/leverage neutral at most conservatively...it probably will add a little leverage actually because they're getting bigger and more diversified. the extra leverage, more so that you assume plus more synergies make the EPS much higher.

With that said thanks for the article...it had very useful facts and info about the deal

21 Oct 2016, 08:15 PM

Dividend Sensei, Contributor
Author's reply » That's why I ran the numbers as an all stock deal, meaning no debt used to buy TWX.

BUT TWX has a ton of debt of its own, that we will be taking onto our balance sheet.

There is no way around it. AT&T is adding $25 billion in debt and the only way that will be ok is if we tap the cash flow from TWX and synergies to pay it down.

As for the idea that the deal will delever us, not sure what you mean.

Management had previously stated that it's goal was to get its debt levels down to more normal levels, to get its credit rating back.

Now our debt is rising. As for the pro-forma leverage ratio, well the exact one, at close of the deal will be slightly different but since regulators aren't going to make AT&T sell off content over antitrust concerns than its pretty much, add up the two revenue, earnings, and cash flow streams, and their debts, and then find the leverage ratio.

21 Oct 2016, 11:50 PM

Clauser1960
Personally, I don't watch tv except some soccer games, but the future is in cord cutting and in tv programs, data and content distributed also if not mainly by phone carriers. VZ has already done something similar with Yahoo. So in my opinion this is a great deal. T will grow faster with a lower yield.

21 Oct 2016, 08:38 PM

Dividend Sensei, Contributor
Author's reply » Grow faster yes, faster dividend growth? Not for awhile.

Lower yield? The markets indications thus far say otherwise.

21 Oct 2016, 11:52 PM

Clauser1960
Of course the yield is now up

22 Oct 2016, 07:04 AM

Dividend Sensei, Contributor
Author's reply » It's why I tolerate rising prices, but am happiest when prices are falling.

22 Oct 2016, 11:36 AM

markhenderson3376@gmail.com
If ATT proceeds with TWX they need to do the following-

1. ATT needs to unload the TW HQ at Columbus Circle and the HBO HQ on 6 Ave and relocate all

necessary staff to Atlanta CNN HQ.
2. ATT needs to clean house @ CNN... the network under ATT ownership can not be known as the 'Clinton News Network' ATT can not be a partisan network that cuts off the satellite feeds of guests interviewed if they mention the HRC Wikileaks emails.
3. ATT should bring in FOX on the deal and sell them the studio. FOX knows how to make movies and the Hollywood community, ATT does not. Get Chase Carey involved, he could be a major help to ATT on this deal. If ATT has a long term 'first look' deal on FOX/TWX movies for HBO exhibition, ATT gets the movies they need to combat HBO churn and not the headaches of the studio business.
I support the deal with these stipulations.

21 Oct 2016, 09:08 PM

Dividend Sensei, Contributor
Author’s reply » CNN stands for "Cable News Network" not "Clinton News Network"

As for the studio, heck no don't sell it.

AT&T isn't going to fire the guys running Warner Studios. They are buying content, and the DC cinematic universe such started. Sure, Dawn of Justice only made $880 million, but that's still pretty good.

We need that DC content, so don't sell it to Fox, especially since their track record with X-Men is hardly stellar.

WB Studios is profitable, not a headache.

21 Oct 2016, 11:55 PM

Basman
@Div-Sensei
👍👍👍

22 Oct 2016, 07:07 AM

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swaps
Thanks for the excellent analysis.

But I wonder why TWX felt the urge to unload itself onto someone else rather than stay independent. A 16 percent premium in stock, is the usual short sighted quick gain for the golden parachute people to cash in on.

T years ago bought Tele-Communications and then unloaded it when it did not figure out how to merge it into its operation. Dr. John Malone got rid of the cable systems iniitially so he could get richer off content providing and overseas cable.

Long T and then I guess eventually TWX

21 Oct 2016, 10:19 PM

Dividend Sensei, Contributor
Author's reply » Keep in mind that the stock shot up 15% AND then a 16% premium on top. So really a 33% premium to before the rumors started.

THEN factor in that TWX is up 28% in the past year.

So it's a very good deal.

Fox tried to buy TWX at $85 and the deal fell through. TWX is now getting $110.

Not anything desperate about it.

21 Oct 2016, 11:57 PM

Basman
Plus Bewkes hates family-ownership that why the Fox deal failed.

22 Oct 2016, 07:03 AM

Basman
@swaps
Peter Chernin entertainment vet for 30 years will be managing Time Warner for AT&T.

22 Oct 2016, 07:05 AM

Dividend Sensei, Contributor
Author's reply » I was unaware of that. Figured he just didn't like $85/share.

22 Oct 2016, 11:38 AM

Dividend Sensei, Contributor
Author's reply » Is this confirmed? Because if so that would be awesome.

22 Oct 2016, 11:38 AM

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swaps
Thanks for the explain.

22 Oct 2016, 12:28 PM

PACKER man
Sold all T today; will stand back and watch this one unfold; too much debt for what formerly was a "widows and orphans" stock;
VZ will now be my second largest holding but am beginning to wonder about it since "bulking up" seems to be the latest craze?

22 Oct 2016, 12:10 AM

Dividend Sensei, Contributor
Author's reply » Well VZ has a ton of debt as well. Personally AT&T remains a widows and orphan stock, just one trying to widen its moat, by acquiring world class content to strengthen its other divisions.

Strategically brilliant, tactically? We'll have to see the terms.

22 Oct 2016, 11:40 AM

TheWallStreetKid
If this deal closes - ATT becomes the "best" stock to own in the USA. If T dips in coming weeks - buy, buy, buy. (especially if you are under age 40) It's like getting a guaranteed First Class ticket to the Moon. Wow! Great dividends, great assets, unlimited growth potential with new creative products. Just unbelievable. Best long term Bull story possible. THIS DEAL MUST CLOSE!

22 Oct 2016, 03:31 AM

Dividend Sensei, Contributor
Author's reply » I like your enthusiasm. But I think there are plenty of other better stocks with more "moon" potential. That being said, AT&T will become my biggest holding if it falls to $35.

22 Oct 2016, 11:41 AM

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wildpitcher
As a shareholder of both T and TWX, I like this deal. I like it very very much. I'm almost giddy.

On the TWX side, I'll have a profit of 70% in a bit more than a year. I can take that portion to buy 1.7x as much stock in a company with a similar growth profile to TWX. On the T side I end up with more growth over the long haul.

It's raining money up in here.

Dave

22 Oct 2016, 05:00 AM

Dividend Sensei, Contributor
Author's reply » Well I can't argue with a 70% gain, converted into a 5% stock.

Congrats sir. Winner winner, chicken dinner.

22 Oct 2016, 11:42 AM

Oldstockguru
Back in the early 50's T was the largest mkt-cap company in the world with GM number 2 looks like the new T is headed in that direction again. Good article, i'm 66 years long on T.

22 Oct 2016, 08:23 AM

Dividend Sensei, Contributor
Author’s reply » In the future Amazon will be the largest company in human history, probably by 2025, when it will overtake Dutch East India Company in inflation adjusted terms. was worth $7 trillion at its peak.

AT&T? Well we'll get there eventually but it will take a long time, and probably a lot more acquisitions and wireless expansion around the globe to make that happen.

5G could be a big game changer. Fiber optic speed wireless internet, without the need for expensive fiber? That could really hit Comcast and Charter, take market share, and give AT&T a huge, cord cutting proof FCF stream.

Heck would also help us to fight our war with Carlos Slim in Mexico.

After all cash flow is the lifeblood of investment capital and we need to beat Verizon and America Movil.

If AT&T can get enough CF to win at 5G? Then we can take that international, potentially into the rest of SA and Africa.

That would be a gamechanger and herald a new golden era for Ma Bell.

22 Oct 2016, 11:45 AM

ChuckXX
I own 2 different AT&T bonds and am thinking very seriously about selling both. Their debt load of 151 Billion after the deal seems just too high for me to wait around for something bad to happen. I'd rather get out a little early than lose a ton of money.

22 Oct 2016, 10:57 AM

Dividend Sensei, Contributor
Author’s reply » You don't need to worry. AT&T isn't going to default on its bonds. The refinancing costs might be higher, but neither the bond holders or AT&T investors are going to end up losing money.

22 Oct 2016, 12:50 PM

Saint Mark
Terrific article, thank you! Are there assets in the TWX stable that could be sold off? Or combined with some current T assets and sold? With T's new reach into Mexico and further south, these content deals bode well over the long term. I'm patient.

22 Oct 2016, 11:36 AM

Dividend Sensei, Contributor
Author’s reply » Yes they're stable, but why sell them off? The idea behind this deal is that we end up owning a bunch of cable channels which means no more content fees for DirecTV.

Add in the FCF TWX is generating, which should be north of $4 billion in a few years, and you have a nice cash cow to help with AT&T's two telecom wars with VZ and America Movil.

22 Oct 2016, 12:52 PM

Anasazi101
Read many of the pro/con comments, and some of the interesting article thanks for all..

Yesterday early we sold a buttload of Reynolds (RAI) during premarket around 8:30a..@$57.50.
You can check what that was all about..?
And later went in and added about 200 more shares of T (not all that much) to a new core I'm trying to finish up...
We believe in AT&T again, and are putting the money near the mouth..
That's Really about all I got to say about her....Good luck to anyone else..
22oct11:50a

22 Oct 2016, 12:02 PM

Dividend Sensei, Contributor
Author’s reply » I am planning on adding MO and PM myself. Was considering RAI but now they are being swallowed by BAT and I'm not a fan of that company. Yield too low.

Laurillard was my favorite tobacco stock, got eaten by RAI. Now they too get eaten. Thankfully MO and PM are too big to eat.

22 Oct 2016, 12:53 PM

Croswell
Foxnews says the deal is 50% stock, 50% cash. Dividend Sensei, what does your model look like with those numbers?

22 Oct 2016, 04:55 PM

Dividend Sensei, Contributor
Author’s reply » Wall Street Journal confirms.

$85.4 billion price, $40 billion in debt $45.4 billion in stock.

1.21 billion new shares.

Details to come in follow up article but the gist is:

Instantly accretive to both EPS and FCF

Depending on what kind of synergy we get, it could ultimately boost EPS and FCF/Share by 50%, and 42% over the next 3 years.

22 Oct 2016, 09:31 PM

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notsosmart
after all these many years why are there still investors who think cos & their management care about the shareholders? care about retirerees? or widows & orphans?LOL.this has become vegas only slower.unless you are an insider its all luck.the many are fooled & lied to by the few lining their pockets.

22 Oct 2016, 05:45 PM

Dividend Sensei, Contributor
Author’s reply » They sure do care about all of us dividend lovers!

Along with this news earnings came out, (flat sales and adjusted EPS not counting DirecTV) BUT dividend hiked! We got our token penny people!

Dividend is now $1.96, 33 straight years! New yield is 5.2%!

And if we manage to drop on Monday? 5.3-5.5% is possible!

22 Oct 2016, 09:33 PM

NJMASC
long T forever. T will likely fall again on Monday and probably Tuesday as well. This will be a good opportunity for new investors to begin a position or to add. When this deal ultimately gets rejected, and it will, T will rise back up.

22 Oct 2016, 09:08 PM

Dividend Sensei, Contributor
Author’s reply » 1. I hope it falls monday.
2. If it does it will rebound tuesday.
3. I hope that market dives both days so I can add on both, in concert with this news.
4. The deal will not be rejected.
5. With 47% cash/53% stock deal it now makes sense. Ugly balance sheet, and leverage ratio is kind of scary, but it makes sense.
6. We got our penny, so it's time to dance:)

22 Oct 2016, 09:41 PM

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jasonjones
How amusing the SA round table thought T was a great buy. Who do you believe?

22 Oct 2016, 09:20 PM

Dividend Sensei, Contributor
Author’s reply » Given that both I and the Round table agree that AT&T is a great buy at the current 5.2% yield, you can't go wrong agreeing with either;)

22 Oct 2016, 09:42 PM

bobcom9017@bellsouth.net
If it hits 36 I'm buying a boatload!!!

22 Oct 2016, 10:07 PM

Dividend Sensei, Contributor
Author’s reply » Me too. It would become my biggest position.

However, now that the truth is out I don't think we'll drop to $36. Not enough dilution to go that low.

23 Oct 2016, 01:14 AM