



A Financial and Competitive Analysis of Rogers Communications Inc and Telus Corporation

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Executive Summary

The telecommunications industry has become more attractive to investors as wireless communication has grown to be an integral part of Canadians’ lives over the past three decades. Rogers Communications Inc. and Telus Corporation are two of the three major players in this industry.

As the market leader, Rogers Communications not only has higher profit margins than Telus, but it also has less debt, superior earnings per share and return on equity. Moreover, Rogers Communications has a lower P/E ratio than Telus suggesting that its stock might not be overvalued and therefore represent a sound investment.

In addition to strong financials, Rogers Communications offers a greater breadth of services (internet, cable, and print publications) than does Telus Corporation. Thus Rogers has greater opportunities for growth and decreased exposure to risk of increased competition in the wireless segment.

Based on these arguments, herein we present evidence to support the recommendation of an investment in Rogers Communications Inc.

# Table of Contents

[Executive Summary i](#_Toc374518251)

[The Telecommunications Industry 1](#_Toc374518253)

[Industry Overview 1](#_Toc374518254)

[Key Industry Characteristics 1](#_Toc374518255)

[Company Overview 3](#_Toc374518256)

[Rogers Communications Inc. 3](#_Toc374518257)

[Telus Corporation 3](#_Toc374518258)

[Comparative Analysis 5](#_Toc374518259)

[Overall Performance 5](#_Toc374518260)

[Profitability 8](#_Toc374518261)

[Investment Utilization 10](#_Toc374518262)

[Return on Investment 11](#_Toc374518263)

[Operating Cycle Performance 14](#_Toc374518264)

[Investment Utilization Summary 15](#_Toc374518265)

[Financial Condition/Liquidity and Solvency 15](#_Toc374518266)

[Current Ratio and Acid-Test Ratio 15](#_Toc374518267)

[The Tests of Financial Condition 17](#_Toc374518268)

[Cash Generated by Operations/Total Debt 18](#_Toc374518269)

[Dividend Policy 19](#_Toc374518270)

[Recommendation 22](#_Toc374518271)

[References 23](#_Toc374518272)

[Appendix A 24](#_Toc374518273)

[Appendix B 27](#_Toc374518274)

# The Telecommunications Industry

## Industry Overview

As wireless communication has grown to be an integral part of Canadians’ lives over the past three decades, investor interest in the telecommunications industry has also grown.

Interest in the industry has been driven by impressive growth and technological development which included in 2011, according to the Canadian Wireless Telecommunications Association (CWTA) (CWTA, <http://cwta.ca/facts-figures/>):

* Over two dozen wireless service providers
* Over 27 million subscribers
* Over 308,000 direct and indirect jobs with an average salary level of over $65,000, compared to a Canadian average salary of $46,000
* A total economic value of $50.2 billion for the Canadian economy ($20.7 billion in direct GDP, 64% of which was retained in Canada)

## Key Industry Characteristics

The Canadian telecommunications industry is highly oligopolistic. The telecommunications providers may be subdivided into those providing internet, fixed line telecommunications, media, wireless communications, or any combination thereof.

According to a report by Rogers Communications Inc, in 2012 the Canadian wireless sector was dominated by Rogers with 34% of the market, followed by Bell Canada and Telus Corporation, each with 28% of the market. The remaining 9% of the market is occupied by approximately 50 local niche players (Rogers Wireless Q4 Report, <http://www.rogers.com/cms/investor_relations/pdfs/At_A_Glance_Highlights-Rogers_Wireless.pdf>).

Despite being controlled by a few large players the Canadian wireless network needs to cover a large territory to service a relatively small market. With 27 million cell phone subscribers spread out over more than 1.3 million km, service providers face high upfront investment and operational costs to build and maintain the network infrastructure (CWTA, <http://cwta.ca/facts-figures/>).

In addition, the government of Canada has promoted a policy for greater competition through more choice, lower prices and better service, thereby stiffening competition and attracting foreign companies (Industry Canada, <http://www.ic.gc.ca/eic/site/icgc.nsf/eng/07389.html>).

However, with wireless penetration in Canada below that of other developed countries, the Canadian wireless sector has the potential for meaningful organic growth (Rogers Wireless Q4 Report, <http://www.rogers.com/cms/investor_relations/pdfs/At_A_Glance_Highlights-Rogers_Wireless.pdf>).

# Company Overview

## Rogers Communications Inc.

Rogers Communications Inc. is a diversified communications and media company. In addition to being Canada’s largest wireless carrier with 9.5M subscribers, Rogers Communications Inc. is the nation’s leading Canadian cable provider. Other services offered by Rogers include high-speed internet access, specialty, print and online media assets, data networking and IP solutions for small, medium and large enterprise, government and carrier customers.

Rogers’ strengths include strong brand recognition, a diversified mix of assets, conservative debt leverage, significant available liquidity and no material near-term debt maturities. In 2013, there will be an annualized dividend of $1.74 per share for investors (Rogers, <https://www.rogers.com/web/Rogers.portal?_nfpb=true&_windowLabel=investor_1_1&investor_1_1_actionOverride=%2Fportlets%2Fconsumer%2Finvestor%2FshowLandingPageAction&_pageLabel=IR_LANDING>).

## Telus Corporation

Telus Corporation offers a variety of products and services, including wireless, data, Internet protocol (IP), voice, television, entertainment and video.

Telus Corporation’s strengths include a strong commitment to corporate and social responsibility, recent capital investments to expand the capacity, speeds and coverage of TELUS’ advanced broadband networks, and sustained growth in market share driven by a customer-first mentality. TELUS declared a quarterly dividend of 36 cents per share on outstanding common shares payable January 2nd, 2014. This level is 12.5% higher than a year ago (Telus, <http://about.telus.com/community/english/investor_relations>).

Given the strengths of both Rogers Communication Inc. and Telus Corporation, a comparative analysis of the two companies will be presented herein, followed by an investment recommendation.

# Comparative Analysis

## Overall Performance

As shown in Table , while both Telus and Rogers have approximately the same market cap and revenue, they are significantly different. Based upon the data presented here, Rogers has a more efficient operation as it has 40% fewer employees than Telus and thus a better revenue/employee ratio. However, an important caveat to this observation is that the numbers do not include contractors and third-party partners (and Rogers could indeed have a big “external” workforce).

From an investor perspective, Rogers appears to offer superior annual earnings and dividends per share. Rogers also shows better dividend yield, earnings and dividends payoff. Dividend yield, earnings and payoffs are important figures to investors as they show performance and profitability. Moreover, with a lower P/E ratio, Rogers would appear to be a better buy than Telus (note though that both companies have below-industry average P/E ratios; telecommunications industry has a 20.60 P/E ratio).

|  |  |  |
| --- | --- | --- |
|  | Telus Corporation | Rogers Communications Inc. |
| Market Cap | $23.06 billion | $24.11 billion |
| Revenue | $11.32 billion | $12.72 billion |
| Employees | 42,400 | 26,801 |
| Revenue / Employee | $267,100 | $474,800 |
| Net Income | $1,381 billion | $1,878 billion |
| Outstanding Shares | 623.3 million | 514.8 million |
| Annual Earnings/Share | $2.14 | $3.65 |
| P/E Ratio | 18.28 | 13.54 |
| Annual Dividends/Share | $1.36 | $2.14 |
| Dividend Yield | 3.57% | 3.63% |

Table 1 - Overall Performance Data; based on trailing 12 months

Good performance and profitability are reflected in stock prices, and Rogers has shown superior performance over the past 5 years (Figure 1).



Figure 1 - Telus and Rogers Stock Market Price, 5 years *(Google Finance)*

Return on assets, return on equity and return on investment for public companies can vary substantially and is highly dependent on the industry. In this report, where both companies are relatively similar these indicators are key to evaluating efficiency and profitability. These ratios clearly show (Table 2) that Rogers Communications Inc. offers better performance on all these indicators.

|  |  |  |
| --- | --- | --- |
| Index | Telus Corporation | Rogers Communication Inc. |
| Earnings Per Share | 2.13 | 3.63 |
| Return on Assets | 6.53 | 9.12 |
| Return on Equity | 7.34 | 47.19 |
| Return on Investment | 7.99 | 10.68 |

Table 2 - Return Indexes

## Profitability

In terms of profitability, both companies are generating positive returns. However, Telus has been performing better in terms of gross margins as shown in Figure 2. No significant difference can be observed in operating margins between the two companies, although the operating margins for Rogers are slightly greater than Telus’ (Figure 3).

Figure 2 - Comparison of Gross Margins for Telus and Rogers (2009-2012)

Figure 3 - Comparison of Operating Margins for Telus and Rogers (2009-2012)

The decrease in the gross margins observed by both Rogers and Telus in recent years is a reflection of the increase in competition in this oligopolistic industry. It is likely that this situation will be further exacerbated as the Canadian government encourages greater competition in the telecommunications industry. As major players in this market, it is likely that Rogers and Telus will suffer from an increase in competition and margins will be further reduced. However, it will likely be a few years before the full effects of this are felt by Rogers and Telus and should not affect one more than the other.

A downwards trend is also observable in the cash available from operating activities. As shown in Figure 4, both companies have seen reduced cash from operating activities over the past few years. Nonetheless, Rogers has outperformed Telus in the amounts of cash realized.

Figure 4 - Comparison of Cash from Operations (2009-2012)

As an indicator of a company's profitability and the portion of a company's profit allocated to each outstanding share of common stock, earnings per share (EPS) serves as an important point of interest for potential investors. Thus, potential investors will be greatly interested to learn that Rogers has consistently outperformed Telus with respect to EPS (Figure 5). Additionally, from 2009 to 2012 Rogers’ EPS grew 28%, whereas that of Telus grew an impressive 22%, but still less than that of Rogers.

Figure 5 – Comparison of Earnings per Share (2009-2012)

Thus, while overall Telus is running more profitable operations, as indicated by their superior gross margin (Figure 2), Rogers has been able to outperform Telus in terms of cash generated from operations, EPS and EPS growth (Figure 3, 4, and 5). Importantly, Buybacks of Rogers’ stock have further supported dividend increases (Rogers, https://www.rogers.com/cms/investor\_relations/pdfs/2013-AGM-Presentation.pdf).

## Investment Utilization

Investment utilization examines the efficiency with which a company is managing their investments. This section will offer insights on how well Rogers and Telus are generating returns from their assets, shareholders’ investment and long-term-liabilities. This analysis will also provide information on whether or not they possess healthy management policies regarding the management of their accounts receivable, inventory and general cash cycles. These indicators substantiate the companies’ trends towards future revenue growth from their investment, as well as potential risk exposure from poor cash management.

### Return on Investment

This first section on investment utilization displays how well Telus and Rogers are able to generate sales revenue (or turnover) from their lump assets, invested capital, equity, fixed assets and inventory.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| INDEX |  | 2009 | 2010 | 2011 | 2012 |
| Total Revenue (in Millions CAD) | **TELUS** | 10,921 | 10,397 | 9,792 | 9,606 |
| **ROGERS** | 12,486 | 12,346 | 12,142 | 11,731 |
| **% OF ROGERS OVER TELUS** | 14% | 19% | 24% | 22% |
| Total Asset (in Millions CAD) | **TELUS** | 20,445 | 19,931 | 19,624 | 19,219 |
| **ROGERS** | 19,618 | 18,362 | 17,033 | 17,018 |
| **% OF ROGERS UNDER TELUS** | 4% | 8% | 13% | 11% |
| Asset Turnover (Times) | **TELUS** | 0.500 | 0.496 | 0.518 | 0.531 |
| **ROGERS** | 0.689 | 0.713 | 0.672 | 0.636 |

Table 3 - Total Revenue, Total Asset and Asset Turnover for Telus and Rogers

As shown in Table 3, Rogers has been generating higher overall turnover from its investments compared to Telus. Additionally, we note that Rogers generated 14 to 22% more revenue with 4 to 11% less total assets, compared to Telus on an annual basis between 2009 and 2012. This statement is also supported by the asset turnover values, which show that Rogers is able to generate more revenues from its assets compared to Telus. This suggests that Rogers made the better use of its investment.

As previously mentioned, these turnover indicators must also be considered in the context of profitability indicators. Table 4 shows that the profit margin for Rogers is slightly greater than that of Telus. Because the general return on investment is the product of the investment turnover (table 3) and profit margin (table 4), we notice that Rogers has higher values in both and consequently a higher return on investment.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| INDEX |  | 2009 | 2010 | 2011 | 2012 |
| Profit Margin | **TELUS** | 10% | 11% | 12% | 12% |
| **ROGERS** | 13% | 12% | 13% | 14% |
| Return on Investment | **TELUS** | 5% | 5% | 6% | 6% |
| **ROGERS** | 9% | 9% | 9% | 9% |

Table 4 - Profit Margin and Return on Investment for Telus and Rogers

Other significant indicators include the invested capital turnover, the equity turnover, the capital asset intensity and the inventory turnover. As shown in Table 5, Rogers is able to use its invested capital, equity, fixed and long-term assets, as well as inventory to generate proportionally more sales revenue than Telus does.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| INDEX |  | 2009 | 2010 | 2011 | 2012 |
| Invested Capital Turnover (Times) | **TELUS** | 0.704 | 0.751 | 0.793 | 0.810 |
| **ROGERS** | 0.921 | 0.978 | 0.793 | 0.879 |
| Equity Turnover (Times) | **TELUS** | 1.272 | 1.256 | 1.374 | 1.412 |
| **ROGERS** | 2.745 | 3.229 | 3.456 | 3.314 |
| Capital Asset Intensity (Times) | **TELUS** | 0.363 | 0.359 | 0.365 | 0.378 |
| **ROGERS** | 0.603 | 0.575 | 0.532 | 0.502 |
| Working Capital Turnover (Times) | **TELUS** | -5.229 | -4.234 | -5.755 | -8.284 |
| **ROGERS** | -23.795 | -11.305 | -19.381 | -15.987 |
| Inventory Turnover  (Times) | **TELUS** | 12.141 | 14.968 | 13.388 | 13.771 |
| **ROGERS** | 8.846 | 40.924 | 37.238 | 26.379 |

Table 5 - Return on investments for Telus and Rogers

Interestingly, we note that the working capital turnover values are all negative values. Because the working capital is equal to the current asset less the current liabilities, we can infer that both Rogers and Telus have more current liabilities than current assets. While this might be a red flag in certain industries, it is not uncommon in the telecommunications industry. This may be explained by companies generally collecting their money within rapid subscription cycles while their size enables them to stretch out their own payment cycles beyond the customers’ subscription cycles. Additionally, most of their capital costs, such as infrastructure and license fees, must be paid up-front.

### Operating Cycle Performance

This section on operating performance examines the ability of Rogers and Telus to properly manage their cash conversion cycles, an indication of whether the firms have healthy cash management policies.

Table 6 shows the main applicable indicators: the Day’s Cash, Day’s Payable, Day’s Receivable, Day’s Inventory and the resulting Cash Conversion Cycle.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| INDEX |  | 2009 | 2010 | 2011 | 2012 |
| Day's Cash (Days) | **TELUS** | 2.526 | 1.021 | 2.542 | 5.651 |
| **ROGERS** | 19.234 | 0.000 | 0.000 | 10.059 |
| Day's Payable (Days) | **TELUS** | 169.284 | 169.426 | 130.968 | 135.148 |
| **ROGERS** | 134.765 | 132.004 | 116.062 | 122.606 |
| Day's Receivable (Days) | **TELUS** | 22.798 | 45.072 | 44.295 | 44.767 |
| **ROGERS** | 40.760 | 43.378 | 46.534 | 44.901 |
| Day's Inventory (Days) | **TELUS** | 30.064 | 24.385 | 27.263 | 26.504 |
| **ROGERS** | 41.261 | 8.919 | 9.802 | 13.837 |
| Cash Conversion Cycle (Days) | **TELUS** | -116.422 | -99.969 | -59.410 | -63.877 |
| **ROGERS** | -52.745 | -79.707 | -59.726 | -63.868 |

Table 6 - Cash Conversion Cycle Values for Telus and Rogers

From the day’s cash indicator, we observe that Rogers is inconsistent from year to year and generally holds more days’ worth of cash than Telus does, indicating that Rogers could potentially manage its available cash more closely.

The day’s payable indicator shows that Rogers consistently keep fewer days’ worth of payables, which indicates a faster payment cycle.

Both Telus and Rogers have similar values for day’s receivable. This is consistent with an industry where customers are expected to pay their monthly bills at constant intervals.

We also observe from the day’s inventory indicator that Rogers manages to keep much less days’ worth of inventory compared to Telus. With approximately 150 to 200 millions of dollars of inventory, this indicates that Telus is tying up much more of its assets into its inventory compared to Rogers.

Finally, an examination of the complete cash conversion cycles of both companies reveals negative values. This is due to the fact that the day’s payables for both companies are much larger than their operating. In effect, they lower inventory and demand payments more rapidly than they are required to make their own payments. Both companies have achieved similar cycle times since 2010, although Telus compensates for its larger inventory by stretching out its payment schedules.

### Investment Utilization Summary

Based upon the investment utilization assessment conducted here, Rogers has achieved better return on their investment as well as better cash management, primarily due to better inventory management. Accordingly, these indicators substantiate better potential growth and stability at Rogers.

## Financial Condition/Liquidity and Solvency

### Current Ratio and Acid-Test Ratio

The current ratio and acid-test ratio measure a company’s liquidity and represent the margin of safety to cover fluctuation in cash flows. These ratios for Telus and Rogers are both well below the industry average of 1.28 and 1.16 (Figure 6). Telus’ current assets increased year by year since 2009, whereas its current liabilities decreased from 4.098 billion in 2010 to 3.520 billion CAD in 2012. The net result of this is an increase in the current ratio of Telus from 0.44 in 2010 to 0.63 in 2012. This indicates that Telus is becoming more solvent as the amount of its current assets near the value of its current liabilities, illustrating that Telus will be better equipped to pay its short-term liabilities.

Rogers is far better positioned than Telus with respect to its liquidity (Figure 6) and has fewer liabilities (Table 7). Therefore Rogers is better positioned with its current assets to pay liabilities.

Nonetheless, as can be seen in Figure 6 and Table 7, while Rogers has outperformed Telus in recent years, Telus has made significant improvements managing its liabilities. In fact, between 2009 and 2012, Telus nearly doubled its results on the current ratio and acid-test ratio signaling an increase in assets relative to liabilities.

In the meantime, the current ratio and acid-test ratio of Rogers remained stable over time (Figure 6 and Table 7), demonstrating that their solvency has remained consistent. Moreover, Rogers' monetary assets exceeded those of Telus, indicating that Rogers has better liquidity than Telus.

Figure 6 – Comparison of Rogers and Telus: Current and Acid-Test Ratios

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Index |  | 2009 | 2010 | 2011 | 2012 |
| Current asset (in Millions CAD) | Telus | 1,127.00 | 1,797.00 | 2,051.00 | 2,210.00 |
| Rogers | 2,255.00 | 1,759.00 | 1,912.00 | 2,221.00 |
| Monetary asset (in Millions CAD) | Telus | 751 | 1397 | 1540 | 1673 |
| Rogers | 1693 | 1443 | 1574 | 1788 |
| Current liabilities (in Millions CAD) | Telus | 2,964.00 | 4,098.00 | 3,845.00 | 3,520.00 |
| Rogers | 2,748.00 | 2,833.00 | 2,549.00 | 3,002.00 |

Table 7 – Comparison of Assets and Liabilities

### The Tests of Financial Condition

The debt to equity ratio measures a company’s leverage. Over the past few years, Rogers has seen a deterioration of its debt to equity ratio as the company significantly incurred total liabilities (from $12.5 in 2009 to $15.5 billion in 2012), while its shareholder equity has been decreasing from $4.2 to $3.7 billion between 2009 and 2012. The debt/equity ratio of Rogers ranges from 2.98 to 4.21, illustrating that total liabilities exceeds shareholders' equity by 2.98 times to 4.21 times (Figure 7). Moreover, during this time period, Rogers has incurred more long-term debt (from $8.4 to $10.4 billion dollars). Thus, with increased long-term debt, Rogers is exposed to greater risk of bankruptcy.

On the other hand, Telus' debt/equity ratio has remained stable at approximately 1.6, as has shareholders' equity ($7.5 to $7.6 billion), while its liabilities increased from $11 to $12 billion (Figure 7). In sum, Telus’ solvency is better than Rogers due to its lower debt/equity ratio. However, debt/equity is quite high for both Rogers and Telus, exposing them to risk of defaulting.

Figure 7 – Comparison of Rogers and Telus: Debt/Equity

### Cash Generated by Operations/Total Debt

From 2009 to 2011, both Rogers and Telus have had comparable cash flow to debt ratios (Figure 8). These ratios for Telus ranged from 47% to 37% with a general downward trend and slight increase in 2012.

Over the same period, both companies’ cash flow from operations has been stable, suggesting here that their total debt has been steadily increasing. In 2012 Rogers’ cash flow/debt ratio decreased to 0.32, whereas its net income increased, thus indicating that Rogers has increased its long-term debt.

Figure 8 – Comparison of Rogers and Telus: Cash Flow/Debt

## Dividend Policy

In recent years, both Rogers and Telus have been consistently awarding dividends (Figure 9). There was a shift in Roger’s dividend policy in 2007/2008 when the company increased its dividend per share by a factor of 3. Following this initial growth, dividend increases have been approximately equal for both companies, reaching 10-11% annual growth since 2010 (Figure 10).

Figure 9 – Comparison of Rogers and Telus: Dividends per Share

Figure 10 – Comparison of Rogers and Telus: Dividend Growth

In terms of dividend yield, both companies have experienced a similar trajectory, ranging between 3.5% and 4.5%, since January 2012 (Figure 11).

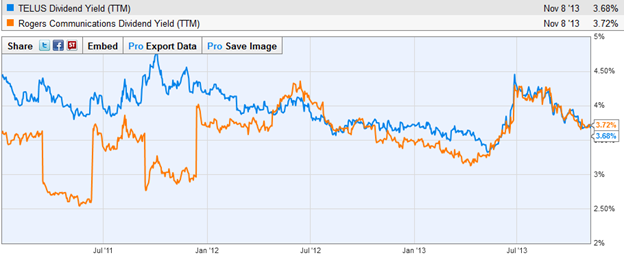


Figure 11 – Rogers and Telus: Historical Dividend Yield *(Google Finance)*

Due to the similarities in dividend yield and growth at Rogers and Telus, other factors must be examined in order to provide an investment recommendation.

Of note is the 2-for-1 stock split effective April 16, 2013 in Telus’ shares. Although the stock split does not bare any impact on Telus’ financial performance, it is likely to result in reduced dividend yield. This may explain in part of the dip in Telus’ dividend yield observed during Q3 2013. Given this, the market has likely already reacted to Telus’ stock split and the impact of the stock split on dividend yield should not be a major concern for potential investors.

Based upon 2012 annual reports, Rogers and Telus both appear to be generating sufficient cash in order to maintain their dividend payments. Specifically, Rogers reported a little over $2 billion in free cash flows (FCF), demonstrating a gain of 8% from 2011, whereas Telus reported $1.3 billion in FCF, 34% growth from 2011. While Rogers has more cash on hand than Telus and thus a greater ability to offer dividends, Telus has had a payout ratio of approximately 60%, whereas Rogers has kept its payout ratio closer to 50% (Figure 12).

Figure 12 – Historical Comparison of Rogers and Telus: Payout Ratio

Base on this information, Rogers appears to be a safer alternative, compared to Telus, when focusing on dividend payouts. Rogers has historically shown a will to improve dividend payments (with significant increases in 2007 and 2008), its operations generate more cash than Telus and their payout ratio is 10% lower than that of Telus. Moreover, as noted above (Table 1), Rogers offered a higher dividend per share in the last year. Consequently, Rogers has the potential to increase its dividend payments in the future as it attempts to be on par with competitors.

Recommendation

Based on the data[[1]](#footnote-1) and arguments provided above, we recommend investing in the market leader, Rogers Communications Inc., rather than Telus Corporation.

Overall, this company offers better financials[[2]](#footnote-2): higher profit margins, less debt, superior earnings per share and return on equity, as well as a lower P/E ratio. This may be due to their better investment utilization. They indeed show better return on investment, as well as better cash and inventory management. They appear more efficient and more profitable than Telus and the indicators discussed above suggest better potential growth and stability at Rogers.

In addition, Rogers Communications provides a greater variety of services, which in turn offers more opportunities for growth. At the same time, this breadth of services lessens the company’s vulnerability to competitors by spreading out risk.

Moreover, consistent growth in dividends awarded and better liquidity and solvency on Rogers’ part are of interest to potential investors.

For all these reasons, Rogers Communications Inc. represents a sound and better investment than Telus Corporation does.

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# Appendix A

Rogers Communications Inc.’s and Telus Corporation Consolidated Financial Statements for the Years 2010 through 2012 (Excluding Notes)

Income Statement

Balance Sheet



Statement of Cash Flow



# Appendix B

Financial Ratio Calculations

Asset Turnover



Invested Capital Turnover



Equity Turnover



Capital Asset Intensity



Day’s Cash



Day’s Payable



Day’s Receivable



Day’s Inventory



Inventory Turnover



Working Capital Turnover



Current Ratio



Acid Test Ratio



Cash Conversion Cycle



Profit Margin



Gross Margin Percentage



1. For complete financial ratio calculations see Appendix B. [↑](#footnote-ref-1)
2. For Rogers Communications Inc. and Telus Corporation’s Consolidated Financial Statements (excluding notes) see Appendix A. [↑](#footnote-ref-2)