

# THE MONTHLY RESEARCH CONFERENCE CALL

## THE COMMUNICATION SERVICES SECTOR



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ARGUS RESEARCH COMPANY



# WHAT'S NEW AT ARGUS

## OCTOBER 2018

### ■ The Argus Weekly Market Podcast

- John Eade addresses the Communication Services sector reclassification  
— Everything you need to know in under 8 minutes
- 2018 Investment Theme Podcast Series  
— Dividend growth, tax cuts, medtech, millennials, etc.
- 3-4 minutes on 10 investment themes

### ■ Argus Quick Notes: Recent Weeks

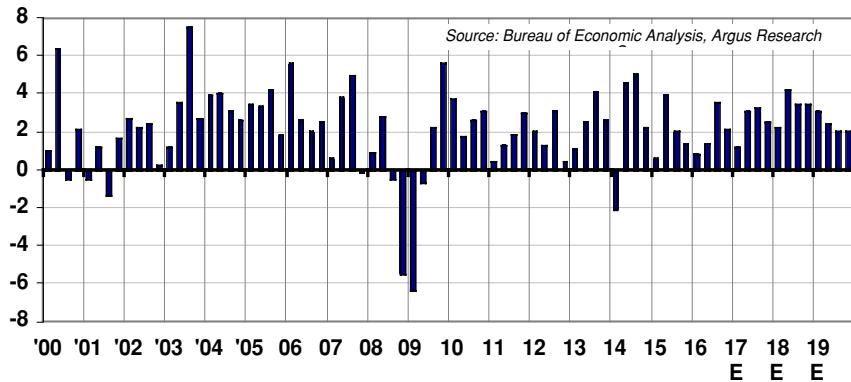
- Defense Stocks
- Hurricane Florence & P/C Insurance stocks
- Healthcare Stocks
- HealthcareETFs

### ■ New on the Argus Site: ETF Screening Tool

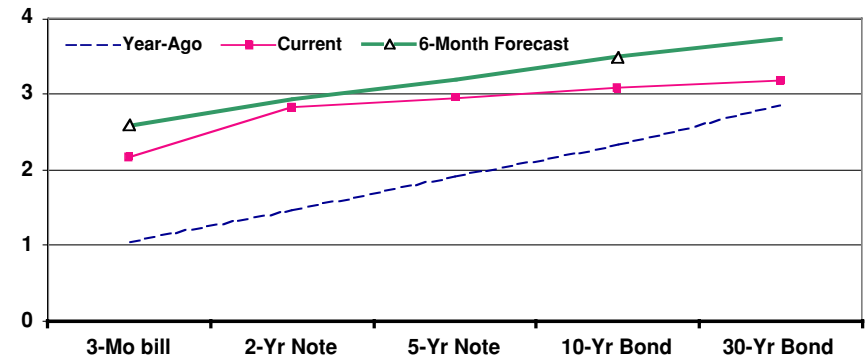
- Enables clients to identify BUY/HOLD/SELLs on specific ETFs
- Allows screening by ratings categories and/or fund families
- Argus uses robust holdings-based approach to rate ETFs
- Future ETF research products to include model portfolios

# MACRO FORECASTS

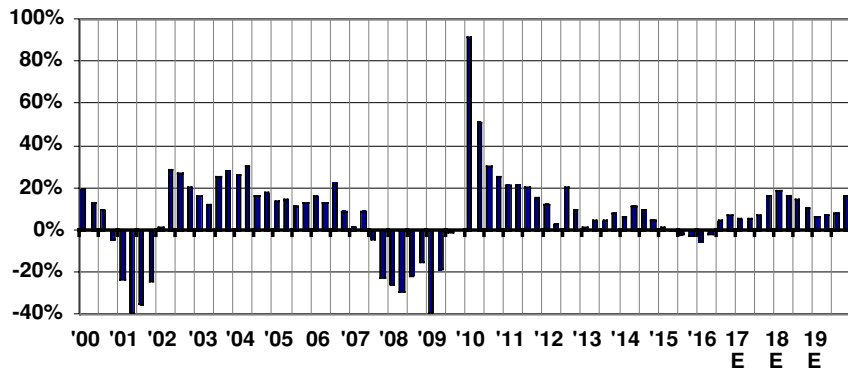
## REAL GDP W/FORECASTS (%)



## TREASURY YIELD CURVE (%)

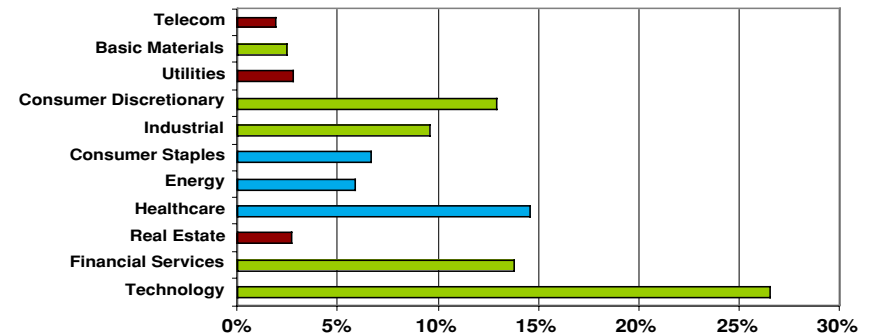


## S&P 500 QUARTERLY EARNINGS GROWTH



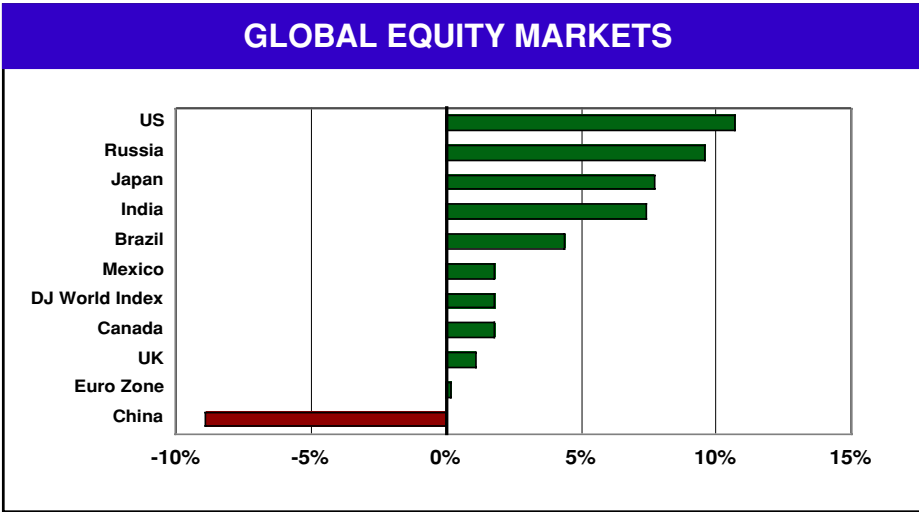
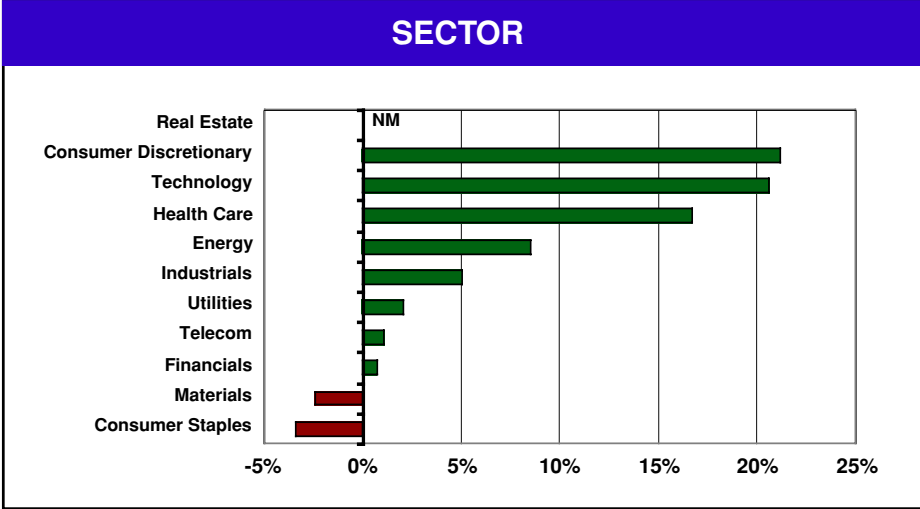
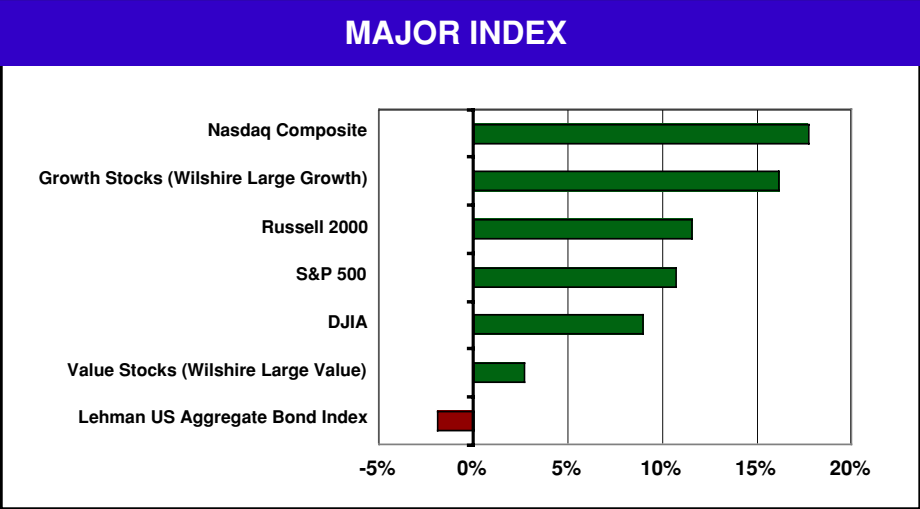
## MARKET SECTOR DISTRIBUTION - PERCENT OF S&P 500

Sectors in Green are Recommended Overweight; Blue are Marketweight; Red are Underweight



# MARKET PERFORMANCE

DATA AS SEPTEMBER 30, 2018



# THE COMMUNICATIONS SERVICES SECTOR — STRUCTURE —

## ■ On 9/ 24/18, MSCI & S&P Dow Jones Indices launched Communication Service sector

- For S&P 500, 26 stocks in Comm. Svc. sector, but only 22 companies
- 23 stocks into Comm. Svc.: 8 from IT, 15 from Consumer Discretionary
- 3 stocks remained from Telecommunications Services

## ■ OLD Sectors: IT (56%), CD (32%), Telecomm (12%)

## ■ NEW Sub-Sectors: Media & Entertainment, and Telecommunications Services

- Media & Entertainment: about 80% of Comm. Svcs sector
- Telecommunications Services: about 20% of sector

# THE COMMUNICATION SERVICES SECTOR — TWO BROAD CATEGORIES —

## ■ Media & Entertainment Industries:

### Media, Entertainment, Interactive Media & Services

- Media subs: Advertising, Broadcasting, Cable & Satellite, Publishing
- Entertainment subs: Movies & Entertainment, Interactive Home Entertainment
- Interactive Media & Services (46% of total sector)

## ■ Telecommunications Services Industries:

### Diversified Telecomm Services, Wireless Telecom Services

- Diversified Telecomm subs: Alternative Carriers, Integrated Telecom Carriers.
- Wireless subs: Wireless Telecommunications services

# THE COMMUNICATION SERVICES SECTOR — HOLDINGS —

## ■ Media & Entertainment Industries:

### Media, Entertainment, Interactive Media & Services

- Media: Advertising (OMC, IPG), Broadcasting (CBS, DISCA), Cable & Satellite (CHTR, CMCSA), Publishing (NWSA, NWSB)
- Entertainment: Movies & Entertainment (DIS, FOX), Interactive Home Entertainment (EA, ATVI)
- Interactive Media & Services (GOOG, GOOGL, FB)

## ■ Telecommunications Services Industries:

- Diversified Telecomm: Alternative (CTL), Integrated (T, VZ).
- Wireless Telecommunications services (none)

# THE COMMUNICATION SERVICES SECTOR — CHARACTERISTICS —

- **Style: new mix is about 2/3rd growth, 1/3rd value; Telecomm Svc. Was 100% value**
- **P/E: nearly triples to 22-times, from prior 8-times**
- **Income: sector yield drops to 1.1%, from a prior 6%**
- **Goodbye, low vol: adjusted pro forma beta rises to 1.1, from 0.73**
- **The payoff is return:**
  - Hypothetical back-tested return, 10-year annualized:
  - Communications Service 15.8%, besting Telecomm Svc. by 12.3% annualized
  - Comm. Svc. lags IT (19.1%) and CD (19.3%) on 10-year annualized return



# THE COMMUNICATION SERVICES SECTOR — IMPLICATIONS OF SECTOR CHANGES —

## ■ FAANG: Scattered to the winds

- AMZN in CD; AAPL in IT; FB, NFLX , GOOGL in Comm. Svc.

## ■ Where's my income?

- Lack of income (1.1%) may step up pressure for cash-rich giants to return cash directly to shareholders.

## ■ Where's my growth?

- Telecomm cos. with slow top- and bottom-line growth may feel pressure to boost revenue, expand margins, and accelerate EPS growth.

## ■ From widely owned to must-own?

- FB, GOOG & GOOGL are more than 45% of Comm. Svc. sector weight
- To get not just sector weight but sector characteristics, index investors must own both GOOG/FB and VZ/T.

# THE COMMUNICATION SERVICES SECTOR — BESTS PICKS —

## ■ ALPHABET INC (GOOGL)

- **Forward revenue growth 20%**

- Non-GAAP operating margin 40%

- **Dominant in digital advertising**

- **New areas of growth**

- Near Term

- YouTube/Google Play/Google Cloud Platform/Nest

- Long Term

- Waymo autonomous vehicle tech/Verily Life Sciences/Loon/Wing/X Labs

- **Possible dividend?**

- Can GOOGL do it? Yes

- \$104 billion in cash on the balance sheet

- TTM free cash flow \$21.3 billion

- Will GOOGL? 50/50

# THE COMMUNICATION SERVICES SECTOR — BESTS PICKS —

## ■ T-MOBILE US INC (TMUS)

- **Forward revenue growth 6%**
  - Non-GAAP operating margin low teens
- **Turnaround story**
  - “Uncarrier” strategy
  - Now challenges the Verizon/AT&T mobile “duopoly”
- **Sprint merger**
- **5G**
  - First use case fixed wireless
  - True wireless 5G in 2019
  - New use cases
    - Internet of Things
    - Wearables
    - Autonomous Vehicle
    - ?

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