Looking for Dividends? Why Bigger Isn't Always Better

Description

Most of us could all use a little more income in our portfolios. But not every income stock that's out there will actually deliver as hoped. That's why investors need to look past the yield and drill down a little deeper to find a dividend stock that will keep the income flowing and growing for years to come.

With that in mind, let's compare two high-yielding Canadian energy stocks that illustrate why bigger yield isn't always better.

A quick look at the numbers shows that **Penn West Petroleum's** (TSX: PWT)(NYSE: PWE) stock is yielding just over 5.6%. That's a lot more than **Enerplus** (TSX: ERF)(NYSE: ERF), which currently yields about 4.4%. However, as we take a closer look at both companies we'll see that Penn West's bigger yield doesn't necessarily make it a better investment.

Drilling down into Penn West
It has been a rough few years for Penn West's investors. The stock is down by two-thirds in just the past three years. One of the reasons for that is the company's conversion from an income trust to a corporation. That switch resulted in its dividend being cut. Its dividend was cut again just last year as the company just can't produce enough income to meet its needs. Needless to say that doesn't bode well for an income investor.

That said, Penn West is working to turn things around. It's cutting its capital spending and its debt while selling off non-core assets. Its new plan is a long-term focus on light oil. The plan is built around Penn West becoming a focused producer in just three core plays where it can achieve high margins and solid returns.

It's a plan that just might work. The only problem is that most of the non-core assets Penn West is planning to sell represent future upside. For example, the $1-1.5 billion in asset sales planned through the end of the year include its position in the promising Duvernay Shale. It's a play that **Encana** (TSX: ECA)(NYSE: ECA), for example, sees becoming one of its core growth plays. Because Penn West is selling its upside early, the company might have trouble growing its dividend in the years to come.

Drilling down into Enerplus

While Enerplus' investors have been on a wild ride as well, its stock isn't down nearly as much. Instead, while Penn West's stock has continued to fall, Enerplus' has headed higher. The reason is quite simple really. Enerplus is already heading in the right direction. The company is taking a much more diversified bet as half of its production is in the U.S. while the other half is in Canada. Similarly, its production is roughly equal as its half oil and half gas. Finally, its portfolio is built upon four strong growth pillars.

Enerplus holds a strong position in the oil rich Bakken Shale along with positions in the gas rich Marcellus and Duvernay. Instead of selling off these growth drivers the company is investing in each. It's investing right alongside Encana in the Duvernay as it has an active plan to complete two horizontal wells this year. Further, it sees 300-400 future wells on its acreage.

That's on top of 145 future wells in its Bakken Shale position, which could actually more than double due to downspacing and the discovery of additional production zones. Needless to say Enerplus has a lot of future growth opportunities.

Foolish bottom line
Right now Penn West is more focused on paring its asset base. That's stripping the company of cash-producing assets as well as future growth opportunities. Enerplus, on the other hand is focused on growing its production and cash flow, both of which are important to growing its dividend. Because of that its slightly smaller dividend looks to be the better buy.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:ERF (Enerplus Corporation)
2. TSX:ERF (Enerplus)

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mdilallo