This Blue Chip Stock Has Increased its Dividend 360%

Description

When it comes to dividend investing, bigger yields aren't necessarily better. Case in point: **Tim Hortons** (TSX: THI)(NYSE: THI).

Canada's top coffee shop pays out only a meagre 2.2%. Throughout most of its history as a publicly traded company, the stock has rarely yielded more than 4%. Yet investors who gave the stock a pass because of its scant payout would have missed one of the country's top dividend growth stories.

Since the company went public in 2006, Tim Hortons has delivered a total return, including dividends, of 114%. Over that time, the company's payout has grown 360%, and more increases are almost certainly on the way as the company's sales continue to climb.

Tim's has a proven ability to grow profits and dividends in good times and bad. Barring some sort of global catastrophe, the company will hike its payout again next year, marking the eighth consecutive dividend increase. Because of this type of long-term consistency, the stock deserves a permanent place in any income portfolio.

The logic behind this idea? Tim Hortons is a powerhouse in Canada, where the doughnut chain has become part of the cultural fabric. The company sells eight out of every 10 cups of coffee sold in the country. Within the fast food industry, the company generates more store traffic than the next 15 chains *combined*.

This is the hallmark of a wonderful business. Companies that can lock in a loyal customer base generate superior profit margins and strong free cash flows, putting them in a better position to return money to shareholders through share buybacks and dividends.

And while most investors think the company's growth story has gone stale, Tim Hortons still has a long growth runway. First, management wants to add 500 more franchise outlets in Canada by 2018. While the Canadian market is seen as saturated, there's still room for expansion in provinces like Alberta and Quebec. The company is also experimenting with smaller, boutique outlets and locations with captive customers like sports stadiums and hospitals.

It also plans to add as many as 300 new locations in the United States over the next four years, a market where it has had difficulty gaining traction. The company has singled out a number of American markets where it already has 100 potential franchises lined up, including Missouri, Ohio, Indiana, and North Dakota.

Perhaps most interestingly, the chain has mapped out an expansion into the Persian Gulf, a region where it has eked out a surprising foothold with 38 locations. The Middle East is untapped territory for North American fast food concepts, with chains like NYFries and South Side Burger expanding into the region.

After adding all of these growth initiatives together, the company is looking to grow earnings per share at an 11% to 13% compounded annual clip over the next four years. Given the fact that the company is paying out less than 40% of profits, Tim Hortons should be able to grow its dividend at twice its earnings growth rate over the next decade.

To be sure, the company has had its share of problems. The Tim Hortons brand doesn't resonate with customers in the United States like it does here in Canada. The company is also facing more competition on its home turf with encroaching American rivals like **McDonald's** (NYSE: MCD) and **Starbucks** (NASDAQ: SBUX).

However, Tim's is fighting back. The company is looking to extract more sales out of existing locations by launching new menu items, renovating its stores, and exploiting social media. Management has pulled the Cold Stone Creamery brand from its restaurants to simplify operations and speed up service, and the company is experimenting with new product offerings to encourage customers to purchase more than one item with each visit.

Tim Hortons will have its ups and downs as weather, commodity prices, and the fickle tastes of customers all affect the bottom line. But given management's commitment to rewarding shareholders through dividend and share buybacks, this stock deserves a core position in any income portfolio.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NASDAQ:SBUX (Starbucks Corporation)
2. NYSE:MCD (McDonald's Corporation)

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