3 Dividend Champions With Wide Economic Moats

Description

An economic moat refers to the ability of a business to retain a competitive advantage over others in the same industry. Factors contributing to a wide economic moat can include high barriers to entry or exclusive patents.

Identifying companies with wide economic moats is a key part of dividend investing, because when a company possesses such a moat it is able to regularly boost dividend payments as margins and profits continue growing.

This is important because investors should focus on companies that are able to consistently grow their dividends and deliver a real rate of return in excess of both inflation and the risk-free rate of return. For the purposes of this article I have taken the yield on 10-year Canadian government bonds as the risk-free rate of return; this currently stands at around 2%.

When a company has a wide economic moat, the sustainability of its dividend increases because of the growing cash flow and profitability it provides.

Let's take a closer look at three Canadian dividend-paying companies that not only have sustainable dividend payments with yields in excess of the risk-free rate of return but also a wide economic moat, allowing them to grow profitability and consistently increase their dividends.

This boring utility company has boosted its dividend nine years in a row

Utilities are perceived as boring defensive stocks, and while this may be true, there is a lot to like about Canadian utility company **Fortis** (TSX: FTS). For the last nine consecutive years it has increased its annual dividend. It's up by a monster 188% over that period, giving it a compound annual growth rate of just over 8%.

This is significantly higher than Canada's annual average inflation rate of 1.9% for that period, and leaves Fortis with a tasty dividend yield of almost 4%. When coupled with a payout ratio of 71% and a five-year payout ratio of 68%, this dividend is certainly sustainable.

More importantly, Fortis possesses a wide, multilayered economic moat. First, the demand for electricity is virtually inelastic because it is one of the primary energy sources for powering our modern lives. Second, the utilities industry has particularly high barriers to entry, making it especially difficult for new companies to enter the industry and thus shielding Fortis from increased competition.

These factors also shield the company from any protracted economic downturn, thus boosting the sustainability of its dividend payment, smoothing out revenue, and providing an almost guaranteed revenue stream.

As a result, Fortis should be a cornerstone dividend stock in any income-focused portfolio.

This integrated energy company maintains a competitive edge that can't be matched

Another dividend champion that stands out because of its wide economic moat and dominant position in Canada's energy patch is integrated energy major **Suncor Energy** (TSX: SU)(NYSE: SU). The company has increased its annual dividend a massive 982% over the last 11 years, giving it a healthy compound annual growth rate of 24%.

This annual growth rate is significantly higher than Canada's average annual inflation rate for the period and gives Suncor a yield of 2% coupled with a conservative payout ratio of 29%.

Even more significantly for investors, major oil companies possess an imposing multilayered economic moat composed of a range of factors including high barriers to entry and inelastic demand for oil globally. In addition, oil companies do not have to market their product, with global demanding setting the spot price and the value of an oil company.

These factors shield Suncor not only from competition but also from any sustained global economic downturn, while guaranteeing revenue, and to a degree, profitability. These things highlight why Suncor is a dividend champion and a stock that should form the cornerstone of any income-focused portfolio.

This troubled midstream company's dividend has risen for 14 consecutive years

The controversy surrounding **TransCanada's** (TSX: TRP)(NYSE: TRP) Keystone pipeline makes the company appear unattractive to investors. However, this controversy illustrates the wide economic moat that exists in the energy sector in general and the oil transportation and infrastructure industry in particular.

It is not only a wide economic moat that makes TransCanada attractive for income hungry investors, but also the fact that it has hiked its annual dividend for 14 consecutive years. As a result, its dividend has grown a massive 140% over that period, which is a compound annual growth rate of just over 6%.

When coupled with a dividend payout ratio of 78% and the wide economic moat associated with the oil industry, it makes TransCanada a compelling addition to any income-focused portfolio, despite its well-publicized problems concerning the Keystone pipeline.

CATEGORY

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