Crescent Point Energy, Canadian Oil Sands, and Penn West Petroleum Have Monster Yields; Should You Buy?

Description

The **S&P TSX 60** index is composed of Canada's 60 largest publicly listed companies and typically these companies are associated with solid market share and financial stability. While many of these companies have relatively conservative dividend policies, there are three monster yields of around 6%, making them key candidates for any dividend-focused portfolio.

But not all dividend yields are made the same with high yields forming part of the risk/reward trade off, which goes hand-in-hand with investing.

Buy: Crescent Point Energy

The highest dividend yield in the S&P TSX 60 is paid by light oil heavyweight **Crescent Point Energy** (TSX: CPG)(NYSE: CPG), at 6.3%, although with a payout ratio in excess of 600%, there are concerns it is unsustainable.

But the company has a history of consistently paying dividends since 2003 while continuing to grow cash flow through growing crude production from accretive transactions and the development of existing assets. Already this year Crescent Point has completed two acquisitions, allowing it to boost its 2014 production guidance and further cash flow growth.

These factors, along with a very conservative degree of leverage, and net debt of a mere 1.1 times cash flow, gives Crescent Point considerable flexibility when managing its balance sheet. This also allows the company to comfortably increase debt if and when required, and Crescent Point will likely be able to sustain this dividend yield for as long as oil production continues to grow.

Buy: Canadian Oil Sands

The second-largest dividend yield in the S&P TSX 60 is paid by **Canadian Oil Sands** (TSX: COS) at a very juicy 6%, and it also boasts a sustainable payout ratio of 82%. The company has been beset by production outages caused predominantly by unexpected maintenance at its upgrader (the machinery that transforms bitumen to light sweet crude).

These outages have caused Canadian Oil Sands to revise its production guidance for 2014 downwards. But despite this and higher than expected operating expenses along with higher debt carrying expense, I believe the dividend is sustainable. Much of the negative impact of these issues on the company's revenue, cash flow, and bottom line will be offset by better than expected industry fundamentals, including significantly higher crude prices.

This monster yield seems sustainable, making Canadian Oil Sands an attractive investment for income-hungry investors seeking better returns than those available from fixed interest investments such as bonds.

Avoid: Penn West Petroleum

The third-highest dividend yield in the S&P TSX 60 is paid by troubled intermediate oil producer **Penn West Petroleum** (TSX: PWT)(NYSE: PWE) at 5.6%, but there are a number of red flags highlighting why this dividend may be unsustainable.

The company reported a net loss for the last two consecutive quarters and continued to have a working capital deficit, despite having made solid progress on implementing its turnaround strategy and divesting itself of a range of unviable assets. In fact, it is the proceeds of these sales that are being used to reduce leverage and fund the working capital shortage. That leads me to speculate that unless Penn West is able to boost margins and cash flow, it will need to continue funding this shortage through debt once asset sales have been completed.

Furthermore, the company continues to see oil and gas production fall which when coupled with a low margin or netback per barrel produced of $36.67 for the first quarter 2014, further highlights profitability remains an issue. This leads me to believe Penn West's juicy dividend yield may be cut again if fundamentals in the energy patch, including oil prices, were to weaken.

Clearly Canada's 60 largest companies offer investors not only the security of investing in large financially stable companies, but also some juicy dividend yields that are attractive for income-hungry investors. But not all of those dividends are created equally, with some being more sustainable than others.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:VRN (Veren)
2. TSX:VRN (Veren Inc.)

Category

1. Investing

Date
2025/09/10
Date Created
2014/07/30
Author
mattdsmith