The Top 5 Dividend Yields of the S&P/TSX 60

Description

There is no better place to hunt for solid dividend yields than among Canada's 60 largest companies, which make up the **S&P/TSX 60 Index**. Not only are there some monster yields available, but also a degree of financial stability.

Not all dividends are created equal as monster yields in excess of 5% are attractive, but do carry a greater degree of risk, with some not as sustainable as others.

Let's take a closer look at the top five dividend yields in the S&P/TSX 60 to see just how risky they truly are.

1. Penn West Petroleum Ltd

It was only a few months back when analysts were trumpeting the success of **Penn West Petroleum Ltd** (TSX: PWT)(NYSE: PWE), which had seen the much-maligned company transform into a star performer. One of the most attractive features of Penn West is its monster dividend yield of 6.9%, which is the highest in the S&P/TSX 60.

But there are signs that the dividend is unsustainable, with the company reporting a net loss in four of the last five quarters and cash flow growth has stalled causing Penn West to divest itself of assets.

Penn West also now finds itself embroiled in an accounting scandal and allegations of stock manipulation, which has seen its share price plunge since the news broke. More concerning is the scandal has resulted in a range of class action lawsuits against Penn West emerge for fraud and breaches of various securities laws.

For a company struggling to deleverage its balance sheet and boost profitability when it is bleeding red ink, these actions will be a costly distraction and this is certainly a dividend stock I believe that investors should avoid.

2. Crescent Point Energy Corp

Perennial investor favourite **Crescent Point Energy Corp** (TSX: CPG)(NYSE: CPG) claims second place with a dividend yield of 6.2%, but there are concerns among analysts that the dividend is unsustainable with a payout ratio of six times its net income.

But with the company continuing to grow light oil production through a range of accretive transactions, driving cash flows up a healthy 25% for the first quarter 2014 compared to the same quarter in 2013, the dividend appears sustainable.

The dividend payout ratio is a mere 48% of operating cash flow, which is a better measure of whether a dividend is sustainable because net income takes into account a number of non-cash items.

3. Canadian Oil Sands Ltd.

The holder of the largest interest in the Syncrude project is **Canadian Oil Sands Ltd.** (TSX: COS), which is a favourite among income-hungry investors and it is not hard to see why. It pays a juicy dividend yield of 6%, which is sustainable when the payout ratio of 86% is taken into account.

However, the company revised its full-year guidance downwards because of ongoing production outages caused by maintenance issues with the upgrader (the machinery that turns bitumen into light sweet crude).

But while this will see cash flow drop, I don’t expect it to have a significant impact on Canadian Oil Sands’ overall financial performance due to stronger fundamentals in the patch.

4. TransAlta Corporation

The fourth-highest dividend yield in the S&P/TSX 60 is paid by **TransAlta Corporation** (TSX: TA)(NYSE: TAC), with a juicy yield of 5.8%, but with the company bleeding red ink for the last two years there are concerns over its sustainability. However, with operating cash flow continuing to grow and the dividend payout ratio being a mere 32% of operating cash flow, there are signs the dividend is sustainable.

Furthermore, electric utilities have a wide economic moat with high barriers to entry protecting them from competition, while the inelastic demand for electricity almost guarantees a revenue stream even during protracted economic downturns.

All of this points to TransAlta’s financial position continuing to improve over the long term and the growing sustainability of the dividend.

5. BCE Inc.

The largest telco in Canada **BCE Inc.** (TSX: BCE)(NYSE: BCE) has the fifth-largest dividend yield in the S&P/TSX 60 at 5%. This yield appears sustainable with a payout ratio of 95%, particularly when BCE’s dominant market position and economic moat are taken into account. The company is also continuing to grow revenues and EBITDA, which for the second quarter were up 4.4% and 3.8% respectively compared to the equivalent period in 2013.

These factors also underscore the sustainability of the dividend yield and the likelihood of further dividend hikes in the future.

Of the five highest dividend yields in the S&P/TSX 60 it is clear there are three companies that every income-hungry investor should consider adding to their portfolio because of their sustainability. These are Crescent Point, Canadian Oil Sands and BCE, while investors may do well to be cautious of TransAlta and avoid Penn West altogether because of its internal issues.

CATEGORY

1. Investing

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1. NYSE:TAC (TransAlta Corporation)
2. TSX:BCE (BCE Inc.)
3. TSX:TA (TransAlta Corporation)
4. TSX:VRN (Veren Inc.)

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Author
mattdsmith