3 Dividend Champions for Every Portfolio: Fortis Inc, Suncor Energy Inc., and BCE Inc.

Description

A dividend champion is a company that has a history of paying a regularly growing sustainable dividend. Typically these companies operate in industries with high barriers to entry such as energy, utilities, and telecommunications. They also possess wide economic moats, virtually guaranteeing revenue streams even during protracted economic downturns.

When selecting dividend champions, I look for three key characteristics. First, their dividend yield must exceed the risk-free rate, for which I typically use the yield on 10-year Canadian government bonds that stands at 1.84%, because dividend investing is a long-term strategy.

Second, the dividend must be growing at a rate that exceeds inflation, ensuring that real rate of return is not being eroded.

Finally, the dividend must be sustainable with a payout ratio of less than 100% and a solid history of consistently paying dividends.

Let's take a closer look at three dividend-paying Canadian companies that possess those characteristics.

1. Fortis Inc

One of my favourite dividend champions by far is Canadian electric utility **Fortis Inc** (TSX: FTS). Currently it pays a dividend with a tasty yield of 3.8% and a sustainable payout ratio of 84%. More impressively, Fortis' dividend has a compound annual growth rate for the last five years of 4%, which is more than double Canada's annual average rate of inflation rate of 1.8% over the same period.

Fortis also possesses a very impressive range of geographically diversified assets covering Canada, the U.S. and the Caribbean. With the demand for electricity being relatively inelastic and high barriers of entry to its industry, its earnings are virtually guaranteed.

The advantages of these attributes are evident from the company's second-quarter financial results in

2014, with cash flow growing a very healthy 21% compared to the first quarter and 19% over the equivalent quarter in 2013. This is particularly impressive cash flow growth for what is a capital-intensive industry and further underscores the sustainability of Fortis' dividend.

2. Suncor Energy Inc.

Despite reporting a shocking 69% fall in net earnings for Q2 2014, **Suncor Energy Inc.** (TSX: SU)(NYSE: SU) still hiked its dividend a whopping 22%, for a yield of 2.4% with a very sustainable payout ratio of 43%. Suncor's dividend has grown consistently since inception in 1992, with a compound annual growth rate of 13% over that period, which is well in excess of Canada's annual average inflation rate.

But it gets better for investors, as the company's core profitability still remains strong with the massive drop in net earnings primarily attributable to the company writing down the value of a range of projects it believes are now non-commercial. While this may be alarming for investors it makes sense, as Suncor is determined to allocate capital only to those projects that deliver the best returns, unlocking further value for shareholders.

Suncor also operates in an industry with high barriers to entry and relatively inelastic demand for its oil and natural gas products. These form the foundation of many of the fuels and energy products that power our modern lives.

Suncor's integrated business model allows it to more effectively manage margins and the price differentials between various crude blends and benchmark West Texas Intermediate and Brent crude prices.

3. BCE Inc.

My third dividend champion is Canada's largest telco, **BCE Inc.** (TSX: BCE)(NYSE: BCE), which has been consistently paying a steadily growing dividend since 1949. BCE currently has a very juicy dividend yield of 5.1% and a sustainable payout ratio of 95%. More impressively, BCE's dividend has grown at a compound annual growth rate of just over 9%, which is well in excess of the rate of inflation for the same period.

Despite the economic moat for telcos weakening in recent years with deregulation removing many of the traditional barriers to entry, BCE still maintains a solid economic moat by virtue of its size and dominant market position.

This allows the company to continue delivering some strong financial and operational performances. For Q2 2014, BCE reported a very healthy EBITDA margin of 41%, while EBITDA grew 6% quarter-over-quarter and 3.8% year-over-year. The company has also embarked on a strategy to privatize **Bell Aliant Inc.** (TSX: BA), which will generate strong free cash flow accretion to further support significant investment in BCE's broadband network.

Each company operates in an industry with considerable barriers to entry, which limits competition, while producing products and services that remain in demand, as they are important components of our modern lives. All of this virtually guarantees earnings growth even in times of depressed economic activity.

CATEGORY

1. Investing

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2. NYSE:SU (Suncor Energy Inc.)
3. TSX:BCE (BCE Inc.)
4. TSX:FTS (Fortis Inc.)
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