Forget Tim Hortons Inc.; Buy These 3 Dividend Stocks Instead

Description

One of the best things about dividend investing is that it's predictable. Case in point: **Tim Hortons Inc.** (TSX: THI)(NYSE: THI).

The stock never boasted a big yield. However, the company generated an enormous amount of cash, carried a small debt load, and paid a steady dividend. That's why it was always popular amongst income investors.

That was until Tim Hortons agreed to a merger with American fast-food giant **Burger King Worldwide Inc.** (NYSE: BKW). Now shareholders have to decide whether to hold on to the stock or take some money off the table. My take: Tim Hortons is no longer a suitable holding for conservative investors, and they should look for new opportunities elsewhere.

If you're a Tim Hortons shareholder, you have to read this

Earlier this week here at The Motley Fool Canada, I highlighted my two concerns with this deal.

First, my main worry is the new company will be saddled with US$11.8 billion in net debt including preferred shares. After the deal is closed, Burger King/Tim Hortons will carry about $7.60 in net debt for every $1 the company generates in earnings before interest, taxes, depreciation, and amortization, or EBITDA. That's a staggering sum relative to Tim's current 1.6 net debt/EBITDA multiple.

You don't need a PhD to see the potential problem here. Like a family that has maxed out all of their credit cards, too much debt leaves a company with little financial wiggle room. That could result in a dividend cut if interest rates rise or the industry sours.

Second, just like in any leveraged buyout, management is going to have to direct all of its excess cash flow to paying off debt. That's going to be the case for the foreseeable future. The days of double-digit dividend hikes are over.

Let me be clear: I'm not saying the merger will be a flop. Rather, Tim Hortons is no longer the conservative, dividend company income investors once loved. And when a stock's investment thesis has completely changed, it's usually best to move on.

Here are three dividend stocks to buy instead

Of course, for most Timmies investors, selling their shares will leave a hole in their portfolios. That's why I created a list of three replacements. Just like Tim's, these companies all sport steady, predictable payouts. And while the yields on these stocks won't blow your socks off, I expect them to grow their distribution significantly in the years to come.

- **Suncor Energy Inc.** (TSX: SU)(NYSE: SU): You need size and scale to tackle the toughest energy challenges, and it doesn't get much bigger than Suncor. The company's oil sands production is on track to grow at a double-digit annual clip over the next decade. And with most of its biggest capital expenditures behind it, I'd expect Suncor to starting gushing cash flow (and dividends). That might be why legendary investor Warren Buffett has been building his position in the company.
- **Royal Bank of Canada** (TSX: RY)(NYSE: RY):Since 1870, Royal Bank has paid a dividend every year to its loyal shareholders. Think of everything that has happened over that time — wars, depressions, financial crises, asset bubbles. Yet for Royal Bank, it has hardly mattered. And given that it's nearly impossible for competitors to enter the Canadian banking industry, I'd expect this company to continue mailing out dividend cheques for another century to come.
- **Enbridge Inc.** (TSX: ENB)(NYSE: ENB): Energy prices may be volatile, but the number of barrels flowing through Enbridge's pipeline network are incredibly consistent. They're so steady, in fact, that the company's cash flows resemble bond coupons. Don't let Enbridge's meager 2.5% dividend yield fool you. I'd expect this company's distribution to grow significantly in the years ahead thanks to North America's booming oil production.

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