The 3 Biggest Dividend Yields on the TSX 60: Are They Truly Sustainable?

Description

The **S&P TSX 60 Index** contains Canada's 60 largest publicly listed companies, which among them possess some of the juiciest dividend yields available to investors. It is no surprise that, after a massive ramp-up of investment in the energy patch over the last two years and the growing popularity of the dividend plus growth model, the three largest yields are paid by energy companies.

But with many of those high dividend yields predicated on growing crude production and higher oil prices, they are now under threat, with crude softening further over recent days.

Let's take a closer look at these high yields to determine which will survive.

1. Penn West Petroleum Ltd.

Troubled intermediate oil producer **Penn West Petroleum Ltd.** (TSX: PWT)(NYSE: PWE), with a dividend yield of 7.4%, pays the juiciest yield in the S&P TSX 60 Index. The company recently emerged from an accounting probe in good health, so some analysts claim now is the time to buy. But it is still plagued by problems, which, in conjunction with softer crude prices, are threatening its dividend.

Penn West continues to bleed red ink as it battles to boost higher-margin light oil production, deleverage its balance sheet by divesting non-core assets, and reduce costs. These efforts continue to negatively impact Penn West's oil production, which has fallen for the last eight consecutive quarters. Its operating margin, or netback, of $39.48 per barrel of crude sold is among the lowest in the patch and leaves little room to absorb softer crude prices.

Of greater concern for dividend sustainability is that after deducting sustaining capital expenditures and debt repayments from operating cash flow, there is a working capital shortage. This shortage is currently funded by the proceeds of asset dispositions, but this can't continue indefinitely. With crude prices continuing to soften and negatively affecting operating cash flow, Penn West's only option may be to cut the dividend.

2. Crescent Point Energy Corp.

The second slot goes to **Crescent Point Energy Corp.** (TSX: CPG)(NYSE: CPG), which pays a monster dividend yield of 6.8%. But with its payout ratio exceeding net income by around six times, there are growing concerns about its sustainability, especially in an operating environment dominated by softer crude prices.

However, unlike Penn West, Crescent Point is not struggling under the weight of a myriad of problems. It has a clean balance sheet and a low degree of leverage, with net debt a mere 1.3 times operating cash flow.

More importantly, with a portfolio of quality low decline rate assets holding in excess of 640 million barrels of crude, Crescent Point can easily boost production to make up for declining revenues due to lower crude prices. This in conjunction with its healthy netback of $54.75 per barrel of oil sold indicates there is sufficient room for it to absorb softer oil prices while maintaining cash flow and sustaining its dividend.

3. Canadian Oil Sands Ltd.

The owner of the largest interest in the Syncrude project, **Canadian Oil Sands Ltd.** (TSX: COS) remains a firm favourite among income-focused investors with a massive 6.8% yield. What makes it more appealing is that, unlike Penn West or Crescent Point, its payout ratio of 86% is well below the 100% mark, indicating that it is truly sustainable.

But softer crude prices coupled with a range of internal issues are potential problems for the dividend. Production outages caused by machinery failures are impacting revenue, while the complex machinery that converts bitumen to synthetic light sweet crude is costly to maintain.

This is causing operating costs to rise and will have an impact on margins when coupled with lower crude prices. These issues as well as ongoing production outages will have a negative impact on cash flows and profitability, and the payout ratio could rise to over 100%. But Canadian Oil Sands' low degree of leverage, with net debt only 1.6 times cash flow and solid liquidity, leaves it well positioned to cover any shortfall.

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