The 3 Largest Dividend Yields in the S&P TSX 60: Are They Sustainable?

Description

It should come as no surprise after the recent plunge in oil prices and the ensuing rout among oil stocks that oil companies now make up the top three dividend yields in the **S&P TSX 60 Index**. But softer oil prices and weaker industry fundamentals certainly do not bode well for the stability of many of the monster dividends in the patch.

Let's take a closer look at these three dividends to determine which are sustainable and which could be slashed if crude prices fall further.

Penn West Petroleum Ltd.

It has been an *annus horribilis* for investors in intermediate oil producer **Penn West Petroleum Ltd.** (TSX: PWT)(NYSE: PWE). Not only is the company struggling to makeover its operations and boost production of higher margin light oil, it is still has a massive pile of debt totalling $2.2 billion. This is despite having completed asset sales of more than $1 billion, the proceeds of which were used to reduce debt.

Its operating margin remains low, with its third-quarter netback of $32.51 being among the lowest in the patch. I expect this netback to fall lower with softer crude prices now the order of the day. When coupled with declining production because of asset sales, it is difficult to see how Penn West can continue to grow cash flow.

Yet it still continues to pay a dividend with a monster yield of 11%, which is the highest in the S&P TSX 60 Index. For these reasons I am skeptical that it can sustain such a juicy yield in the current operating environment.

Canadian Oil Sands Ltd.

The second largest dividend yield is **Canadian Oil Sands Ltd.'s** (TSX: COS) tasty 8%. While there are concerns about the dividend's stability because of cost blowouts and production outages caused by unscheduled maintenance on the complex machinery that transforms bitumen to light synthetic crude, I believe it remains sustainable.

This is because Canadian Oil Sands is one of the lowest cost operators in the patch, with third-quarter 2014 lifting costs of $38.80 per barrel even after allowing for this unscheduled maintenance. As a result, it has one of the highest netbacks in the patch, which for the same period was $47.16 per barrel.

Such a high netback leaves plenty of room to absorb lower crude prices. Plus, with a range of capital projects set for completion by the end of 2014, further cash flow will be released that can be used to shore up the dividend over the shorter term if crude prices fall further.

This I believe, makes Canadian Oil Sands a solid yield play for income hungry investors.

Crescent Point Energy Corp.

Plunging crude prices have seen the usual chorus of naysayers emerge claiming **Crescent Point Energy Corp.'s** (TSX: CPG) (NYSE: CPG) monster 7.5% dividend yield is unsustainable.

But unlike many of its smaller peers, Crescent Point has built a considerable portfolio of high quality oil assets, of which only around 40% are developed and producing. These assets also have low decline rates and relatively low production costs, leading Crescent Point to report one of the best netbacks in the patch of $51.25 per barrel for the third quarter.

This essentially means there is a significant buffer available to absorb lower crude prices before margins are affected. While the company is able to continue growing production from its existing assets base without having to continue making acquisitions.

Its low degree of leverage and net debt of a mere 1.4 times cash flow mean Crescent Point is well positioned to grow cash flow by boosting production, while being able to access additional funds when required.

For all of these reasons, I believe Crescent Point's dividend is truly sustainable even if there is sustained softness in crude prices for some time, making it another solid yield play for income-hungry investors.

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