2 Reasons to Buy Pembina Pipeline Corp.

Description

Undoubtedly, some of the best investments in Canada over the past 10 years have been in the pipeline space. Pipelines are unique in that they offer high barriers to entry, revenue stability, and the dividend yield of a utility, while also offering a double-digit growth profile linked to rapidly expanding oil production.

The question for investors is which pipeline operator to buy? While large export pipeline players like **Enbridge Inc.**(TSX:ENB)(NYSE:ENB) and **TransCanada Corporation** (TSX:TRP)(NYSE:TRP) have dominated media coverage, it is the smaller "feeder" pipeline operators like **Pembina Pipeline Corp.** (TSX:PPL)(NYSE:PBA) that have been leading performers.

While Enbridge posted an impressive total return (share price growth plus reinvested dividends) of 626% between 2004 and 2014, and TransCanada a decent 312%, Pembina posted a stunning a 833% total return. Here are two reasons this is likely to continue.

1. Pembina offers strong, secure growth

Pembina offers some key advantages over its large-cap peers. While Enbridge and TransCanada can be considered export pipelines, transporting oil and natural gas across national and provincial boundaries, Pembina operates entirely in Western Canada, moving conventional oil, heavy oil, and natural gas liquids directly from batteries and storage facilities located at production sites to major marketing hubs and larger national/international pipelines.

In doing so, Pembina has carved itself an excellent niche in Western Canada, capturing the massive growth in production that needs to be transported from oil fields to hubs in Edmonton and other locations before being shipped elsewhere. Currently, Pembina transports 50% of Western Canadian light oil, and 30% of NGL volumes. On top of this, Pembina is situated in Canada's strongest plays including the Cardium, Montney, and Duverney plays.

Operating strictly in Western Canada prevents many of the massive political hurdles that Enbridge and TransCanada need to jump through to achieve their growth. With TransCanada, the Energy East, and Keystone XL projects, together comprising nearly half of the companies ambitious $46 billion capital program, are stuck in regulatory limbo with no guarantee of approval, and subject to expensive cost overruns in the process.

Pembina has strong relationships with aboriginal communities and other stakeholders, allowing the company to progress on its massive $8 billion capital program unhindered over the next five years. In addition, 100% of these projects are fee-for-service and underpinned by long-term 20+-year contracts, which will guarantee Pembina returns in excess of its cost of capital.

The result? Pembina has an expected CAGR on its EBITDA of 17% over the next five years, compared to 14% EPS growth for Enbridge and 10% for TransCanada. This growth comes at a reasonable valuation, with Pembina trading at a forward price-to-earnings ratio of 19.6 compared to 20 for TransCanada and 22.1 for Enbridge.

This is likely because Pembina shares sold off more during the recent oil price decline, due to the fact that it is a much smaller “pure play”, compared to TransCanada, which is diversified into power generation, and Enbridge, which is significantly larger. Since Pembina has no direct commodity risk due to its fee-for-service contracts, this is a great chance to pick it up at a bargain.

2. Pembina has a dividend you can count on

Pembina is currently leading its large-cap peers in terms of dividend yield as well, with a current yield of 4.40% compared to 2.34% for Enbridge and 3.56% for TransCanada. Careful investors may remark that high yield is not necessarily better, since it may be unsustainable, but in Pembina’s case, this is not an issue.

Pembina is expecting to grow its dividend 4-5% annually, and this is easily supported by the company’s earnings growth. In addition, Pembina has the strongest balance sheet out of all its peers based on the total debt/EBITDA ratio, giving Pembina significant ability to utilize debt to fund its dividend in a worst-case scenario.

With a lower debt/equity ratio then both Enbridge and TransCanada, much lower interest expenses, and strong stable growth secured by long-term contracts, Pembina shareholders can enjoy a higher yield than their large-cap peers, with a similar growth rate and lower risk.

CATEGORY

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1. NYSE:ENB (Enbridge Inc.)
2. NYSE:PBA (Pembina Pipeline Corporation)
3. NYSE:TRP (Tc Energy)
4. TSX:ENB (Enbridge Inc.)
5. TSX:PPL (Pembina Pipeline Corporation)
6. TSX:TRP (TC Energy Corporation)

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Date
2025/08/26
Date Created
2015/01/22
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