Dividend Investors: The Case to Buy Imperial Oil Limited

Description

The rout in oil prices have clobbered equities, and no stock has been hit harder than **Imperial Oil Limited** (TSX:IMO)(NYSE:IMO).

Over the past month, shares of the country's largest energy producer have plunged nearly 10%.

Time to bail? Hardly. If you believe in buying wonderful businesses when Mr. Market throws a sale, then Calgary-based Imperial may be worth a look.

Here's why.

1. It's a cash machine

Over the past decade, the yield on Imperial shares has averaged just 1.5%. That's certainly not enough to attract the attention of most income investors, but dismissing this stock because of its meager payout would be a mistake.

That's because yield doesn't factor into buybacks. Since 1994, Imperial has repurchased over half of its outstanding shares. This has allowed investors to more than double their stake in a wonderful business *tax-free*.

Imperial is now a cash-gushing machine. Between 2004 and 2013, the company has paid out nearly $13 billion in dividends and buybacks. That's more than rivals **Suncor**, **Cenovus**, and **Canadian Natural Resources** *combined*.

2. Shareholder-first management

Imperial is the best steward of shareholder capital in the oil patch, bar none.

Now, I don't throw out praise like that willy-nilly. We have a handy tool to determine how well oil executives are managing our money, and that is return on capital employed (ROCE).

ROCE measures the profits a business generates, while accounting for the amount of capital needed to earn those returns. Over the past 10 years, Imperial has generated an average annual ROCE of 27%, nearly double its nearest oil sands rival.

How did the company pull this off? Discipline. Executives will only invest in a new project if it can earn a sufficient return for shareholders. If they can't find enough new ventures to fund, they will return the extra cash to investors.

That might sound like common sense, but this type of discipline is rare in the oil industry. Most managers would rather guide over a larger business empire, even if this might hurt shareholder returns over the long haul. But happy executive egos never funded anyone's retirement.

3. It's reasonably priced

Imperial has the raw size to survive the industry's current rout. The firm boasts a AAA credit rating and fortress-sized balance sheet. This is exactly the type of company you want to own during a prolonged period of low energy prices.

And there has never been a better time to scoop up the stock at a discount. Imperial shares now trade at a reasonable 14 times forward earnings, which is a tad below the company's peers and historical average.

Of course, no one can predict where oil prices are going next. Patient shareholders will almost certainly be rewarded with growing production, dividends, and a stock price that—while it remains unpredictable in the short term—should gradually rise over time.

CATEGORY

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2. Energy Stocks
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