These 2 Dividend-Growth Stocks Could Double Their Dividends by 2018

Description

If you consider yourself a dividend investor, you're primarily looking for three things—dividend stability, growth, and yield. If you are curious about why I listed them in that particular order, it was intentional.

Yield is a poor measure of dividend quality, with growth and stability being far more important. In fact, a study by JP Morgan found that companies that grow their dividends regularly significantly outperform their slower-growing peers.

In this regard, **Agrium Inc.** (TSX:AGU)(NYSE:AGU) and **Enbridge Inc.** (TSX:ENB)(NYSE:ENB) stand out from their peers and possess some of the best dividend-growth profiles on the TSX. Here is why both of these companies are poised to double their dividends by 2018.

Why Agrium's dividend is set to double

Agrium has had a complicated dividend history. From 2002-2011, Agrium's dividend remained static at a low US$0.11 per share. This worked out to a 0.8% yield when Agrium's shares reached their lowest point during this period. Agrium's payout ratio was even worse, and on average, Agrium paid out only about 4% of earnings.

Dividends were clearly not the focus of Agrium's management, but starting in 2011, a series of events occurred that put Agrium on a high dividend-growth trajectory. Agrium had been significantly lagging behind its closest competitor **Potash./Corp Saskatchewan Inc.** in both yield, growth, and payout, and sought to play catch up.

Agrium had seen its stable retail segment grow to a level where it could begin paying out a dividend. The result was that Agrium has hiked its dividend 27 times between 2011 and today.

This trajectory is far from over. In January 2015, Agrium signaled an increased focus on dividends by boosting its target payout ratio from 35% of free cash flow to 50% of free cash flow. On top of this, Agrium is expected to see an impressive 15-20% growth in earnings before interest, taxes, depreciation, and amortization (EBITDA), as well as rapidly falling capital expenditures.

This EBITDA growth and capital expenditure reduction is due to Agrium completing major nitrogen and potash expansions, and the result is that Agrium is expected to produce $1.3 billion in free cash flow by 2017. With a 50% payout ratio, this would result in a dividend of US$5.24, a 72% upside from today's US$3.02 dividend.

This is a conservative measure, and CEO of ValueAct Capital Jeffrey Ubben predicts a US$6.00 dividend by 2016. With this is mind, it is likely that Agrium will double its dividend by 2018.

Why Enbridge is set to double its dividend

Unlike Agrium, Enbridge needs no introduction as a dividend payer. Enbridge has boosted its dividend every year since 1953 and shows no signs of slowing. Going forward, Enbridge is set to rapidly increase its dividend-growth rate.

The reason for this increase lies in the fact that Enbridge is set to grow its earnings per share (EPS) by an impressive compound annual growth rate (CAGR) of 10-12% between now and 2018. This strong earnings growth profile will be driven by Enbridge's historic $44 billion capital program, $34 billion of which is secured. $10 billion of this capital program was executed in 2014, with $9 billion more to be executed in 2015, driving EPS growth.

It may seem curious how Enbridge is able to increase its dividend so dramatically with such large annual capital expenditures, even with strong earnings growth. The answer lies in the fact that Enbridge has exceptional access to funding, thanks to its strong operating cash flows. In 2014 alone, Enbridge was able to supplement its operating cash flows with $9.8 billion in financing by issuing equity, using its credit facilities, and using its sponsored vehicles to "drop down" some of its assets.

Enbridge will be able to continue accessing this type of funding going forward, and this will drive earnings growth, and with it, dividend growth. Enbridge plans to boost its payout ratio from 70% to 85%, which will result in a dividend-growth CAGR of 14-16% by 2018.

According to **Royal Bank of Canada** analysts, this could result in a dividend of $2.83 per share by 2018, approximately double 2014's dividend of $1.40.

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Author
amancini