Why TransCanada Corporation Will Grow its Dividend by 8% Per Year for 2 Years

Description

When it comes to visible dividend growth, few companies can match **TransCanada Corporation** (TSX:TRP)(NYSE:TRP). The company boldly states that it expects to grow its payout by 8% per year for the next two years—if this goal is met, then that would result in a $0.61 quarterly dividend. That's nearly a 5% yield based on today's share price.

So, how can TransCanada make such a bold prediction? We take a look at three reasons below.

1. Steady, reliable income

Some dividend investors may be turned off by TransCanada because it's involved in the energy sector.

But TransCanada doesn't actually produce energy. Rather, it transports other companies' output to market through pipelines. This changes the story completely, because the company is able to generate revenue from long-term contracts, with practically no exposure to commodity prices.

The first quarter of 2015 paints a perfect picture. While energy companies were struggling with lower prices (many of them reported losses), TransCanada showed no ill effects whatsoever. Revenue from gas pipelines increased by 1.5% year over year, and revenue from liquids pipelines surged by 28%. The company was thus able to increase its dividend by more than 8%.

It's not as if last quarter was a fluke either. Since 2000 TransCanada has raised its dividend every year by an average of 7%. That's a track record few Canadian companies can match.

2. A big demand for pipelines

Much attention has been paid on the Keystone XL pipeline, which may never be built. And with lower oil prices, producers have cut back on drilling. That leads to a very obvious question: will TransCanada eventually suffer from a lack of demand for oil pipelines?

There's no way this will happen. Lower oil prices are caused by high supply, and this product needs to be moved somehow. Currently, trains are playing a big role, but this is a very expensive way of moving oil. Even worse, transporting oil by rail is far more unreliable than pipelines are.

Tellingly, TransCanada has over $46 billion of new projects under secured contracts or regulated business models. That should provide plenty of growth for the company's dividend ambitions.

3. Tax savings

Late last year, TransCanada faced increasing pressure to sell its U.S. assets to its Master Limited Partnership (MLP). The move, according to those pushing the idea, would have allowed the company to save on taxes and increase its dividend.

TransCanada agreed that assets should be transferred to its MLP, but wanted to do so more gradually. In the end, its argument won the day. Consequently, TransCanada should get a small boost in earnings every year.

While I'm not convinced TransCanada's choice is the right one, it will allow the company to steadily increase its payout. And that's not something easily found in Canada these days.

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