Why Billionaire Ray Dalio Just Bought Enbridge Inc. Shares

Description

Investing—like any profession—has a group of people who seem to do it far better than most. One of the best ways to improve is to not only study the methodology of these individuals, but also to pay attention to their current investment decisions, as those decisions are likely informed by the same methodology that drove strong performance in the past.

This is why when billionaire founder of Bridgewater Associates Ray Dalio initiated a position in **Enbridge Inc.** (TSX:ENB)(NYSE:ENB), it is very important to take note. With $169 billion in assets under management, Bridgewater is the world's largest hedge fund, and is one of the few funds to perform positively in 2008-09. Over the past five years, its popular Pure Alpha fund generated a 14.7% average annualized return, outperforming the S&P 500.

How much of Enbridge did Dalio buy? Dalio started by purchasing $11.8 million in Enbridge shares in Q2 2015—his third-largest purchase during the quarter. This is significant, given the fact that 110 new stocks were purchased in total during the quarter. In total, Enbridge is now Bridgewater's 41st-largest holding out of 307 stocks. Here are some possible reasons why Dalio decided to buy Enbridge now.

Enbridge has very predictable double-digit earnings growth

While it is never easy to determine the exact motivations behind an investor's decisions, Enbridge's strong and extremely predictable growth profile is almost certain to factor in. While earnings growth ultimately determines a stock's value, the predictability of the growth is key because it allows the investor to say with confidence whether or not a stock is reasonably valued.

Through 2018, Enbridge expects to grow its earnings by 10-12% annually. In addition, Enbridge just released a new measure of cash flow growth called "adjusted cash flow from operations" (ACFFO). This measure looks specifically at how much cash the company is generating (as opposed to earnings, which includes many non-cash items), and subtracts maintenance capital to create a good idea of much cash is left over to pay dividends or fund its growth program.

According to Enbridge, ACFFO is expected to grow by an impressive 18% compound annual growth rate through to 2018, well above the 10-12% expected for earnings, and this strong cash flow growth will afford Enbridge a higher multiple.

Most important, however, is the certainty of this growth, which stems from Enbridge's large $44 billion capital-growth program that is unfolding between now and 2018. Currently, $34 billion of the $44 billion capital program is not only commercially secured, but also politically secured, and scheduled to be in service by 2018. This means Enbridge's growth is also secure, and over $10 billion of this $34 billion is already in service.

Not only are the projects secure, but the funding for the projects is also fairly secure thanks to Enbridge's "financial optimization strategy." This simply refers to Enbridge selling, or "dropping down" to its subsidiary companies. The latest major drop-down was the $30 billion drop-down of Enbridge's Canadian mainline and regional oil sands assets to its Enbridge Income Fund subsidiary.

Enbridge receives dividend-paying shares in Enbridge Income Fund in exchange for the assets, plus a special $8 million management fee, and a claim to 25% of Enbridge Income Funds cash flow above $1.295 per share.

The end result? By dropping down its assets, Enbridge will fully offset the lost earnings from selling the assets, and even earn an additional 2%. On top of this, Enbridge Income Fund will be responsible for funding the growth program for the dropped-down assets, meaning Enbridge will benefit from the growth program through its equity in Enbridge Income Fund without needing to issue shares and dilute Enbridge shareholders.

Following Dalio and buying Enbridge now is a smart idea

With highly certain double-digit returns, a reasonable valuation, very low volatility, and a growing dividend, Enbridge is poised to do well in almost all market conditions. With Dalio's track record, it is a wise bet to make.

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