Is Canadian Utilities Limited or ATCO Ltd. a Better Buy Today?

Description

In the past year utilities have come down. **Canadian Utilities Limited** (TSX:CU) is over 24% below its 52-week high and **ATCO Ltd.** (TSX:ACO.X) is 26% below its 52-week high.

Usually dips like these imply that shares may be cheap. Utility businesses are generally stable because their products and services are needed whether the economy is doing fine or not.

ATCO actually owns 53% of Canadian Utilities. So, by buying ATCO shares, investors would also own a piece of Canadian Utilities. Still, we have the choice to buy both on the Toronto Stock Exchange.

Which utility is a better investment today?

Each investor has different considerations for their investments. If you are a retiree, you likely want more income now. If you're a younger investor, you might want more growth and don't mind a lower yield.

So, let's compare the fundamentals of these utilities.

Yield: At $32.5 a share, Canadian Utilities yields 3.6%. At $36.2 a share, ATCO yields 2.7%. If you're looking for higher income today, Canadian Utilities wins.

Payout ratio: Based on the estimated 2015 earnings per share (EPS) and its current dividend, Canadian Utilities's payout ratio is just under 62%. In contrast, ATCO's is just above 37%.

Because ATCO has a lower payout ratio, its dividend is safer and has higher growth potential.

Dividend-growth history: Canadian Utilities has increased dividends for 43 years in a row. On the other hand, ATCO has increased dividends for 21 years in a row.

It may seem that Canadian Utilities wins, but let's not be too hasty and look at the dividend-growth rate as well.

Company	1-Yr DGR	3-Yr DGR	5-Yr DGR	10-Yr DGR
Canadian Utilities	10.3%	10%	8.7%	7.3%
ATCO	14.7%	14.7%	11.5%	9.4%

DGR: dividend-growth rates based on a compound annual growth rate (CAGR)

Comparing the two, ATCO has a higher income-growth potential. Still, assuming the dividend-growth rates stay the same at 10.3% and 14.7% in future years, it'd still take ATCO eight years to catch up and exceed Canadian Utilities's income.

That said, higher dividend growth should also push ATCO's share price higher and, as a result, the total return from an investment in ATCO should be higher as well.

10-year earnings growth: Over 10 years, Canadian Utilities's EPS grew at a CAGR of 6.3%. ATCO's grew at a CAGR of 8%.

So, ATCO has had faster earnings growth. Dividends come from earnings. This explains why ATCO has had higher dividend growth.

Financial strength: Both utilities have an S&P credit rating of A, but Canadian Utilities has a debt-to-cap ratio of 55% and ATCO's is at 53%.

Performance: Recently, in the six-month, one-year, and two-year periods, Canadian Utilities's price has outperformed ATCO. This is probably due to the near-term poor performance in ATCO's Structures & Logistics business that isn't present in Canadian Utilities.

If you look at longer time frames though, ATCO has typically outperformed Canadian Utilities.

Conclusion

In the past two years, Canadian Utilities has increased dividends by 10.3%, while ATCO has increased dividends by close to 14.7% in 2013 and at 15.1% in 2014. Generally, businesses don't increase dividends (or at least not at a high rate) if they anticipate lots of hardships.

Because both businesses continued to grow dividends over 10% recently, they are both good buys after their double-digit dips.

That said, I believe the poorer near-term performance of ATCO is only temporary because ATCO's dividend growth continues to be stellar while it maintains a payout ratio of under 40%.

If Foolish investors want more current income, Canadian Utilities is the better buy with a 3.6% yield. If you prefer more growth and ultimately higher returns, ATCO is a good buy around the $36 level.

CATEGORY

1. Dividend Stocks
2. Investing

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2. TSX:CU (Canadian Utilities Limited)

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