How Can Canadian Utilities Limited Offer Stable Returns?

Description

After two years of declining adjusted earnings per share (EPS) from 2014 to 2015, **Canadian Utilities Limited** (TSX:CU) is showing signs of turning around. The utility reported its first-quarter results on Wednesday, and EPS was 50% higher. The shares responded by spiking 3%.

What contributed to earnings growth?

Canadian Utilities reported higher earnings in its business segments compared with the first quarter of 2015:

- The electricity segment reported about $36 million growth (55% higher)
- The pipelines and liquids segment reported about $30 million growth (40% higher)

On top of business-wide cost-reduction initiatives, other factors helped each business segment achieve higher earnings.

Capital investment and rate base growth were main factors contributing to higher earnings in the electricity and pipelines and liquids segments. Additionally, in the first quarter of 2015, these segments' regulated earnings were reduced by a one-time impact from multiple regulatory decisions.

In January, Canadian Utilities's parent company, **ATCO**, sold its interests in the Edmonton Ethane Extraction Plant. These non-core assets resulted in proceeds of $21 million.

Dividend-growth track record

Canadian Utilities has increased its dividend for 44 consecutive years. Even though it has experienced multi-year earnings decline from 2014 to now, it has hiked its dividend by 10.2% per year on average. This is thanks to the company maintaining a sustainable payout ratio.

Most recently, Canadian Utilities raised its dividend by 10% in March, so its payout ratio for the first quarter is about 44%. So, the utility has room to continue its dividend-growth streak next year.

Future growth

To meet customers' distributed-generation needs, Canadian Utilities built a fleet of portable natural gas-fired units that can be used for temporary or permanent projects.

Canadian Utilities reported, "In the first quarter of 2016, ATCO Power signed a 10-year contract to build and operate a two-unit, three MW natural gas-fired power facility, located southeast of Grande Prairie, Alberta. With a capital investment of $8 million, this project is under construction and will be operational in the second quarter of 2016." Once this project is up and running, it'll help contribute to earnings and cash flows.

ATCO and Canadian Utilities plan to invest roughly $5.3 billion in regulated utilities and contracted capital growth projects from 2016 to 2018. Specifically, $2.1 billion is planned for regulated utilities, and $2 billion is planned to upgrade the natural gas transmission and distribution networks in Alberta and Australia.

Conclusion

After rising 3%, Canadian Utilities is trading at about 19 times its earnings. So, the shares are a bit expensive today. However, it has been increasing its dividend by 10% per year in the past few years. At under $36 per share, it offers a safe 3.6% yield. Total-return investors should consider it on dips of $33 or lower for better returns.

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