These Are the Oil Sector's 3 Safest (and Growing) Dividends

Description

Before the oil crash of 2014 and 2015, energy sector dividends in North America were some of highest yields, were the most stable, and grew steadily. At the beginning of 2014, for example, **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) paid an 8% dividend yield, **Baytex Energy Corp.** paid out around 7% , and **Penn West Petroleum Ltd**. paid out around 6.5%.

Two years later, both Baytex and Penn West suspended their dividends, Crescent Point cut its dividend by 86%, and south of the border in the U.S., Q1 2016 saw 189 firms cut their dividends, 51% of which were oil and gas names (the other 49% included 15 other industries combined). Over $7.4 billion of shareholder income vanished.

With this in mind, dividend investors have begun looking elsewhere for yields, and at their own peril. The oil sector currently offers several attractive, safe yields (especially in today's 0% interest rate world) that have a combination of dividend and share-price growth that will be supported by what should be a multi-year bull run in oil prices.

The key is to look for names with through-the-cycle dividend sustainability; that is to say, names that will maintain their dividend regardless of oil prices. In Canada three names weathered what was the second-worst oil plunge in history almost unscathed, and these names should prove to be leaders going forward.

Crescent Point Energy

Crescent Point was the worst performing on the dividend-front of this group, having slashed its dividend in August 2015 as well as in March 2016. The dividend was always a core part of Crescent Point's strategy (which is why the company never eliminated it), and while the current yield of 1.7% is certainly conservative, it is highly secure under the expected oil-price outlook for the next two years (with free cash flow coverage of two times the 2017 dividend at average oil prices of US$50/bbl).

The company has stated that dividend growth is a priority for its expected growth in free cash flow, and it is heavily focused on improving capital efficiency through technology like waterflooding, which will support free cash flow growth even if oil prices stay stagnant. With Crescent Point, investors also get impressive share upside with any increase in oil prices.

Vermilion Energy Inc.

It would not be controversial to say **Vermilion Energy Inc.** (TSX:VET)(NYSE:VET) is Canada's top energy sector dividend name. The company is not only one of the few names to not cut its dividend at all during its history, but it also managed to maintain a yield that was often above 8% (and is currently around 5.9%).

Vermilion can thank its unique business model for this, which includes a roughly 50% oil and natural gas split as well as global geographic exposure, which allows the company to sell at higher-value benchmarks (for example most of Vermilion's production was sold at higher-value Brent prices, and at NBP natural gas prices, which are three times Canadian natural gas prices).

Vermilion has the highest netback production in the Canadian market, and this combined with strong capital efficiency and expected production growth of 17% in 2016 is expected to generate positive free cash flow over the next couple of years. Vermilion should have no issues supporting an industry-leading yield.

Suncor Energy Inc.

Suncor Energy Inc. (TSX:SU)(NYSE:SU) also managed to make it through the oil rout without cutting its dividend, although this was of little surprise to many observers. Suncor's integrated business model and oil sands focus allowed it to both sell its lower-value oil sands production at higher prices through its upgrading and refining facilities, while also benefiting from the relatively low level of sustaining capital required for mining operations (since most capital costs are up front).

Suncor currently has a dividend yield of over 3%, and this yield is strongly supported by a highly visible production-growth outlook (via Hebron, Fort Hills, and Syncrude). This is expected to provide Suncor with a free cash flow yield of about 4% in 2019 at US$50 per barrel, which should strongly support the dividend going forward.

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