Fortis Inc. Is Great but There’s 1 Problem

Description

Who doesn’t love a predictable business with a reliable dividend that increase every year like clockwork? **Fortis Inc.** (TSX:FTS) has increased its dividend for more than four decades, which is rare for a Canadian company.

How can it continue growing its dividend?

A quality, predictable business

At the end of the first quarter Fortis had 96% of regulated assets, which give consistent returns with a return on equity of 8-10% and have a low-risk profile.

Fortis has a diversified portfolio of assets, which serve more than three million electricity and gas clients across North America and in the Caribbean.

Fortis has maintained a strong S&P credit rating of A- while making strategic acquisitions and integrating them successfully.

Because Fortis is a predictable business, it is also a predictable income investment. The utility has hiked its dividend every single year for 42 consecutive years!

Its dividend is 10% higher than it was a year ago and equates to an annual payout of $1.50 per share with a payout ratio of about 70%.

Diversified portfolio with U.S. exposure

In the last few years Fortis has gained exposure to the U.S. by acquiring the regulated gas and electric utilities of Central Hudson and UNS Energy in New York and Arizona, respectively. Fortis earns about 36% of its operating earnings from these utilities and 57% from its regulated assets in Canada and the Caribbean.

Fortis is in the midst of acquiring **ITC Holdings Corp.** (NYSE:ITC), the largest independent regulated electric transmission utility in the U.S. The transaction is expected to close by the end of this year. Fortis will earn 61% of its operating earnings from the U.S. with 38% coming from ITC and 23% coming from Central Hudson and UNS Energy.

Through ITC, Fortis will further diversify its operations in the U.S. by gaining a presence in eight additional states: Michigan, Iowa, Minnesota, Illinois, Missouri, Kansas, Oklahoma, and Wisconsin.

Conclusion

Fortis posted record earnings in 2015. With a $9 billion capital plan through 2020 and growing operations in the U.S., the utility should continue to deliver strong results.

The diversified utility is confident about its future prospects and predictability as it aims to increase its dividend by 6% per year through 2020.

Fortis is a top 25 North American utility, and it is expected to be listed on the New York Stock Exchange later this year. Fortis is an uncommon opportunity in the utility space as it's expected to grow its earnings per share by more than 6% per year in the medium term. That's why it's likely Fortis will continue to trade at a premium valuation.

That's the only problem with investing in Fortis today.

It's a great, predictable business to invest in for income and steady price appreciation, but it trades at about 20 times earnings. The more you pay for a company, the lower your returns will be.

When Fortis yields 3.8%, it'll be a good place to start averaging in.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:FTS (Fortis Inc.)

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