



## Will the Enbridge Inc. and Spectra Energy Corp. Merger Succeed?

### Description

On September 6 **Enbridge Inc.** ([TSX:ENB](#))([NYSE:ENB](#)) disclosed that it would buy **Spectra Energy Corp.** ([NYSE:SE](#)) for \$37 billion (US\$28 billion). The takeover will combine two Canadian and American behemoths, creating North America's largest energy infrastructure company. In total, the new company will have an enterprise value of nearly \$130 billion.

Spectra shares jumped 13%, while Enbridge popped roughly 4%.

No cash will be exchanged because it's an all-stock deal. Enbridge will issue about 694 million new shares and take on about \$22 billion of Spectra debt.

What should you think about the move?

### This is not a low-risk deal

"Over the last two years, we've been focused on identifying opportunities that would extend and diversify our asset base and sources of growth beyond 2019," commented Enbridge CEO Al Monaco. The transaction "allows us to extend our anticipated 10-12% annual dividend growth through 2024," he added.

Meeting investors' expectations for growth has been weighing on Enbridge. Production growth in Canada's oil sands—long expected to drive long-term earnings growth—has flattened or even fallen due to high production costs and falling oil prices. It's also getting some regulatory pushback on an oil pipeline taking oil sands production in Alberta to Canada's east coast. To meet its growth targets, management was forced to grow inorganically.

How Spectra will help it do that is unclear. Spectra's pipeline, storage, and processing operations extend from gas fields in northern British Columbia through the U.S. Midwest and to the Gulf of Mexico. Compared to Enbridge, these operations haven't performed that well. Over the last decade, Enbridge has consistently shown an ability to outpace Spectra's growth. Adding Spectra's business to its mix will likely slow overall earnings growth.

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But management is banking on investors looking at raw earnings-per-share growth rather than increases in shareholder value. Note that CEO Al Monaco cited “10-12% annual dividend growth through 2024” as one of the driving factors behind the deal—not necessarily improving overall shareholder profits.

A great example of this can be seen by tracking earnings per share over time. While the company has expanded aggressively, boosting sales and assets, shareholders have been continually diluted, leaving them with a lower share of earnings than back in 2010. Still, management has forged on with their double-digit annual-dividend-increase promise. Dividends have outpaced earnings in every quarter but one since 2012.

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### **Spectra shareholders are the winners**

There's a reason why Spectra was up three times more than Enbridge on the day the deal was announced. Spectra shareholders will be the winners of the transaction because they'll be bought out at a premium. Enbridge shareholders, meanwhile, will be stuck with an ever-growing business that isn't necessarily growing shareholder value. They'll likely be pleased with another dividend bump next year, but don't be fooled into thinking it's sustainable.

If you're looking at buying the newly combined company, stay far away.

### **CATEGORY**

1. Dividend Stocks
2. Energy Stocks
3. Investing

### **TICKERS GLOBAL**

1. NYSE:ENB (Enbridge Inc.)
2. NYSE:SE (Sea Limited)
3. TSX:ENB (Enbridge Inc.)

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