



## 2 Utilities for Stable Income and Growth

### Description

Stock price dips are opportunities for investors to pick up quality shares at lower prices. If you're looking for a safe income of roughly 4% and price-appreciation potential, you should have your eyes set on **Fortis Inc.** ([TSX:FTS](#)) and **Algonquin Power & Utilities Corp.** ([TSX:AQN](#)).

But which is the better stock to buy today?

#### Fortis

Fortis is a regulated utility with \$29 billion of assets and highly predictable returns. For example, the allowed return on equity (ROE) on five of its utilities was between 8.3% and 10% in 2015.

Fortis has nine utility operations, which serve 3.2 million electric and gas customers across Canada, the United States, and the Caribbean.

The utility is making great progress in its recent acquisition of **ITC Holdings**, which is expected to close late this year. ITC will strengthen Fortis's business by adding the new business of electric transmission.

Moreover, ITC will increase Fortis's geographic footprint in the U.S., enhance its regulatory diversity, and lower its overall rate regulatory risk. Since ITC's allowed ROE and rate-base growth are higher than Fortis's other utilities with allowed ROE greater than 11% and rate-base growth expected to be about 7.5% per year through 2018 (compared to Fortis's rate-base growth of about 4.5% per year), ITC will be an important growth driver for Fortis.

Fortis has increased its dividend for more than 40 years, and it aims to continue increasing it at an average rate of 6% per year. In fact, Fortis just hiked its dividend by 6.7%.

#### Algonquin Power & Utilities

Algonquin Power & Utilities is a diversified North American utility with about \$5.5 billion of assets. It has a portfolio of wind, solar, hydroelectric, thermal, and natural gas power-generating facilities, which have

an installed capacity of 1,300 megawatts.

Algonquin Power & Utilities provides essential water, electricity, and natural gas utility services to more than 560,000 U.S. customers. These are rate regulated and generate stable and predictable earnings for the utility.

It's also involved in rate-regulated electric transmission and natural gas pipeline systems in the U.S. and Canada.

Algonquin Power & Utilities yields 4.8% with a reasonable payout ratio of about 74% this year.

Since 2010 the utility has increased its dividend by nearly 10% per year. Its cash flow is expected to grow 13-15% per year in the next few years, so it should be able to continue to grow its dividend at a 10% clip.

Some of Algonquin Power & Utilities's biggest growth drivers include the more than 500 megawatts of projects, which are under construction or in development. These projects have a weighted-average power-purchase agreement of 20 years, which will increase the utility's stable earnings and cash flows and support a growing dividend when they come online.

### **Which is a better buy today?**

Both Fortis and Algonquin Power & Utilities are safe utilities that earn stable cash flows. Comparatively though, Fortis is the higher-quality name—it has an S&P credit rating of A-, a 40-year track record of dividend growth, and more predictable returns.

On the other hand, Algonquin Power & Utilities has an investment-grade S&P credit rating of BBB, has increased its dividend for the sixth year this year, and has more unpredictable returns.

At about \$41 per share, Fortis trades at a forward price-to-earnings ratio of 18.9 and is expected to grow its earnings by 6-7% a year. So, investors can expect returns of about 10-11%.

At about \$11.50 per share, Algonquin Power & Utilities trades at a forward price-to-cash-flow ratio of 11.1 and is expected to grow its cash flows by 12-15% a year. So, investors can expect returns of about 16-20%.

If you want to sleep well at night, Fortis is the obvious choice. The utility will be especially a good buy at a yield of 4% or higher. If you want to take on more risk, you can consider Algonquin Power & Utilities for higher returns potential. That said, there's nothing stopping you from investing in both utilities for a blended risk-and-reward approach.

### **CATEGORY**

1. Dividend Stocks
2. Investing

### **TICKERS GLOBAL**

1. TSX:AQN (Algonquin Power & Utilities Corp.)
2. TSX:FTS (Fortis Inc.)

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