A Top Dividend-Growth Stock With a 6.7% Yield

Description

Altagas Ltd. (TSX:ALA) yields 6.7% at about $31.20 per share. It can sustain its high yield and grow its dividend because of the type of assets it owns and the way they generate stable cash flows.

The business today

Altagas is a diversified energy infrastructure company. It generates roughly an equal amount of earnings before interest, taxes, depreciation, and amortization (EBITDA) from Canada and the United States.

Based on its business segments, Altagas generates about 41% of its EBITDA from contracted power, 36% from regulated gas distribution, and 23% from highly contracted midstream.

Specifically, the company processes and moves about two billion cubic feet of natural gas and natural gas liquids per day. It also has 1,688 MW of power-generation capacity across clean fuel sources: natural gas, hydro, wind, and biomass.

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hydroelectricity facility
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Additionally, it has five regulated gas-distribution utilities, which deliver clean and affordable natural gas to more than 565,000 customers (22% in Canada and 78% in the U.S.).

Sustainable dividend

In 2010, Altagas had 50% of its normalized EBITDA exposed to commodity pricing. It has now reduced the exposure to about 2%. Contracted power and regulated utilities contribute about 75% of its

EBITDA. These factors help reduce the volatility of the company’s EBITDA.

Most importantly, Altagas’s cash flows are supported by long-term contracts. For example, the weighted average term of Altagas’s power contracts is about 14 years.

Additionally, more than half of Altagas’s midstream business has take-or-pay arrangements with a weighted average term of about 17 years.

In fact, the funds from operations (FFO) from Altagas’s regulated utilities and 60-year contracts (indexed to the B.C. consumer price index) with BC Hydro across three facilities more than cover the company’s dividend.

Investments to support dividend growth

Altagas has more than $2.6 billion of investments across its three businesses which are expected to come into service through 2020. They are expected to support Altagas’s dividend growth.

If Altagas successfully acquires **WGL Holdings** by the second quarter of 2018, management is confident about a dividend-growth target of 8-10% per year through 2021.

Other than doubling Altagas’s rate base, tripling its customers in its utility segment, and increasing its gross capacity to about 1,900 MW for its power segment, WGL Holdings will add another $4.6 billion to Altagas’s investment pipeline.

The takeaway

Altagas offers an attractive yield of 6.7%, which is supported by a normalized FFO payout ratio of about 61%. The company has hiked its dividend for five consecutive years by 8.8% per year.

Altagas’s acquisition of WGL, if successful, will be accretive to its earnings and cash flows and support dividend growth of 8-10% per year.

So, Altagas is an attractive income-growth investment today.

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