



## 2 Dividend Yields That May Be Too Good to Be True

### Description

Investors looking for dividends search high and low, looking for the best yields along with decent capital appreciation as well. In commodity and/or cyclical stock plays, dividend yield can be a hard fundamental to gauge in the medium to long term. Due to the nature of the respective industries, in times of boom, dividends are iron-clad; however, when times get tough, the dividend yields sometimes aren't so stable.

I'll be looking specifically at **Peyto Exploration & Development Corp.** ([TSX:PEY](#)) and **Vermilion Energy Inc.** ([TSX:VET](#))([NYSE:VET](#)) as two examples of companies that may struggle to maintain their dividend yields moving forward. Both companies currently have attractive yields at 5%, but how long they last?

### Times are tough at the oil patch

Canadian oil producers have been hit hard since the middle of 2014. Industry reports show that over 50,000 direct jobs have been lost since 2014 in Alberta alone, largely due to the large drop in the commodity price of crude. Capital-expenditure budgets are down, and the Alberta oil industry continues to face the harsh realities that increased U.S. shale production and limited OPEC pumping reductions are likely to lead to a "lower for longer" scenario for the price of oil in 2018 and 2019.

Peyto is a company I have followed for a while. I was bullish on it until the beginning of last year, when profitability began to seriously deteriorate at this once-solid oil and natural gas producer in western Canada.

The operations of Peyto are solid; however, the reality facing the company is that the current dividends paid to investors are double the annual profits of the company, meaning that unless the company wants to continue to pile on more debt (currently at \$886 million), it will need to consider cutting its dividend in the next few years in the absence of real price improvements.

Vermilion is a great example of a company with a legacy dividend; it refuses to give it up for existing investors. With diversified operations around the globe, its centre of operations lies in Alberta, where the company has also felt the sting of crude prices.

Vermilion is operating at a significant loss (approximately -\$166 million per year) and pays out approximately \$313 million per year in dividends, meaning its annual shortfall currently sits close to a half a billion dollars annually. With a debt load of \$1.38 billion, this is a dividend which may be seriously in danger in the coming quarters.

### **Another commodity company forced to cut dividend**

In looking at the oil industry in Alberta, I see a lot of similarities to the potash market. Another one of my favourite names to analyze is **Potash Corporation of Saskatchewan Inc.** (TSX:POT)(NYSE:POT).

Potash Corp. had a very similar yield hovering around the 6-7% range before it was cut after the bottom fell out of the commodity price of potash. The market began devaluing Potash Corp. shares, the dividend yield climbed, and Potash Corp. investors felt the eventual wrath of the market when the company was forced to cut its dividend to bolster profitability.

While history doesn't often repeat, sometimes it rhymes.

Stay Foolish, my friends.

### **CATEGORY**

1. Dividend Stocks
2. Energy Stocks
3. Investing

### **TICKERS GLOBAL**

1. NYSE:VET (Vermilion Energy)
2. TSX:PEY (Peyto Exploration & Development Corp)
3. TSX:VET (Vermilion Energy Inc.)

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### **Date**

2025/08/05

### **Date Created**

2017/04/19

**Author**

chrismacdonald

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