Dividend Income: Is Inter Pipeline Ltd.'s 7% Payout Safe?

Description

Income investing is all about seeking long-term stability and steady cash flows. To achieve that goal, you should always look for high-yielding opportunities. But often, an above-average return should be a sign of danger.

Let's see if 7% annual dividend yield offered by **Inter Pipeline Ltd**. (TSX:IPL) is safe and if it presents a good opportunity for income investors.

What's IPL strength?

IPL is a Calgary-based energy infrastructure company, running a large oil pipeline network, transporting energy products from Canada's western province, processing natural gas, and managing bulk storage facilities for liquid energy assets in Europe.

IPL has recently acquired Williams Canada for $1.35 billion and plans to build a $1.85 billion polypropylene manufacturing plant by 2021.

You might have noticed that IPL has diversified assets, and it's not a pure oil play.

Unlike traditional energy producers, IPL generates most of its revenue and cash flows from long-term, fee-based contracts. This reduces the company's exposure to volatile energy prices and increases the stability and consistency of the company's cash flows.

Dividend growth

IPL stock has been under pressure this year, falling 24%, largely on concerns that the company may have to cut its payout as it borrows heavily to fund its expansion.

The issue has become more urgent as the Bank of Canada raises interest rates, which should increase the borrowing costs and project costs.

But if you look at the company's dividend history, you'll note that IPL has very successfully ridden through a tough operating environment, especially after the 2014 plunge in oil prices.

For the past 10 years, IPL's dividend has grown ~7%. This is quite an impressive performance, putting the company in the camp of solid dividend payers, which are consistent in rewarding their shareholders. At a 7% annual dividend yield, investors are getting $0.14 a share monthly payout. This payout has increased for the last 14 years without a break.

Bottom line

I think IPL's highly stable and consistent revenue and cash flow sources make its current dividend yield safe. On the other hand, IPL's expansion plans provide a new source of cash generation.

If you're a long-term dividend investor and plan to buy and hold IPL's stock, you'll likely benefit from both attractive yield and future upside. Its risk profile doesn't warrant a discount, which the market is attaching to this top dividend player in the energy space.

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