



Big Value and Fat Yields Are in Energy Stocks Now

Description

Energy stocks have generally had a meaningful pullback since the start of this year. You may be interested to know that the energy index is made roughly half of oil and gas producers and half of energy infrastructure companies.

Energy infrastructure companies largely generate stable cash flows from long-term contracts, so they're lower risk and safer investments than oil and gas producers, which are directly impacted by the volatility of the underlying commodity prices.

Here are two energy infrastructure companies, **Inter Pipeline Ltd.** (TSX:IPL) and **Altagas Ltd.** ([TSX:ALA](#)), which offer high yields of 6.7-7.4%.

Last week, when commodity prices went higher, Altagas shares saw a smaller pop than Inter Pipeline shares. This is because only 25% of Altagas's earnings before interest, taxes, depreciation, and amortization come from its pipeline business, while the rest comes from its rate-regulated gas-distribution utilities and power-generation assets.

However, Inter Pipeline has infrastructure assets to transport oil sands and other oil products, process natural gas liquids, and store bulk liquids.



Both stocks are still undervalued with big yields

Despite the fact that their share prices popped ~3-5% last week, Inter Pipeline and Altagas stocks are still a long way off from their highs. As a result, they offer big sustainable yields that are uncommon in today's market.

At about \$24.20 per share, Inter Pipeline offers a yield of nearly 6.7%. Its funds from operations (FFO) payout ratio is estimated to be less than 73% this year.

Altagas offers a yield of 7.4% at about \$28.40 per share. Altagas management targets a FFO payout ratio of 50-60%. And about 90% of its dividend is supported by long-term contracted cash flow, which improves the safety of its dividend.

How much upside is there?

The Street consensus from **Thomson Reuters** has a 12-month target of \$29.30 for Inter Pipeline, which represents nearly 21% upside potential for the stock. The Street consensus for Altagas is \$34.10, which implies 20% upside potential.

Let's not forget that their high yields of 6.7-7.4% also add significantly to returns. In fact, the average market returns are 7-10%, so one could say that their yields already pretty much guarantee getting market returns.

Investor takeaway

If you have shied away from the energy space, it may be a good time to take a look at it again. Consider energy infrastructure companies in particular, such as Inter Pipeline and Altagas, which offer value and big yields.

If you only have enough capital for one, consider Altagas, which is more diversified and is more depressed from the short-term uncertainty of its pending acquisition of **WGL Holdings**.

To further reduce risk, buy the Altagas subscription receipts (TSX:ALA.R), which trade at a slight premium to the common shares at \$28.90 per receipt. You get \$31 per receipt back if the WGL acquisition falls through.

In the meantime, you get a dividend-equivalent payment as the common shares. If the acquisition goes through, the receipts convert to Altagas common shares.

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