3 Utility Stocks to Lead in the Future

Description

Utilities have quietly kept up with the **S&P 500** market, up ~13% year to date. A case could be made for a sector rotation with investors moving into more stable utility stocks. Here I consider three great companies.

Northland Power Inc. (TSX:NPI) develops and builds power projects largely in Canada, but it now has wind farms in Germany and the Netherlands. How does it look in the rear-view mirror? Northland dropped its dividend amount in 2009 and 2011. Despite a high annual growth in revenue and operating cash flow, both ~22% per year, this has not translated into consistent earnings per share (EPS). In fact, the average EPS dating back to 2008 is negative $0.05 per share. Northland's balance sheet is a bit bumpy, which reflects the nature of the business, but the recent quarter shows the earnings margin is up significantly.

Algonquin Power & Utilities Corp. (TSX:AQN)(NYSE:AQN) has a diverse business in electricity, gas, water and wind energy in Canada and the United States. Algonquin has a comparable dividend yield with Northland at 4.4% and a payout ratio that is high, but it has been steadily dropping to safer levels. Algonquin cut its dividend back in 2010, so, like Northland, it fails the dividend test, but Algonquin has been steadily increasing the dividend ever since.

Algonquin is a better pick compared to Northland, in my opinion. Revenue and operating cash flows are very solid. EPS are increasing modestly each year. Algonquin also has substantially less debt than Northland, which is worth considering as interest rates on debt climb.

Capital Power Corp. (TSX:CPX) builds, owns, and operates power plants primarily in Alberta. Capital is a solid pick for dividend investors because the yield is high at 6.8%, making it the highest dividend payer among the three. It also passes a dividend test, since Capital has maintained or increased the dividend. Although revenue has fallen slightly in recent years, the balance sheet shows positive margins and solid performance.

Capital has been trading sideways — that is, in a narrow price range in 2017 — after bottoming in 2016. A patient investor could wait until this stock drops to the low 20s for a great buying point. It is hard to predict how much this stock would drop, but a word of caution is warranted if the stock drops below $24 per share — a support level.

Looking ahead and the best pick

All three of these companies have a potentially exciting future. Capital looks to be the best pick from among the three. Algonquin is a close second. Capital gets the nod largely because it has the lowest financial leverage. But Capital also appears to be taking Alberta’s Carbon Competitiveness Regulation seriously and intends to phase out coal facilities by end of 2030 or earlier.

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1. Energy Stocks
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2. TSX:AQN (Algonquin Power & Utilities Corp.)
3. TSX:CPX (Capital Power Corporation)
4. TSX:NPI (Northland Power Inc.)

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