A Quick Analysis on a Stock Through its Dividend

Description

A company's dividend can tell you a lot about the business. Does the company have a culture of growing dividends? If yes, is the dividend being increased in a responsible way?

Here, I'll use **Pembina Pipeline Corp.** (TSX:PPL)(NYSE:PBA) as an example.

Does Pembina Pipeline pay a growing dividend?

Pembina Pipeline has increased its dividend for six consecutive years. Its five-year dividend-growth rate is 4.9%. Typically, a dividend-growth company is lower risk, and its stock is less volatile. It should also be a better long-term investment than a company that pays a dividend but doesn't grow it all the time.

However, a company has a record of growing its dividend won't necessarily continue to grow it. The first line of defence you can check for dividend safety is the company's payout ratio.

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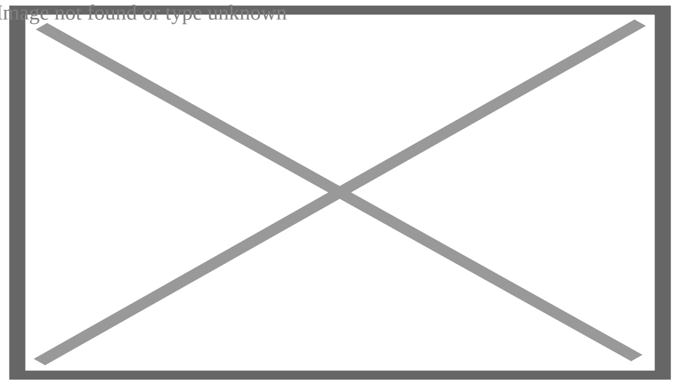

The payout ratio

Pembina Pipeline's payout ratio is roughly 65%. That is, it's paying out 65% of its operating cash flow. Even if a company's payout ratio is sustainable, it could spell trouble for the company (and its dividend) if it has too much debt.

Pembina Pipeline's net debt to cash flow is estimated to be about 4.2 times this year, which is a little high. The elevated debt level is due to the 2017 Veresen acquisition, which was partly funded by a $2.5 billion credit facility. Pembina Pipeline's strong cash flow generation should allow the company to lower its debt levels over time in the next few years.

The dividend yield

Pembina Pipeline currently offers a dividend yield of 5.2%, which is at the high end of its one-year yield range, which may indicate that it's at a good place to buy some shares if you're looking for income.

The estimated return

With the transformative Veresen acquisition, as Pembina Pipeline calls it, management aims for an 8-10% cash flow per share growth. Combining that growth with the dividend yield of 5.2%, investors can estimate a near-term return of 13-15%, assuming the shares are fairly valued.

Is Pembina Pipeline fairly valued?

At roughly $41.50 per share, Pembina Pipeline trades at a multiple of about 12.8. So, it's a good value here. At worst, the stock is fairly valued.

The analyst consensus from **Thomson Reuters** has a 12-month price target of $51.10 per share on the stock, which indicates there's more than 23% upside potential, a total return of ~28% in the near term.

Investor takeaway

A stock that has increased its dividend in the last five years is a good start. Then see if the company's payout ratio and debt levels are reasonable. If they are, see if the company is a good value to buy. Right now, Pembina Pipeline is trading at a good valuation. It offers a juicy 5.2% yield and some decent price appreciation potential.

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