Can You Bear the Uncertainties of This +9% Yielder?

Description

One of the things that attract people to invest in the stock market is dividends. Dividend stocks are especially popular in low interest rate environments, such as the one we are in now.

High yields can be mesmerizing, but when yields rise by 6%, 7%, and 8% or even higher, investors should ask why. It could well be that the companies in question have increased uncertainty or risk.

I'll use **Altagas Ltd.** (TSX:ALA) as an example here.

The focus is on the WGL acquisition

Altagas currently offers a +9% yield; this high yield comes with a number of uncertainties. The biggest uncertainty about Altagas is its ~CAD$8.4 billion pending the acquisition of **WGL Holdings**.

In the latest quarter, Altagas provided an update on its financing for the acquisition: it had a mix of debt and essentially stock, including a bridge facility from which ~US$3 billion can be drawn and CAD$2.6 billion of subscription receipts, which it made available in the first quarter of 2017. (The receipts will convert to common shares when Altagas completes the acquisition.)

Management has also identified CAD$4 billion of potential assets for selling and expects to sell more than $2 billion this year. The company is also open to other financing options, including offerings of senior debt, hybrid securities, and preferred shares.

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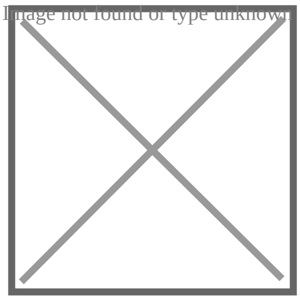

Will its asset sales go smoothly, including getting a good price on them? Can Altagas complete the acquisition in ~3.5 months as planned? Will the company at least maintain its dividend this year? (Altagas aims to grow its dividend by 8-10% per year through 2021, but that estimation is more or less based on the expectation of closing the WGL acquisition by mid-2018.)

These are all the uncertainties that shareholders must bear. Interestingly, the subscription receipt (purchased via the symbol TSX:ALA.R) traded at a 7% premium to the common stock at market close on Monday.

The receipts used to trade roughly in line with the stock. In other words, the market finds the common stock higher risk than the receipts right now. (If the WGL acquisition falls through, receipt holders will get $31 per receipt back.)

Investor takeaway

Altagas seems committed to its dividend, as it has increased its dividend for six consecutive years with a three-year dividend growth rate of 7.8%. The uncertainties around the WGL acquisition have pulled down the stock and pushed Altagas' yield to 9.1%.

Notably, such factors as higher interest rates affect debt-heavy stocks. This is evidenced by the stocks of other energy infrastructure companies (e.g., **Enbridge** and **Inter Pipeline**) performing poorly in the last 12 months.

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