3 Canadian Dividend Aristocrats With Dangerously High Payout Ratios

Description

At times, investors can be enamoured by the allure of a high dividend yield. For those living off dividends in retirement, a high yield can be appealing, as it provides greater income. However, not all dividends are created equal, and some companies have dangerously high payout ratios. A high dividend payout ratio as a percentage of earnings may be acceptable in the short term, but it is not sustainable and not a good allocation of funds over the long term. This may lead to a dividend cut, suspension, or cancellation.

Canadian dividend aristocrats are TSX-listed companies that have raised dividends for five consecutive years. Investors attribute a certain level of safety to these companies, as they have demonstrated reliable dividend growth over the long term. Unfortunately, historical patterns are not necessarily a precursor to future success. The three companies below all have payout ratios well above 100% on a trailing 12-month basis. Their situations do not improve when looking forward to next year's earnings.

One company that has garnered plenty of attention recently is **Cineplex Inc.** (TSX:CGX). Hollywood has taken its lumps, and the box office has been on a steady decline over the past couple of years. This does not bode well for Canada's largest film exhibition company. The company's current payout ratio is a hefty 150%. It is also an unattractive 144% based on 2018 earnings. The company's dividend has also been eating up the company's cash flows by a greater percentage each year.

Enercare Inc. (TSX:ECI) is engaged in home services and sub-metering businesses. The company's current payout ratio is a massive 182%, and although it drops to 124% base on its next 12 months' earnings, it is still painfully high. The company did raise dividends by 4% in early March, but its dividend-growth rate has been on a downward trajectory over the past year. Its payout ratio as a percentage of earnings before interest, taxes, depreciation, and amortization (EBIDTA) has grown to 104% in 2017 from 94% in 2016, which is further reason for concern.

Last on the list is **Parkland Fuel Corp.** (TSX:PKI). Parkland's conundrum is the most interesting of the three. It has a current payout ratio of 340% and 329% based on next year's earnings. The company's dividend-growth rates are unspectacular and hover between 2% and 3% over the past five years.

Parkland is considered a high-growth company which has been fueled by acquisitions. Herein lies the issue. A high-growth strategy, particular one with high capital expenditures or with high acquisition costs, is at odds with a dividend-growth strategy. As opposed to paying dividends to its shareholders, it should re-invest its funds to offset these costs and sustain its growth strategy.

Bottom line

It's important for investors to understand the sustainability of a company's dividend. These aristocrats all have a history of raising dividends, but their high payout ratios are reason for concern. This does not necessarily mean they are bad investments, but investors looking for sustainable dividends may be better off looking elsewhere.

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