Energy Investors: 2 Dividend-Growth Stocks That Look Undervalued

Description

The rebound in oil prices is bringing interest back into the producer side of the energy sector, but the infrastructure plays are struggling.

Let's take a look at **Inter Pipeline Ltd.** (TSX:IPL) and **TransCanada Corporation** (TSX:TRP)(NYSE:TRP) to see why they might be attractive picks.

IPL

Inter Pipeline owns natural gas liquids (NGL) extraction assets, oil sands, pipelines, conventional oil pipelines, and a liquids storage business in Europe.

The company navigated through the oil rout in good shape, and management even took advantage of the downturn to add strategic assets at cheap prices, including the purchase of two NGL extraction facilities from **The Williams Companies** for $1.35 billion. The deal was done at a significant discount to the cost of building the assets and is already paying off as market prices improve.

In fact, IPL's gas-processing group reported a 20% year-over-year increase in Q1 funds from operations. This helped IPL generate record Q1 net income of $143 million.

Growth is also coming from organic developments, including the $3.5 billion Heartland Petrochemical Complex. The facility is scheduled for completion in 2021 and is expected to deliver long-term average annual EBITDA of $450-500 million.

IPL raised its dividend late last year, and more gains should be on the way, supported by improved throughput on the pipelines and better market conditions in the NGL processing business. Once the new assets come online, cash flow should get an additional boost.

IPL's payout ratio for Q1 was 63%, so the distribution should be safe, even if the sector hits another rough patch. At the time of writing, investors can pick up a 7% yield.

TransCanada

TransCanada also reported strong Q1 2018 results. Net income came in at $734 million, or $0.83 per share, compared to $643 million, or $0.74 per share, in the same period last year.

Revenue from the completion of $7 billion in new growth projects helped offset the cash flow lost through the sale of the company's northeast U.S. power assets.

Looking ahead, TransCanada continues to work through a $21 billion near-term capital program, of which $11 billion in assets should be wrapped up in 2018, and the remainder through 2021. As a result, management expects revenue and cash flow to improve enough to support annual dividend growth of at least 8% per year over that time frame.

Beyond 2021, TransCanada is evaluating an additional $20 billion in opportunities, including Keystone XL, Coastal GasLink, and the Bruce Power life extension. If one of these large projects gets the final go-ahead, the dividend-growth guidance could get an upgrade.

TransCanada's current dividend provides a yield of 5%.

The bottom line

IPL and TransCanada pay above-average distributions with solid dividend-growth prospects. An equal investment in the two stocks would provide a 6% yield and a shot at some nice capital gains once investors return to the energy infrastructure sector.

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Date
2025/07/24
Date Created
2018/05/29
Author
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