



Here Is Why Hydro One Ltd. (TSX:H) Stock Is a Buy on a Dip

Description

Judging by the stock performance of Ontario's largest electricity distribution and transmission utility **Hydro One Ltd.** ([TSX:H](#)), you can't tell that something bad is brewing up after the majority win for the province's Progressive Conservative leader Doug Ford, who vowed to remove the company's chief executive.

Ford has promised voters ahead of the June elections that he will fire the utility's CEO Mayo Schmidt due to his "unacceptable" \$6.2 million pay package. Ford has also promised to replace the company's board of directors during his first days as premier. The province of Ontario owns 47% of this \$12 billion utility.

Investors, however, remain cool, even after Ford's party won enough seats to push through its reform agenda. Hydro One shares, after dipping to \$18.93 in the middle of May, have continued to trade around \$19-20 range since the June 7th elections.

Complex problem

The possible reason for this calm is that investors realize that it won't be easy for the populist premier-elect Mr. Ford to fulfill his campaign promises regarding [Hydro One](#) due to the many complexities involved.

First, under the existing rules, the government has no right to fire the Mr. Schmidt. It can replace the existing directors, but a committee of independent shareholders can influence who the new nominees are. And the replacement directors "must meet the same qualification and independence standards" as any other director.

Hydro One's largest independent shareholders include **Investors Group**, **Bank of Nova Scotia's** investment management arm, and **Fidelity Investments**.

According to a report in *The Globe and Mail*, the real test of Ford's populism will be whether "he still tries to boot the board despite these constraints, simply to keep his campaign promise." If he does try to kick out of the directors, Hydro One's share price will likely sink, because independent investors are

averse to political meddling of this kind.

Another risk is that any political intervention in the affairs of Hydro One may jeopardize the company's pending US\$4.4 billion acquisition of Washington-based **Avista Corp.** This deal, which is going through the regulatory approvals in the U.S., is the key element of Mr. Schmidt's growth strategy at a time when the power and gas utilities are consolidating, and there aren't many growth opportunities left in Canada.

The bottom line

Despite these challenges, Hydro One remains one of the top utility stocks in Canada that pays steadily a growing dividend. In the first quarter, the company reported that net income attributable to common shareholders rose 33% to \$222 million. Hydro One also boosted its quarterly dividend by 5% to \$0.23 per share.

With stakes too high for the government, which is the largest shareholder in Hydro One, and general consumers, I don't think Mr. Ford's coming government will take a step that will derail this utility's future. That said, Hydro One stock is likely to [underperform](#) until Mr. Ford finds a face-saving compromise with management.

Trading at \$19.45 at the time of writing, and with an annual dividend yield of 4.3%, Hydro One is a buy on any possible dip due to this political uncertainty.

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