Dividend Investors: Should You Buy BCE Inc. (TSX:BCE) or Hydro One Ltd. (TSX:H)?

Description

A number of Canada's dividend darlings have taken a hit in recent months, giving income investors a shot at picking up some attractive yield while making a contrarian bet on potential upside.

Let's take a look at **BCE Inc.** (TSX:BCE)(NYSE:BCE) and **Hydro One Ltd.** (TSX:H) to see if one deserves to be in your portfolio.

BCE

BCE traded for close to $63 per share last November. Today the stock is below $55. Not much has changed with respect to the company's outlook, but investors are becoming concerned about interest rates.

Why?

The Bank of Canada and the U.S. Federal Reserve are raising interest rates at a steady clip, and more increases are likely on the way.

Higher interest rates can be negative for dividend stocks that tend to attract conservative investors who are seeking safe returns on their savings. BCE's dividend is widely viewed as one of the safest in Canada, so the stock likely benefitted in recent years from money that left savings accounts and fixed-income products that paid little interest.

Now that rates are on the rise again, GICs are starting to look attractive and investors appear to be heading for the exits before the expected shift of funds occurs.

BCE raised its dividend by 5% for 2018, and investors should see the payout continue to increase in step with rising free cash flow. The company expects EBITA growth to be 2-4% in 2018 and free cash flow growth to be 3-7%. Going forward, I would expect the trend to continue along those lines.

BCE is a giant in the Canadian communications market with the power to boost prices when it needs some extra cash. The company’s fibre-to-the-premises rollout should serve as a competitive advantage over the medium term and people continue to consume more data.

At the current stock price, investors can pick up a 5.5% yield with steady dividend growth on the horizon. If trade wars erupt, the Bank of Canada and the Fed could put the rate hikes on hold, which would probably provide a tailwind for BCE.

It’s a bit of a contrarian play, as more downside could be on the way, but BCE is starting to look attractive as a buy-and-hold dividend pick at this price.

Hydro One

Hydro One traded for close to $26 per share two years ago. Today, investors can buy the stock for about $19. The interest rate scenario can take part of the blame in this case, but the bigger issue facing the stock is the current uncertainty regarding its future leadership and strategy in the wake of the Doug Ford provincial election win.

Hydro One’s CEO and the entire board of directors are out and the market in trying to figure out what will happen in the coming months. The company is in the process of trying to close its US$5.3 billion purchase of Washington-based **Avista Corp.** — a deal that was expected to make Hydro One a major utility player in North America.

Volatility should be expected in the coming months, but the long-term potential of Hydro One as a dividend play makes it interesting. At the time of writing, investors can pick up a 4.8% yield and book a shot at an upside move once all the dust settles on the Avista deal and the management changes.

Is one a better contrarian bet?

If you have some cash on the sidelines and think the pullbacks are overdone, I would probably split a new investment between the two companies.

Otherwise, there are other opportunities to consider right now.

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