

Hungry for Income? These Stocks Have Dividend Yields of up to 9%

Description

Attention income investors: **AltaGas** ([TSX:ALA](#)), **Pattern Energy Group** (TSX:PEG)(NASDAQ:PEGI), and **TransAlta Renewables** ([TSX:TA](#))([NYSE:TAC](#)) currently have dividend yields of 9%, 8.3%, and 7.8%, respectively. Are these gifts from the market? Or is it all too good to be true? Let us take a closer look at these three stocks and see if we can come to a verdict.

AltaGas

AltaGas is a diversified energy infrastructure company that is headquartered in Calgary. The company has three business segments: gas, power, and utilities. Its gas segment is involved in natural gas gathering and processing as well as natural gas liquid (NGL) extraction and fractionation, storage, transmission, and the marketing of natural gas and NGL.

AltaGas's power segment supplies energy generated from natural gas, hydro, wind, and biomass. The company's utility segment provides natural gas to homes and businesses across North America.

AltaGas's 2017 revenue came in at \$2.6 billion, while net income was \$91.6 million. For the second quarter of 2018, the company reported revenue of \$609.8 million and a net income of \$17.8 million. The company has a strong dividend history; it has increased dividend payments every year since 2011.

The company's trailing 12-month dividend-payout ratio is very high at 675%. Payout ratios for the 2017, 2016, and 2015 financial years were also well over 100%. These consistently high payout ratios immediately raise [red flags](#) and suggest that AltaGas's dividend payments may not be sustainable.

Before we make our conclusions, let's take a look at the free cash flow payout ratio (defined as dividend/free cash flow, and expressed as %), as this is often a better indication of dividend sustainability. For the last 12 months, this ratio is 630%, while it was over 800% for financial year 2017. This analysis indicates that AltaGas's current free cash flow is not nearly enough to pay its dividend.

Pattern Energy Group

Pattern Energy is an independent U.S.-based renewable energy company that owns and operates wind and solar power projects. Revenue is derived from selling electricity and renewable energy credits. The company has utility-scale projects in the United States, Canada, Japan, and Chile. Since its IPO in 2013, the company's revenue has more than doubled, reaching US\$411 million for the 2017 financial year.

For the past four consecutive quarters, Pattern recorded a total revenue of US\$454 million, a net income of US\$131 million and a dividend-payout ratio of 135.9%. Its current free cash flow payout ratio is 98%, which is much lower than AltaGas's. Pattern's dividend per share has steadily increased over the past five years.

TransAlta Renewables

TransAlta Renewables is a Calgary-based company that owns and operates renewable power-generation facilities including wind, hydro, and gas. Its facilities are located in Australia, Canada, and the United States. TransAlta's year-over-year revenue increased by 84% to \$441 million in 2017, while net income was \$9 million.

TransAlta has increased its dividend every year since 2013. The company's trailing 12-month dividend-payout ratio is high at 275%; however, its free cash flow payout ratio over the same period is reasonable at 86%. This suggests that the company's operations currently generate enough free cash to sustain its dividend payments.

Verdict

Income investors hunting for high dividend yield stocks should ensure that the relevant companies generate enough [free cash flow](#) to sustain dividend payments. If dividend payments exceed free cash flow for a long period, then the company may be forced to reduce capital expenditures, sell assets, and/or raise additional funds through debt or equity financing, all of which could negatively impact growth and/or stock price in the long term.

Both Pattern Energy Group and TransAlta Renewables have a reasonable free cash flow payout ratio and have historically increased dividend payments each year. These facts combined with impressive recent revenue growth make these two companies great options for income investors.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:TAC (TransAlta Corporation)
2. TSX:ALA (AltaGas Ltd.)
3. TSX:TA (TransAlta Corporation)

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