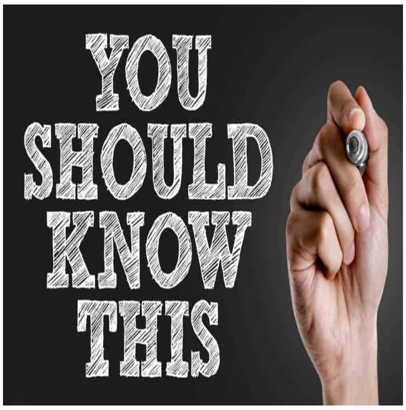

Investors: Don’t Buy Another Energy Stock Until You Read This

Description

A couple of years ago, during the depths of the energy crisis, I swore off owning most oil and gas stocks forever.

You might think this was a knee-jerk reaction to bad news. After all, oil eventually bottomed out at less than $30 a barrel. Shares of many of the major oil producers are up handily since then. Besides, it seems silly to not have any energy exposure in my portfolio.

I regret nothing. In fact, if I had life to live over again, I would have put this ban on a decade ago when oil was really rocking. Ultimately, my problem with the industry comes down to the price of the commodity. I don’t know where oil will be a week, a month, or a decade from now. If the best in the business can’t consistently get it right then what chance do I have?

An oil company can’t innovate and come up with a premium product. Oil is the same no matter where it comes from. Sure, there are different types of oil — heavy oil from Alberta’s oil sands immediately comes to mind — but at the end of the day it’s all a commodity. A refinery set up to convert heavy oil into gasoline and other products doesn’t care who produced the commodity.

Once you eliminate all oil producers from your search, investing in the sector becomes incredibly easy. The only companies left are oil services companies — which suffer from the same commodity fate — and the pipelines.

The pipelines are where you want to focus your investment dollars. They truly are wonderful companies you’ll want to own over the long term.

Why pipelines?

I’m constantly amazed at how difficult it has become to build a major pipeline in North America. Companies are forced to spend billions on environmental impact studies, working with various population groups, and lobbying government officials. And once an approval is granted, the whole process can grind to a halt because of an order by a judge.

This is bad news for Alberta's energy industry, which desperately needs ways for its products to be transported to markets. It's great news for investors in the pipelines that already exist.

Inter Pipeline Ltd. (TSX:IPL) owns two of the largest oil sands pipelines, among its other assets. They transport some two million barrels of crude every day to refineries in the Edmonton area and beyond. These pipelines are only about 50% full today, meaning that they're well positioned to handle any extra output from the region.

Oh, and Inter Pipeline pays a 7.4% dividend. Not only is this payout well covered by cash flow, but the company also has a demonstrated history of raising its distribution.

TransCanada Corporation (TSX:TRP) and **Enbridge Inc.** (TSX:ENB)(NYSE:ENB) are even bigger than Inter Pipeline. TransCanada has nearly $100 billion worth of assets, including the Keystone Pipeline system. The company's planned Keystone XL expansion is facing some legal issues right now, but it should still happen. It will build the natural gas pipeline that feeds the LNG Canada export terminal and should be completed by 2022.

Enbridge, meanwhile, is even bigger. It has more than $160 billion worth of assets, a number that has recently been bolstered by a series of acquisitions. It is currently spending $9 billion to upgrade parts of its Line 3 pipeline, which will transport about 750,000 barrels of crude each day from Canadian producers to refineries in the United States when completed.

TransCanada and Enbridge are also dividend growth studs. TransCanada shares pay out a 5.3% dividend; Enbridge pays out 6.1%. Both companies have aggressive dividend growth ambitions, which can likely be obtained by new assets coming online.

During the 2014-15 oil bear market, most energy producers cut their dividends. Both Enbridge and TransCanada raised their payouts. This serves to demonstrate that the pipelines have earning power that far outweighs conventional oil producers.

The bottom line

Simply put, I regret the time I spent trying to bottom feed energy stocks. I missed out on years of capital appreciation and dividend growth opportunities by dabbling in oil producers instead of buying the pipelines.

Shares of Canada's three major pipelines are flirting with multi-year lows. It's the perfect time to start a position in these fantastic businesses.

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