AltaGas Ltd. (TSX:ALA) Stock Is Still Risky Even After a Massive Dividend Cut

Description

The Calgary-based **AltaGas Ltd.** (TSX:ALA) tested investors' nerves for a good part of the past one year. The company is a classic example of how an ambitious growth plan can go wrong if executed by an inefficient management.

As I have warned in my November 2 article, a dividend cut is imminent for the company, which had amassed a lot of debt on its balance sheet following its acquisition of the Washington-based WGL Holdings.

Though this acquisition added a lot of growth assets under the AltaGas umbrella, it also compromised management's ability to fulfill its promise with investors to grow its payout with annualized rate of 8-10%.

After running out of its options to improve its balance sheet, AltaGas finally announced a massive dividend cut last week that lowered its annual payout to $0.96 per share starting 2019, a 56% cut from what its paid in 2018.

After the dividend cut, AltaGas shares surged as investors, who already priced in this possibility, thought the worst is probably over for this power and gas utility. Even after the spike of the past week, the company's shares are still down 51% during the past 12 months, showing the outcome of a debt-loaded growth path that company took.

What's next?

According to management, the slashing of its dividend was a necessary step in order to restore the company's financial health and "ensure greater funding flexibility" after the company paid nearly $6 billion in cash to WGL shareholders as part of the acquisition. That money was funded with a short-term loan and an equity offer.

In my view, that scenario is still extremely ambitious given the fast deteriorating energy markets and investors' reluctance to commit new funds to buy energy assets at a time when the global macro environment has been changing fast.

No doubt the company will achieve higher cash flows after its WGL acquisition, but it will find it extremely difficult to continue with its ambitious capital budget plan to generate cash flows. The company may have to use proceeds from the new round of asset sales for both debt repayment and capital spending, which appears to be a tough balancing act.

Bottom line

Trading at $13.90 at writing with an annual dividend yield of 6.61%, I still find AltaGas stock a risky bet. Investors are better off to stay on the sidelines and watch the company's progress in its asset-sale drive and its ability to perform after the WGL acquisition. The company has taken a tougher medicine, but we yet don't know whether it will cure the wounds.

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