Income Investors: Lock In This Special $11.40/Share Dividend by December 31

Description

Although they might not get much attention from average investors, I always scrutinize any [special dividend] situations very carefully.

Skeptics don't care for special dividends. They feel it's just transferring wealth from a company back to its shareholders. Since the stock goes down by the same amount as was just paid, it's a zero-sum game.

I couldn't disagree more. It isn't the special dividend that should be examined. It's the situation surrounding this odd payout. That's where the opportunity lies. Often, a special dividend can be a signal of some pretty significant changes.

This next stock is one such example. Here's why **Kinder Morgan Canada** (TSX:KML) and its special dividend of $11.40/share is much more than just rewarding shareholders with excess cash.

A company in flux

I doubt any Kinder Morgan Canada shareholders could have predicted just how much the company would change a year ago.

The company was charging full speed ahead with its Trans Mountain pipeline expansion until a number of issues caused it to slam on the brakes. Support for the project dried up in British Columbia. A small group of very active protesters consistently made headlines with their opposition to the project. And reports indicated various First Nations groups were opposed to the expansion project.

Seeing all of this, Kinder Morgan Canada reacted in a fairly predictable way. It shut down all non-essential activities on the expansion until these question marks subsided. Management decided it was simply too dicey to risk any additional shareholder money pursuing something that looked more and more like it wasn't going to happen.

We all know what happened next; it was one of the biggest business stories of the year. In a shocking twist, the federal government swooped in and bought Trans Mountain, including the expansion project. In total, the feds spent $4.5 billion.

For Kinder Morgan Canada shareholders, the timing was impeccable. On the very day they voted to approve the deal, a judge yanked the Trans Mountain expansion approval, which, at best, will delay the project for years. There's even a chance the new Trans Mountain pipeline won't get approved at all.

Flush with cash, Kinder Morgan Canada embarked on a new plan. Rather than use it to expand, the money would be returned to shareholders. Note that its main shareholder, **Kinder Morgan**, is awash with debt and planned to use the windfall to strengthen its balance sheet.

The special dividend is $11.40 per share, a large chunk of the current stock price, which is just over $15. Shares will then be consolidated on a three-to-one basis, meaning investors who buy today will pay $15.30 per share and almost immediately get $11.40 per share back. This translates into a cost per share of $3.90.

Once the three-for-one reverse split happens, investors will have a cost basis of approximately $11.70 per share. The transformed company expects to generate approximately $0.90 per share in distributable cash flow and pay a $0.65 annual dividend, which gives it a forward earnings yield of approximately 8% and a dividend yield of 5.6%.

There's also upside potential that could come from various value-creation strategies. Kinder Morgan Canada's management has acknowledged exploring all sorts of different options to maximize shareholder value, including the sale of certain assets or the whole company.

The bottom line

This situation is one of the more interesting investments available in Canada right now, at least in this analyst's opinion. Kinder Morgan Canada offers total return potential of between 15% and 20% in 2019, with the majority of cash coming back to investors in just a few weeks. But don't delay; this deal will only be around for a few more days. It's scheduled to close on January 4, meaning investors should buy their shares by December 31 to ensure they get to take part.

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