Canada's Top Dividend Stock Is Yielding a Tasty 4%

### Description

Investors seeking a combination of a steadily increasing sustainable income stream, strong capital returns and solid defensive characteristics need look no further than energy infrastructure giant **Pembina Pipeline Corp.** (TSX:PPL)(NYSE:PBA).



## Record results

The provider of transportation, storage and other midstream services to the energy patch reported a stellar 2018 announcing record annual results. This included cash flow from operating activities soaring by 49% year over year to almost $2.3 billion, adjusted EBITDA shot up by an impressive 67% to $2.8 billion  and net earnings surged 45% to almost $1.3 billion.

A range of factors including firmer crude, oil and natural gas transportation bottlenecks, growing hydrocarbon production and greater demand for Canadian crude all point to Pembina unlocking further value for investors during 2019.

Already, its stock has soared by 23% since the start of 2019, roughly matching West Texas Intermediate's (WTI) 27% gain. Even if crude doesn't perform as strongly as some analysts have predicted, Pembina will continue to rally.

The company's pipeline network is a crucial link between Alberta's oil sands and crucial U.S. refining markets that are dependent on heavy crude. Pembina's transportation and storage assets also form an important connection between Canadian natural gas producers and east coast markets.

Existing pipeline bottlenecks and growing bitumen production, which were responsible for a creating an oil glut in Western Canada that suppressed Western Canadian Select (WCS) prices continue despite Alberta's mandatory production cuts — temporarily buoying prices. This is due to the pipeline exit capacity that's preventing oil sands producers from shipping the bitumen produced to U.S. refineries cost effectively.

Pembina expects that its portfolio of projects will allow the hydrocarbon transportation capacity of its network to reach three million barrels daily by 2021.

That expansion in capacity will essentially be utilized once it comes online because of the existing lack of pipeline capacity coupled with the Canadian Association of Petroleum Producers forecasting that Canada’s crude production will expand by 33% by 2035.

Growing transportation volumes combined with stronger demand for the utilization of Pembina’s infrastructure and higher pricing means that adjusted 2019 EBITDA according to company forecasts could rise by up to 6% year over year to $3 billion.

Along with 64% of Pembina’s adjusted EBITDA generated by contracted sources, these factors virtually guarantees the company’s earnings. When combined with the steep barriers to entering the energy infrastructure industry, it endows Pembina with a wide, almost insurmountable economic moat that protects its earnings.

It is these defensive characteristics that make it a highly appealing investment and shield Pembina from economic downturns.

The difficulties associated with entering the petroleum transportation sector including pipelines and storage infrastructure is underscored by the lack of transportation capacity in Canada. This was caused by an almost perfect storm of a lack of investment, community opposition and steep regulatory requirements.



Oil’s collapse in late 2014 has further exacerbated the lack of investment, as has Alberta’s decision to prop up bitumen prices by introducing mandatory production cuts in January 2019. By artificially supporting the Canadian heavy oil benchmark price, Edmonton has removed a key incentive for oil sands producers to invest in and lobby for further pipeline exit capacity.

This means that the major players in Canada such as Pembina hold a dominant and almost unassailable position and will continue to do so for the foreseeable future.

## Is it time to buy Pembina?

Pembina’s market position, solid financial condition and the growing capacity of its pipeline network coupled with ever growing demand makes it a must-own stock that possesses a unique combination of growth and defensive characteristics.

The almost guaranteed nature of a large portion of Pembina’s earnings supports the sustainability of its dividend, which is currently yielding a juicy 4%. Along with growing earnings and a payout ratio of around 88%, that means that further dividend hikes are likely.

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