Income Investors: Get 5% From This Stock

Description

Rates are staying lower for even longer. After a very brief period of rising interest rates, responsible savers were told that their cash returns would be negatively impacted in order to support Canada's borrowing addiction. It appears that the general population has gotten itself into such a pickle that interest rates, which still sit at the ultra-low level of 1.75%, are threatening to collapse the country's economy.

Nevertheless, it appears investors are forced to make a choice. Even before the Bank of Canada dropped the much-anticipated news that interest rates will be staying at this level for the foreseeable future, rates on GICs had already begun to collapse, with some five-year yields dropping a whole percentage point. As it stands, the five-year rate on a guaranteed investment is essentially the same as that of a one-year GIC. This means there is little incentive for would-be savers.

Those savers looking for yield, the real backbone of the economy, are again being driven into riskier high-yield bonds and the stock market. There is one positive fact for income investors who are heavily invested in high-dividend stocks, however. The rush for yield should push up dividend stocks, supporting their prices for a while longer. At this point, putting some money into higher-growth dividend companies with yields in excess of 5% is not a bad idea.

Capital Power (TSX:CPX) could definitely be added to portfolios at the current level. It has a healthy yield, a decent growth profile, and has relatively stable earnings to support the payout if this period of ridiculously low yields continues to linger. This utility company focuses on renewable resources and natural gas as its primary form of power generation. Although it is heavily concentrated in Alberta, CPX has multiple power stations around North America, which gives investors a degree of diversification.

One of the benefits of this company is its fantastic dividend. Even after a huge run-up in the share price as investors run to dividend stocks, CPX's dividend remains above 5%. Furthermore, the company expects to continue raising the dividend by around 7% annually for the next several years.

The dividend-payout ratio target for Capital Power is around 45% of adjusted funds from operations (AFFO). Since the company is expected to grow its AFFO by 22% and its adjusted EBITDA by 16% in 2019, the dividend growth going forward looks fairly secure.

Besides having a generous, growing yield, CPX is also in the position to grow going forward. The utility has a number of capital expenditure projects underway, it also has the ability to fund up to $500 million in growth per year without tapping the equity markets for cash. It has done a decent job of keeping the share count somewhat stable over the years, so it looks keen to maintain this promise.

There are income alternatives

While I would not suggest dumping all your cash into a stock like Capital Power, it is a reasonable income alternative now that GIC and bond yields are once again heading south. Besides, lower yields will help support the value of these bond proxies, at least until rates go up again someday.

Central banks around the world are bent on continuing the decade-long debt binge, it seems likely that investors will be reaching for yield for a long time, potentially even years. Income investors have to focus on companies that pay a good yield and have the potential for future growth over the long term. While a company like CPX isn't the same as owning a GIC, it is a fairly stable company that will fill in the income gap created by falling rates.

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