Is This Big Dividend Stock Suitable for Your Portfolio?

Description

The first thing that makes **Vermilion Energy** (TSX:VET)(NYSE:VET) stand out is its big dividend, which yields close to 9%. Moreover, it has steadily increased its dividend since 2003 — through the last market crash and the oil price collapse.

Why Vermilion offers a big dividend

One reason the stock offers such a big yield is that the stock price has declined by about 34% over the last 12 months. Another reason is that the global oil and gas producer has raised its dividend over time. The combination of its lower stock price and higher dividend per share has pushed Vermilion's yield to 8.9% at about $31 per share as of writing.

Vermilion estimates that its total payout ratio will be about 88% this year. So, its dividend should be sustainable. After all, there were years since 2003, in which it had payout ratios of more than 100%, but it was still able to maintain its monthly dividend.

Unlike other energy companies such as **Suncor Energy**, Vermilion doesn't tend to return capital to shareholders through stock buybacks, which allows more capital to be paid out as dividends.

Notably, Vermilion has a dividend reinvestment plan, which allows shareholders to reinvest their dividends for more shares every month. So, Vermilion's share count has been rising. From 2012 to 2017, Vermilion increased its outstanding shares on average by about 4.3% per year. From 2017 to 2018, Vermilion's outstanding shares increased by about 16.3% largely due to the Spartan Energy acquisition. Thankfully, the acquisition was accretive.

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First-quarter results

In Q1, Vermilion produced on average 103,404 barrels of oil equivalent per day (boe/d), which aligned with its guidance of 101,000 to 106,000 boe/d for the year.

The company generated funds flows from operations of $1.66 per share, 14.5% higher than the same quarter in the prior year. The increase was primarily due to higher Canadian realized oil prices and increased sales volumes during the quarter.

Foolish takeaway

According to Vermilion's estimated payout ratio of about 88% this year coupled with the fact that the company has maintained or increased its dividend since 2003 despite certain years having payout ratios of more than 100%, Vermilion's 8.9% yield appears to be sustainable.

However, the stock is quite volatile due to its sensitivity to and reliance on commodity prices. So, investors should have a high tolerance for risk and aim to buy the stock on meaningful dips. Currently, it's trading at a relatively low valuation at about five times cash flow at writing.

Thomson Reuters has a 12-month mean target of $42.70 per share on the stock, which represents nearly 38% near-term upside potential. Combined with the big dividend, buyers today are looking at potential total returns of about 46% over the next year.

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