



Hydro One (TSX:H) Is Your Bulletproof Stock for the Coming Recession

Description

If you're worried about the [upcoming recession](#), it's critical to position your portfolio to weather the storm. Be careful, though. There are countless stocks that investors believe will be recession-proof, but when a bear market hits, these companies aren't as reliable as once thought.

To find a truly bulletproof stock is rare, but **Hydro One** ([TSX:H](#)) meets all of the requirements.

If you want to endure the next recession with little to no impact on your wealth, take a closer look at Hydro One.

A simple secret

Why is Hydro One the perfect recession-proof stock? It's not because it has a savvy management team or a special technology. The secret is surprisingly simple: its revenues and profits are essentially guaranteed by the government.

Hydro One is one of the largest electric utilities in North America. It has no material exposure to commodity prices given it sources its power from hydro facilities. Critically, 99% of its business is rate-regulated, meaning that it has near-perfect visibility into its revenue and profit streams.

Because of the unique visibility of its financial future, growth can be predicted years ahead of time. Management is targeting 5% annual EPS growth over the next five years while targeting a 70% to 80% payout ratio. Over the past few years, the dividend yield has averaged roughly 4%.

Notice that these statistics aren't overly impressive, however. A 4% dividend is respectable, but hardly breaks the bank. Annual EPS growth of 5%, meanwhile, is downright paltry. But remember, you're not paying for huge upside.

Instead, you're paying for absolute resilience no matter where the global economy heads. If the stock market fell 50% next month, I'd be surprised if Hydro One shares dipped more than 10%. If the market reallocates capital to defensive stocks, Hydro One shares could actually *rise* during a downturn.

How to invest

In 2019, Hydro One is set to earn \$1.46 per share. That pegs the current share price at 16.8 time earnings. That's certainly a reasonable price to pay in the current environment.

If the global economy remains intact, I'd expect Hydro One shareholders to earn an annual return of 5% or 6% over the next few years. Again, that isn't overly impressive, but sketching out what could happen during a bear market makes the investment case clear.

During the 2008 financial collapse, market multiples compressed by 50% in a matter of months. The vast majority of stocks fell by double digits. Still, the cyclically-adjusted valuation multiple for the **S&P 500 Index** remained at 15 times earnings on January 1, 2009, the depth of the crisis.

If Hydro One were to fall to this level, there would only be 11% downside. When factoring in 5% EPS growth, which is nearly guaranteed, there would only be roughly 6% downside during another financial collapse. Add in the 4% dividend and you're close to breakeven.

The exact impact on the valuation multiple during a recession is uncertain, but the dividend payout and earnings profile should remain constant. If you want portfolio protection at all costs along with mid-single-digit growth if the economy *doesn't* sour, Hydro One is your best bet.

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