Warning: Your “Safe” Dividends From Utility Stocks Could Be Under Threat!

### Description

Utility stocks are widely considered to be some of the safest investments on the market. There’s a good reason for that — providing utilities is a natural monopoly. A centralized energy producer can be the only distributor within a certain region. Regulations and the capital-intensive nature of the industry raise barriers to entry, while demand is impervious to the market cycle.

That’s why so many passive-income portfolios rely heavily on utility stocks that pay hefty dividends, like **Fortis** or **Algonquin Power & Utilities**. However, there seems to be an emerging threat to this industry’s centuries-old state of natural monopolization.



## Microgrids

As the name suggests, microgrids are self-contained power networks that serve consumers on a smaller scale. The declining costs of renewable energy-generating technologies, along with the expanding capacity of batteries, has made these microgrids viable, at least on a commercial level.

For now, universities and enterprises are adopting these microgrids to power their operations independently. All the major American technology companies, from **Amazon** to **Apple**, have deployed their own microgrids in recent years to power their data centres and headquarters.

Universities like Illinois Tech, Ohio State University, and Cornell Tech also have their own facilities. Meanwhile, in Canada, remote communities and government institutions are also adopting independent microgrids.

Since energy is created and distributed within a short distance, these microgrids can improve transmission efficiency and lower the risks of severe outages. In short, they’re an elegant solution to a persistent problem.

This new solution threatens to undermine the traditional business model for utilities. Giant utility companies with massive power plants serving millions of homes and offices together stop making sense when every corporation or condo developer can deploy their own microgrid to meet their energy needs.

"This technological transformation raises a threshold question of whether distribution utilities and the grid will continue to be needed or become a historic relic," say researchers from the U.S. Department of Energy.

## Should you dump utilities?

Not really. Utilities are reliable sources of robust dividends that have been built up over decades. Power infrastructure could take many more decades to revolutionize. So, income-seeking investors can rest easy about their utility holdings.

However, I believe it's worth keeping an eye on this emerging threat and the gradually shifting dynamics of the global energy market. Several utility companies seem to be aware of the threat and are already being proactive to secure their businesses long term.



Fortis, for example, said one of its subsidiaries deployed US$370 million in a wind farm located in New Mexico that can power roughly 100,000 homes. Similarly, **Canadian Utilities** has been offloading its fossil fuel plants to shift investments to renewables.

Several other utility companies are diversifying their business to secure their long-term prospects. I believe investors should avoid the ones who aren't, because they remain vulnerable to imminent disruption.

## Foolish takeaway

Utilities have been traditionally used to hedge against the risk of recessions. However, the industry is gradually evolving away from the natural monopoly and high barriers to entry model, which could undermine this industry's ability to churn out lucrative cash flows and sustain dividends over the long term.

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