Why This Dividend Stock Is My Favourite — and Should Be Yours Too!

Description

When it comes to dividend investing, it is prudent to look for long-term earnings stability. Because if a company is generating stable earnings, it will pay stable dividends over a longer period.

A fair yield and a steadily increasing dividend make an apt combination for a perfect dividend stock. In my view, **Algonquin Power and Utilities** (TSX:AQN)(NYSE:AQN) checks in all these boxes.

Utility stocks are many times called widow-and-orphan stocks due to their slow stock movements and stable dividends. However, they can generate significant returns over the years and outperform a usual growth stock.

Stable earnings

Algonquin generates a large portion of its earnings from regulated operations. These regulated operations offer earnings stability and predictability. The company has a significant investment in renewable power generation as well.

Algonquin has shown superior earnings growth in the last few years. In the last three years, its profits have increased by almost 40% compounded annually.

In my view, this seems significantly higher for a utility and might not continue at the same pace over the future. It will likely fall to industry average levels eventually.

Stable yield and growth

Algonquin stock is currently trading at a dividend yield of 3.4%, which seems very reasonable. Its dividends increased by 7.5% in the last five years, compounded annually. What's striking here is the company's dividend predictability.

Algonquin's management aims to increase its dividends by 10% per year through 2021. Beyond that, its dividend growth pace could lower marginally, albeit will likely stay impressive.

Many utility companies convey their future dividend growth due to their earnings predictability. In my view, this is very important for long-term investors.

Of course, things can go wrong, and companies sometimes have to trim their forecast, albeit this doesn't appear to be a concern right now. Such is the advantage of investing in a non-cyclical and safe-play stocks.

At the same time, the utility giant **Fortis** has been growing its bottom line more slowly. It also yields 3.3% and expects to increase dividends by 6% through 2024.

Market performance

Algonquin stock has risen more than 50% in the last 12 months, largely outperforming many utility peers. It is trading 23 times its forward earnings, and thus looks expensive at the moment.

It should be noted that Algonquin has shown superior earnings growth recently and hence deserves a higher multiple. However, it would be more prudent to enter at weakness.

Interestingly, utility stocks have been on a notable run since last year; almost all of these stocks look expensive. Fortis stock is currently trading at 22 times its earnings and the stock is up almost 25% in the last 12 months.

Algonquin Power will report its Q4 earnings later this week. It will probably set the path for its stock in the short term. Management commentary for 2020 will also be an important trigger for its stock.

Bottom line

As mentioned, earnings stability is a key aspect for dividend stability, which Algonquin Power offers in the foreseeable future. Its expected dividend growth is one of the highest among peers. Importantly, higher earnings growth will likely continue to drive the stock upward in short to intermediate future.

Thus, even if investments into utility stocks look lackluster, stocks such as Algonquin Power and Utilities could reap significant benefits over the long-term.

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