



Should You Put \$5,000 Into This 8.2% Dividend Stock?

Description

Enbridge Inc ([TSX:ENB](#))([NYSE:ENB](#)) was once one of the most reliable dividend stocks in Canada.

In 2008, when global equities were falling by 50% or more, Enbridge stock ultimately *gained* in value. In 2014, when oil prices were cut in half and parts of Canada entered a brief recession, Enbridge stock gained yet again.

The events of 2020, however, appear too much to handle. Coronavirus fears and another [oil price collapse](#) have pushed Enbridge stock lower by 28%, causing the dividend yield to spike to 8.2%.

Some investors are looking at the company's long history of success, seeing the high dividend as a clear buying opportunity. Others are more skeptical, arguing that this time could be different.

So which one is it? Should you be buying or selling Enbridge stock during the market crash?

This dividend was rock-solid

If there was ever a dividend to trust, it would be Enbridge. Over the past 20 years, the dividend has grown by 12% per year. The company targets a payout ratio of 65% or less, ensuring its long-term stability without sacrificing the ability to invest in growth initiatives.

Just last quarter, management bumped the dividend by 10%. It now stands at \$3.24 per share on an annualized basis. Before the market crash, the stock had a forward yield of 5.8%. After the correction, shares now yield 8.2%.

After 20 years of consecutive increases, it's difficult to see the dividend stagnating, or even *falling*. But that's a stronger possibility than ever. To understand why the dividend is in danger, we must understand why it exists in the first place.

Built on volumes

Enbridge is the largest pipeline company in North America. It ships around 20% of the continent's crude oil, and a similar amount of its natural gas.

Pipelines are like toll roads. If you own the only road in town, your pricing power is steep. Because pipelines are so costly and complex to build, they typically *are* the only road in town.

With this pricing power, companies like Enbridge opt to charge customers on volumes, not commodity prices. This is why profits were barely impacted in 2014, when oil prices were cut in half. Volumes remained steady, so Enbridge profits were uninterrupted.

Canada and the U.S. have experienced rising fossil fuel volumes for more than a decade. New technologies that enabled massive shale and oil sands projects were a big contributor. Unfortunately, Enbridge's biggest advantage — a volume-based business — could soon be its Achilles heel.

Out of your hands

At the start of 2019, oil traded at US\$60 per barrel. Today, that price is closer to US\$20 per barrel. Investors might assume that Enbridge's volume-based business will be insulated from the plunge, but this time could be different.

In 2014, oil prices moved from US\$100 per barrel to US\$50 per barrel. That was painful, but the vast majority of onshore production was still profitable, so output continued undeterred. Enbridge, therefore, was unaffected.

In the recent plunge, however, prices fell *below* the breakeven level for most producers. No oil producer will continue to pump if it remains in loss-making territory.

If oil prices stay depressed, a significant amount of volume will come offline. Some supply will never return. That would be a direct blow to Enbridge. The dividend likely wouldn't survive intact.

If oil prices normalize, however, long-term industry volumes will be unaffected. Enbridge can continue business as usual.

How likely is it that conditions will normalize quickly? It's all up to Saudi Arabia.

Saudi Arabia has been slashing prices and boosting output to force the global oil market into chaos. Its goal may be to take higher-cost industry supply offline. Because the country has the cheapest production costs in the world, it can continue the price war as long as it wishes.

As I wrote [last week](#), "Many analysts believe that the current pricing war could continue until scores of North American production permanently exit the market. Canadian producers are holding on as long as they can, but they can't sustain losses forever."

While Enbridge is a terrific company with a strong dividend, its future is now solely in the hands of Saudi Arabia. This is not a situation in which I'm willing to put money on the line. The market crash has

provided plenty of other opportunities worth pursuing.

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Date

2025/08/25

Date Created

2020/04/05

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