AltaGas (TSX:ALA) Stock De-Risked As Company Maintains 2020 Financial Outlook

Description

Diversified utility and midstream assets operator **AltaGas** (TSX:ALA) released an encouraging set of first-quarter 2020 financial results on Thursday. The latest quarterly results demonstrate AltaGas's resilience as a defensive stock. Most striking, however, was management's maintenance of its earlier earnings guidance for this year during a period of high uncertainty due to the COVID-19 pandemic.

First-quarter revenue at $1.87 billion was slightly lower than the $1.9 billion reading last year. This is understandable given the significant asset sales concluded last year to pay down debt. Normalized EBITDA grew to $499 million from $482 million last year and both normalized net income and funds from operations were much higher for the first quarter of this year.

Many dividend-paying companies have cut their payouts and withdrawn their earnings guidance for 2020. But AltaGas maintains both its dividend and its financial outlook for this year.

The company expects its normalized EBITDA to range between $1.275 billion and $1.325 billion for 2020, and its normalized earnings per share to range between $1.20 and $1.30 per share.

How does AltaGas enjoy certainty during volatile times?

The company enjoys significant earnings protection from U.S. utility contracts and regulated rates. About 60% of AltaGas's normalized EBITDA this ear will come from its utilities segment, which provides stable and predictable results.

The utilities segment generated a 10% year-over-year growth in normalized EBITDA during the first quarter thanks to favourable rate case settlements in 2019, rate base growth, and lower operating costs. The consolidated utilities rate base is expected to grow by 8-10% per annum over the next five years.

The company also boasts of tight long term take-or-pay contracts and a comprehensive hedging program in its midstream operations in Canada. Its first-quarter results were strongly buoyed by contributions from the Ridley Island Propane Export Terminal (RIPET), which continues to see strong demand from Asia.

Most noteworthy, comprehensive hedging activity has come in handy this year. The company has hedged about 80% of its expected export volumes at RIPET. Including tolling arrangements, about 86% of RIPET's propane export volumes are hedged. In total, management says hedges are in place for 93% of the company's frac-exposed natural gas liquids volumes.

I'm not sure whether ALA management would have been so confident in reiterating its prior earnings guidance had they not had such comprehensive hedges in place for this year.

Buy AltaGas stock for the safe dividend?

ALA's $0.08 per share quarterly dividend yields a respectable and nice 5.8% today. I wouldn't be concerned about a potential dividend cut on AltaGas stock in the near term. It's a profitable company whose earnings and future cash flows are so clearly visible.

The company has a $900 million capital investment budget that will be funded largely from internally generated cash flows. The investments are primarily within the low-risk utilities segment. Sustained investments in 2020 should help increase AltaGas's utilities rate base and help support future dividend payments.

Foolish takeaway

AltaGas stock is a strong defensive play that was once mistaken for a regular energy stock during the 2020 oil and stock markets crash. However, shares have rallied in April as the market reassessed the resilience and safety of the company's business and cash flows.

A prior dividend cut after an ambitious WGL acquisition might have shaken some income investor confidence, but as the company's latest quarterly earnings show, buying U.S. utility assets wasn't such a bad idea after all.

Earlier asset disposals to pay down debt are beginning to pay off. The company reported a 25% reduction in quarterly interest expenses year-over-year as net debt declined.

Lower interest payments free up cash flows for growth capital investments and dividend payments. Investors should welcome the company's improved risk profile from declining leverage.

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