Canadian Investors: Ride Out the Volatility With Fortis (TSX:FTS) Stock

Description

The S&P/TSX Composite Index has bounced back strongly, rising close to 40% from its March lows. Improving investor sentiment and the reopening of the economy are supporting the broader market growth. However, economic indicators are still weak, with the unemployment rate in both the U.S. and Canada being on the higher side.

Citing the slow pace of recovery, the International Monetary Fund has lowered its GDP projection for 2020. The international organization now expects the global GDP to shrink by 4.9% this year. While the GDP projection is gloomy, rising COVID-19 infections are likely to add to the pain. With too much uncertainty and weak economic condition, the stock market could remain volatile in 2020.

I believe **Fortis** (TSX:FTS)(NYSE:FTS) could be an excellent defensive bet in this volatile market, given its diversified and stable business and predictable cash flows.

Fortis's operating metrics

Fortis runs a rate-regulated utility business, making it less susceptible to volatility in the market. It has allocated only 7% of its assets towards energy generation, while the rest of its assets are allocated for transmission and distribution of electricity and gas. As the energy transmission and distribution businesses are regulated, they are of low risk and deliver predictable cash flows.

For investors who don't know, regulatory mechanisms protect about 63% of Fortis's revenues. Of the remaining revenues, 19% comes from residential customers, while 18% is derived through commercial and industrial customers.

With the decline in economic activities, the commercial and industrial sales of Fortis could take a back seat. However, as more and more people have started to work from home, residential sales could rise, offsetting some of the declines from commercial customers. So, overall, 82% of the company's revenues would be risk-free.

Fortis has seen significant growth in the last three years with its assets growing by 11.5% to $53.4

billion. Further, the company expects its rate base to increase from $28 billion in 2019 to $34.5 billion by 2022. Moreover, it is projected to reach $38.4 billion by 2024. A growing utility rate base is likely to support its future earnings and payouts.

Liquidity and dividends

At the end of the first quarter, Fortis's cash and cash equivalents stood at $272 million. Meanwhile, the company's liquidity position looks strong with $1.2 billion worth of new equity offerings and the sale of 51% ownership in the Waneta Expansion Hydroelectric Facility for $1 billion in 2019.

This year, the company has completed a new credit facility of $740 million, which has raised its total unutilized credit facility to $4.6 billion. So, along with its cash, the company's liquidity at the end of the first quarter stood at $4.9 billion.

Fortis is a Dividend Aristocrat and has raised dividends for 46 consecutive years. In the last 10 years, the company has increased its dividends at a CAGR of 5.8%. For the second quarter, the company's board has announced quarterly dividends of $0.4775 at an annualized rate of $1.91. So, the company's dividend yield stands at 3.68%. The company's management has planned to raise its dividend at an average of 6% every year through 2024.

Bottom line

Fortis stock trades at a forward P/E multiple of 18.9. The company is trading at a premium compared to its average forward P/E multiple of 18.2 for the past three years. However, the company's high valuation is justified, given the defensive nature of its business, predictable cash flows and consistent dividend growth. So, I believe investors who look to protect their capital and earn regular dividends amid the volatility should buy Fortis.

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Date
2025/08/22
Date Created
2020/07/12
Author
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