Should You Buy Enbridge (TSX:ENB) Stock for the 7.6% Yield?

Description

Enbridge (TSX:ENB)(NYSE:ENB) stock used to be a staple in the portfolio of Canadian dividend-growth investors. Then came the 2014 plunge in oil prices and the COVID-19 crisis, which acted as significant one-two punches in the gut of the pipeline kingpin.

Enbridge stock: A smooth ride to a downhill rollercoaster ride

Shares of Enbridge have been endearing a downward roller coaster ride that's lasted for around five years. At the time of writing, the stock is down over 33% from its 2015 all-time high with valuation metrics that suggest the stock is close to the cheapest it's been in recent memory.

With a 7.6% dividend yield that management is reluctant to slash as it opts to pull other levers to improve upon its financial flexibility, income-oriented value investors have a lot to gain from the heavily out-of-favour midstream company that's fallen upon hard times.

Enbridge's management team has already demonstrated its shareholder-friendliness. Although the dividend has been stretched, management is unlikely to bring it to the chopping block unless that's the only option available. Borrowing to finance a dividend is hardly a great long-term strategy.

Still, management seems willing to swim to great lengths to keep its dividend "promise" to its shareholders, many of whom are likely income-oriented.

The opportunity is real, but your patience will be tested

Given the firm's commitment to its bountiful dividend, Enbridge stock grants investors an opportunity to lock-in a swollen dividend yield alongside outsized capital gains if the company can turn the ship around and stage a rebound. Given the unprecedented pressures facing the energy sector, though, I'm not so sure that Enbridge is a timely bet here.

Why?

The company has faced its fair share of regulatory hurdles, and it'll likely continue to run into them over the years. That's added pressure on top of industry woes that could worsen if this pandemic were to weigh further on demand for fossil fuels.

In a recent blow to Enbridge, the Minnesota Department of Commerce appealed the Line 3 Replacement (L3R) once again. The L3R was seen as a significant source of growth and financial relief for the firm, so as you can imagine, further delays have not been taken so great by investors amid mounting macro headwinds. Despite the regulatory setback however, L3R will eventually come online in due time, but investors are going to need to demonstrate patience.

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Fellow Fool contributor Kay Ng recently did a good piece covering Enbridge and its performance in the first half. Kay thinks that Enbridge is a passive income investment that will serve contrarian investors well over the long run, but notes that dividend growth could stall for the next several years.

"In the first half of the year (H1), Enbridge stock reported adjusted EBITDA, a cash flow proxy, of more than $7 billion — up marginally by 1.4% against H1 2019. Its distributable cash flow (DCF), from which it pays its dividend, also increased at a similar rate of 1.5% to $5.1 billion." Kay wrote. "Importantly, management reaffirmed Enbridge's 2020 DCF-per-share guidance of $4.50-$4.80. The midpoint of $4.65 implies a 2020 payout ratio of approximately 70%. This is a little high versus its target payout ratio of 65%."

The dividend is stretched, but it's probably going to survive. I'd have to agree with Kay that Enbridge is a great long-term hold for income investors with the stock at these depths, but would discourage young growth-savvy investors from jumping in here because the stock will likely continue to be stuck in limbo for another few years.

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