37% OFF: Buy Pembina Pipeline Stock Right Now for an 8.8% Dividend Yield

Description

The coronavirus led to one of the sharpest downturns in energy demand, weighing heavily on the stock prices of the companies operating in the sector. While energy producers took most of the heat, energy infrastructure companies weren't spared either.

Take **Pembina Pipeline** (TSX:PPL)(NYSE:PBA), for example. The leading North American energy infrastructure giant registered a 42% decline in its earnings for the first six months of 2020. Pembina blamed lower margins on crude oil and NGL (natural gas liquids) sales and a slump in marketed NGL volumes amid a lower pricing environment for the decline. Nevertheless, the acquisition of Kinder and increased supply volumes at the Redwater Complex drove the overall volumes higher.

Despite the improvement in volumes, Pembina Pipeline shares are still down about 37% year to date, as an uncertain energy outlook and weakness in oil prices continue to remain a drag. However, I believe Pembina Pipeline has all the right ingredients that should keep it afloat amid challenges.

Further, as the massive selloff in Pembina Pipeline stock eroded significant value, it's time to invest in it to gain big from the recovery rally in the medium to long term. Though challenges prevail, a considerable discount of about 37% and a high dividend yield of over 8.8% make it an attractive bet at the current levels.

The bull case

Investors should note that Pembina Pipeline runs a low-risk business, which is supported by long-term, fee-based contracts and includes take-or-pay or cost-of-service arrangements with no volume or price risk. Further, the company has diversified its exposure to different commodities, including NGL, crude and condensate, and natural gas.

Pembina Pipeline expects businesses with fee-based contracts to contribute about 90-95% to its adjusted EBITDA in 2020. Moreover, Pembina expects to maintain the ratio to about 80%. The highly contracted nature of its business suggests that the company could continue to generate stellar cash flows that will drive its growth and support the dividend payouts.

Pembina Pipeline pays dividends through its fee-based cash flows and has managed to reduce its standard payout ratio to 60% in 2020 from 72% in 2015. With strong fee-based cash flows and a sustainable payout ratio, Pembina Pipeline's dividends are pretty safe.

Investors should note that Pembina Pipeline's annual dividends have grown by 6.5% over the last five years. Besides, it paid about $4.5 billion in dividends. While the company is unlikely to announce any dividend hike in 2020, its resilient fee-based cash flows indicate that investors could continue to benefit from its high dividend yield amid lower rates.

Shares of Pembina Pipeline also look attractive on the valuation front. Pembina stock is trading at the next 12-month EV-to-EBITDA multiple of 9.1, which is about 20% lower than its historical average. Also, its valuation looks favourable when compared to **Enbridge's** forward EV-to-EBITDA multiple of 11.3.

Final thoughts

The uncertain near-term outlook could continue to limit the upside in Pembina Pipeline stock. However, the outlook for all forms of energy remains favourable in the medium to long term, which could support the recovery rally in Pembina Pipeline stock.

Pembina's low-risk business, an attractive dividend yield of over 8.8%, and valuation make it a top recovery play for outsized gains.

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