Warning: Michigan Might Destroy Enbridge (TSX:ENB) Stock!

Description

Enbridge (TSX:ENB)(NYSE:ENB) stock is in a precarious place. This week, we learned that its long-term future could be more difficult than many anticipate.

This is the problem

Enbridge is North America's largest shipper of fossil fuels. It's responsible for 20% of the continent's crude oil, plus a big share of its natural gas.

If fossil fuel production rises, it can ship higher volumes, boosting revenue. If production falls, the opposite happens.

Because pipelines are so costly to build — some sections cost millions per kilometre to construct — the investment costs are recouped over a long period of time.

For example, Enbridge might spend $500 million to extend one of its current pipelines with the belief that the construction costs will be recouped over a seven-year period. All proceeds after that time span would represent profit.

These initial high costs have made the company a cash flow machine. Much of its infrastructure was put into place years ago. Expansion plans consume some of the cash flow, but the rest looks like pure profit.

Here's the problem: if a pipeline is shut down earlier than expected, the payoff dynamics shift dramatically. The project can go from a multi-decade profit generator to a huge writedown at the stroke of a pen.

Enbridge could lose big

If prematurely shutting down a pipeline would be devastating to the pipeline owner, prepare for some difficult news.

“Michigan is taking steps to shut down a pipeline that carries Western Canadian oil and natural gas into the U.S. and Ontario,” reported *Western Standard* last week. “Michigan Gov. Gretchen Whitmer’s office notified Calgary-based Enbridge Inc. it was revoking an easement granted 67 years ago to extend a 6.4 km section of the pipeline through the Straits of Mackinac.”

“Any disruption would have devastating consequences,” an Enbridge spokesperson commented.

What’s the problem here? Is it something that can be resolved?

Unfortunately, this seems to be another domino in the world’s shift away from oil, which faces growing challenges due to environmental concerns.

“Enbridge has routinely refused to take action to protect our Great Lakes and the millions of Americans who depend on them for clean drinking water and good jobs,” Michigan’s governor explained. “They have repeatedly violated the terms of the 1953 easement by ignoring structural problems that put our Great Lakes and our families at risk.”

What does this mean?

If the line is shut down, that’ll mean lost cash flow for Enbridge. The bigger story, however, is that this isn’t a singular event. Fossil fuel participants face a difficult environment that won’t improve anytime soon, if ever.

“Over time, companies and countries that do not respond to stakeholders and address sustainability risks will encounter growing skepticism from the markets, and in turn, a higher cost of capital,” wrote Larry Fink, CEO of $7 trillion asset manager **BlackRock**.

What Fink is claiming would be disastrous to Enbridge.

Right now, he argues that the investing world is turning away from these stocks. That raises their cost of capital, reducing their ability to invest in growth or pay dividends. In turn, that reduces the appeal for other investors, raising the cost of capital further.

We could truly be in a free-fall situation. Enbridge has a monopoly-like business and a terrific historical record. But if the world is moving away from oil, that’ll keep a tight lid on the stock price, even if the shift takes a decade or more to play out.

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Date
2025/08/25
Date Created
2020/11/20
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