Enbridge (TSX:ENB) Announces a Dividend Increase: Buy Now?

Description

The energy sector is the only major sector on the TSX that's on a downward trajectory since 2008. There is a lot of variety in the performance of the individual underlying stocks, but the sector's performance seems to be getting weaker every year.

The S&P/TSX Capped Energy Index (TTEN) is down almost 80% from its 2008 peak, and the pandemic, which dried up oil demand, only worsened the situation. The sector has recovered quite a bit from the recent crash (120% growth since March), but chances of reclaiming its glory days are still low.

A major victim of the pandemic's blow to the energy industry is **Suncor's** dividends. The beloved aristocrat had to slash its dividends after 18 years. Even though it was a pragmatic choice, it would have hurt the dividend-based portfolios that leaned quite heavily on this industrial giant. Many investors assumed that others would follow suit, considering the condition of the industry, but **Enbridge** (TSX:ENB)(NYSE:ENB) did the opposite.

Enbridge's dividend hike

Enbridge has been a dividend aristocrat for 24 years, making it the second-oldest aristocrat in the energy sector. But its history is not what investors love most about this aristocrat; they love its generous yield. Even though the industry has been going through a rough patch, and Enbridge itself is struggling with a 330% payout ratio, it has increased its dividends, asserting its position as an aristocrat for another year.

Thanks to the discounted price tag, this aristocrat is offering a mighty 7.8% yield. Still, it is rare enough among the aristocrats, especially with dividend-growth streaks stretching back more than two decades. Whether the company increased its dividends for sheer pride or because it prioritizes retaining investor loyalty over profits and returns is hard to tell.

The question is whether Enbridge is a buy at this point or not.

Is Enbridge a good buy?

If we consider its yield and tenacity to maintain (and even increase its dividends), Enbridge seems like a solid bet. But the question isn't just what it is, but what it could be in the future. Enbridge has a 10-year CAGR of 9% (dividend adjusted), but if we consider its recent stock price history, a five-year CAGR of negative 0.2% doesn't inspire a lot of confidence.

If you are basing your decision solely on dividends, even then, you might have to consider the underlying value of the asset. Let's say Enbridge can maintain (not increase) its dividends for the next 10 years. If you buy now when the stock is offering a 7.8% yield, you will earn about $7,800 on your $10,000 investment in the next decade.

If the price stays almost consistent (highly improbable) and you sell your stake in 10 years, the $7,800 would be all you would have made over your initial investment (and you will get your $10,000 capital back). If you are okay with this level of return, and you think that the energy industry would be in better shape after 10 years, then Enbridge is a good buy for you.

Foolish takeaway

The energy sector might not be as doomed as many people think, but it's clear that the glory days of oil and an energy-based economy are over. The sector is slowly waning. Enbridge is in a relatively strong position because of its dependence on pipeline contracts for cash flow, but a major blow to the sector would impact Enbridge as well.

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