Cheap Defensive Dividend Stocks Could Shine in 2021!

Description

Defensive dividend stocks have been treading water for quite some time now. While most other stocks have gone on to stage a strong recovery from the 2020 coronavirus crash, many bond-proxy-like utility stocks have continued to fluctuate around in limbo, with no ultimate direction. The value to be had in such names, I believe, is remarkably high amid the increased appetite for taking risks.

Ever since the curtain was pulled on **Pfizer**'s COVID-19 vaccine breakthrough, investors have been rotating money out of reliable dividend stocks in favour of names that could hold greater gains in a post-pandemic environment. With mutated variants that could lengthen this pandemic, the rotation out of defensive utilities has happened far too soon.

While I have no idea whether defensive dividend stocks will be great again in 2021, I can say that I'm a huge fan of their risk/reward at this critical market crossroads, even now that we've got additional clarity on the vaccine timeline.

One of the most undervalued defensive dividend stocks on the TSX

Fellow Fool contributor Ryan Vanzo certainly seems to think there's a huge opportunity in the utility space. Vanzo named **Hydro One** (TSX:H), one of the most defensive dividend stocks out there, as his top Canadian pick for February 2021.

"Hydro One is a rate-regulated utility. Around 99% of sales come from rate-regulated sources. That means pricing is extremely reliable, as rates are dictated years in advance by regulators," Vanzo wrote.

"Volumes, meanwhile, are similarly stable, as power demand doesn't fluctuate as much as economic volatility."

In essence, you're getting a highly-regulated business, which is the closest thing to a guarantee that you'll find in the equity markets. Hydro One has a virtual monopoly, which I view as both a blessing and a curse. On the one hand, you’re not getting much in the way of surprises with the firm’s rock-solid operating cash flow stream. Investors who detest surprises can appreciate the stock in this volatile, pandemic-plagued and borderline expensive market.

The stock sports a 3.4% dividend yield at the time of writing. I’ll admit, H stock leaves a lot to be desired as far as dividend stocks are concerned. And while shares have outperformed other top utilities like **Fortis**, shares are so undervalued that it’s absurd.

A far better deal than bonds!

At first glance, Hydro One seems like an unremarkable stock. But when weighed against bonds, the name looks like one of the better deals in town. The 3.4% yield and the ridiculously low valuation are both reasons that shares of Hydro One blow fixed-income debt securities right out of the water.

Bonds are close to the most unrewarding they’ve ever been. The meagre coupons you’ll get from them make them seem ridiculously expensive and not worth owning for younger investors who seek real returns on their investment over time.

Foolish takeaway

Hydro One has a juicy dividend, and its shares are starting to become too cheap to ignore. The stock trades at 9.9 times trailing earnings, 2.5 times sales, and 1.7 times book value, which is far too low a price to pay for the calibre of defensive business you’re getting.

Vanzo is right on the money. Hydro One is one of the best bargains in the defensive space in February.

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