You Don’t Need Both of These Dividend Stocks in Your Portfolio

Description

Income investors, especially retirees, love the stable income that **Fortis** (TSX:FTS)(NYSE:FTS) and **Emera** (TSX:EMA) provide. However, if you overlap the charts of the two stocks, you’ll realize there’s no need to own both dividend stocks in your portfolio. They move in tandem!

Data by YCharts. The 10-year stock price chart of Fortis and Emera.

You’ll hear pundits emphasizing building a diversified stock portfolio, which should have components that *don’t* move in a similar fashion.

Why the two dividend stocks move in tandem

Fortis and Emera are both regulated utilities in North America with similar risk and return profiles.

First, they both earn about 66% of their earnings in the United States. Second, their assets are largely regulated, which allows them to generate predictable returns. As a result, both are low-beta stocks that tend to have low volatility versus the stock market.

Specifically, about 99% of Fortis's assets are regulated. Fortis's high-quality portfolio consists of 10 regulated utilities, including an independent electricity transmission utility in the U.S. Approximately 93% are transmission and distribution assets that deliver electricity and gas to 3.3 million customers.

More than 95% of Emera's assets are regulated. About 85% of its portfolio is electric utilities and 15% is gas utilities.

Dividends and growth

Fortis has increased its dividend for 47 consecutive years with a five-year dividend growth rate of 6.8%. It currently yields 3.7% with a safe payout ratio of about 70%.

Fortis's 2020 rate base was $30.5 billion. Through 2025, it has a capital program to grow its rate base by approximately $10 billion (equating to a growth rate of about 6% per year). This will also drive annual dividend growth of about 6% in the period.

Emera has increased its dividend for 14 consecutive years with a five-year dividend growth rate of 8.3%. Currently, the regulated utility yields 4.5% with a payout ratio of about 88%.

Emera's 2020 rate base was $21.3 billion. Through 2023, it has a capital program to grow its rate base by about $8 billion (equating to a growth rate of about 8% per year). It estimates a dividend growth rate of 4-5% through 2022.

Which is a better buy?

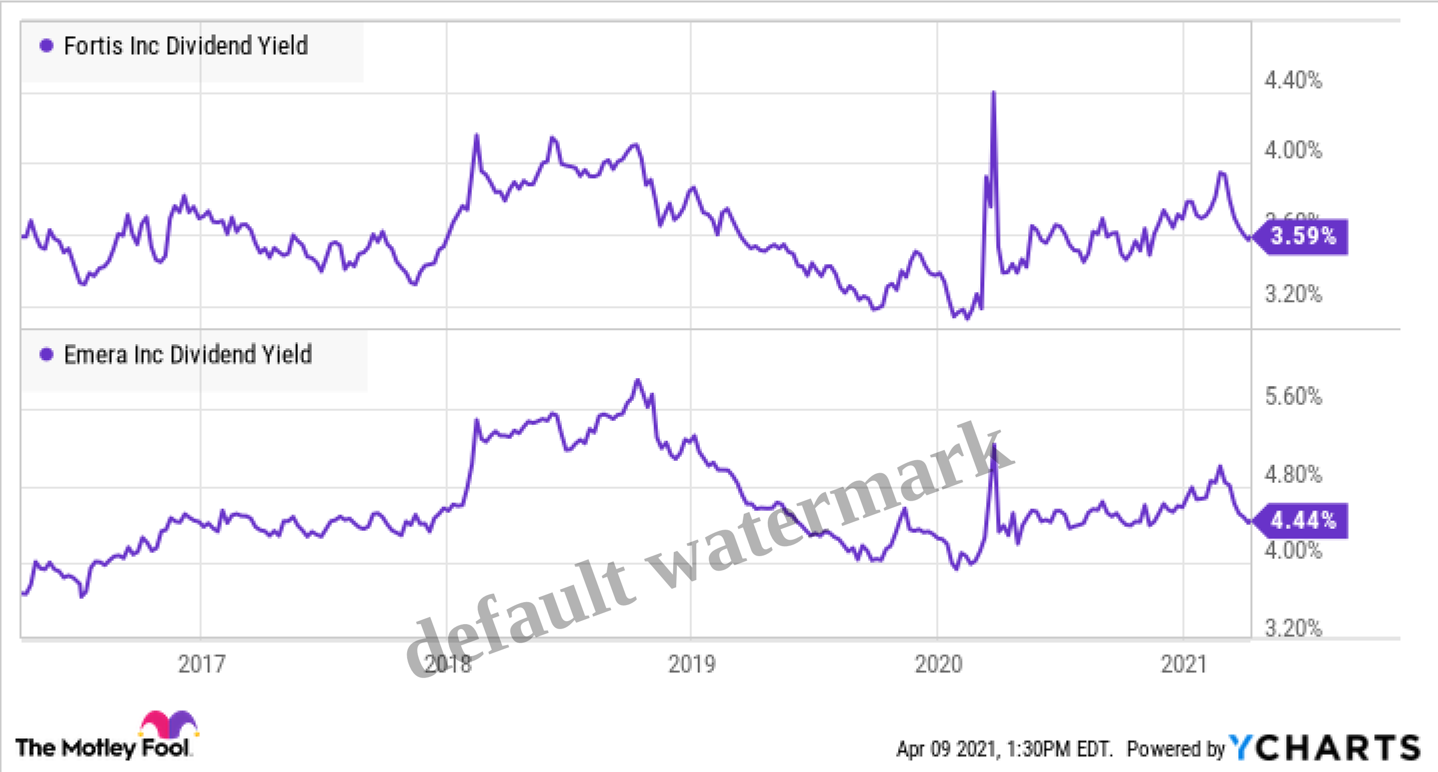
Fortis seems to provide a tad more predictability and safety. This is suggested by it commanding a slightly higher valuation and lower dividend yield on the stock market. Additionally, it maintains a safer payout ratio. That said, both companies' dividends should be sustainable.

The utility stocks dipped in February, which would have been a good time to buy some shares for conservative income investors. Both have since recovered from the dips and are trading at fair valuations.

That said, analysts believe Fortis trades at a slightly bigger discount — about 6.5% from its fair value versus Emera's 4.2%.

The Foolish takeaway

Investors primarily invest in Fortis and Emera for passive income. Since Fortis and Emera are similar regulated North American utilities whose stocks move in tandem, holding both stocks in your portfolio doesn't help much in diversifying.



Dividend Yield data by YCharts.

By the looks of their recent dividend yield histories, interested investors can buy the low-risk stocks for more attractive income and total returns at specific yields — a minimum yield of 4% for Fortis and 4.8% for Emera. They're not quite there at the moment.

That said, if you account for their expected dividend increases by October, their forward yields of 3.9% and 4.7%, respectively, would get awesomely close!

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