Buy the Dip: Enbridge (TSX:ENB)

Description

You may be wondering why I said buy the dip for a stock like **Enbridge** (TSX:ENB)(NYSE:ENB), which is enjoying a recovery rally. This is a stock to buy and hold forever at the current price and even better in a dip. No stock can continue to grow forever. It goes through dips and rallies. The current topic that is moving the entire stock market is the state of the COVID-19 pandemic.

What is the state of the pandemic?

Prime Minister Justin Trudeau has addressed concerns around the third wave of the pandemic. The question we're all grappling with is how long until this pandemic is over, as we can't live in a state of emergency forever. When the vaccine rolled out in November 2020, everyone thought, "Now this pandemic will end." But issues with the vaccine rollout and the mutation of the virus are causing shorter waves.

However, there are hopes that the vaccine will work, and the pandemic might end by 2022.

Enbridge stock in the pandemic storm

The hope of a world without the pandemic is driving Enbridge stock to recovery, and the pandemic waves are pulling it down. In the first wave, the stock fell 27% as the nationwide lockdown created a sudden dip in oil demand. Enbridge stock took a hit as it earns money from supplying oil and natural gas to major cities in North America through its widespread pipeline infrastructure.

The second wave in December 2020 pulled Enbridge stock down 6.5%. Now comes the third wave. If the government once again imposes lockdown, planes, cars, and trains won't run, and oil demand will slow again. Lockdown or the fear of lockdown would likely pull down Enbridge stock by 6%-9% to around $43.

How will you benefit from buying the dip?

A decline in stock price will increase its dividend yield from 7.23% to 7.77%. Consider you invest $1,000 in Enbridge, you bought the stock at $43 per share and Nicole at $46.22. In this case, you will earn an annual dividend of $77.7 for a lifetime, which is $5.4 more than Nicole. Assuming Enbridge does not cut dividends and retains the same dividend per share, in 10 years, you will earn $54 more than Nicole.

But that’s not the case. Enbridge has a 26-year history of increasing dividends at a compounded annual growth rate (CAGR) of 10%. I will be pessimistic and assume it increases the dividend at a CAGR of 5% in the next 10 years. In 2031, you will earn an annual dividend income of $120.5, which is $8.3 more than Nicole’s dividend income of $112.2.

You may ask, is it right to place a 10-year bet on Enbridge’s ability to increase and pay dividends?

The long-term game

The times are changing as the energy industry is making the shift to renewable energy. **Air Canada**, one of the major consumers of jet fuel (made from crude oil), is investing in sustainable aviation fuel and fuel-efficient aircraft. The government is promoting electric vehicles (EV) over gasoline cars. Although Enbridge is increasing its exposure to renewable energy of wind and solar, they still form less than 20% of its cash flow.

The shift to renewable energy and sustainable fuels that can substitute oil and natural gas and bring a material difference in their demand is slow. This shift could take 10 to 20 years to make a difference to Enbridge’s cash flows — enough time for Enbridge to increase its exposure to renewable. It has the capital and the resources and managed to pull through controversial pipeline projects. That the government is backing renewable energy projects could be the icing on the cake for Enbridge.

Given the shift to renewable, I have put a pessimistic expectation of a 5% dividend compound annual growth rate (CAGR). Enbridge stock is in a business in which even billionaire investor Warren Buffett sees value. Hence, his company **Berkshire Hathaway** invested US$8 billion last year to acquire **Dominion Energy’s** natural gas pipeline business.

Final thoughts

As Enbridge doesn’t sell oil, it is less prone to oil prices. But the weak oil volumes are troubling. As the pandemic eases, Enbridge stock could see another 10% recovery rally in the long term.

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