Why Fortis (TSX:FTS) Stock Tumbled to 18-Month Lows Last Week

### Description

Defensives like utilities are some of the investor-favourite sectors when markets turn uncertain. Their slow stock movements and stable dividends generally stand tall when broader markets fall. However, Canada's top utility **Fortis** (TSX:FTS)(NYSE:FTS) has been on a consistent decline this year. Since May, Fortis stock has dropped 18%, notably underperforming peer TSX utility stocks.



Fortis is one of the biggest utilities in Canada. It serves more than three million customers in Canada, the US, and the Caribbean. Fortis has exceptional earnings stability as almost all of its earnings come from regulated operations. As a result, FTS has increased its dividends for 49 consecutive years, the second-longest dividend growth streak in Canada.

## Why is FTS stock falling this year?

Still, FTS has been a laggard this year among utilities. That's because FTS had been trading at a premium valuation for so long. So, the steeper correction than that of peers was, in fact, justified. Moreover, higher energy commodity prices have boosted its operating expenses, denting its profit margins in the last few quarters.

Apart from these, a challenging macro environment also weighed on FTS stock this year. Interest rates and utility stocks generally move inversely to each other. As a result, as central banks have been raising rates rapidly this year, stocks like Fortis have trended lower. That's because utility stocks are considered bond proxies. When rates rise, bond yields become more attractive in comparison with utility stocks. So, investors dump utilities and take shelter in bonds in search of higher yields.

Another reason behind their inverse relationship is utilities are capital-intensive businesses and carry a high amount of debt on their books. So, as rates rise, their debt servicing costs also increase, ultimately hitting their profitability.

## Benefits of holding utility stocks

As earlier stated, utilities are perceived as safe-havens because of their regularly growing dividends and less volatile stocks. Fortis is one of the investor-favourite defensive names among utilities. Its dividend currently yields 4.3%, higher than peers. Note that although FTS recently raised its dividends by 6%, the premium yield is mainly due to the steep price correction.

They often distribute a higher percentage of their net income as dividends among shareholders. Fortis had an average payout ratio of 50% in the last five years. Utilities at large dish out around 60%-70%.

In the last 12 months, FTS stock has returned 3%. Taking a longer view, the stock has climbed 41% in the last five years, including dividends. Once again, it has reached favourable valuation levels. It is trading 22 times its earnings, in line with TSX utility peers. So, investors can expect a limited downside from the current levels. Plus, as markets continue to look uncertain, safer stocks like Fortis could gain the limelight.

## The Foolish takeaway

What matters more in these markets is its earnings and dividend stability. As growth stocks could see larger drawdowns in bear markets, stocks like FTS will likely be relatively stable. So, Fortis' weakness could be an opportunity to lock in its current juicy dividend yield. You may not be rich overnight with Fortis, but it will create a decent reserve in the long term.



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