Should You Buy Algonquin Stock Now or Wait?

Description

Algonquin Power and Utilities (TSX:AQN) stock has been absolutely battered in 2022. It is incredibly unusual for a once-considered safe utility to fall by over 40% in the span of one year. However, ever since it announced worse-than-expected third-quarter results, its stock has drastically collapsed, and now it has flat lined.

Why is Algonquin stock down so much in 2022?

The company has long endorsed a faster-than-average growth plan (at least for a utility). At its 2021 Investor Day, Algonquin promoted 7-9% annual adjusted earnings-per-share growth for the coming five years.

However, after several project delays and a higher-than-anticipated levels of floating rate debt, third-quarter earnings were consumed by rising costs. Algonquin was forced to lower its 2022 guidance and noted that it may amend its longer-term growth forecast.

This has left current and prospective investors wondering what to do. Here are some points that are both for and against buying the stock. Ultimately, the decision to buy, sell, or hold will have to be based on your level of risk tolerance, patience, and contrarianism.

Why Algonquin stock could be interesting

For investors willing to take on some serious risk, Algonquin stock could be interesting. Firstly, it is very cheap today. It trades for around 10 times earnings, where many utilities are trading with mid-teens earnings multiples. It has a portfolio of very good assets and has a good long-term history of market-leading returns.

Secondly, its dividend yield of 9.9% could seem very attractive. Now, I say this with a high level of skepticism. Other than the March 2020 market crash, I have almost never seen a stock sustain a dividend yield over 8% for a long period.

The market is pricing a dividend cut and often the market is right on these things. If you buy this stock, it should be as a contrarian value play, not as an income investment. Right now, the company is not sustaining the dividend by earnings or cash flow, so its dividend payout is very speculative.

Now, keep in mind, Algonquin management just bought over $1 million of stock. Insider buying is often a bullish signal, indicating that management may not be as concerned, as the market appears to be. However, there are still more reasons to be cautious.

Why you should wait

If the current debt/operating issues persist (and earnings further decline), Algonquin may have to take drastic measures to shore up its balance sheet. This could include selling off prime assets, refinancing debt, issuing more equity (at a very inopportune time/low price), or reducing its dividend.

Algonquin already has a lot of debt (net debt to earnings before interest, taxes, depreciation, and amortization of 8.5 times). It will have to take on more floating rate debt to finance the Kentucky Power acquisition. This could further hamper earnings and may even lead to a credit re-rating, which would further increase its cost to borrow.

Overall, the balance sheet risks make the stock very speculative. Macro-economic issues are only expected to get worse next year, so that is also weighing on the stock.

Play it safe and stay on the sidelines

While this is a worst-case scenario, it is one reason the market is so skittish on Algonquin stock. Given the risks, there are just too many factors that could go wrong for its business today. As a result, it is not the safest bet, especially if you are buying it for dividend income.

Algonquin will be having an Investor Day in the next few months. This may provide some better insight into Algonquin's plan going forward. I would wait until then before making a further decision to buy or hold on.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:AQN (Algonquin Power & Utilities Corp.)

PARTNER-FEEDS

1. Business Insider
2. Flipboard
3. Koyfin
4. Msn
5. Newscred
6. Quote Media
7. Sharewise
8. Smart News
9. Yahoo CA

PP NOTIFY USER

1. kduncombe
2. robbybrown

Category

1. Dividend Stocks
2. Investing

Date
2025/07/17
Date Created
2022/12/05
Author
robbybrown