Should You Buy Emera Stock in February 2023?

Description

Investors dislike utilities because of their slow-moving stocks and boring business models. However, when it comes to risk vs. reward, utilities offer an attractive proposition. For example, consider Canada's second-largest utility stock, **Emera** (TSX:EMA).

It has returned 9% compounded annually in the last 10 years, including dividends. Although that falls way short of the return of some high-growth tech stocks, it still comfortably beats the **TSX Composite Index**. Moreover, very few stocks and sectors provide decent returns with reasonable stability.

Emera and its financial growth

Emera caters to 2.5 million customers in the U.S., Canada, and the Caribbean. Electric services contribute 84% of its revenues, while the rest comes from gas services.

Emera generates 95% of its earnings from regulated operations, which enables visibility and stability. In the last 10 years, its per-share earnings have grown by 3%, compounded annually.

That's lower than the broader market average, but what matters more for utilities is stability. They don't try to do extravagant things where their capital goes for a toss. However, they keep investing money in their rate bases where they can generate a stable rate of return in the long term. Due to such slow-but-stable growth, utility stocks like EMA outperform in bear markets and underperform in rallying markets.

Emera aims to invest $8.5 billion in capital projects, which is expected to grow its rate base by 7.5% annually through 2025. That's a pretty decent rate base growth rate, enough to finance Emera's guided annual 5% dividend growth. The rate base is the value of the property where a utility operates and generates a regulated rate of return.

Emera dividend profile

Dividend stability is key for a utility and its investors. Emera has a handsome dividend profile and has increased its payouts for the last 16 consecutive years. In 2023, it is expected to pay a dividend of $2.76 per share, implying a yield of over 5%. TSX utility stocks offer an average yield of 4%.

Utilities give away a large portion of their profits to shareholders as dividends. Emera had a payout ratio of 62% in the last 12 months. Such a high payout ratio is quite common among utilities. In comparison, the broader market average payout ratio is around 20-30%. In the last five years, Emera's average payout ratio has been around 61%.

Utility stocks turn lower in rising-rate environments. As a result, EMA lost more than 20% of its value in September last year. When rates increase, bonds become more attractive compared to utility stocks. So, investors move to bonds by dumping utilities.

Conclusion

As rate hikes are expected to slow down or pause this year, utility stocks could once again move higher. EMA stock has shown some recovery, gaining almost 10% since its bottom in late October.

Note that utility stocks like Emera might not be suitable for all kinds of investors. If you are an aggressive investor and have a higher risk appetite, slow-moving utilities might not do justice to your capital. But if you are someone looking for stability and regular passive income, utilities like Emera are quite fitting for your portfolio.

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