Buy This 1 Cheap Dividend Stock in December That Yields 7.80%

Description

Right now is not the best time in the world to be a phenomenal pipeline company. It's a tough operating environment, and these types of companies are unloved by investors, regulators, and the general public because of the negative headlines that make pipelines equate to undesirable climate change in people's minds.

So, what should smart investors do when an investment opportunity of a lifetime in a pipeline stock comes along? My view is they should take full advantage and load up on the stock because the dust will settle on the pipeline debate soon enough, and the industry will thrive once again.

Inter Pipeline (TSX:IPL) is one of the best pipeline stocks that has just found itself on the wrong side of the stock trade, and the stock price has suffered terribly, going from $35 per share in its heyday in 2015 to a modest $21.91 per share at the time of writing.

The company, in very simple terms, transports, processes, and stores energy, operating out of western Canada and Europe. The company's pipeline systems span an impressive 7,800 kilometres, and it transports an enviable 1.4 million barrels per day.

Even as the stock price has tumbled over the last few years, the funds from operations (FFO) has kept increasing from approximately $700 million in 2015 to $1,100 million in 2018. What is even more interesting and heartening as an investor is that the dividends have increased in tandem with the FFO and have gone from $1.49 per share in 2015 to $1.71 per share in 2018.

All of this points to a healthy company that is chugging along, despite headwinds in the form of investors who feel that the company's strategy is higher risk, especially with its foray into new products with its multi-billion-dollar investment in the Heartland Petrochemical Complex.

Healthy dividend growth

As I mentioned, Inter Pipeline has never had a problem with its cash flow generation and continues to grow it, which means that it can also continue to maintain and indeed grow its dividend.

The company's dividend strategy seems to be simple in that it grows its dividends in line with cash flows to ensure dividends are highly sustainable. FFO per share has gone from $2.19 in 2015 to $2.80 per share at the end of 2018. In line with that, the company predictably raised its dividend from $1.49 to $1.69 per share.

Actually, the only reason the company hasn't increased its dividend more is that it has an aggressive capital-spending plan that is designed to create significant value for shareholders, and the company has held on to a good chunk of the cash flow it has generated the last couple of years to partially fund that growth.

At a current stock price of $21.91, the dividend yield is a tantalizing 7.80%, which is an extremely high yield but also extremely stable and secure.

Heartland petrochemical complex

The Heartland project is the company's biggest and most complex undertaking to date, and while it may feel like a high-risk move to investors, it is a master stroke because the company will be able to produce polypropylene, which is a product used in the manufacture of consumer packaging, automobile parts, medical equipment, currency, and textiles.

In other words, this will diversify the company's customer base as well as reduce its reliance on strictly conventional oil and gas energy for its cash flow. The company estimates that once this project is up and running, it will add up to $500 million in EBITDA to Inter Pipeline's earnings every single year.

Investor takeaway

Almost 85% of the company's earnings are stable and predictable due to the long-term nature of its contracts and 97% of the company's earnings are linked to investment grade and very stable counterparties, further reducing the company's risk profile.

At the time of writing, the company had a stock price of $21.91, which is very close to its five-year low. As Heartland comes into production in 2021, I strongly believe that investors will re-rate this stock much higher, because the perceived project execution risk has been mitigated.

In the meantime, investors who get into the stock now will be laughing all the way to the bank with that 7.80% yield into 2020 and beyond.

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