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Putting Canada's Renewable Energy Industry on the Map

Steve Snyder, President & CEO

Good morning. Thank you for the introduction and the opportunity to join you today. I also want to thank the EuroMoney Energy Events for organizing this forum. It certainly says something about the potential of the renewable energy business and the strength of the Canadian capital markets that we can host such a conference in Toronto.

I'd like to use the time I have for formal remarks to share with you a little about TransAlta, how renewables fits into our business strategy and investment plans, and how the role of development and M&A plays into our plans to expand our renewable business across Canada.

What is TransAlta - we're Canada's #1 renewable energy company

As many people in this room know, TransAlta is Canada's largest wholesale generator and marketer of electricity. We are headquartered in Calgary and have approximately 50 per cent of our installed generation located in the province. The other 50 per cent of the portfolio is located primarily in eastern Canada and Washington State.

And while we got our start building and operating run of river hydro facilities more than 100 years ago, many are surprised to hear we are Canada's #1 publicly held provider of renewable energy.

Including the two wind farms and one hydro facility we have under construction, TransAlta's renewable portfolio today includes over 2000 megawatts:

- Over 1000 MW of wind;
- Over 900 MW of hydro; and
- 164 MW of geothermal.

Including our current projects, over the last decade we've invested close to $3 billion in renewable energy infrastructure through a combination of acquisitions and greenfield development:

- In 2002 we made our first acquisition of renewables when we bought a company called Vision Quest. Vision Quest was a first mover in the whole wind energy movement. They had a super development and construction team as well as an inventory of Class A development sites. We've been capitalizing on this first mover competitive advantage ever since;
- In 2003, we completed purchasing a 50 per cent interest

in California Energy Generation Company from El Paso Energy Corp. Through this acquisition we acquired a net interest of 164 MW of geothermal generation and access to over 1,000 MW of geothermal reserves in the Salton Sea Basin. Our partner in this venture is MidAmerican Energy;

- We've also developed and constructed four new wind facilities in the last number of years – totaling over 300 MW; and

- Last year, we completed the acquisition of Canadian Hydro Developers for $1.7 billion, including the assumption of debt. The acquisition accelerated the expansion of our renewables portfolio, added immediate financial value for our shareholders and positioned TransAlta as Canada's fastest growing renewable energy company.

From our perspective, we think the most successful companies are those able to develop their own projects as well as take advantage of market timing to buy assets at a good price. Being able to flex between building and buying assets gives TransAlta more ability to grow our business consistently over time and maintain our balance sheet strength.

Having a strong development team and pipeline of growth projects allows us to harness the best sites and control the timing of growth investments. Maintaining a strong balance sheet and having acquisition capabilities lets us take advantage of the M&A cycle and buy assets that may not be fully valued or where synergies can be captured. It also removes development risk.

From TransAlta's perspective, what we're looking for in acquisition prospects are proven assets in our existing core markets of western Canada and western U.S.
We will also look across Canada to continue to expand our renewable portfolio. And, with any acquisition we make, we ensure there is a strategic fit with our low to moderate risk profile through long-term contracts on the assets or the capability to contract them. We try to avoid assets with too much "hair" on them or investments outside our strategic focus or proven technologies.

Our strategy and how renewables fit it

For the past decade investment in renewable energy has become a strategic priority for TransAlta.

As everyone in this room knows all too well these days, wholesale electricity is a commodity business subject to market cycles. Given TransAlta is a non-regulated company we have purposely built our company to deliver sustainable shareholder value through market cycles. We maintain a strong balance sheet and investment grade credit ratios and make certain we have ample liquidity available to us. We have diversified our fleet by fuel type and technology. This reduces our commodity risk while increasing our development potential. But it's not an easy task in our industry. And we are the leading provider of GreenEnergy throughout Alberta and a growing provider of offsets and renewable energy credits throughout the western region of the U.S. and Canada.

In our core markets, natural gas sets the marginal price most of the time. This, as you can imagine – given what's happened with gas prices over the past decade -- has led to electricity price volatility. To provide for more stable and predictable cash flow and earnings, we have a highly contracted business with approximately 70 per cent of the portfolio contracted through long-term contracts and the Alberta PPAs. The balance of our portfolio is contracted through a four-year ladder hedge program which combines a mix of medium and short term contracts which gives us leverage to the upside and protection to the extremes of downside exposure.

For decades, environmental leadership and a commitment to sustainability has been a core value and we've been recognized for it by organizations like the Dow Jones Sustainability Index, the FTSE4 Good Index and the Jantzi Social Index.

A little more than 10 years ago we saw the potential for new regulations that would require even stricter control over atmospheric emissions such as mercury, NOx, SO2, and CO2. We were early movers in testing and investing in control technologies such as SO2 scrubbers and low NOx burners at our Centralia coal plant and mercury capture technology at our Alberta coal plants. Today, with our government and industry partners we are piloting the world's first large scale integrated carbon capture and storage project at our Keephills 3 coal facility in Alberta.

This is truly an exciting and break through project and, in perhaps typical Canadian fash is far more recognized internationally than in our own backyard. It plays to Canada's and Alberta's strengths and competitive advantages. And it allows Canada to be a world leader in developing the technologies needed to retrofit the world's thermal power plants. Without it, I simply can't make the math work to achieve the world's goals for CO2 emissions reductions.

Another key part of our environmental management strategy was investing in renewable energy such as wind in Alberta. Today, our investment in renewables is more than an environmental management strategy, it has become the primary focus of our growth strategy as we invest hundreds of millions of dollars to green our portfolio, serve customers' growing desire for lower carbon electricity, and reduce our climate change risk.

Renewables are a good business; not just a good deed. From a purely capitalist perspective - we like renewables because we make good money from them. We target to earn approximately a 10 per cent unlevered, after tax internal rate of return on each of our investments. Years ago this meant we didn't win a lot of "calls for energy" because we weren't willing to cut our margins or hype our capacity factors. Patience and our reputation for building reliable wind farms paid off and now we're developing projects across the country. And from a cash flow cycle time, the payback from our wind farms is pretty quick when you consider it takes us eight to 10 months from the time the shovel hits the ground to when the farm is operational and we start earning a return on our investment.

Accelerating our renewable growth with Canadian Hydro Developers

So with a development pipeline as strong as the one we have – what appealed to us about Canadian Hydro Developers? The key strategic drivers behind the deal were:

- The acquisition accelerated our renewables growth strategy, increasing renewables as a percentage of our total portfolio from 15 per cent to 22 per cent and adding new projects at various stages to our development pipeline;
- It met our financial return requirements; and
- It was consistent with our low to moderate risk profile.

What does that mean? It means Canadian Hydro had a unique set of 100 per cent renewable generation assets. But more than just being renewable, these assets provided us with further geographic diversity while still being located in markets we know well. They were highly contracted with credit worthy counterparties – which added a year to the overall contractedness of our portfolio. With very little overlap in our operations and a team of operators and experts at Canadian Hydro we wanted to keep, we saw very little integration risk.

And with the strong support of our banks, shareholders and debt capital markets, we knew we could finance the acquisition. In round numbers, we assumed some Canadian Hydro debt, raised a further $900 million of debt and $400 of equity to come up with the approximately $ 1.7 billion enterprise value for Canadian Hydro.

From a deal financing perspective, TransAlta approached the equity market first in order to underpin the transaction and get rating confirmations. The market priced the shares at a discount inside 3 per cent and a strong book built allowing the greenshoe to get exercised by the underwriters and raising about $ 400 million.

After the share offering, the credit agencies quickly affirmed debt ratings (BBB stable).

TransAlta then approached the US bond market with a benchmark issue in the 5-year maturity and drove hard on spread. The market responded strongly and we printed a 4.75 per cent coupon on a very tight spread. We then used that benchmark to anchor a Canadian 10-year issue and raised a further $400 million in Canada.

Overall TransAlta was able to fund the acquisition with equity of only 25 per cent of the total value because we had the strength in our balance sheet to remain within our overall targeted range of leverage and coverage at the corporate level. While our credit metrics move to the higher end of our targeted range post acquisition we expect to return to middle ground within a year of the acquisition.

The acquisition was good for TransAlta shareholders and it was good for Canadian Hydro shareholders too. At the end of what turned out to be a competitive process, they walked away with $5.25 per share of cash in their pockets at a time when most investors and analysts were questioning the timing and strength of a market recovery.

Greening our growth is a priority for TransAlta

As TransAlta looks ahead we certainly see a lot more investment in renewable energy. After sustaining our operations and paying dividends to our shareholders, we have between $300 - $400 million a year of free cash flow. At this time, the best place we can see to deploy this cash and create long-term value for our shareholders is by investing in proven renewable energy projects. There is too much uncertainty around climate change regulation that I'm not comfortable putting money into a new coal fired generation plant – at least not until we know more about the scalability of carbon capture which will probably take a decade. Natural gas plants will continue to play a role in our industry, but unless you can get a long-term natural gas agreement – which generally you can't -- these plants are difficult to justify. I've been in this industry long enough to have seen natural gas at $2.50 and $14 per MMBtu. And while the recovery rates from shale gas are very promising the truth is we don't have enough data to know how reliable the reserves will be.

From a corporate valuation perspective it also makes sense for TransAlta to invest more in renewables. On an enterprise value to EBITDA basis, looking at 2011 expectations Canadian-listed renewable companies trade at a 10 – 10.5 times multiple compared to TransAlta and other traditional corporations which are trading around 7 - 7.5 times. We're starting to see a little more appreciation from investors of the low carbon growth of our EBITDA. Based on our existing portfolio and construction projects - renewables are expected to account for approximately 30 per cent of EBITDA by 2012. If you include EBITDA from our natural gas assets, low carbon fuels are expected to account for over 50 per cent of our EBITDA by 2012…and we expect to growth this further.

More specifically, our near-term plans are to invest in wind in Canada. The Canadian federal government did a great job kick-starting the wind industry by providing the $1.4 billion ecoEnergy Renewable Power Program. That was a one-time fund that is now fully committed. But, the increase in the accelerated capital cost allowance presented in the federal budget earlier this month which allows for a 50 per cent tax depreciation on a declining basis provides further industry support. In addition, provinces are beginning to compete for capital investment in renewable power. Examples include Renewable Portfolio Standards (RPSs) in New Brunswick and Saskatchewan, specific clean power calls in British Columbia and the new Green Energy Act/Feed-in-Tariff (FIT) program in Ontario.

TransAlta has construction projects underway in Alberta, B.C. and New Brunswick and other projects in late stage development in Saskatchewan and Quebec.

Beyond wind, we would like to expand our geothermal facilities in Southern California to help meet the state's 30 per cent RPS standards. We also see the potential for investments in our Alberta hydro fleet longer-term. So we've got a full development pipeline and the people with the capabilities to execute.

We're also looking at acquisition opportunities in our core markets – and no I won't tell you what they are. But certainly stay tuned because I think the future of renewable energy finance is only just starting to grow in Canada.

I thank you for your time and attention. I welcome your questions.