Letter to Shareholders

Clean Energy Investment Plan

On September 16, 2019, we held an investor day in Toronto where our team announced TransAlta's *Clean Energy Investment Plan*. We laid out a blueprint for achieving our vision of becoming a leader in clean electricity — committed to a sustainable future. Our plan includes a commitment to invest between $1.8 billion to $2.0 billion in growth and reinvestment from here to the end of 2023 and, more importantly, our plan is funded and in execution. And in 2019, we delivered strong performance, beating our expectations.

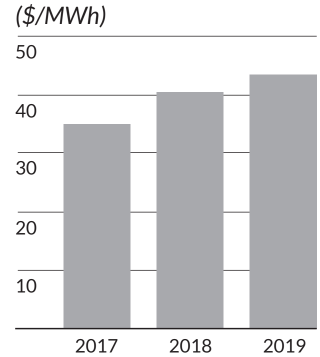
> **"We have a clear and simple plan that we advanced exceptionally well in 2019."**

Today, we are on firm ground financially with a strategy that fits inside the overall energy decarbonization that we are witnessing globally. As countries move to set more stringent greenhouse gas regulations and commitments, and as consumers demand sustainability, we are positioned as a leader in renewable and clean natural gas generation. We believe that over the next ten years, electrification using clean natural gas, wind, water, solar and batteries will provide the opportunity to lower the carbon intensity of almost every good that is produced by our customers. We are experts in the forms of generation our customers demand and we can build them a plant or sell them a contract — in Alberta, across Canada, the US and Australia.

We have a clear and simple plan that we advanced exceptionally well in 2019. I am going to take you through some of the behind-the-scenes work that occurred throughout 2019 so that you can see why now, more than ever, is the time to invest in TransAlta.

Navigating 2019

Gross Margin
($/MWh)



One of our most important initiatives in 2019 was raising the cash we needed to make final decisions on converting our coal plants to gas. Having the Pioneer Pipeline commissioned early allowed us to significantly increase co-firing of our Alberta thermal units and accelerate our conversion plans. Plus, the forecast for $50/tonne carbon pricing by 2022 meant that every year that we stayed on coal was the potential for higher future carbon costs and much lower margins. If we stood still, our carbon bill would eventually climb to $405 million — an amount greater than our free cash flow! We had the pieces lined up to finalize our decisions, but we needed additional capital if we wanted to accelerate implementation and get ahead of the curve.

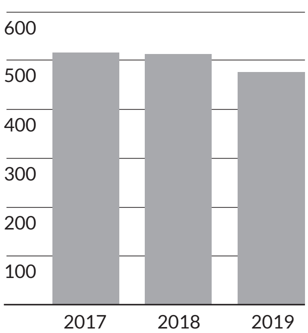
Raising capital at competitive rates in the markets was difficult. We felt our stock price was undervalued because investors were not yet convinced that we'd be able to move off coal and use gas — even with the Pioneer Pipeline in place — and early in 2019 they still didn't attribute enough value to our anticipated, higher future cash flows from our hydro assets once the PPA ended. We were also determined to repay our 2020 bonds and not raise additional corporate level debt. Our goal had been to finish 2020 with $1.2 billion in senior level corporate debt at the TransAlta level. We were determined to find an innovative way to raise cash that didn't result in a long-term debt burden.

We also engaged extensively with our larger shareholders in 2018 and Q1 2019, including Brookfield, and these discussions helped catalyze our desire to find a way to translate TransAlta's long-term potential into nearer-term value, accelerate our coal-to-gas strategy, return capital to shareholders, and crystalize the future, higher value of the hydro assets.

> **"We are rapidly building a natural gas-fired fleet that allows us to become Canada's leading clean electricity company."**

We had been engaged in discussions with the Brookfield team for several years — including in both 2015 and 2017 concerning potential transactions — and trusted their integrity and business judgement. We saw them as the right strategic partner to construct an innovative deal that could bring all the pieces together. On March 25, we announced our strategic partnership and closed the transaction on May 1, after our annual general meeting, so that our shareholders could elect to ratify our approach through their support for the Board. The deal was financed against a percentage of our hydro assets at a 13 times future EBITDA[(1)] value — which crystallized the anticipated enhanced future value of our hydro assets. Further, we intentionally designed the debt to be convertible only after we had the anticipated higher cash flows from the hydro assets after they rolled off the PPA in 2020. We also used the opportunity to bring Brookfield in as a cornerstone partner, which meant that they would increase their equity ownership and offer us two very experienced and outstanding corporate directors. And we designed a performance incentive element. If our stock is trading over $17 by 2025, Brookfield can buy up to 49% of the hydro assets. This gives Brookfield the incentive to see all elements of our strategy advancing, including coal to gas — but also ensures we always retain a majority interest in the hydro assets.

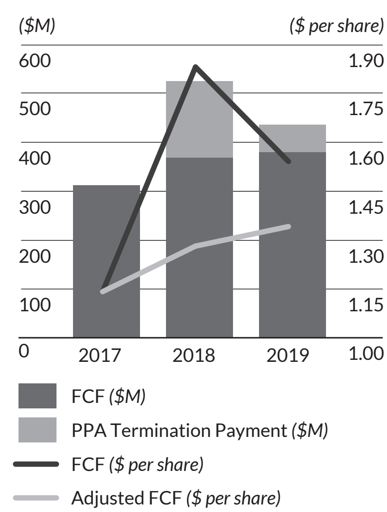
Operating Maintenance and Administration *($M)*



Having the cash early and an accelerated path off coal has proved to be the right decision. When the new Alberta government confirmed a carbon levy of $30 per tonne starting in 2020 for large emitters, our strategy was solidified. We believe that carbon pricing for large emitters in Canada is here to stay under all governments. We also believe that the odds are that over time, carbon will be priced more aggressively.

That is the back story to the decisions we made in 2019 that were presented at the September investor day conference. As of today, we will convert Sundance Unit 6 to gas by the end of 2020 and Keephills Units 2 and 3 in 2021. And we are also developing a re-powered combined cycle plant at Sundance Unit 5. As you can see, we are rapidly building a natural gas-fired fleet that allows us to become Canada's leading clean electricity company.

Free Cash Flow



As we approached the end of the year, 2019 was coming together better than we expected from a free cash flow ("FCF") perspective. FCF is our key metric as it's the cash that is left after we pay all the bills and reinvest in sustaining capital. It's the cash that can pay down the principal on our debt, be returned to shareholders or be used for reinvestment. We also announced our updated dividend policy in September where we, in a highly disciplined way, tied future dividend increases to our deconsolidated funds from operations.

(1) $10 million is deducted for capital expenditures.

An Outstanding Year for Business Performance

I am proud to say that the team at TransAlta delivered $379 million of Adjusted FCF, or $1.34 per share, representing almost a five per cent increase compared to 2018 and an 18 per cent increase to 2017 levels on a per share basis, excluding the additional $56 million of FCF that our legal team brought home through our successful arbitration against the Balancing Pool — an amount that few thought we could recover. All told, we delivered a total of $435 million of FCF or $1.54 per share.

> **"All told, we delivered a total of $435 million of FCF or $1.54 per share."**

Why did our year end so well when just a year before we had been concerned enough to guide the market to a potential downside of $270 million? Three reasons. First, our traders used their asset positions in transmission and their knowledge of real-time and day-ahead markets to take advantage of the volatility that now exists because of the high level of renewables in the system. They simply woke up every day and moved power to where it was needed — earning us an extra $50 million in cash that we had not anticipated. Second, commissioning the Pioneer Pipeline four months early allowed us to take advantage of low-priced summer gas in Alberta and blend gas into our boilers, significantly reducing our carbon emissions and costs. Finally, we were able to lower our costs at Sundance with the restructuring of our fleet and the 2018 mothball decisions. All told, we are proud of the cash flow performance coming out of the Canadian thermal fleet.

It is important to note that, while exceeding our original FCF expectations, we also operated without any injuries in our Wind, Hydro and Australia operations, and delivered a Total Injury Frequency ("TIF") across the entire fleet of only 1.12, an outstanding result compared to our TIF of 1.91 in 2018. Availability was also strong across our facilities, achieving 90 per cent availability fleet-wide.

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Finally, 2019 is the culmination of the great work that our team has done to contain costs and build efficiencies through our Greenlight project.

Continuing to Grow Our Renewables Business

Another key priority of ours that we announced in 2019 was to execute over $800 million of renewables and on-site construction projects. Both Antrim and Big Level, our new US wind projects, reached commercial operations in December 2019 and have commenced generating cash flow for 2020.

Project execution for Windrise, our wind project located in Alberta, commenced and we were excited to receive Alberta Utilities Commission ("AUC") approval ahead of schedule, providing further opportunities to optimize construction costs and integration. Windrise is targeting COD in 2021. Skookumchuck, a wind project in Washington State that we are pursuing, is progressing and we expect it to reach commercial operations by the end of June 2020.

We also have an extensive history of on-site generation that extends back to the early 1990s. Our experience and our team make us a strong partner in this segment. Building on this, we executed an agreement with SemCAMS Midstream to construct and operate a new cogeneration facility. Detailed construction activities have commenced and COD is targeted for 2021 as well.

Importantly, we received AUC approval for our WindCharger battery storage project, an innovative 10 MW/20 MWh energy storage project using lithium-ion batteries. The project, the first of its kind in Alberta, will store energy produced by our nearby Summerview II wind farm and discharge electricity onto the Alberta grid at times of high-peak demand — this is innovation in action.

We also have a team focused on building a pipeline of renewables and co-generation projects in the US. Demand for new wind in the US is expected to grow approximately 10 GW per year in the near term. As part of our plan, we acquired a portfolio from a US developer that now puts our own development pipeline at over 2,000 MW.

Strong Financial Position & Capital Allocation

A strong balance sheet underpins our plan and we have built off-ramps in the event that conditions change. Overall, we have tethered the investment strategy to maintaining a strong balance sheet and a dividend policy that allows investors to benefit as we move through our execution.

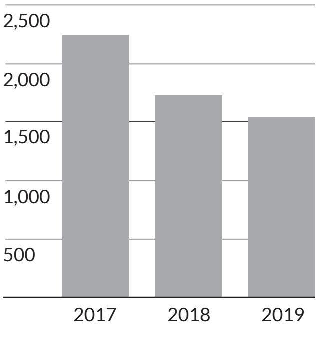
Above, I outlined the strategic reason to partner with Brookfield. The first-tranche proceeds of $350 million were received in May 2019 and allowed us to advance our coal-to-gas conversion strategy and return capital to shareholders. By the fourth quarter of 2020, we will receive the next tranche of the Brookfield proceeds to support our next phase of coal-to-gas conversions. This tremendous plan also allows us to achieve our goal of $1.2 billion of senior unsecured debt by the end of 2020.

The Brookfield investment has enabled us to accelerate our share buyback program allowing us to return capital more quickly to our equity shareholders. During the year, we returned $68 million of capital to shareholders through the NCIB program. We are making this investment as we believe that one of the best investments we can make is in our own strategy. We also raised our common dividend by a cent a share annually to reflect that we are now confident and ready to restore the idea of a growing dividend over time.

Our dividend policy is now also presented in our annual report, allowing investors to understand how the dividends received from our ownership of TransAlta Renewables are either being returned or reinvested for TransAlta shareholders.

We are confident that the above program balances the demands associated with reinvestment, new growth, debt repayments and, not the least of which, providing shareholders a return on and of their capital.

Net Recourse Debt, Exc. US Tax Equity Financing *($M)*



Continued Focus on Environmental, Social and Governance

The significance of environmental, social and governance ("ESG") has increased exponentially over the past few years, being driven in large part by investors that are spending more time understanding the sustainability of future cash flows. TransAlta has a long history of adopting leading sustainability practices, including 25 years of ESG reporting and voluntarily integrating sustainability reporting into our annual report since 2015. Three decades ago, in 1990, we were the first Canadian company to purchase carbon offsets, and in 2000 we were an early adopter of wind technology — and we are now one of the largest wind generators in Canada.

TransAlta continues to drive industry-leading ESG practices and I'm proud of the ambition represented in our 2020 ESG goals, including:

- minimizing environmental incidents and undertaking significant reclamation work;
- by 2030, achieving a 95 per cent reduction of SO_2 emissions and a 50 per cent reduction of NO_X emissions over 2005 levels from TransAlta's coal facilities;
- supporting equal access to all levels of education for youth and Indigenous peoples; and
- adopting a target of 50 per cent female membership on the Board by 2030 and achieving gender diversity of at least 40 per cent female employment by 2030.

"TransAlta continues to drive industry-leading ESG practices and I'm proud of the ambition represented in our 2020 ESG goals."

We are focused on ESG because it matters — and it makes good business sense. We will continue to lead the way as we have for 30 years.

Organizational Health

When we started our transformation journey in 2016, we focused on improving the organizational health of the Company. Organizational health for TransAlta is defined as "how we get work done together." It is not about morale and it is not narrowly defined as employee engagement. It's broadly about getting all our people in the boat rowing together. For TransAlta, it's also about nurturing innovation in every corner of the Company. We measure our performance on health against other organizations and use an external service provider to tabulate and analyze our results. In 2019, we made a significant jump in our health scores. We are now top decile across our Company in *front line innovation* — one of the key measures we wanted to improve. Watching our award winners at our President's Awards in early January talk about all the innovation we are undertaking across the fleet was a highlight for me. To improve our health while we are going through so much change was a testament to the unrelenting determination of our people to keep TransAlta competitive.

Changes in the Alberta Market

In 2019 we had a change in government in Alberta. The new government decided to stay with the existing energy-only market rather than move to a capacity market. Under a capacity market, we would have stuck more closely to converting our boilers to gas. Under an energy-only market, generating more output is more valuable, so having low-cost, efficient units as part of our fleet would increase returns to shareholders over time. In November, we strengthened this strategy by purchasing the gas turbines and related equipment from Kineticor. Overall, our portfolio and position in Alberta allow us to pivot and create value for shareholders. We know the energy-only market and have 20 years of experience in it as we move off the PPAs at the end of 2020.

So that was 2019 — an exciting step in our journey as we accelerate off coal.

Preparing for 2021 and Beyond

> **"As the PPAs roll off post-2020, we will be ready with a diverse competitive portfolio of electricity for Alberta customers."**

TransAlta's performance in 2019 is the culmination of the work undertaken to shift our strategy, cost structure and operating models to adapt to the new market and regulatory realities. We have made some great progress, but our work is not done yet. We are still fine-tuning the business with the right cost structure and business model to ensure we are competitive as we enter a fully deregulated market in Alberta as the remaining Coal and Hydro PPAs come to their completion.

Despite this change to our merchant risk profile, our diverse Alberta portfolio provides diversification to our cash flows from our Alberta business. As the PPAs roll off post-2020, we will realize market pricing, which will provide sufficient cash for returns to investors and for reinvestment in reliable supply.

We are tracking ahead of our *Clean Energy Investment Plan*. As I highlighted at the beginning of this letter, we think TransAlta presents an excellent opportunity for an attractive investment. We have developed a sound reinvestment strategy in Alberta, which will continue to extend Alberta portfolio cash flows for a long time into the future.

I am spending my time in 2020 looking for ways to accelerate our strategy, studying new technologies for future investment, and working on policy at the provincial and federal levels. I believe that Canada is further ahead than any other OECD country on climate initiatives and it's time to stand up and be acknowledged for that. Canadians need to know our story and the story of how we can produce energy for the global energy markets more responsibly than almost anyone else. I have been working for 35 years on sustainability and I am an expert when it comes to who is acting and who is talking. We are a country of action.

To ensure I can do this work well, we appointed a COO, John Kousinioris, in the summer of 2019, to take on the day-to-day operational work and to continue driving our innovation. John, who was an excellent partner on the regulatory and policy side of our business, is a fast study on operations and, quite frankly, is an exceptional leader for our people. We also appointed Todd Stack to CFO. Todd is a 25-year TransAlta veteran who quickly earned the trust of the market and the Board. These appointments have given me and other members of the team the time to work on what's next.

Ambassador Gordon Giffin retires in April as Chair of our Board and I have to say that I will miss Gordon immensely. He has been our Chair since I started as CEO and his patience, guidance, determination and partnership got me through some bleak days. He spent countless hours helping the Board and the management team make the right strategy choices in the face of an early shut down of our coal fleet. I cannot close this letter without thanking him personally for all that he has done and how his contributions helped us achieve such an exceptional year in 2019.

On behalf of the leadership, we sincerely appreciate your support and we thank our employees for all that they do to ensure we are powering economies and communities sustainably and growing our Company along the way.

Dawn L. Farrell
President and Chief Executive Officer
March 3, 2020