Is Now The Time To Buy Transalta?

Description

Shares in **Transalta** (TSX:TA)(NYSE:TAC) have fallen almost 50% from 2010 highs of $23.65 to Friday's close of $12.82. The last three plus years haven't been pretty for the company, as it delivered an almost never-ending parade of crummy results to investors, culminating in a slashing of the quarterly dividend from 29 to 18 cents. Even after the dividend cut, the stock still yields 5.6%. Is this a company a good candidate for investors who want to collect the dividend while waiting for the price to improve?

Transalta is a diversified power generation company. While the majority of its power is generated via coal plants in Alberta, Transalta also has operations in British Columbia, eastern Canada, western United States, and Australia, operating coal, gas, and wind powered operations.

The company signs contracts with local utility companies to supply power for a set period of time, at a price that floats depending on the cost of the fuel used to generate power. This helps the company maintain margins, and ensures investors get steady returns. So what happened?

In 2013 EBITDA was down almost 20% on coal-fired plants in Canada, thanks to higher priced contracts expiring, expensive planned and unplanned maintenance, lower prices, and higher penalties. U.S. coal-based EBITDA profits decreased substantially as well, from $148 million in 2012 to just $66 million in 2013.

The company also had to deal with flooding in southern Alberta and a massive ice storm in Ontario, further cutting into margins. While increases in gas, hydro, and wind generation helped the company avoid a huge decrease in cash flow, not going backwards wasn't enough for the company to weather this crisis with the dividend intact.

Transalta has been selling off assets as well, including its share of CE Generation and spinning off a number of company-owned hydro and wind plants into **Transalta Renewables** (TSX:RNW), of which the company retains majority control. The company countered those moves by acquiring a wind farm in Wyoming and pledging to spend $178 million on a natural gas pipeline to an Australian plant.

Transalta is making the right moves. It's obvious governments don't want coal burning power plants in their backyards, so the company is slowly moving away from coal, adding gas and wind generation assets. Cutting the dividend frees up cash to pay down debt, and management is focusing on improving plant efficiency. The firm also shouldn't have to deal with the severity of unplanned outages it was forced to deal with in 2013.

As much as coal-generated power makes the environmentally conscious uncomfortable, it's not going away anytime soon. It's more efficient than gas generation, and Alberta's oil sands depend on Transalta generated power. The results of its coal plants should start to pick up at some point, but in the meantime the 72 cent yearly dividend is pretty easily covered. 2013 cash flow was $1.12 per share.

Insiders are also buying shares. CEO Dawn Farrell picked up 20,000 shares on March 3, boosting her total holdings to 66,980 shares. CFO Brent Gellner also was buying, increasing his ownership in the company by 17.8%. Insiders buying shares is usually a bullish signal since it's not often you'll see a CEO plunk down more than $250,000 of her own money without having confidence the shares are cheap.

Foolish bottom line

Coal operations for the company will be challenging in the near term, but management is doing a good job reducing its dependance on coal-fired plants. The company has increased financial flexibility because of the dividend cut, and a lot of the misfortune which plagued Transalta in 2013 was just due to bad luck. Insiders are buying, and the market is pessimistic on the company going forward. This could be an intriguing entry point.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TAC (TransAlta Corporation)
2. TSX:RNW (TransAlta Renewables)
3. TSX:TA (TransAlta Corporation)

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