



Are These 2 Power Companies Poised to Double?

Description

There are certain industries that investors tend to associate with being predictable, dependable, and almost a little bit boring. Pipelines are a terrific example. Sure, they have huge upfront costs that end up on company balance sheets as debt, but profits are dependable and operators are fairly certain that revenues will consistently rise at a rate just a little above inflation.

Traditionally, power companies have been another example of businesses with huge startup costs and dependable cash flows. Power companies could also rest easy knowing that their position in a market was usually very strong, thanks to government intervention or a lack of competition. This also paved the way for steady, if unspectacular, results.

Then, it all started to unravel.

Provinces across Canada either privatized their existing power monopolies or invited other companies in to compete alongside incumbents. More competition is always going to be a challenge for existing companies in the space. And so, investors in certain names in the sector have experienced some pretty significant meltdowns.

As the mantra goes, investors need to buy low and sell high. These two companies qualify for the first part of the equation, but are they poised to recover and head back to previous highs?

Transalta

Shares in **Transalta** ([TSX: TA](#))([NYSE: TAC](#)) have been cut by more than 60% since the highs of 2008. The company's recent history also includes a dividend cut in February, and several quarters of dismal results. Things are starting to turn around, and the company's most recent quarter was pretty solid, thanks to cold weather across North America.

The company's biggest problem is its dependence on coal-fired power plants, which make up the majority of its generating capacity, especially after it spun off its renewable assets into a separate company, **Transalta Renewables** ([TSX: RNW](#)). Transalta has also dealt with higher maintenance costs and a decrease in rates, leading to its underperformance. These extra costs should be behind

the company.

It also has to deal with political and environmental pressure. It's not a popular time to own coal-fired plants, and there is pressure being put on the government not to allow additional coal plants to get built. But, technology is quickly coming to market that can help make coal a much cleaner fuel, which should lessen these concerns.

Investors who get in now could be rewarded with nice returns. And they'll get paid a 5.3% dividend to wait.

Atlantic Power

Atlantic Power (TSX: ATP)(NYSE: AT) is a Boston-based power producer with operations throughout the United States and Canada. Most of its generating facilities run on natural gas, which is supposed to be a nice growth area in the power market because it's cheap, abundant, and burns relatively cleanly. So what's the problem?

The company is burdened with a lot of debt, declining cash flows, and results so weak that it was forced to cut its dividend in 2013. It is also dealing with contract renewals that aren't quite as lucrative as previously expected.

The company is addressing these problems. Debt repayment is a priority. The current dividend's payout ratio was only 65% of the last quarter's cash flow, and is currently yielding more than 12%. The company is currently sitting on more than a third of its market cap in cash, which should mean dividend stability, at least in the short term.

If the company can make it through this rough patch, investors will be rewarded handsomely. Atlantic's \$400 million market cap also makes it an interesting acquisition target for a large company in the sector.

Foolish bottom line

Buying beaten up companies like TransAlta and Atlantic Power seems like a risky move. But investors with the ability to look past short-term weakness could find some solid long-term gains. These two companies certainly fall into that category.

CATEGORY

1. Investing

TICKERS GLOBAL

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

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