



The Upcoming Crisis for Fortis Inc and TransAlta Corporation

Description

Allow me to begin this article with a bit of a controversial statement. Power generators aren't nearly as safe as investors think they are.

Of course, shareholders in **TransAlta Corporation** ([TSX: TA](#)) ([NYSE: TAC](#)) already know this well. Since the company's shares hit their peak of over \$37 in August 2008, things have not gone well.

First the financial crisis hit, then it was forced to spend millions doing unscheduled repairs and upgrades to its aging fleet of coal power plants. As earnings continued to dwindle, the company finally cut its quarterly dividend from 29 cents per share to 16 earlier this year. It's been a tough time to be a TransAlta shareholder.

Meanwhile, **Fortis Inc.** ([TSX: FTS](#)) has done everything right. The company has been a growth by acquisition machine, picking up two power generators in the U.S. over the last couple years. Since 2008 shares are up 24%, but once investors add in the ever-increasing dividend — 41 straight yearly increases and counting — their annual return has been in the 6-7% range, exactly what would be expected from a utility.

On the one hand we have TransAlta, which has been so beaten up that many market observers (including myself), think it's bound to recover. And on the other we have Fortis, which has been a rock solid performer for decades. The case could be made to buy either one of these companies, albeit for slightly different reasons.

So what's the problem? What's the upcoming crisis?

It's solar energy.

Yes, I know both these companies have made substantial investments in renewable energy already. Fortis generates the vast majority of its power from hydroelectric dams, while TransAlta has been investing heavily into wind turbines to help wean it off its coal dependence. Most of TransAlta's renewable assets have been transferred to a recent spinoff called **TransAlta Renewables Inc.** ([TSX: RNW](#)), which is still majority-controlled by the parent.

The risk doesn't come from other companies swooping in and installing huge tracts of solar panels, even though that's starting to happen in Ontario, which has given attractive tax incentives to do so. Current estimates are that about 1% of the province's power is generated by solar energy. It's an encouraging start, but at this point it's not worth getting excited about.

No, the risk is you and I putting solar panels on our roof.

When solar panels first came out, they were expensive, difficult to install, and no tax incentives existed for doing so. The payback period was often longer than a decade, which is just too long for the average person to wait. So for the most part, folks didn't bother.

Nowadays things are a little different. Decreasing our carbon footprint is important to many people. Solar is getting to be an accepted technology. Heck, you can even buy solar panels at **Costco**.

And most importantly, the return on investment has skyrocketed. Depending on the amount of sunlight, people who install solar panels are looking at a two- to five-year payback period with an estimated 30-year life for the system.

Suddenly that starts to look pretty attractive. People can get behind saving the environment and decreasing their power bill at the same time.

It's not quite that simple, at least without adequate battery technology. Without somewhere to store excess energy generated during the day, it must be sold back to the grid, often at a much lower price than the consumer pays. When the consumer draws back off the grid at night they're stuck paying market rates, theoretically buying back their own power.

That's a good deal for the power company, but it still doesn't address the fact that widespread adaptation of solar energy will lessen demand on the whole system. And that will ultimately cut into profits.

This isn't about to happen overnight. The numbers are tiny at this point, but there are studies that estimate home solar systems could generate 5% of Canada's electricity by 2025. It's not an immediate concern, but investors in Canada's power generators should keep an eye on this trend. It will end up being important.

CATEGORY

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Author

nelsonpsmith

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