Why TransCanada Corporation’s Biggest Risk Isn’t Keystone XL

Description

Recently, Canada and the other G7 countries made an important commitment to end fossil fuel use by 2100. This is significant because it demonstrates a larger trend—the change in the energy supply mix from fossil fuels to more renewable energy resources. In the interim, natural gas will continue to play an increasing role, and all this is bad news for companies like **TransCanada Corporation** (TSX:TRP)(NYSE:TRP), which has a $46 billion capital program largely focused on expanding oil pipelines.

Just recently, Economist Jeffrey Rubin stated that projects like Keystone XL or Energy East “aren’t worth the paper they’re printed on” due to the fact that oversupply of oil combined with lack of future demand (as renewable energy and natural gas become more dominant) will result in production declines.

The numbers seem to confirm this trend. In 2013 renewable power growth exceeded growth in new capacity for all fossil fuels combined, with 143 gigawatts of renewable power generation capacity being added compared to 141 gigawatts for fossil fuel resources. By 2035 four times more renewable capacity will be added, and oil is expected to be the slowest growing major fuel, growing only 0.8% annually and having market share decline from 32% to 28%.

With the energy mix changing rapidly, should TransCanada shareholders be worried about the relevance of the over $20 billion in oil pipelines being proposed for the next five years? Fortunately, TransCanada is investing heavily in the energy mix of the future.

TransCanada is investing heavily in liquid natural gas pipelines

While it is true that renewable energy resources will see a quadrupling of capacity by 2035, natural gas will also play an essential and growing role as the energy mix transfers to renewable energy. In fact, as oil loses energy market share, natural gas will see its global market share increase from 21% to 25%, making it the fastest-growing fossil fuel, with some estimating a 40-50% increase in global consumption by 2040.

Natural gas is 70% cheaper than oil on an energy equivalent basis, which is driving more vehicles to convert to natural gas. Liquid natural gas (LNG) will be a key component of this demand growth. LNG allows gas to be transported over long distances because it is liquefied, which allows distant sources of demand, like Asia, to be connected to supply reserves, like the large Montney and Horn River formations in Canada.

Economies like China, Japan, and South Korea rely extensively on LNG imports, and this is only expected to grow, with current LNG imports being 207 billion cubic metres per year (bcm), and demand expected to grow 216 bcm by 2025.

TransCanada is investing heavily to be a part of the growing demand for LNG by connecting natural gas reserves in western Canada to LNG facilities and export terminals that are being proposed in British Columbia. TransCanada is planning on constructing its $5 billion Prince Rupert Gas Transmission project to connect production from the Montney natural gas formation to the Pacific Northwest LNG facility, as well as its $5 billion Coastal Gaslink project at the Kitimat LNG facility, which has been approved and is awaiting construction.

TransCanada is also investing heavily in clean energy

TransCanada is Canada’s largest private sector power company, and this position alone provides the company with tremendous opportunity to not only diversify its asset base, but to capitalize on changing energy trends. Currently, one-third of the companies generating capacity comes from emissionless sources, and this is only expected to grow as the company invests more in solar, wind, hydro, and nuclear power.

Just recently, TransCanada acquired the Liskeard-1 solar facility from **Canadian Solar Inc.**, representing the eighth solar facility that TransCanada has acquired from Canadian Solar as part of a purchase agreement from 2011. With four facilities purchased in 2013, three in September 2014, and the most recent Liskeard-1 facility acquired in December 2014, TransCanada has invested $450 million in Ontario solar projects.

This is part of the $5 billion in emissionless energy capacity that TransCanada has recently invested in. These projects not only add stability and growth to earnings due to 20-year power purchase agreements with the Ontario Energy Authority, but also serve to provide an additional growth platform to capitalize on renewable energy growth.

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