TransAlta Corporation: Is the 12% Dividend Still at Risk?

Description

TransAlta Corporation (TSX:TA)(NYSE:TAC) has been on a downward slide for the better part of four years, and investors are wondering if another dividend cut is in the cards.

Up until the end of last week, I would have said yes, but now I'm not so sure.

Alberta coal plan

TransAlta found a bit of support on November 22 after the Alberta government announced its plan to accelerate the phase-out of coal generation.

Under the new schedule Alberta will eliminate the use of coal to produce electricity by 2030 and plans to boost its investment in renewable energy to replace the lost capacity.

TransAlta and its shareholders were concerned that the timeline could have been tighter than that, but the 2030 target actually fits in with the company's own plan, which was implemented under the existing federal regulations.

The stock jumped more than 10% on the news.

Capital raise

The good news from the government coincided with the announcement of a $200 million investment in **TransAlta Renewables Inc.** (TSX:RNW) by Alberta Investment Management Corporation (AIMCo) as well as a drop-down deal that is moving $540 million in assets from TransAlta to TransAlta Renewables.

The AIMCo investment plus the cash proceeds from the asset transfer will provide TransAlta with about $350 million that will be used to lower the company's debt and strengthen the balance sheet.

TransAlta completed another drop down earlier this year, which consisted of the company's Australian assets. Combined, the two transactions provide proceeds of about $575 million, which will enable

TransAlta to meet its debt-reduction targets for 2015.

Cash flow

TransAlta reported Q3 2015 EBITDA of $219 million, up $7 million compared with the same period last year. Funds from operations (FFO) for Q3 came in at $126 million, down $19 million in Q3 2014.

For the first nine months of the year, EBITDA was $677 million and FFO was $497 million. The company spent $253 million on capital expenditures during that time frame.

The company is working hard to lower debt and reduce overhead expenses. Staff cuts and other admin reductions have reduced costs by about $47 million so far in 2015.

FFO for 2015 is expected to be $725-755 million. EBITDA should come in at about $1 billion.

For 2016, the company expects EBITDA to be similar to 2015, while FFO is forecast to be $755-835 million. TransAlta plans to spend $330-350 million in capital programs next year and is providing free cash flow guidance of $250-300 million.

Dividend safety

TransAlta pays a quarterly dividend of $0.18 per share, which translates to about $50 million. In the near term the distribution is probably safe, but low power prices in Alberta are putting a squeeze on cash flow, and that could force the company to reduce the payout if rates do not improve.

Any time investors see a 12% yield they should assume it is not sustainable for the long term.

Should you buy TransAlta?

The company is still facing difficult conditions in the Alberta power market, but the uncertainty around the Alberta government’s climate plan is now out of the way. The stock looks cheap based on the value of its stake in TransAlta Renewables and the fact that it is still cash flow positive.

I wouldn’t buy TransAlta for the yield, but it might be worth taking a position based on the fact that it looks oversold at this point.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

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

Category

1. Dividend Stocks

2. Energy Stocks
3. Investing

Date
2025/07/04
Date Created
2015/11/24
Author
aswalker