



## RRSP Investors: 1 Cheap TSX Stock to Buy in September

### Description

The **TSX Index** still offers RRSP investors some deals for their self-directed portfolios. Let's take a look at **TransAlta** ([TSX:TA](#))([NYSE:TAC](#)) to see why it might be an interesting stock to buy right now.

### TransAlta

TransAlta is a power company based in Alberta. The stock had a rough run over the past decade, when high debt and falling power prices forced the company to slash the dividend a number of times. This upset investors who had relied on TransAlta for reliable payouts for years.

The stock peaked around \$37 in the summer of 2008 and then went into a seven-year slide, with the eventual bottom occurring below \$4 per share in early 2016. Management put a turnaround program in place that reduced debt and included a deal with the Alberta government that saw TransAlta receive payments to help it fast track the transition from coal-fired power production to the use of natural gas. The [off-coal agreement](#) announced in late 2016 pays TransAlta about \$37.4 million per year from 2017 to 2030.

### Rebound

TransAlta's share price has gradually increased off the 2016 low and currently trades near \$13.

This year marked the transition of the Alberta power market from power-purchase agreements (PPAs) to a merchant basis. The change should benefit TransAlta in the long run.

TransAlta reported solid [Q2 2021 results](#) and revised its outlook to the upside for the year. Comparable EBITDA is now expected to be at least \$1.1 billion. That's above the top end of the previous guidance range. Free cash flow was originally expected to be \$340 to \$440 million. The company now anticipates free cash flow of \$440 to \$515 million in 2021.

Power prices are much higher than the original 2021 forecast. Alberta spot prices for the year are now

expected to average \$80-\$100 per MWh versus previous guidance of \$58-\$68.

## Undervalued?

Fans of the stock have long maintained the [market capitalization](#) doesn't fully reflect the company's value. Even today, TransAlta has a market cap of roughly \$3.5 billion. Its ownership position of subsidiary **TransAlta Renewables** ([TSX:RNW](#)) is worth about that amount at the time of writing. Pundits argue the market is allocating very little value to the legacy assets that have not been dropped down to RNW, yet they still generate strong cash flow.

As the utility sector consolidates and alternative asset managers search for reliable cash flow, TransAlta could become a takeover target. **Brookfield Asset Management**, for example, already owns a large stake in TransAlta and could potentially move to buy the whole thing at some point.

## Dividend

With debt levels reduced and free cash flow improving, TransAlta raised the dividend by 6% for 2021. The annualized dividend of \$0.18 per share provides a yield of 1.4%.

Investors should see another decent payout increase for 2022, supported by the strong financial results this year.

## The bottom line

TransAlta has put its worst days in the rearview mirror. The balance sheet is in good shape, power prices are improving, and the stock appears undervalued when you look at the sum of the parts.

The stock isn't going to rocket higher, unless there is a takeover bid, but investors should see a continued slow move to the upside. It wouldn't be a surprise to see TransAlta get to \$20 in the next two or three years.

### CATEGORY

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