

**Capital Power**  
**Fourth Quarter 2014 Results Conference Call**  
**February 23, 2015**

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**Corporate Participants**

**Randy Mah**

Senior Manager, Investor Relations

**Brian Vaasjo**

President and CEO

**Stuart Lee**

SVP, Finance and CFO

**Conference Call Participants**

**Paul Lechem**

CIBC World Markets

**Linda Ezergailis**

TD Securities

**Andrew Kuske**

Credit Suisse

**Robert Kwan**

RBC Capital Markets

**Matthew Akman**

Scotia Capital

**OPERATOR:** Good day ladies and gentlemen and welcome to Capital Power's fourth quarter 2014 results conference call. At this time all participants are in listen-only mode. Following the presentation we will conduct a question and answer session. Instructions will be provided at that time for you to queue up for questions. I would like to remind everyone that this call is being recorded on Monday, February 23<sup>rd</sup>, 2015 at 9:00 am Mountain Standard Time. I will now turn the call over to Randy Mah, Senior Manager Investor Relations. Please go ahead.

**RANDY MAH:** Good morning and thank you for joining us today to review Capital Power's fourth quarter 2014 results, which were released earlier this morning. The financial results and the presentation slides for this conference call are posted on our website at [capitalpower.com](http://capitalpower.com). We will start the call with opening comments from Brian Vaasjo, President and CEO, and

Stuart Lee, Senior Vice President and CFO. After our opening remarks we will open up the lines to take your questions.

Before we start, I would like to remind listeners that certain statements about future events made on this conference call are forward-looking in nature and are based on certain assumptions and analysis made by the company. Actual results may differ materially from the company's expectations due to various material risks and uncertainties associated with our business. Please refer to the cautionary statement on forward-looking information on Slide 2.

In today's presentation we will be referring to various non-GAAP financial measures, as noted on Slide 3. These measures are not defined financial measures, according to GAAP, and do not have standardized meanings described by GAAP and, therefore, are unlikely to be comparable to similar measures used by other enterprises. Reconciliations of these non-GAAP financial measures can be found in the Management's Discussion and Analysis for 2014. I'll now turn the call over to Brian for his remarks, starting on Slide 4.

**BRIAN VAASJO:** Thanks, Randy, and good morning. I'll start off by reviewing our highlights for 2014. During 2014, significant progress was made on our two construction projects. The final stages of construction at the Shepard Energy Project, our joint venture with ENMAX, were completed. Shepard is currently in the commissioning phase with the start of commercial operations expected next month. For our K2 Wind project in Ontario, the project financing was completed in the first quarter of 2014 and the project commenced construction. Construction is on schedule and K2 Wind is expected to begin commercial operations in mid-2015. Our future growth plans in Alberta is focused on Genesee 4 and 5. In 2014 we executed agreements with ENMAX to develop, construct, and operate the Genesee 4 and 5 project. Last month, the project

received all major regulatory approvals to proceed with construction. I'll provide more details on the construction plans later in the call. In late 2014, we acquired Element Power and its attractive portfolio of wind and solar development sites in the United States that will provide Capital Power with a solid foundation for future growth. Finally, we announced the company's first common dividend share increase, a 7.9% increase in the annual dividend, that was effective with the third quarter payment.

Turning to Slide 5 – this slide summarizes the plant availability operating performance of our plants for the fourth quarter of 2014, compared to the same period a year ago. Overall, we had strong operating performance with an average plant availability of 94% in the fourth quarter, compared with 93% for the fourth quarter of 2013. Of note, we achieved this mark despite the 74% availability at Genesee 3, which reflected a 27-day planned outage that occurred in September and October last year.

Turning to Slide 6 – the chart on this slide shows our average plant availability over the past six years. As you can see, our track record has been strong with our plant availability consistently above 90% over the six-year period. In fact, in 2014 we achieved our highest operational performance in the past five years, with a 95% average plant availability. We have a similar operational target for 2015 of 94%. I'll now turn the call over to Stuart to review our financial performance.

**STUART LEE:** Thanks, Brian. I'll start my comments on Slide 7. In the fourth quarter, the company generated \$102 million in Funds from Operations, which was in-line with our expectations. Normalized EPS of \$0.20 in the fourth quarter was lower than expected, due to the non-cash impact of 2014 deferred tax expenses and lower wind generation at Quality Wind and Port Dover & Nanticoke. Alberta spot prices

in the fourth quarter were weak; averaging \$30/MWh compared to \$49/MWh in the fourth quarter of 2014. However, despite this 39% price decline our trading desk captured realized price of \$58/MWh, which was 93% higher than the spot prices. Our realized price was 31% above spot in Q4 2013.

Slide 8 presents our Alberta power market trading performance over time. You can see that over the past five years our trading desk has captured an average realized power price that is 16% higher on average, compared to the spot power price. Not only does our portfolio optimization activities continue to create incremental value by capturing a higher realized Alberta power price than spot, it also helps to manage our exposure to commodity risk and reduce volatility, as illustrated by the flatter orange line of the chart in contrast to the more volatile spot power price, shown by the blue line.

Turning to Slide 9, I'll review our fourth quarter 2014 financial performance compared to the fourth quarter of 2013. Revenues were \$432 million, up 32% from Q3 2013, due primarily to higher unrealized changes in the mark to market of our commodity derivatives and emission credits. The Alberta Commercial Plants and Portfolio Optimization segment also contributed higher revenues, which were offset by the 2013 November sale of the New England assets. Adjusted EBITDA, before unrealized changes in fair values, was \$104 million in Q4 2014, up 2%, primarily due to lower corporate expenses. Normalized earnings per share of \$0.20 was lower than the \$0.40 in the fourth quarter a year ago, primarily due to higher coal costs to Alberta Contracted Plants and the non-cash impact of 2014 deferred tax expenses. As I highlighted earlier, Funds from Operations of \$102 million were in-line with our expectations for the fourth quarter.

Turning to Slide 10, I'll review our financial performance for the year. Revenues of \$1.23 billion for 2014 were 12% lower than the \$1.39 billion in 2013, due mainly to the sale of the New England assets in 2013 and lower revenues from the Alberta Commercial Plants and Acquired Sundance PPA. Adjusted EBITDA, before unrealized changes in fair values, was \$387 million in 2014; down 20%, primarily due to lower results in the Alberta Commercial Plants and Acquired Sundance PPA segment, a function of weaker average spot price, and lower production. This is also reflected in Normalized earnings per share, which came in at \$0.72, compared to \$1.74 in 2013. Finally, Funds from Operations of \$362 million were within our 2014 financial target of \$360 to \$400 million.

I'd now like to review our 2015 outlook, starting with an outlook on the Alberta power market on Slide 11. This chart shows the 2015 forward price curve, starting from September 1, 2014 to February 17, 2015. Last September, 2015 forward prices were in the mid-\$50/MWh range and the price has gradually drifted downwards. You can see a sharp decline in 2015 forward, starting in late-January, which were associated with a number of factors, including: the decline of spot prices, Shepard Energy Centre reaching material generation levels during its commissioning process, and declining natural gas prices.

Turning to Slide 12. From a macroeconomic perspective, due to a significant decline in global oil prices that is expected to lower both economic and power demand growth in Alberta, along with lower forward natural gas prices for 2015, Alberta power price forwards over the next couple of years have recently declined. As shown on the previous slide, forward prices for 2015 are currently in the mid-\$30/MWh range, which is lower than our original forecast assumption of \$44/MWh. The actions taken

over the last several years, including our hedging and cost-reduction programs, were initiated in anticipation of lower pricing in 2015. With our Alberta baseload position fully hedged for 2015, it will have a reduced financial impact on our 2015 financial guidance.

Despite the lower forecast for Alberta power prices for the year, our 2015 Funds from Operations expectations remains in the target range but at the lower end of the \$365 to \$415 million guidance.

Capital Power's financial strength is based on the foundation of strong contracted cash flow, which is not impacted by changing Alberta power price outlook. We remain confident in our credit rating and dividend growth outlook. I will now turn the call back to Brian.

**BRIAN VAASJO:** Thanks Stuart. Starting on Slide 13, I'll conclude my comments by reviewing our 2014 operational and financial performance versus targets, and recap our 2015 targets.

As mentioned, we achieved our 95% plant availability target for 2014 and have a 94% target for 2015, which includes major plant outages at Genesee 1 and Keephills 3. Our sustaining CAPEX was \$75 million in 2014, which is below our \$85 million target due to lower spending at the Genesee mine land purchases; we are targeting \$65 million for 2015. Our plant operating and maintenance expense for 2014 came in at \$185 million, which was in-line with our target range of \$165 to \$185 million. For 2015, we are targeting \$180 to \$200 million for plant operating and maintenance expenses, which includes Shepard. And, as Stuart indicated, we were within our 2014 cash flow guidance by generating \$362 million in Funds from Operations. For 2015, we are now expecting to be at the lower end of the \$365 to \$415 million guidance range.

Slide 14 outlines our development and construction targets for 2015. For K2 Wind, we expect to complete

construction with commercial operations near the middle of the year. The Genesee 4 & 5 project has been on a path to reach completion as early as 2018. We have incorporated tremendous contractual flexibility to push the project timing out, if appropriate, with minimal cost consequences. The flexibility was developed to allow Capital Power and our partner, ENMAX, to adjust completion based on market dynamics. Certainly, lower demand for power as a result of lower demand growth in Alberta could have the impact of targeting a completion date after 2018, and reducing our 2015 construction activity. In conjunction with our partner, we are currently assessing the market dynamics and the appropriateness of targeting a completion date after 2018. We should arrive at a conclusion sometime over the next quarter.

To conclude, I want to comment on our financial strength going forward. Slide 15 is a slide we presented before, illustrating the coverage of our financial obligations, including dividends, to cash flow, showing specifically the relationship for contracted cash flow and contracted cash flow plus a sensitivity to merchant cash flow at various Alberta price levels. The first point is that the contracted cash flow line, on which we based our dividend increase we announced last July, is virtually unchanged. This line continues to support the existing dividend plus future dividend growth. The second point is that even under low price scenarios, the merchant cash flow line continues to make a strong contribution to total cash flow. I'll now turn the call back over to Randy.

**RANDY MAH:** Thanks Brian. Matthew, we're ready to start the Question and Answer Session.

### **QUESTION AND ANSWER SESSION**

**OPERATOR:** All right, perfect. So, ladies and gentlemen, if you do have any questions please go

ahead and hit '01' on your telephone keypad. Perhaps we'll give everyone a few moments here to queue up. So, '01' now if you have any questions. And our first question comes from Paul Lechem of CIBC. Please go ahead, Paul.

**PAUL LECHEM:** Thank you. Good morning. Just wanted to ask about the adjustments to the coal costs of the Genesee units. You seem to suggest in the write up that it impacted the earnings but if it's just shifting them from one unit to the other, how is that an overall impact on your results? And can you give us the magnitude of that?

**STUART LEE:** It shifts them, Paul, but obviously with a portion of G3 going to TransAlta it also has an impact overall. So, the extent that more gets picked up by G1 and G2, it has an overall impact on us. And it's a couple million dollars; it's not real significant but it does have a modest impact.

**PAUL LECHEM:** Ok, thanks. Can you discuss the disallowances of your US tax NOLs for accounting purposes?

**STUART LEE:** Sure. So, obviously, a true-up at year-end but also a portion of it's related to Q4 and the fact that we're not recognizing those. So, on a go-forward basis, I think we would expect that a project like Element will hopefully be successful in generating taxable US income in the future, which will have substantive NOLs to use against, and potential for re-recognition. But, for the quarter, we haven't recognized any of the US NOLs – consistent with the write-down we took in Q3.

**PAUL LECHEM:** Ok. And, finally, can you give us the magnitude of the cost for winding up your defined benefit plan at the Genesee coal mine?

**STUART LEE:** It was about \$2 million.

**PAUL LECHEM:** All right, thank you.

**STUART LEE:** Thank you.

**OPERATOR:** All right. Our next question comes from Linda Ezergailis of TD Securities. Please go ahead, Linda.

**LINDA EZERGAILIS:** Thank you. I'm wondering what the seasonality might be and the duration of your planned outages scheduled for 2015 at G1 and K3?

**STUART LEE:** Seasonality – expect for the Genesee facility to be in Q2, and for K3, expect it will be Q4, and similar type of timing as what we saw this year for G2 and G3. So, typically those outages run, for G1 and G2, about three weeks and for K3 and G3, typically around four.

**LINDA EZERGAILIS:** That's very helpful. And just a follow-up question – are you starting to see or think about, maybe a silver lining to all of this oil and gas activity weakness as translating, perhaps, into some sort of a cost relief or relief, at least, of inflationary pressures in your operations? And can you comment on that?

**BRIAN VAASJO:** So, certainly there are implications to the overall decreasing activities in the province. We would see that there certainly; one of the offsets associated with potentially lower demand is that there continues to be lower crude oil prices. A number of the oil sands projects that have co-gens associated with them may not be proceeding so that's a fairly significant offset to a declining demand.

The other thing, from an overall cost perspective, is we're already seeing costs being lowered in the province. You're seeing wage settlements being lower; you're seeing companies such as ours, with annual compensation increases significantly below what they

otherwise would have been or were planned to have been. So you're seeing, certainly, some decreasing cost pressures.

As we move forward, with a lower level of activity, generally in Alberta, we would see the eventual construction of Genesee 4 and 5 benefit from greater labour availability and, certainly in our maintenance costs we would see not only potentially lower costs but, probably tapping into a more experienced labour force. So there are certainly some benefits to a – I'll call it a lower level of economic activity in the province.

**LINDA EZERGAILIS:** That's very helpful. And just one other clean-up question – at your Investor Day, your hedging was at slightly different levels for 2016 and 2017 and also the average level of pricing shifted around a little bit. Can you comment on – is that just a shift in your production mix or is there something else going on?

**STUART LEE:** So, the 2016 changes, I think, were pretty modest, Linda. For 2017, I think, the quote that we had in for average power price hedges in the low-\$60's was inaccurate and it should have been probably stated in the mid-\$50's.

**LINDA EZERGAILIS:** Ok, that's very helpful. Thank you.

**STUART LEE:** Yes.

**OPERATOR:** All right. Our next question comes from Andrew Kuske of Credit Suisse. Please go ahead, Andrew.

**ANDREW KUSKE:** Thank you, good morning. Just a question on the hedging. Given the rapid decline in Alberta power prices and, sort of, a very divided view on outlook on whether prices go up or down, just how do you think about your hedging strategy now as it

stands for the next couple years? Is it more of the same as we've seen in the past or do you anticipate revising your strategy just a little bit on the laddering?

**STUART LEE:** I think you'd expect to see some changes in our strategy on the laddering. I think our view on 2015 is fairly consistent with where the market is at. As you move out, 2016 and beyond, particularly as you get into the latter years, there's not a lot of liquidity in the market and I don't think the forwards necessarily reflect our view of where power prices are likely to move. I think, our view that additional demand will create higher prices in the province, going forward, and, therefore, I think we'll probably look at 2016 and beyond at layering in stuff at a pretty modest basis.

**ANDREW KUSKE:** Ok, so probably a bit more open position than you would normally have in the last few years, just because you take the view of the price is just too depressed right now, relative to what we might see?

**STUART LEE:** Correct. And, a good example of that is we went into 2013, about 50% of our baseload position we left open on a view that the forwards weren't reflective of our fundamental view on prices. And, obviously, it reflected in 2013 performance – and similar as we move out to 2016 and beyond.

**ANDREW KUSKE:** Ok, that's helpful. And then, are you seeing significant changes in just your customers' behaviour, given the fact that we're going to see a few of the PPAs rolling off in '17? Is there really a reluctance, right now, to lock into any kind of structured term for a period of time at what you would view reasonable prices?

**BRIAN VAASJO:** We're actually seeing no real level of identifiable increase or decrease in activity. This is, typically, going through the first quarter, a time of less activity for say industrials to be hedging and that's

consistent. What we're seeing is consistent with that view. Typically, it's the fourth quarter and the third quarter that you see more of the activity in the market.

**ANDREW KUSKE:** Ok, that's great. Thank you.

**OPERATOR:** Our next question comes from Robert Kwan of RBC. Please go ahead, Robert.

**ROBERT KWAN:** Good morning. If I could just follow up on the hedging but more so as it relates to your outlook? So, I'm understanding that you're bullish on the curve for '16 and '17 and so, with the lower oil prices it sounds like you still think we're going to see decent demand growth in the province?

**STUART LEE:** I don't know if I'd call it decent relative to historical, Robert. Again, I think historically we've seen 3 to 3.5% demand growth and certainly under the current expectations around GDP growth in the province, we'd scale that back. I think, we're still working through our current update to the forecast but expect it that's likely move down to probably 1 or 1.5% but even that level of GDP growth and demand growth in the province, coupled with likely a push-out in some of the co-generation facilities that may get built in the province, provides some additional support for pricing going forward.

**ROBERT KWAN:** Ok. Just, do you have any updated thoughts on how CASA might play out? There were some comments from somebody else that there may be a decision imminently that would involve a harmonization or effectively, a harmonization with the carbon rules?

**BRIAN VAASJO:** Well, currently there are a number of avenues of discussions taking place with the government. Generally speaking, those discussions are to be confidential so not really appropriate for me

to comment on it. I would say it's pretty early to speculate on anything.

**ROBERT KWAN:** Ok. I guess, if we went back into the fall, you were pretty confident that the existing rules would stick. I guess, directionally, are you maybe a little less confident then at this point?

**BRIAN VAASJO:** No.

**ROBERT KWAN:** Ok.

**ROBERT KWAN:** Ok. Last question here – if you look at Slide 15, based on your contracted cash flows you've got good coverage of the dividend; you've got room to increase it. I guess I'm just wondering, with the weak Alberta power prices, though, does that change the thought process on whether it's prudent to increase it annually and/or your thoughts on just the magnitude of the increases?

**BRIAN VAASJO:** So, I think, going back to when we first showed you this slide probably over a year ago. The whole concept was that we've got a very strong base of contracted cash flow and that's what we look to, to support both the dividend, dividend growth and certainly supports our credit rating. What we referred to as the upside in the Alberta market and the range that you see there, is more a function of, certainly the general upside that utilized more, or considered more, or rebuilding the balance sheet for capital expenditures or paying down debt, potentially buying back shares, that kind of more capital-intensive views. So, really, our perspective isn't changed that much by the changes in power prices. On the other side of the coin, if power prices went up dramatically and we're looking at an \$80 power price today, we wouldn't be looking at necessarily increasing the dividend more than we otherwise would. We're looking for a long-term sustainable dividend based on secured cash flows. So,

our proposition around dividends really hasn't changed with the lower oil prices.

**ROBERT KWAN:** Ok, that's great. Thank you very much.

**OPERATOR:** Our next question comes from Matthew Akman of Scotia Capital. Please go ahead, Matthew.

**MATTHEW AKMAN:** Thanks. Good morning. Stuart, I'm just wondering if G4 and 5 are delayed, have you thought about what to do with the surplus cash flow this year?

**STUART LEE:** So, yes, good question Matthew. I think the impact, overall, is about \$15 million, \$15 to \$20 million of CAPEX that we had earmarked for G4 and G5 in 2015. So, not all that material but as we look at our excess cash, which is substantive for 2015. I think absent a new development opportunity and, obviously, the team's working hard on some of the Element portfolio and some of the wind and solar opportunities – but, absent an opportunity there, would expect that we'll look at both debt reduction and potentially some share buybacks associated with it.

**MATTHEW AKMAN:** Is there anything on the debt reduction front that you see as urgent or is the decision between debt reduction and share buybacks and the balance there going to be more related to your stock price?

**STUART LEE:** So, there's nothing urgent whatsoever on the debt buybacks. We did, over the course of, I think, as we noted in the MD&A, we bought back about \$50 million of debt in late 2014 and continued with a small buyback through 2015. So we've reduced our overall debt balances by about \$70 million. But nothing urgent. We're very, very comfortable with where the credit metrics are and where our ratings are at. As we look at the combination of debt reduction and potential

share buybacks going forward, it's really a function of where share price is at as well as the overall balance sheet. And, so, expect that there might be a mix of both.

**MATTHEW AKMAN:** Ok. Thank you. Those are my questions.

**OPERATOR:** All right. So the last question currently comes from Paul Lechem of CIBC. Please go ahead, Paul.

**PAUL LECHEM:** Oh, thanks. Just, maybe, a follow-up on some of the previous questions. On the emissions front in Alberta, you paid your SGER compliance requirements by using cash rather than your CO2 credits. Just wondering, given your expectation that there's going to be no change in the environment, why continue to pay cash? Why not use the credits?

**STUART LEE:** So, we will be for this most recent compliance year, Paul. We will be using our inventory.

**PAUL LECHEM:** Ok, and then just on the Element portfolio. Is there anything in terms of the tax environment that you're waiting for? Do you need further clarity on the US production tax credits before moving forward on any of those sites or how should we think about when you might move forward on some of those projects?

**BRIAN VAASJO:** So, Paul, the situation is that there tends to be, around the existing regulations, there's a lot of clarity around them and around interpretation. So, as it relates to the Element portfolio, what we've done is, as there's a number of those that are in very, very late development stages and what we've done is we've actually gone out at the end of last year and put orders down for transformers, for two transformers, which will make two of those properties eligible for the current tax credit regime. So, we're definitely moving ahead on

trying to obtain PPAs on two of those projects. And those projects one would, under the current regulations, would have to be complete by the end of 2016. So, a significant amount of work focused on that. And, again, those would be with tax partners, et cetera, so the capital cost commitment isn't as significant as one would expect on those projects, in total.

There's also, we've got one of the projects was a small solar project in North Carolina that we—that, actually, has a PPA associated with that and we're moving forward on that, subject to continuing to do some work that may well start construction on that by, say, early July for completion this year. So, there is, certainly some promising activities around the Element portfolio.

**PAUL LECHEM:** Ok. Thanks very much.

**OPERATOR:** So there are no other questions at this time.

**RANDY MAH:** Ok, if there are no more questions we will conclude our conference call. Thanks again for joining us today and for your interest in Capital Power. Have a good day, everyone.

**OPERATOR:** Ladies and gentlemen, this concludes Capital Power's fourth quarter 2014 conference call. Thank you for your participation and have a great day.

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