QC INVESTMENT MEMO

To:	Queen's Capital
From:	Danielle Harrs
Date:	January 12, 2016
Re:	**TransCanada (TSX:TRP)**

COMPANY PROFILE

Industry: Oil and Gas Storage and Transportation

Main Asset(s): Natural Gas Pipelines, Liquid Pipelines, & Energy

Market Cap (M): $ 31,146.5
Debt (M): $ 33,122
Cash (M): $ 755
Enterprise Value (M): $ 67,847.5

NTM(E) Revenue (M): $ 1,562
NTM(E) EBITDA (M): $ 5,753
NTM(E) FCF (M): $ 3,892

INVESTMENT PROFILE

Current (Proposed) Investment Size:

Position Cost Basis: n/a

Current Share Price: $43.93
Target Price: $57.89

COMPANY

TransCanada is a leading North American energy infrastructure company operating in Canada, the US, and Mexico. TRP holds a $66bn portfolio of critical infrastructure across three business segments: Natural Gas Pipelines, Liquid Pipelines, and Energy. TRP directly owns and retains all cash flows from liquids and energy segments. In Natural Gas segment, TRP plans to continually drop US Natgas pipeline assets in TCP. TRP owns ~28% of TCP and in 2014 TCP began issuing equity decreasing TRP's LP interest in TCP.

VALUATION

Based on a two stage dividend discount model averaging dividend growth of 8-10% through 2020 and a growth rate of 1.5%-2.5% afterwards driven by investments in small to mid-sized projects and the Bruce Power contract.

First Stage Duration	5	Cost of Equity	7%
Run-Rate Dividend	2.08	Average Price	57.89

Dividend Growth

Terminal Growth Rate		6%	7%	8%	9%	10%	11%	12%
	1%	$43.51	$45.41	$47.37	$49.40	$51.5	$53.68	$55.94
	1.5%	$46.73	$48.78	$50.90	$53.10	$55.37	$57.73	$60.17
	2%	$50.59	$52.82	$55.14	$57.63	$60.02	$62.59	$65.26
	2.5%	$55.30	$57.76	$60.32	$62.96	$65.70	$68.53	$71.47
	3%	$61.20	$63.94	$66.79	$69.74	$72.79	$75.95	$79.23

Valuation II: Comparables

Company Name	Price	Market Cap	Total EV	LTM Tangible BV/Share	LTM Revenue	LTM EBITDA	NTM EPS
Enbridge Inc.	31.22	27,089.6	62,981.8	8.23	23,720	3,027.2	1.67
Williams Companies	18.69	14,013.1	48,473.1	(5.09)	7,495	2,967.0	1.47
Fortis Inc.	26.34	7,415.0	17,456.7	8.04	4,727	1,571.4	1.47
Pembina Pipeline Corporation	19.94	7,420.3	10,732.8	5.7	3,277	614.2	0.89
Gibson Energy Inc.	9.15	1,154.0	2,020.2	2.06	4,432	262.4	0.21
Spectra Energy Corp.	24.11	16,187.7	33,444.7	3.99	5,518	2,684.0	1.27
ONEOK Inc.	22.61	4,731.8	17,051.6	(2.89)	8,677	1,398.2	1.67
Targa Resources Corp.	21.87	1,225.2	12,094.7	(13.66)	7,044	1,075.8	1.34
ONEOK Partners, L.P.	24.01	6,862.7	14,362.7	19.57	8,675	1,391.0	2.01
TransCanada Corporation	30.94	21,937.6	47,787.4	9.2	7,793	3,717.5	1.81
Mean	21.13	8,856.5	22,852.0	4.08	8,061	1,607.4	1.26
Median	22.24	7,138.8	15,707.1	4.85	7,044	1,394.6	1.4

Conservative business profile and solid growth not reflected in valuation

- Low risk business model w/ less exposure to commodity price and volumetric risk
- Superior B/S and access to capital; attractive diversity across 3 energy infrastructure vertical
- Solid visibility long-term with 8-10% dividend growth potential means they deserve to trade at a premium when currently trading at higher EPS

INVESTMENT THESIS

- *Investment Thesis I - Commitments to Capital Expenditure Fuelling Future Growth*

  47+ billion spending program of mega projects including the Energy East Pipeline (15.7B), Keystone XL (US8B), Prince Rupert Gas Transmission (5B), Coastal GasLink (4B), upgrades to Alberta gas system and renewable thermal power facilities. If all are successful there is expected to be a 12% EBITDA CAGR from 2013 by end of 2020.

- *Investment Thesis II - Stalwart Business Model Delivers Visible and Stable Earnings*

  Specializes in secured revenues with >90% of EBITDA underpinned by regulated assets or LT, ship or pay contract. TRP's strategic assets have high barriers to entry that drive strong and stable CF. All assets incur immaterial direct commodity price exposure underpinned by cost of service fees for natural gas pipelines, long term capacity reservations for liquids pipelines and long term electricity sales agreements for power. Presenting TRP as a stable, low risk investment in high quality, critical assets with upside from continued energy infrastructure investment

- *Investment Thesis II - Bruce power Agreement Supports Long Term CF Stability*

  TRP announced that Bruce Power ahs entered into an amended agreement w/ the Independent Electricity System Operator (100% Government of Ontario) to enable progress with series of life extension and refurbishment investments for Bruce Power facilities extending contracted cash flow to TRP through 2064. TRP also exercised option to acquire additional 16.9% interest in Bruce Power from OMERS. Refurbishment in line with management's estimate of cost. Management expects investment to be accretive to earnings and cash flow modestly over short term and significant over long term based on low after tax IRR. Power price escalation provides long term growing earnings stream as capital program is executed. 88% of price escalated each year (based on CPI) resulting in better matching revenues and costs and power price will be adjusted prior to each significant investment.

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KEY INVESTMENT RISKS

RISK I Depressed oil prices (and impact on future oil sands production growth) will foster a volatile, negative backdrop for the upcoming project TRP undertakes

Mitigation: little commodity price exposure because of service fees for natural gas pipelines, long term capacity reservations for liquids pipelines and long term electricity sales agreements for power

RISK II Transcanada's regulated assets subject to regulatory frameworks in which company operates. Has yet to obtain regulatory approval from Energy East. Risk lies in the extent these regulations change could be negative impact on TRP and customer business operations, with regulations preventing new construction or influencing tariffs. Potential for near term political risk following recent elections that could result in greater environmental regulations

Mitigation: Strong relationships with government seen with its contingent cost sharing mechanism with the government over the Bruce Power project

RISK III Failure to achieve earnings, dividend growth targets could negatively re-rate. Should realized worse than expected earnings, dividends or new DCF growth company may re rate to higher yield. Devaluation increases TRP's cost of equity and reduces accretion from future growth projects

Mitigation: Conservative growth and earning estimates going forward

RISK IV Certain projects require commercial sanctioning to proceed (Prince Rupert Gas Transmission, coastal GasLink)

Mitigation: Consider a variety of projects so TRP has the margin of error for some sanctioning to half indefinitely

RISK V Power Price Exposure: only half of power sales are under LT contract, with remainder sold to market. Also maintains an active power marketing business energy results are tied to power and capacity prices in its key markets (Alberta, Ontario, NY, New England, and PJM)

Mitigation: Even though energy prices expected to increase in the future, TRP is still exposed to market volatility which can be mitigated by hedging and keeping some emergency cash on hand

KEY INVESTMENT STRENGTHS

STRENGTH I **Filed amendment on existing regulatory application with National Energy Board**

700 changes to route and scope of pipeline resulted in project cost increased to 15.7B from 12B (cost of transferred Mainline gas pipeline 1.5B and total project cost at 19.3B) which was not unexpected. Cost be borne through shippers via increased tolls and only responsible for cost once final regulatory approval received from government then 50/50 w/ shippers. Strength is management's ability to predict costs.

STRENGTH II **Superior access to capital and B/S capacity position TRP for opportunistic asset or entity level M&A from struggling peers**

TRP has a best in class credit rating with conservative dividend payout. It has peer leading A-/Baa1 (S&P/ Moody's) credit ratings and conservative dividend policy. It financial strength further demonstrated in its strong B/S, <50% DCF dividend payout, no equity needs, and its share reductions from buyback plan (where it plans to buyback~3% of shares).

STRENGTH III **US Shale displaced exports but Montney appears promising and FX will help**

Natural gas oversupply in North America caused by shale revolution displaced some traditional Canadian exports to the US Canadian production in 2014 as producer netbacks suffer in low commodity prices and lack of access to incremental demand. Demand from oil sands production, coal to gas switching and significant favorable FX move support Canadian production.

STRENGTH IV **TransCanada the major transmission player most activity in West**
Like Canada's liquid pipelines, natural gas transmission system dominated by few incumbents positioning lion's share of long distance transport capacity where Transcanada is the dominant player w/ expansive mainline system connecting producing regions to major Canadian and US markets

KEY INVESTMENT CATALYSTS

CATALYST I: **LNG export potential provides potential gateway to sustained growth**
LNG exports to Asia present key driver for LT Canadian production. Established west coast ports at Kitimat and Prince Rupert possess closest North American routes to Asia: 8 sailing days to Japan and 11 to China. It makes sense on a long term economic basis for both parties because it allows Asian buyers to obtain a lower cost natural gas while Canadian producers gain access to higher pricing.

CATALYST II: **Stakeholder agreements (particularly in Quebec) for the Energy East Pipeline**
Energy East project would run crude oil from western Canada to eastern ports making it suitable for export to Europe.

CATALYST III: **Northern Portion Keystone XL pipeline & Energy East project**

Northern portion of TRP's Keystone XL pipeline which would carry heavy crude from Alberta and the Bakken Shale to Gulf Coast refineries potentially delayed indefinitely. Its commencement catalysts for future growth.