

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

This Management's Discussion and Analysis ("MD&A") contains forward-looking statements. These statements are based on certain estimates and assumptions and involve risks and uncertainties. Actual results may differ materially. See the Forward-Looking Statements section of this MD&A for additional information.

This MD&A should be read in conjunction with the unaudited interim condensed consolidated financial statements of TransAlta Renewables Inc. as at and for the three months ended March 31, 2014 and 2013 and should also be read in conjunction with the audited consolidated financial statements and MD&A contained within our 2013 Annual Report. In this MD&A, unless the context otherwise requires, 'we', 'our', 'us', 'TransAlta Renewables', and the 'Corporation' refers to TransAlta Renewables Inc. and 'TransAlta' refers to TransAlta Corporation and its subsidiaries. All dollar amounts in the tables presented in this MD&A are in thousands of Canadian dollars, unless otherwise noted. The condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). Certain financial measures included in this MD&A do not have a standardized meaning as prescribed by IFRS. These measures may not be comparable to similar measures presented by other issuers and should not be considered in isolation or as a substitute for measures prepared in accordance with IFRS. See the Non-IFRS Measures section of this MD&A for additional information. This MD&A is dated May 1, 2014. Additional information respecting the Corporation is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on our website at [www.transaltarenewables.com](http://www.transaltarenewables.com).

**OPERATIONS OF THE CORPORATION**

On Aug. 9, 2013, we indirectly acquired 28 wind and hydroelectric ("hydro") generating assets (the "Acquired Assets") from TransAlta (the "Acquisition") and completed an initial public offering of 22.1 million common shares. Prior to that, we had no active operations. Please refer to the Significant Events section of our 2013 Annual MD&A for more information.

**RESULTS OF OPERATIONS**

The results of operations are presented on a consolidated basis. The results of operations for the comparative three months ended March 31, 2013 have been prepared in accordance with IFRS using consistent accounting policies as those outlined in Note 2 of our 2013 audited consolidated financial statements. Historically, financial statements had not been prepared for the Acquired Assets as they had not been operated as a separate business by TransAlta. Accordingly, the results of operations for the comparative three months ended March 31, 2013 reflect the results of operations for the Acquired Assets in a manner consistent with how TransAlta managed the Acquired Assets and as though the Acquired Assets had been a separate company. All material assets and liabilities specifically identified to the Acquired Assets and all material revenues and expenses specifically attributable to the Acquired Assets and allocations of overhead expenses have been included in the results of operation. These may not necessarily reflect the financial position, results of operations, or cash flows that the Acquired Assets might have had in the past had they existed as a separate business during the periods prior to the Acquisition. For purposes of presenting comparative amounts per share, the Corporation's common shares issued under its initial public offering have been assumed to be outstanding as of the beginning of each period presented. We have no dilutive or potentially dilutive instruments.

## HIGHLIGHTS

### First Quarter Highlights

	3 months ended March 31	
	2014	2013
Production (GWh) <sup>(1)</sup>	818	768
Revenues	67,965	60,917
Operating income <sup>(2)</sup>	33,158	27,474
Comparable operating income <sup>(3)</sup>	37,523	27,474
Net earnings attributable to common shareholders <sup>(4)</sup>	21,134	14,004
Comparable EBITDA <sup>(3)</sup>	55,662	46,384
Funds from operations <sup>(3)</sup>	46,354	39,191
Cash flow from operating activities	45,210	53,228
Cash available for distribution <sup>(3)</sup>	16,835	36,902
Net earnings per share attributable to common shareholders, basic and diluted <sup>(4)(5)</sup>	0.18	0.12
Comparable net earnings per share <sup>(3)(5)</sup>	0.18	0.12
Funds from operations per share <sup>(3)(5)</sup>	0.40	0.34
Cash available for distribution per share <sup>(3)(5)</sup>	0.15	0.32
Dividends paid per common share <sup>(5)</sup>	0.19	-

As at	March 31, 2014	Dec. 31, 2013
Total assets	1,994,963	2,013,638
Total long-term liabilities	813,915	846,724

- Comparable Earnings Before Interest, Taxes, Depreciation, and Amortization ("EBITDA") increased \$9.3 million in the quarter to \$55.7 million compared to 2013, primarily due to a full quarter of operations at New Richmond, higher wind volumes in Eastern Canada, and dividend income from our investment in preferred shares, partially offset by lower wind volumes and prices in Western Canada and the G&A Reimbursement Fee.
- We received our first dividends on the Wyoming Wind Preferred Shares in the amount of \$4.4 million in the quarter.
- Funds from Operations ("FFO") were \$46.4 million compared to \$39.2 million in the prior year. The increase is primarily due to higher cash from operations.
- Reported and comparable net earnings attributable to common shareholders were \$21.1 million (\$0.18 per share) up from \$14.0 million (\$0.12 per share) in 2013, primarily due to an increase in comparable EBITDA, partially offset by increases in net interest and income tax expenses.
- Production increased 50 gigawatt hours ("GWh") to 818 GWh compared to 2013, primarily due to a full quarter of production at New Richmond and high wind volumes at other Eastern Canada facilities, partially offset by lower wind volumes in Western Canada.

(1) Excludes production from the Wyoming Wind Farm.

(2) These items are Additional IFRS Measures. Refer to the Additional IFRS Measures section of this MD&A for further discussion of these items.

(3) These items are not defined under IFRS. Presenting these items from period to period provides management and investors with the ability to evaluate earnings trends more readily in comparison with prior periods' results. Refer to the Non-IFRS Measures section of this MD&A for further discussion of these items, including, where applicable, reconciliations to measures calculated in accordance with IFRS.

(4) A non-controlling interest exists in the Kent Hills wind farm which is not presented as a part of net earnings attributable to common shareholders.

(5) Amounts are presented in whole numbers to the nearest two decimals.

## SUBSEQUENT EVENTS

### *Secondary offering of TransAlta Renewables shares by TransAlta*

On April 29, 2014, TransAlta completed a secondary public offering of 11,950,000 common shares of the Corporation at a price of \$11.40 per common share. As a result of the offering, TransAlta now owns approximately 70.3 per cent of the common shares of TransAlta Renewables. The Corporation will not receive any of the proceeds from the sale of common shares, as these shares were owned and held by TransAlta.

## OPERATIONAL RESULTS

*TransAlta Renewables owns and operates wind farms and hydro facilities in Western and Eastern Canada and holds an economic interest in the 144 MW Wyoming Wind Farm. At March 31, 2014, our generating assets had 1,139 MW of gross generating capacity<sup>(1)(4)</sup> in operation (1,111 MW net ownership interest). The full capacity of the facilities in which we have a share of ownership is 1,232 MW.*

The results of operations are as follows:

	3 months ended March 31	
	2014	2013
Revenues	54,089	53,001
Government incentives	6,546	6,738
Lease revenue <sup>(2)</sup>	7,330	1,178
<b>Total revenue</b>	<b>67,965</b>	<b>60,917</b>
Royalties and other	3,999	3,560
<b>Comparable gross margin<sup>(3)</sup></b>	<b>63,966</b>	<b>57,357</b>
Operations, maintenance, and administration	10,864	9,174
Taxes, other than income taxes	1,805	1,799
Dividend income from investment in preferred shares	(4,365)	-
<b>Comparable EBITDA<sup>(3)</sup></b>	<b>55,662</b>	<b>46,384</b>
Depreciation and amortization	18,139	18,910
<b>Comparable operating income<sup>(3)</sup></b>	<b>37,523</b>	<b>27,474</b>
Production (GWh) <sup>(4)</sup>	818	768
Gross installed capacity (MW) <sup>(1)(4)</sup>	1,139	1,139
Net installed capacity (MW) <sup>(1)(4)</sup>	1,111	1,111

Comparable gross margin for the three months ended March 31, 2014 increased by \$6.6 million compared to the same period in 2013, primarily due to higher wind volumes and contract price escalations in Eastern Canada, and a full quarter of operations at New Richmond, partially offset by lower wind volumes and prices in Western Canada.

(1) We measure capacity as net maximum capacity (see Glossary of Key Terms for definition of this and other key terms), which is consistent with industry standards. Capacity figures represent capacity owned and in operation unless otherwise stated. Gross capacity reflects the basis of consolidation of underlying assets, while net capacity deducts capacity attributable to non-controlling interest in these assets.

(2) Under IFRS the agreements for the sale of electrical energy for the Akolkolex, Bone Creek and New Richmond facilities are considered operating leases. Accordingly, revenues earned for sale of electrical energy produced by these facilities are reported as lease revenue.

(3) Comparable figures are not defined under IFRS. Refer to the Non-IFRS Measures section of this MD&A for further discussion of these items, including, where applicable, reconciliations to net earnings attributable to common shareholders and cash flow from operating activities.

(4) Production and installed capacity do not include results from our economic interest in the Wyoming Wind Farm.

OM&A expense for the three months ended March 31, 2014 increased \$1.7 million compared to the same period in 2013, primarily due to a net increase in corporate costs under the G&A Reimbursement Fee that came into effect in August 2013, and increased costs from a full quarter of commercial operations at New Richmond.

Dividend income is from the investment in preferred shares associated with the Wyoming Wind Farm, acquired in December, 2013.

### Production and Gross Margins

3 months ended March 31, 2014	Gross installed capacity (MW)	Production (GWh)	Revenues	Royalties and other	Gross margin	Revenues per produced MWh <sup>(1)</sup>	Royalties and other per produced MWh <sup>(1)</sup>	Gross margin per produced MWh <sup>(1)</sup>
Western Canada wind	418	286	13,628	1,295	12,333	47.65	4.53	43.12
Eastern Canada wind	616	511	52,700	2,467	50,233	103.13	4.83	98.30
Hydro	105	21	1,637	237	1,400	77.95	11.29	66.66
	1,139	818	67,965	3,999	63,966	83.09	4.89	78.20

3 months ended March 31, 2013	Gross installed capacity (MW)	Production (GWh)	Revenues	Royalties and other	Gross margin	Revenues per produced MWh <sup>(1)</sup>	Royalties and other per produced MWh <sup>(1)</sup>	Gross margin per produced MWh <sup>(1)</sup>
Western Canada wind	418	362	20,641	1,592	19,049	57.02	4.40	52.62
Eastern Canada wind	616	379	38,262	1,778	36,484	100.96	4.69	96.27
Hydro	105	27	2,014	190	1,824	74.59	7.04	67.55
	1,139	768	60,917	3,560	57,357	79.32	4.64	74.68

#### Western Canada Wind

Our Western Canada wind assets consist of 10 facilities with a total gross and net generating capacity of 418 MW.

Production for the three months ended March 31, 2014 decreased 76 GWh compared to the same period in 2013 primarily due to lower wind volumes.

Gross margin for the three months ended March 31, 2014 decreased \$6.7 million compared to the same period in 2013, primarily due to lower prices under the TransAlta PPAs compared to the previous merchant prices, lower government incentives, and lower emission reduction credit sales, partially offset by lower transmission costs.

#### Eastern Canada Wind

Our Eastern Canada wind assets consist of 6 facilities with a total gross generating capacity of 616 MW (591 MW net ownership interest).

Production for the three months ended March 31, 2014 increased 132 GWh compared to the same period in 2013, primarily due to higher wind volumes and a full quarter of production at New Richmond.

For the three months ended March 31, 2014, gross margin increased \$13.7 million compared to the same period in 2013, primarily due to higher wind volumes and contract price escalations, and a full quarter of operations at New Richmond, partially offset by higher royalties.

(1) The amounts per MWh are presented in whole dollars to the nearest two decimals.

## Hydro

Our Hydro assets consist of 12 facilities with a total gross and net generating capacity of 105 MW.

Production for the three months ended March 31, 2014 decreased 6 GWh compared to the same period in 2013, primarily due to lower water resources in Western Canada.

Gross margin for the three months ended March 31, 2014 decreased \$0.4 million compared to the same period in 2013, primarily due to lower water resources in Western Canada and lower prices under the TransAlta PPAs.

### Economic Interest in Wyoming Wind Farm

We have an economic interest in the 144 MW Wyoming Wind Farm which is fully operational and contracted under a long-term PPA until 2028 with an investment grade counterparty. As we have an economic interest, and not direct ownership, the operational results of the Wyoming Wind Farm are not consolidated into our results; however, the dividends we receive on our Wyoming Wind Preferred Shares are included in our consolidated results, and are based on the pre-tax earnings from the Wyoming Wind Farm.

Dividends of \$4.4 million were recognized as income during the three months ended March 31, 2014. After considering the Wyoming Wind Acquisition Loan interest expense of \$1.1 million, the incremental contribution to earnings for the period is \$3.3 million.

Production at the Wyoming Wind Farm was 163 GWh during the three months ended March 31, 2014.

### NET INTEREST EXPENSE

The components of net interest expense are shown below:

	3 months ended March 31	
	2014	2013
Interest on debt	9,025	7,702
Interest on letters of credit and guarantees pledged by TransAlta	21	1,540
Capitalized interest	-	(2,147)
Interest income	(3)	(4)
<b>Interest expense</b>	<b>9,043</b>	<b>7,091</b>
Accretion of provisions	220	198
<b>Net interest expense</b>	<b>9,263</b>	<b>7,289</b>

The change in net interest expense for the three months ended March 31, 2014, compared to the same period in 2013, is shown below:

	<b>3 months ended</b>
	<b>March 31</b>
Net interest expense, 2013	7,289
Higher interest from addition of Amortizing Term and Wyoming Wind Acquisition Loans	3,049
Lower capitalized interest	2,147
Other	16
Lower interest on letters of credit and guarantees	(1,518)
Lower interest charged from TransAlta on capital projects	(1,720)
<b>Net interest expense, 2014</b>	<b>9,263</b>

## INCOME TAXES

A reconciliation of income taxes and effective tax rates on earnings excluding non-comparable items is presented below:

	<b>3 months ended March 31</b>	
	<b>2014</b>	<b>2013</b>
Earnings before income taxes	<b>28,184</b>	19,425
Income attributable to non-controlling interest	<b>(1,159)</b>	(619)
<b>Earnings attributable to common shareholders excluding non-comparable items subject to tax</b>	<b>27,025</b>	18,806
Income tax expense	<b>5,891</b>	4,802
<b>Income tax expense excluding non-comparable items</b>	<b>5,891</b>	4,802
<b>Effective tax rate on earnings attributable to common shareholders excluding non-comparable items (%)</b>	<b>22</b>	26

The income tax expense excluding non-comparable items for the three months ended March 31, 2014 increased compared to the same period 2013 due to higher comparable earnings offset by certain earnings that are not subject to tax.

The effective tax rate on earnings attributable to common shareholders excluding non-comparable items for the three months ended March 31, 2014 decreased compared to the same period in 2013 due to certain earnings that are not subject to tax.

## NON-CONTROLLING INTEREST

Natural Forces Technologies Inc. owns a 17 per cent interest in the Kent Hills 1 and 2 wind farms, which have 150 MW of gross generating capacity.

Net earnings attributable to the non-controlling interest for the three months ended March 31, 2014 increased \$0.5 million compared to the same period in 2013, primarily due to higher wind volumes.

## FINANCIAL POSITION

The following chart highlights significant changes in the Condensed Consolidated Statements of Financial Position from Dec. 31, 2013 to March 31, 2014:

	<b>Increase/ (Decrease)</b>	<b>Primary factors explaining change</b>
Cash and cash equivalents	(7,311)	Timing of receipts and payments
Accounts receivable	(3,329)	Timing of customer receipts
Prepaid expenses	1,830	Annual insurance premiums paid in the period
Property, plant, and equipment, net	(13,841)	Depreciation, partially offset by additions
Intangible assets	(1,762)	Amortization
Investment in preferred shares	4,357	Increase due to favourable foreign exchange rates
Risk management assets (current and long-term)	719	Fair value changes as a result of the appreciation of the hedge on foreign-denominated debt
Bank overdraft	(891)	Addition of master banking agreement to allow offset
Accounts payable and accrued liabilities	(3,337)	Timing of payments
Dividends payable	(14,525)	Payment of dividends declared on common shares
Long-term debt (including current portion)	(21,698)	Principal repayments on the amortizing term loan and Wyoming Wind Acquisition Loan, partially offset by changes in foreign exchange rates
Deferred income tax liabilities	6,110	Decreases in tax loss carryforwards and increases in taxable temporary differences
Equity attributable to shareholders	13,805	Net earnings for the period, partially offset by dividends declared

## FINANCIAL INSTRUMENTS

Refer to *Note 13* of the Corporation's most recent annual consolidated financial statements and *Note 6* of our interim condensed consolidated financial statements as at and for the three months ended March 31, 2014 for details on Financial Instruments. Also refer to the Financial Instruments section of our most recent Annual MD&A for additional details. Our risk management profile and practices have not changed materially from Dec. 31, 2013.

## STATEMENTS OF CASH FLOWS

The following chart highlights significant changes in the Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2014 compared to the same period in 2013:

<b>3 months ended March 31</b>	<b>2014</b>	<b>2013</b>	<b>Primary factors explaining change</b>
Cash and cash equivalents, net of bank overdraft, beginning of period	<b>18,365</b>	3,205	
Provided by (used in):			
Operating activities	<b>45,210</b>	53,228	Higher cash from operations of \$7.2 million and unfavourable changes in working capital of \$15.2 million
Investing activities	<b>(1,052)</b>	(37,351)	Decrease in additions to property, plant and equipment of \$28.5 million and a favourable change in non-cash investing working capital balances of \$9.9 million, partially offset by a decrease in realized risk management gains of \$2.1 million
Financing activities	<b>(50,592)</b>	(17,110)	Addition of long-term debt repayments of \$27.3 million and dividends paid on common shares of \$21.9 million, partially offset by a decrease in the repayment of net parental investment and related party advances of \$15.9 million
Translation of foreign currency cash	<b>14</b>	-	
Cash and cash equivalents, end of period	<b>11,945</b>	1,972	

## LIQUIDITY AND CAPITAL RESOURCES

Liquidity risk arises from our ability to meet general funding needs, engage in trading and hedging activities, and manage the assets, liabilities, and capital structure of the Corporation. Liquidity risk is managed by maintaining sufficient liquid financial resources to fund obligations as they come due in the most cost-effective manner.

Our liquidity needs are met through a variety of sources, including cash generated from operations and funding from TransAlta. Our primary uses of funds are operational expenses, capital expenditures, distributions to non-controlling interest, interest and principal payments on debt, and dividends.

### **Debt**

Long-term debt, including amounts owing to TransAlta, totalled \$662.5 million at March 31, 2014, compared to \$684.2 million Dec. 31, 2013. Long-term debt decreased from Dec. 31, 2013 primarily due to principal payments made during the period, partially offset by an increase due to unfavorable foreign exchange rates.

At March 31, 2014, \$285.6 million of our long-term debt was due to TransAlta (Dec. 31, 2013 - \$308.5 million).

### **Working Capital Credit Facility**

We have a \$100.0 million unsecured working capital credit facility with TransAlta available to us. The facility is available for general corporate purposes, including financing ongoing working capital requirements. At March 31, 2014, no amounts were drawn on the facility.



### ***Share Capital***

On March 31, 2014 and May 1, 2014, we had 114.7 million common shares issued and outstanding.

During the three months ended March 31, 2014, no common shares were issued.

## **2014 OUTLOOK**

### ***Business Environment***

#### **Economic Environment**

We expect moderate growth in Alberta and low growth in Eastern Canada in 2014. We monitor global events to assess their potential impact on the economy and our supplier and commodity counterparty relationships.

Counterparty credit risk is monitored and we operate in accordance with established risk management policies. We do not anticipate any material change to our existing credit practices and continue to deal primarily with investment grade counterparties.

#### **Environmental Legislation**

The siting, construction, and operation of electrical energy facilities requires interaction with many stakeholders. Recently, within the renewables industry, certain stakeholders have brought actions against government agencies and owners over alleged adverse impacts of wind projects. We are monitoring the activities and claims within the industry in order to assess the associated risks.

Changes in current environmental legislation do have, and will continue to have, an impact upon our operations and our business. The regulatory framework applicable to electricity generation varies between regions. Over the past few decades, a number of regions have restructured their power markets, allowing power to be generated by IPPs. Generally, there has been broad support from governments to facilitate growth in renewable power generation through the development of incentives and long-term revenue arrangements designed to encourage the adoption of renewable power.

In addition, government climate change policies and regulations can have an impact on our operations and business in that they frequently influence government support for renewables generation, or influence the price competitiveness of renewables generation in comparison to fossil-fuel based generation.

### ***Operations***

#### **Production**

We expect production in 2014 to be in line with the 3,059 GWh long-term average for our facilities and slightly higher than 2013 due to the full year of production expected from the New Richmond facility.

#### **Contracted Cash Flows**

Through the use of PPAs, including the TransAlta PPAs, all of our capacity is currently contracted. Substantially all of our capacity is contracted over the next 10 to 20 years. In addition, for 2014, approximately 76 per cent and 95 per cent of the environmental attributes from our wind and hydro facilities, respectively, have been sold.

### **Operations, Maintenance, and Administration Costs**

We expect OM&A costs for 2014 to increase primarily due to a full year of operations at New Richmond. However, we have long-term service agreements in place for many of our wind facilities, which allow us to stabilize costs. Over time, OM&A costs are also expected to increase due to inflation. Due to the acquisition of the economic interest in the Wyoming Wind Farm, the G&A Reimbursement Fee will increase by an additional \$0.4 million in 2014.

### **Wyoming Wind Economic Interest**

We expect dividends on the Wyoming Wind Preferred Shares to be in the range of U.S.\$8.0 to U.S.\$9.0 million in 2014. Actual dividend amounts may vary from this range as the dividends are based on pre-tax earnings and free cash flow generated by the Wyoming Wind Farm.

### **Exposure to Fluctuations in Foreign Currencies**

In 2014, we expect that we will be exposed to fluctuations in the exchange rate between the Canadian and U.S. dollars as a result of our economic interest in the Wyoming Wind Farm, as both the Wyoming Wind Preferred Shares and the related dividends received are denominated in U.S. dollars. However, these exposures will be partially offset by the U.S.-denominated Wyoming Wind Acquisition Loan and the related payment of U.S.-denominated interest, as well as the U.S.-denominated interest on our U.S.\$20.0 million CHD debenture.

All of our other assets are located in Canada, and as a result, there is minimal additional exposure to fluctuations in foreign currencies. We may acquire equipment from foreign suppliers for future capital projects, which could create exposure to fluctuations in the value of the Canadian dollar related to these currencies.

Our strategy is to minimize the impact, if any, of fluctuations in the Canadian dollar against the U.S. dollar, euro and other currencies by entering into foreign exchange contracts, to the extent that foreign denominated expenses and revenues do not offset.

### **Net Interest Expense**

We are not exposed to interest rate risk from long-term debt as all instruments bear interest at a fixed rate. Net interest for 2014 is expected to increase compared to 2013 due to interest on the most recent loans from TransAlta and lower capitalized interest.

### **Liquidity and Capital Resources**

If there are low wind volumes, low hydro resources, or unexpected maintenance costs, we may need additional liquidity in the future. We expect to maintain adequate available liquidity under our working capital credit facility with TransAlta.

### **Income Taxes**

The effective tax rate on earnings excluding non-comparable items for 2014 is expected to be approximately 20 to 25 per cent, which varies from the statutory tax rate of 25 per cent primarily due to certain earnings that are not subject to tax.

## Accounting Estimates

A number of our accounting estimates, including those outlined in the Critical Accounting Policies and Estimates section of our most recent Annual MD&A, are based on the current economic environment and outlook. As a result of the current economic environment, market fluctuations could impact, among other things, future commodity prices, foreign exchange rates, and interest rates, which could, in turn, impact future earnings and asset valuations for our asset impairment calculations.

## Capital Expenditures

Our capital expenditures are primarily sustaining in nature.

## Sustaining Capital

Our sustaining capital is comprised of the ongoing capital costs associated with maintaining the existing generating capacity of our facilities. For 2014, our estimate for total sustaining capital expenditures, net of any contributions received, is allocated among the following:

<b>Category</b>	<b>Description</b>	<b>Spend to date<sup>(1)</sup> in 2014</b>	<b>Expected spend in 2014</b>
Routine capital	Expenditures to maintain our existing generating capacity	430	5,326
Planned maintenance	Regularly scheduled maintenance	378	6,210
<b>Total sustaining expenditures</b>		<b>808</b>	<b>11,536</b>

## Financing

Financing for these capital expenditures is expected to be provided by cash flow from operating activities and existing borrowing capacity through TransAlta.

## RELATED PARTY TRANSACTIONS AND BALANCES

### *Post-Acquisition Relationship with TransAlta*

After the Acquisition, we entered into certain agreements and transactions with TransAlta. Please refer to the Related Party Transactions and Balances section of our most recent Annual MD&A for more information.

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(1) As at March 31, 2014

## A. Related Party Transactions

Amounts recognized from transactions with TransAlta or subsidiaries of TransAlta are as follows:

	3 months ended March 31	
	2014	2013
Revenue from TransAlta PPAs	7,951	-
Preferred share dividends	4,365	-
G&A Reimbursement Fee	2,523	-
Interest expense on amortizing term loan	1,914	-
Interest expense on letters of credit and guarantees	21	1,540
Interest expense on Wyoming Wind Acquisition Loan	1,135	-

## B. Related Party Balances

Related party balances include the following balances:

As at	March 31, 2014	Dec. 31, 2013
Trade accounts receivable	5,212	10,232
Trade accounts payable	4,607	5,048
Dividends payable	11,876	23,600
Interest payable	1,038	3,311
Investment in preferred shares	113,682	109,325
Net risk management assets (liabilities)	589	(104)
Amortizing term loan	189,321	200,000
Wyoming Wind Acquisition Loan	96,257	108,528
Letters of credit issued by TransAlta on behalf of the Corporation	4,503	4,503
Guarantees provided by TransAlta on behalf of the Corporation	226,500	226,500

All of these balances are with TransAlta or subsidiaries of TransAlta.

### *Pre-Acquisition Relationship with TransAlta*

The Acquired Assets have historically been managed and operated in the normal course of business by TransAlta along with other TransAlta operations and affiliates. Financial statements for periods prior to Aug. 9, 2013 were not historically prepared for the Acquired Assets as they had not been operated as a separate business. Please refer to the Related Party Transactions and Balances section of our 2013 Annual MD&A for more information.

### **Allocation of Corporate Costs**

Certain shared costs have been allocated to the Acquired Assets and reflected as expenses in the pre-Acquisition period financial statements. Allocated corporate costs include TransAlta charges for, but not limited to: corporate accounting, human resources, government affairs, information technology, shared real estate expenses, legal, treasury, and pension and other post-employment benefits. These costs are included in OM&A expenses. The costs were allocated to the Acquired Assets based on GWh of production. Note that these expenses may have been different had the Acquired Assets been a separate entity during the periods presented. For the comparative three months ended March 31, 2013, these pre-tax costs were \$1.4 million.

## **ADDITIONAL IFRS MEASURES**

An additional IFRS measure is a line item, heading, or subtotal that is relevant to an understanding of the financial statements but is not a minimum line item mandated under IFRS, or the presentation of a financial measure that is relevant to an understanding of the financial statements but is not presented elsewhere in the financial statements. We have included line items entitled “gross margin” and “operating income” in our Condensed Consolidated Statements of Earnings for the three months ended March 31, 2014 and 2013. Presenting these line items provides management and investors with a measurement of ongoing operating performance that is readily comparable from period to period.

## **NON-IFRS MEASURES**

We evaluate our performance using a variety of measures. Those discussed below, and elsewhere in this MD&A, are not defined under IFRS and, therefore, should not be considered in isolation or as an alternative to or to be more meaningful than net earnings attributable to common shareholders or cash flow from operating activities, as determined in accordance with IFRS, when assessing our financial performance or liquidity. These Non-IFRS measures are not necessarily comparable to a similarly titled measure of another company.

Typically, for comparability purposes, we exclude the impact of asset impairment charges and other adjustments to earnings, such as gains on sales of assets, as management believes these transactions are not representative of our business operations. We also exclude the income tax expense related to changes in corporate income tax rates as these amounts relate to the impact of the rate change on future income taxes as opposed to the impact on current earnings.

Earnings on a comparable basis per share are calculated using the weighted average common shares outstanding during the period.

Presenting comparable EBITDA from period to period provides management and investors with a proxy for the amount of cash generated from operating activities before net interest expense, non-controlling interest, income taxes, and working capital adjustments.

Comparable operating income and EBITDA also include the dividend income from the preferred share investment in the Wyoming Wind Farm. The dividend income is used as a proxy for the operating income and EBITDA of Wyoming Wind.

A reconciliation of comparable results to reported results is as follows:

	3 months ended March 31, 2014		
	Reported	Comparable adjustments	Comparable total
Revenues	67,965	-	67,965
Royalties and other	3,999	-	3,999
<b>Gross margin</b>	<b>63,966</b>	-	<b>63,966</b>
Operations, maintenance, and administration	10,864	-	10,864
Taxes, other than income taxes	1,805	-	1,805
Dividend income from investment in preferred shares	-	(4,365) <sup>(1)</sup>	(4,365)
<b>Earnings before interest, taxes, depreciation, and amortization</b>	<b>51,297</b>	<b>4,365</b>	<b>55,662</b>
Depreciation and amortization	18,139	-	18,139
<b>Operating income</b>	<b>33,158</b>	<b>4,365</b>	<b>37,523</b>
Foreign exchange loss	(76)	-	(76)
<b>Earnings before interest and taxes</b>	<b>33,082</b>	<b>4,365</b>	<b>37,447</b>
Dividend income from investment in preferred shares	(4,365)	4,365	-
Net interest expense	9,263	-	9,263
Income tax expense	5,891	-	5,891
<b>Net earnings</b>	<b>22,293</b>	-	<b>22,293</b>
Non-controlling interest	1,159	-	1,159
<b>Net earnings attributable to TransAlta Renewables common shareholders</b>	<b>21,134</b>	-	<b>21,134</b>
Weighted average number of common shares outstanding in the period (millions)	114.7	-	114.7
<b>Net earnings per share attributable to common shareholders</b>	<b>0.18</b>	-	<b>0.18</b>

	3 months ended March 31, 2013		
	Reported	Comparable adjustments	Comparable total
Revenues	60,917	-	60,917
Royalties and other	3,560	-	3,560
<b>Gross margin</b>	<b>57,357</b>	-	<b>57,357</b>
Operations, maintenance, and administration	9,174	-	9,174
Taxes, other than income taxes	1,799	-	1,799
<b>Earnings before interest, taxes, depreciation, and amortization</b>	<b>46,384</b>	-	<b>46,384</b>
Depreciation and amortization	18,910	-	18,910
<b>Operating income</b>	<b>27,474</b>	-	<b>27,474</b>
Foreign exchange loss	(760)	-	(760)
<b>Earnings before interest and taxes</b>	<b>26,714</b>	-	<b>26,714</b>
Net interest expense	7,289	-	7,289
Income tax expense	4,802	-	4,802
<b>Net earnings</b>	<b>14,623</b>	-	<b>14,623</b>
Non-controlling interest	619	-	619
<b>Net earnings attributable to TransAlta Renewables common shareholders</b>	<b>14,004</b>	-	<b>14,004</b>
Weighted average number of common shares outstanding in the period (millions)	114.7	-	114.7
<b>Net earnings per share attributable to common shareholders</b>	<b>0.12</b>	-	<b>0.12</b>

(1) The dividend income is used as a proxy for the operating income and EBITDA of Wyoming Wind.

### ***Funds from Operations***

Presenting FFO from period to period provides management and investors with a proxy for the amount of cash generated from operating activities, before changes in working capital, and provides the ability to evaluate cash flow trends more readily in comparison with results from prior periods.

	<b>3 months ended March 31</b>	
	<b>2014</b>	<b>2013</b>
Cash flow from operating activities	<b>45,210</b>	53,228
Change in non-cash operating working capital balances	<b>1,144</b>	(14,037)
<b>Funds from operations</b>	<b>46,354</b>	39,191
Weighted average number of common shares outstanding in the period (millions)	<b>114.7</b>	114.7
<b>Funds from operations per share</b>	<b>0.40</b>	0.34

### ***Cash Available for Distribution***

Cash available for distribution represents the amount of cash generated from operations by our business, before changes in working capital that is available to invest in growth initiatives, make principal repayments of debt, pay additional common share dividends, or repurchase common shares. Changes in working capital are excluded so as not to distort free cash flow with changes that we consider temporary in nature, reflecting, among other things, the impact of seasonal factors and the timing of capital projects.

Sustaining capital and productivity expenditures for the three months ended March 31, 2014 represent total additions to PP&E and intangibles per the Condensed Consolidated Statements of Cash Flows less nil (March 31, 2013 - \$28.3 million) that we have invested in growth projects.

The reconciliation between cash flow from operating activities and cash available for distribution is outlined below:

	<b>3 months ended March 31</b>	
	<b>2014</b>	<b>2013</b>
Cash flow from operating activities	<b>45,210</b>	53,228
Add (deduct):		
Changes in non-cash operating working capital	<b>1,144</b>	(14,037)
Sustaining capital and productivity expenditures	<b>(808)</b>	(1,089)
Distributions paid to subsidiaries' non-controlling interest	<b>(1,436)</b>	(1,200)
Principal repayments of debt	<b>(27,275)</b>	-
<b>Cash available for distribution</b>	<b>16,835</b>	36,902
Weighted average number of common shares outstanding in the period (millions)	<b>114.7</b>	114.7
<b>Cash available for distribution per share</b>	<b>0.15</b>	0.32

We seek to maintain sufficient cash balances and working capital credit facilities to fund periodic net cash outflows related to our business.

## CURRENT ACCOUNTING CHANGES

On Jan. 1, 2014, we adopted the amended disclosure requirements of IAS 36 *Impairment of Assets*. The amended disclosure requirements did not have an impact on the condensed consolidated financial statements.

## FUTURE ACCOUNTING CHANGES

Accounting standards that have been previously issued by the IASB but are not yet effective, and have not been applied by the Corporation include IFRS 9 *Financial Instruments*. In February 2014, the IASB indicated that IFRS 9 will be effective for annual periods beginning on or after Jan. 1, 2018. The Corporation continues to assess the impact of adopting this standard. Please refer to our Future Accounting Changes section on our most recent Annual MD&A for more information.

## SELECTED QUARTERLY INFORMATION

	Q2 2013	Q3 2013	Q4 2013	Q1 2014
Revenue	70,940	43,535	69,949	67,965
Net earnings attributable to common shareholders	19,512	1,207	15,535	21,134
Net earnings per share attributable to common shareholders, basic and diluted	0.17	0.01	0.13	0.18
Comparable earnings per share	0.17	0.03	0.15	0.18

	Q2 2012	Q3 2012	Q4 2012	Q1 2013
Revenue	48,099	41,896	67,344	60,917
Net earnings (loss) attributable to common shareholders	(6,845)	2,812	18,522	14,004
Net earnings (loss) per share attributable to common shareholders, basic and diluted	(0.06)	0.02	0.16	0.12
Comparable earnings per share	0.03	0.02	0.16	0.12

Basic and diluted earnings per share ("EPS") attributable to common shareholders and comparable EPS are calculated each period using the weighted average common shares outstanding during the period. As a result, the sum of the EPS for the four quarters making up the calendar year may sometimes differ from the annual EPS.

## FORWARD-LOOKING STATEMENTS

This MD&A, the documents incorporated herein by reference, and other reports and filings made with the securities regulatory authorities include forward-looking statements. All forward-looking statements are based on our beliefs as well as assumptions based on information available at the time the assumption was made and on management's experience and perception of historical trends, current conditions, and expected future developments, as well as other factors deemed appropriate in the circumstances. Forward-looking statements are not facts, but only predictions and generally can be identified by the use of statements that include phrases such as "may", "will", "believe", "expect", "anticipate", "intend", "plan", "foresee", "potential", "enable", "continue", or other comparable terminology. These statements are not guarantees of our future performance and are subject to risks, uncertainties, and other important factors that could cause our actual performance to be materially different from that projected.



In particular, this MD&A contains forward-looking statements pertaining to our business and anticipated financial performance including, but not limited to, for example: spend on growth and sustaining capital and productivity projects; expectations in terms of the cost of operations, capital spend, and maintenance, and the variability of those costs; expectations related to future earnings and cash flow from operating and contracting activities; the anticipated impact of our economic interest in the Wyoming Wind Farm on cash available for distribution; the payment of future dividends; expectations for demand for electricity in both the short term and long term, and the resulting impact on electricity prices; expectations in respect of generation availability, capacity, and production; expected financing of our capital expenditures; expected governmental regulatory regimes and legislation and their expected impact on us, as well as the cost of complying with resulting regulations and laws; estimates of future tax rates, future tax expense, and the adequacy of tax provisions; accounting estimates; anticipated growth rates in our markets; expectations for the outcome of existing or potential legal and contractual claims; expectations for the ability to access capital markets at reasonable terms; the estimated impact of changes in interest rates and the value of the Canadian dollar relative to the U.S. dollar; the monitoring of our exposure to liquidity risk; expectations regarding entering into additional financial instruments; expectations in respect to the global economic environment; estimated cash flow required to settle decommissioning and restoration activities; and expectations regarding borrowing rates and our credit practices.

Factors that may adversely impact our forward-looking statements include risks relating to: changes in general economic conditions including interest rates; operational risks involving our facilities, including unplanned outages at such facilities; disruptions in the transmission and distribution of electricity; the effects of weather; disruptions in the source of water or wind required to operate our facilities; natural disasters; the threat of domestic terrorism, cyber-attacks and other man-made disasters; equipment failure and our ability to carry out repairs in a cost-effective or timely manner; industry risk and competition; fluctuations in the value of foreign currencies; the need for additional financing; structural subordination of securities; counterparty credit risk; insurance coverage; our provision for income taxes; legal and contractual proceedings involving the Corporation; reliance on key personnel; the regulatory and political environments in the jurisdictions in which we operate; environmental requirements and changes in, or liabilities under, these requirements; and development projects and acquisitions. The foregoing risk factors, among others, are described in further detail in the Risk Factors section of our 2014 AIF for the year ended Dec. 31, 2013 and our 2013 Annual MD&A, both available on SEDAR at [www.sedar.com](http://www.sedar.com).

Readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on these forward-looking statements. The forward-looking statements included in this document are made only as of the date hereof and we do not undertake to publicly update these forward-looking statements to reflect new information, future events or otherwise, except as required by applicable laws. In light of these risks, uncertainties, and assumptions, the forward-looking events might occur to a different extent or at a different time than we have described, or might not occur. We cannot assure that projected results or events will be achieved.

**TRANSALTA RENEWABLES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS**  
*(in thousands of Canadian dollars, except as otherwise noted)*

Unaudited	3 months ended March 31	
	2014	2013
Revenues	54,089	53,001
Government incentives	6,546	6,738
Lease revenue	7,330	1,178
<b>Total revenue</b>	<b>67,965</b>	<b>60,917</b>
Royalties and other	3,999	3,560
<b>Gross margin</b>	<b>63,966</b>	<b>57,357</b>
Operations, maintenance, and administration	10,864	9,174
Depreciation and amortization	18,139	18,910
Taxes, other than income taxes	1,805	1,799
<b>Operating income</b>	<b>33,158</b>	<b>27,474</b>
Dividend income from investment in preferred shares <i>(Note 8)</i>	4,365	-
Net interest expense <i>(Note 3)</i>	(9,263)	(7,289)
Foreign exchange loss	(76)	(760)
<b>Earnings before income taxes</b>	<b>28,184</b>	<b>19,425</b>
Income tax expense <i>(Note 4)</i>	5,891	4,802
<b>Net earnings</b>	<b>22,293</b>	<b>14,623</b>
<b>Net earnings attributable to:</b>		
Common shareholders	21,134	14,004
Non-controlling interest <i>(Note 5)</i>	1,159	619
	<b>22,293</b>	<b>14,623</b>
<b>Weighted average number of common shares</b>		
<b>outstanding in the period</b> <i>(millions)</i> <i>(Note 10)</i>	<b>114.7</b>	<b>114.7</b>
<b>Net earnings per share attributable to common</b>		
<b>shareholders, basic and diluted</b> <i>(Note 10)</i>	<b>0.18</b>	<b>0.12</b>

See accompanying notes.

**TRANSALTA RENEWABLES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(in thousands of Canadian dollars)

Unaudited	3 months ended March 31	
	2014	2013
<b>Net earnings</b>	<b>22,293</b>	14,623
Gains (losses) on derivatives designated as cash flow hedges, net of tax <sup>(1)</sup>	60	(112)
Reclassification of losses on derivatives designated as cash flow hedges to non-financial assets, net of tax <sup>(2)</sup>	-	1,266
<b>Total items that will not be reclassified subsequently to net earnings</b>	<b>60</b>	1,154
Gains on derivatives designated as cash flow hedges, net of tax <sup>(3)</sup>	597	119
Reclassification of gains on derivatives designated as cash flow hedges to net earnings, net of tax <sup>(4)</sup>	(629)	(295)
<b>Total items that will be reclassified subsequently to net earnings</b>	<b>(32)</b>	(176)
<b>Other comprehensive income</b>	<b>28</b>	978
<b>Total comprehensive income</b>	<b>22,321</b>	15,601
<b>Total comprehensive income attributable to:</b>		
Common shareholders	21,162	14,982
Non-controlling interest (Note 5)	1,159	619
	<b>22,321</b>	15,601

(1) Net of income tax expense of 20 for the three months ended March 31, 2014 (2013 - 37 recovery).

(2) Net of income tax of nil for the three months ended March 31, 2014 (2013 - 422 recovery).

(3) Net of income tax expense of 208 for the three months ended March 31, 2014 (2013 - 40 expense).

(4) Net of income tax expense of 217 for the three months ended March 31, 2014 (2013 - 168 expense).

See accompanying notes.

**TRANSALTA RENEWABLES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
*(in thousands of Canadian dollars)*

Unaudited	March 31, 2014	Dec. 31, 2013
Cash and cash equivalents	11,945	19,256
Accounts receivable	34,084	37,413
Prepaid expenses	4,205	2,375
Risk management assets <i>(Note 6)</i>	744	22
Inventory	40	140
	<b>51,018</b>	<b>59,206</b>
Property, plant, and equipment <i>(Note 7)</i>		
Cost	2,023,762	2,021,386
Accumulated depreciation	(330,604)	(314,387)
	<b>1,693,158</b>	<b>1,706,999</b>
Intangible assets	103,522	105,284
Risk management assets <i>(Note 6)</i>	11	14
Other assets	3,042	3,059
Investment in preferred shares <i>(Note 8)</i>	113,682	109,325
Deferred income tax assets	30,530	29,751
<b>Total assets</b>	<b>1,994,963</b>	<b>2,013,638</b>
Bank overdraft	-	891
Accounts payable and accrued liabilities	27,930	31,267
Risk management liabilities <i>(Note 6)</i>	54	73
Income taxes payable	345	364
Dividends payable <i>(Note 10)</i>	14,714	29,239
Current portion of deferred revenue	425	425
Current portion of long-term debt <i>(Note 9)</i>	56,993	37,596
	<b>100,461</b>	<b>99,855</b>
Long-term debt <i>(Note 9)</i>	605,524	646,619
Decommissioning provisions	14,647	12,410
Deferred revenues	6,871	6,977
Deferred income tax liabilities	186,761	180,651
Risk management liabilities <i>(Note 6)</i>	112	67
<b>Total liabilities</b>	<b>914,376</b>	<b>946,579</b>
<b>Equity</b>		
Common shares <i>(Note 10)</i>	1,223,845	1,223,845
Deficit	(182,486)	(196,263)
Accumulated other comprehensive income	215	187
<b>Equity attributable to shareholders</b>	<b>1,041,574</b>	<b>1,027,769</b>
Non-controlling interest <i>(Note 5)</i>	39,013	39,290
<b>Total equity</b>	<b>1,080,587</b>	<b>1,067,059</b>
<b>Total liabilities and equity</b>	<b>1,994,963</b>	<b>2,013,638</b>

Contingencies *(Note 11)*.

Subsequent events *(Note 14)*.

See accompanying notes.

**TRANSALTA RENEWABLES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
*(in thousands of Canadian dollars)*

Unaudited	Common shares	Deficit	Accumulated other comprehensive income	Attributable to shareholders	Attributable to non-controlling interest	Total
Balance, Dec. 31, 2013	1,223,845	(196,263)	187	1,027,769	39,290	1,067,059
Net earnings	-	21,134	-	21,134	1,159	<b>22,293</b>
Other comprehensive income:						
Net gains on derivatives designated as cash flow hedges, net of tax	-	-	28	28	-	<b>28</b>
Total comprehensive income	-	21,134	28	21,162	1,159	<b>22,321</b>
Common share dividends (Note 10)	-	(7,357)	-	(7,357)	-	<b>(7,357)</b>
Distributions to non-controlling interest	-	-	-	-	(1,436)	<b>(1,436)</b>
<b>Balance, March 31, 2014</b>	<b>1,223,845</b>	<b>(182,486)</b>	<b>215</b>	<b>1,041,574</b>	<b>39,013</b>	<b>1,080,587</b>

See accompanying notes.

Unaudited	Net parental investment	Accumulated other comprehensive income (loss)	Total net parental investment	Attributable to non-controlling interest	Total
Balance, Dec. 31, 2012	1,660,166	(970)	1,659,196	40,416	1,699,612
Net earnings	14,004	-	14,004	619	14,623
Other comprehensive income:					
Net gains on derivatives designated as cash flow hedges, net of tax	-	978	978	-	978
Total comprehensive income	14,004	978	14,982	619	15,601
Net transfers to Parent	(21,000)	-	(21,000)	-	(21,000)
Distributions to non-controlling interest	-	-	-	(1,200)	(1,200)
Balance, March 31, 2013	1,653,170	8	1,653,178	39,835	1,693,013

See accompanying notes.

**TRANSALTA RENEWABLES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands of Canadian dollars)

Unaudited	3 months ended March 31	
	2014	2013
<b>Operating activities</b>		
Net earnings	22,293	14,623
Depreciation and amortization	18,139	18,910
Accretion of provisions (Note 3)	220	198
Deferred income tax expense (Note 4)	5,319	4,802
Unrealized foreign exchange loss	60	491
Unrealized (gain) loss from risk management activities	46	(128)
Deferred credits	-	(91)
Other non-cash items	277	386
Cash flow from operations before changes in working capital	46,354	39,191
Change in non-cash operating working capital balances	(1,144)	14,037
<b>Cash flow from operating activities</b>	<b>45,210</b>	<b>53,228</b>
<b>Investing activities</b>		
Additions to property, plant, and equipment (Note 7)	(832)	(29,285)
Additions to intangibles	-	(122)
Proceeds on sale of assets	312	-
Change in other assets	-	273
Realized risk management gain	100	2,278
Change in non-cash investing working capital balances	(632)	(10,495)
<b>Cash flow used in investing activities</b>	<b>(1,052)</b>	<b>(37,351)</b>
<b>Financing activities</b>		
Repayment of net parental investment and related party advances	-	(15,910)
Long-term debt repayments	(27,275)	-
Dividends paid on common shares (Note 10)	(21,881)	-
Distributions to non-controlling interest (Note 5)	(1,436)	(1,200)
<b>Cash flow used in financing activities</b>	<b>(50,592)</b>	<b>(17,110)</b>
<b>Decrease in cash and cash equivalents</b>	<b>(6,434)</b>	<b>(1,233)</b>
<b>Effect of translation on foreign currency cash</b>	<b>14</b>	<b>-</b>
<b>Decrease in cash and cash equivalents</b>	<b>(6,420)</b>	<b>(1,233)</b>
<b>Cash and cash equivalents, net of bank overdraft, beginning of period</b>	<b>18,365</b>	<b>3,205</b>
<b>Cash and cash equivalents, end of period</b>	<b>11,945</b>	<b>1,972</b>
Cash income taxes paid	592	181
Cash interest paid	7,208	8,793

See accompanying notes.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Tabular amounts in thousands of Canadian dollars, except as otherwise noted)

### 1. BACKGROUND AND ACCOUNTING POLICIES

#### A. Formation of the Corporation

TransAlta Renewables Inc. (the "Corporation" or "TransAlta Renewables") was incorporated on May 28, 2013 under the *Canada Business Corporations Act* and was formed to own a portfolio of renewable power generation facilities. The Corporation had no active operations from the date of incorporation until Aug. 9, 2013, when it indirectly acquired 28 wind and hydroelectric ("hydro") generating assets (the "Acquired Assets") from TransAlta Corporation ("TransAlta" or the "Parent") (the "Acquisition") and completed an initial public offering of 22.1 million common shares. Information regarding the Acquisition and initial public offering can be found in Note 4 of the Corporation's most recent annual consolidated financial statements.

#### B. Basis of Preparation

These unaudited interim condensed consolidated financial statements have been prepared by management in compliance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting* using the same accounting policies as those used in the Corporation's most recent annual consolidated financial statements, except as outlined in Note 2(A). These unaudited interim condensed financial statements do not include all of the disclosures included in the Corporation's annual consolidated financial statements. Accordingly, these should be read in conjunction with the Corporation's most recent annual consolidated financial statements which are available on SEDAR at [www.sedar.com](http://www.sedar.com).

The unaudited interim condensed consolidated financial statements include the accounts of the Corporation and the subsidiaries that it controls.

The unaudited interim condensed consolidated financial statements have been prepared on a historical cost basis, except for derivative financial instruments, which are stated at fair value.

The unaudited interim condensed consolidated financial statements reflect all adjustments that consist of normal recurring adjustments and accruals that are, in the opinion of management, necessary for a fair presentation of results. The Corporation's results are partly seasonal due to the nature of electricity, which cannot be stored; and the nature of wind and run-of-river hydro resources, which fluctuate based on both seasonal patterns and annual weather variation. Typically, run-of-river hydro facilities generate most of their electricity and revenues during the spring and summer months when the melting snow starts feeding the watersheds and the rivers. Inversely, wind speeds are historically greater during the cold winter months when the air density is at its peak.

These unaudited interim condensed consolidated financial statements were authorized for issue by the Board of Directors on May 1, 2014.

### **C. Use of Estimates**

The preparation of these condensed consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") requires management to use judgment and make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the period. These estimates are subject to uncertainty. Actual results could differ from these estimates due to factors such as fluctuations in interest rates, foreign exchange rates, inflation and commodity prices, and changes in economic conditions, legislation, and regulations. Refer to Note 2(P) of the Corporation's most recent annual consolidated financial statements for a more detailed discussion of the significant accounting judgments and key sources of estimation uncertainty.

### **D. Basis of Preparation Prior to the Acquisition**

The unaudited interim condensed consolidated financial statements for the March 31, 2013 comparative period include the combined financial statements of the Acquired Assets, as the Acquired Assets are ultimately controlled by TransAlta before and after the Acquisition and there has been no substantive change in operations.

Historically, financial statements have not been prepared by TransAlta for the Acquired Assets as they had not been operated as a separate business by TransAlta. Accordingly, the financial statements for periods prior to the Acquisition reflect the financial statements for the Acquired Assets in a manner consistent with how TransAlta managed the Acquired Assets and as though the Acquired Assets had been a separate Corporation. All material assets and liabilities specifically identified to the Acquired Assets and all material revenues and expenses specifically attributable to the Acquired Assets and allocations of overhead expenses have been presented in the financial statements for periods prior to the Acquisition. The financial statements for periods prior to the Acquisition may not necessarily reflect the financial position, results of operations, or cash flows that the Acquired Assets might have had in the past had they existed as a separate business during the periods prior to the Acquisition (see Note 13).

## **2. ACCOUNTING CHANGES**

### **A. Adoption of New or Amended IFRS**

On Jan. 1, 2014, the Corporation adopted the amended disclosure requirements of IAS 36 *Impairment of Assets*. The change did not impact disclosures presented in this period.

### **B. Comparative Figures**

Certain comparative figures have been reclassified to conform to the current period's presentation. These reclassifications did not impact previously reported net earnings.

### **C. Future Accounting Changes**

Accounting standards that have been previously issued by the IASB but are not yet effective, and have not been applied by the Corporation include IFRS 9 *Financial Instruments*. In February 2014, the IASB indicated that IFRS 9 will be effective for annual periods beginning on or after Jan. 1, 2018. The Corporation continues to assess the impact of adopting this standard.



### 3. NET INTEREST EXPENSE

The components of net interest expense are as follows:

	3 months ended March 31	
	2014	2013
Interest on long-term debt	9,025	7,702
Interest on letters of credit and guarantees pledged by TransAlta	21	1,540
Capitalized interest	-	(2,147)
Interest income	(3)	(4)
<b>Interest expense</b>	<b>9,043</b>	<b>7,091</b>
Accretion of provisions	220	198
<b>Net interest expense</b>	<b>9,263</b>	<b>7,289</b>

### 4. INCOME TAXES

The components of income tax expense are as follows:

	3 months ended March 31	
	2014	2013
Current income tax expense	572	-
Adjustments in respect of deferred income tax of for previously unrecognized tax loss, tax credit or temporary difference of a prior period	93	-
Deferred income tax expense related to the origination and reversal of temporary differences	5,226	4,802
<b>Income tax expense</b>	<b>5,891</b>	<b>4,802</b>

Presented in the Condensed Consolidated Statements of Earnings as follows:

	3 months ended March 31	
	2014	2013
Current income tax expense	572	-
Deferred income tax expense	5,319	4,802
<b>Income tax expense</b>	<b>5,891</b>	<b>4,802</b>

## 5. NON-CONTROLLING INTEREST

The non-controlling interest in the Corporation's operations is comprised of a 17% interest in the Kent Hills wind farm.

Summarized financial information relating to the Kent Hills wind farm is as follows:

	3 months ended March 31	
	2014	2013
<b>Results of operations</b>		
Revenues	10,839	7,702
Net earnings and total comprehensive income	6,818	3,656

As at	March 31, 2014	Dec. 31, 2013
<b>Financial position</b>		
Current assets	6,193	5,708
Long-term assets	225,134	227,256
Current liabilities	(1,360)	(1,435)
Long-term liabilities	(474)	(414)
Total equity	(229,493)	(231,115)

## 6. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### A. Financial Assets and Liabilities – Measurement

Financial assets and financial liabilities are measured on an ongoing basis at fair value or amortized cost.

### B. Fair Value of Financial Instruments

#### I. Financial Instruments – Measured at Fair Value

During the three months ended March 31, 2014, the net risk management position has gone from a net liability of \$0.1 million to a net asset of \$0.6 million, principally as a result of the appreciation of the hedge on foreign-denominated debt. The change has been recognized in other comprehensive income.

The hedge on foreign-denominated debt is classified as a Level II fair value measurement, for which the Corporation uses observable inputs other than unadjusted quoted prices that are observable for the financial instrument, such as credit valuation adjustments and currency rates.

## II. Financial Instruments – Not Measured at Fair Value

The fair value of long-term debt is as follows:

	Fair value				Total carrying value
	Level I	Level II	Level III	Total	
Long-term debt <sup>(1)</sup> - March 31, 2014	-	688,207	-	688,207	662,517
Long-term debt <sup>(1)</sup> - Dec. 31, 2013	-	700,723	-	700,723	684,215

(1) Includes current portion

The fair value of the Corporation's debentures is determined using prices observed in secondary markets. The fair value of other long-term debt is determined by calculating an implied price based on a current assessment of the yield to maturity.

The book value of other short-term financial assets and liabilities (cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and dividends payable) approximates fair value due to the liquid nature of the asset or liability.

## C. Nature and Extent of Risks Arising from Financial Instruments and Derivatives

The following discussion is limited to specific risk measures, which are more fully discussed in Note 13(C) of the most recent annual consolidated financial statements.

### I. Credit Risk

The Corporation's maximum exposure to credit risk at March 31, 2014, without taking into account collateral held or right of set-off, is represented by the current carrying amounts of accounts receivable and risk management assets as per the Condensed Consolidated Statements of Financial Position.

The Corporation uses external credit ratings, as well as internal ratings in circumstances where external ratings are not available, to establish credit limits for counterparties. As at March 31, 2014, significantly all of the Corporation's counterparties were considered investment grade.

At March 31, 2014, the Corporation had two unrelated customers whose outstanding balances each accounted for greater than 10 per cent of the total trade receivables outstanding. The Corporation has evaluated the risk of default related to these customers to be minimal.

### II. Liquidity Risk

The following table presents the contractual maturities of the Corporation's financial liabilities as at March 31, 2014:

	2014	2015	2016	2017	2018	2019 and thereafter	Total
Accounts payable and accrued liabilities	27,930	-	-	-	-	-	27,930
Long-term debt <sup>(1)</sup>	10,957	194,171	67,063	24,413	287,091	82,511	666,206
Net risk management (assets) liabilities	(689)	(7)	(2)	4	4	101	(589)
Interest on long-term debt <sup>(2)</sup>	23,467	29,514	22,407	20,076	12,341	5,889	113,694
<b>Total</b>	<b>61,665</b>	<b>223,678</b>	<b>89,468</b>	<b>44,493</b>	<b>299,436</b>	<b>88,501</b>	<b>807,241</b>

(1) Excludes impacts of derivatives.

(2) Not recognized as a financial liability on the Condensed Consolidated Statements of Financial Position.

## 7. PROPERTY, PLANT, AND EQUIPMENT

The changes in the cost of major categories of property, plant, and equipment and related accumulated depreciation are as follows:

	Hydro generation	Wind generation	Capital spares and other	Total
<b>Cost</b>				
As at Dec. 31, 2013	246,950	1,766,824	7,612	2,021,386
Additions	268	290	274	832
Disposals	(38)	(435)	-	(473)
Revisions and additions to decommissioning costs	1,274	743	-	2,017
<b>As at March 31, 2014</b>	<b>248,454</b>	<b>1,767,422</b>	<b>7,886</b>	<b>2,023,762</b>
<b>Accumulated depreciation</b>				
As at Dec. 31, 2013	51,314	263,073	-	314,387
Depreciation	1,772	14,501	-	16,273
Disposals	(35)	(21)	-	(56)
<b>As at March 31, 2014</b>	<b>53,051</b>	<b>277,553</b>	<b>-</b>	<b>330,604</b>
<b>Carrying amount</b>				
As at Dec. 31, 2013	195,636	1,503,751	7,612	1,706,999
<b>As at March 31, 2014</b>	<b>195,403</b>	<b>1,489,869</b>	<b>7,886</b>	<b>1,693,158</b>

## 8. INVESTMENT IN PREFERRED SHARES

The investment in preferred shares as at March 31, 2014 and Dec. 31, 2013 is comprised of the U.S.\$102.7 million investment in Class A preferred shares of a subsidiary of TransAlta, and represents the Corporation's economic interest in the Wyoming Wind Farm.

Dividend income from the investment in preferred shares is recognized when dividends are declared. Monthly declarations of dividends track pre-tax earnings of the Wyoming wind farm. Dividends received are recognized in cash flows from operating activities in the Condensed Consolidated Statements of Cash Flows.

## 9. LONG-TERM DEBT

### A. Amounts Outstanding

As at	March 31, 2014			Dec. 31, 2013		
	Carrying value	Face value	Interest <sup>(1)</sup>	Carrying value	Face value	Interest <sup>(1)</sup>
Unsecured debentures <sup>(2)</sup>	342,079	345,628	5.91%	340,866	344,780	5.91%
Secured debenture	34,860	35,000	5.28%	34,821	35,000	5.28%
Amortizing term loan	189,321	189,321	4.00%	200,000	200,000	4.00%
Wyoming Wind Acquisition Loan <sup>(3)</sup>	96,257	96,257	4.00%	108,528	108,528	4.00%
	662,517	666,206		684,215	688,308	
Less: current portion	(56,993)	(56,993)		(37,596)	(37,596)	
<b>Total long-term debt</b>	<b>605,524</b>	<b>609,213</b>		<b>646,619</b>	<b>650,712</b>	

(1) Interest rate reflects the stipulated rate or the average rate weighted by principal amounts outstanding.

(2) Includes U.S.\$20 million (2013 - U.S.\$20 million).

(3) U.S.\$87.0 million (2013 - U.S.\$102.0 million).

The Corporation has a \$100.0 million working capital credit facility with TransAlta. As at March 31, 2014 and Dec.31, 2013 no amounts were drawn on this facility.

### B. Restrictions

Unsecured debentures include restrictive covenants requiring the proceeds received from the sale of certain assets to be reinvested into similar renewable assets.

## 10. COMMON SHARES

### A. Authorized and Outstanding

The Corporation is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. The common shares entitle the holders thereof to one vote per share at meetings of shareholders. The preferred shares are issuable in series and have such rights, restrictions, conditions, and limitations as the Board of Directors (the "Board") may from time to time determine. No preferred shares have been issued.

The Corporation has 114.7 million issued and outstanding common shares as at March 31, 2014 and Dec. 31, 2013.

## B. Dividends

The declaration of dividends on the Corporation's common shares is at the discretion of the Board.

The following table summarizes the common share dividends declared and paid or payable within the three months ended March 31, 2014:

<b>Date declared</b>	<b>Payment date</b>	<b>Dividend per share (\$)</b>	<b>Total dividends</b>	<b>TransAlta</b>	<b>Other shareholders</b>
Oct. 29, 2013	Jan. 31, 2014	0.06250	7,167	5,786	1,381
Dec. 20, 2013	Feb. 28, 2014	0.06416	7,357	5,938	1,419
Dec. 20, 2013	Mar. 28, 2014	0.06416	7,357	5,938	1,419
Dec. 20, 2013	Apr. 30, 2014	0.06416	7,357	5,938	1,419
Feb. 13, 2014	May 30, 2014	0.06416	7,357	5,938	1,419

## C. Earnings per Share

Basic earnings per share is based on net earnings attributable to the common shareholders and is calculated based upon the weighted average number of common shares outstanding during the periods presented. For comparative purposes, the Corporation's common shares issued under its initial public offering have been assumed to be outstanding as of the beginning of each period presented. The Corporation has no dilutive or potentially dilutive instruments.

## 11. CONTINGENCIES

### Litigation

In the normal course of business, the Corporation may become party to litigation claims. There are currently no known claims that the Corporation has determined as significant enough to require disclosure.

## 12. RELATED PARTY TRANSACTIONS AND BALANCES

Prior to the Aug. 9, 2013 acquisition of the Acquired Assets and separation of TransAlta Renewables as a stand-alone public entity, the Acquired Assets were historically managed and operated in the normal course of business by TransAlta along with other TransAlta operations and affiliates and not as a separate business.

After the Acquisition, the Corporation entered into certain agreements and transactions with TransAlta which are discussed in more detail in Note 27 of the Corporation's most recent annual consolidated financial statements.

### A. Related Party Transactions

Related party transactions include the dividend income from the investment in preferred shares, as well as the interest on letters of credit and guarantees pledged by TransAlta disclosed in Note 9.

Significant related party transactions that are not otherwise presented elsewhere consist of the following:

	<b>3 months ended March 31</b>	
	<b>2014</b>	2013
Revenue from TransAlta PPAs	7,951	-
G&A Reimbursement Fee	2,523	-
Interest expense on amortizing term loan	1,914	-
Interest expense on Wyoming Wind Acquisition Loan	1,135	-

All of these transactions are with TransAlta or subsidiaries of TransAlta.

#### **B. Related Party Balances**

Related party balances include the investment in preferred shares, the risk management assets and liabilities, as well as the amortizing term loan, Wyoming Wind Acquisition Loan, and credit facility disclosed in Note 9.

Significant related party balances that are not otherwise presented elsewhere consist of the following:

<b>As at</b>	<b>March 31, 2014</b>	Dec. 31, 2013
Trade accounts receivable	5,212	10,232
Trade accounts payable	4,607	5,048
Dividends payable	11,876	23,600
Interest payable	1,038	3,311
Letters of credit issued by TransAlta on behalf of the Corporation	4,503	4,503
Guarantees provided by TransAlta on behalf of the Corporation	226,500	226,500

All of these balances are with TransAlta or subsidiaries of TransAlta.

### **13. PRE-ACQUISITION RELATIONSHIP WITH PARENT**

The Acquired Assets have historically been managed and operated in the normal course of business by TransAlta along with other TransAlta operations and affiliates. Financial statements for periods prior to Aug. 9, 2013 were not historically prepared for the Acquired Assets as they had not been operated as a separate business. Transactions between TransAlta and the Acquired Assets prior to the Acquisition have been identified as related party transactions in the pre-Acquisition period financial statements. See Note 28 of the Corporation's most recent annual consolidated financial statements for additional information on the relationship and transactions not discussed below:

#### **Allocation of Corporate Costs**

Certain shared costs were allocated to the Acquired Assets and reflected as expenses in the pre-Acquisition period financial statements. These allocated corporate costs include TransAlta charges for, but not limited to: corporate accounting, human resources, government affairs, information technology, shared real estate expenses, legal, treasury, and pension and other post-employment benefits. These costs are included in OM&A expenses. The costs were allocated to the Acquired Assets based on GWh of production. Note that these expenses may have been different had the Acquired Assets been a separate entity during the periods presented. For the comparative three months ended March 31, 2013, these pre-tax costs were \$1.4 million.

#### **14. SUBSEQUENT EVENTS**

##### *Secondary offering of TransAlta Renewables shares by TransAlta*

On April 29, 2014, TransAlta completed a secondary public offering of 11,950,000 common shares of the Corporation at a price of \$11.40 per common share. As a result of the offering, TransAlta now owns approximately 70.3 per cent of the common shares of TransAlta Renewables. The Corporation will not receive any of the proceeds from the sale of common shares, as these shares were owned and held by TransAlta.



## GLOSSARY OF KEY TERMS

**Amortizing Term Loan** - A \$200 million, unsecured, Amortizing Term Loan from TransAlta.

**Capacity** - The rated continuous load-carrying ability, expressed in megawatts, of generation equipment.

**Force Majeure** – Literally means “greater force”. A force majeure clause excuses a party from liability if an unforeseen event beyond the control of that party prevents it from performing its obligations under the contract.

**Gigawatt** - A measure of electric power equal to 1,000 megawatts.

**Gigawatt Hour (GWh)** - A measure of electricity consumption equivalent to the use of 1,000 megawatts of power over a period of one hour.

**Greenhouse Gas (GHG)** - Gases having potential to retain heat in the atmosphere, including water vapour, carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, and perfluorocarbons.

**Megawatt (MW)** - A measure of electric power equal to 1,000,000 watts.

**Megawatt Hour (MWh)** - A measure of electricity consumption equivalent to the use of 1,000,000 watts of power over a period of one hour.

**Net Maximum Capacity** - The maximum capacity or effective rating, modified for ambient limitations, that a generating unit or power plant can sustain over a specific period, less the capacity used to supply the demand of station service or auxiliary needs.

**PPA** – A power purchase and sale agreement between a power generator and a third party acquirer of electricity.

**Renewable Power** - Power generated from renewable terrestrial mechanisms including wind, hydro, geothermal, and solar with regeneration.

**Reserve Margin** – An indication of a market’s capacity to meet unusual demand or deal with unforeseen outages/shutdowns of generating capacity.

**TransAlta PPAs** – PPAs between TransAlta and the Corporation providing for the purchase by TransAlta, for a fixed price, all of the power produced by certain wind and hydro facilities. The price payable by TransAlta for output is \$30.00/MWh for wind facilities and \$45.00 per MWh for hydro facilities, which amounts are adjusted annually for changes in the Consumer Price Index.

**Unplanned Outage** - The shutdown of a generating unit due to an unanticipated breakdown.

**Working Capital Credit Facility** - A \$100 million unsecured working capital credit facility with TransAlta. The facility is available for general corporate purposes including financing ongoing working capital requirements.

**Wyoming Wind Acquisition Loan** – A U.S.\$102 million unsecured loan from TransAlta to fund the December, 2013 acquisition of the economic interest in the 144 MW wind farm in Wyoming.

**Wyoming Wind Preferred Shares** – A U.S.\$102.7 million investment in Class A Preferred Shares of a TransAlta subsidiary to acquire the economic interest in the 144 MW wind farm in Wyoming.

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**Ticker Symbol**

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