

Inter Pipeline Ltd. Security Analysis

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### **Introduction**

This report is intended to provide an analysis and recommendation of Inter Pipeline Ltd. (IPL) based in Canada. The report consists of five components: a market analysis, an analysis of IPL, forecast, valuation, and a recommendation. The market analysis section will focus on the pipeline industry, products provided by the industry, typical firm revenue and cost structure, typical firm strategies, and the regulatory environment. The analysis of IPL will focus on its business strategy and operations, the management team, and financial statements. The forecast section will focus on identifying value drivers of IPL and their future outlook. Additionally factors having an adverse effect on the future outlook will be discussed. The valuation section will focus on the approach, including all the factors considered and their weight, as well as the application of this approach. The recommendation will discuss the opinion and final decision of the author based on the material presented in the previous four sections.

## **Market Analysis**

### **The Pipeline Industry**

IPL is in the pipeline industry, which focuses on the transportation of liquid petroleum, natural gas, and liquid by-products of both commodities. Transportation is executed through pipelines which connect production areas with processing areas as well as end users (Canadian Energy Pipeline Association, 2014). In addition to the transportation role, firms in the pipeline industry may be involved in the gathering, processing, and storage of commodities, and fractionation. The pipeline industry itself is not involved in the exploration or production (with some exception for fractionation) of the commodities it transports. It is characterized by predictable revenue streams and cash flows, high barriers to entry including high capital expenditure requirements, and an interdependency on the oil and gas industry.

The interdependency on the oil and gas industry heavily affects the pipeline industry. To understand the structure and strategy in pipelines it is important to understand oil and gas. The oil and gas industry involves the exploration and production of crude oil and natural gas, along with their by-products. The oil and gas industry is divided into three streams: upstream involving exploration and production, midstream involving transportation and gathering, and downstream involving refining and retailing (American Petroleum Institute, 2014). The pipeline industry is in the midstream of this process, connecting producers to refineries. Oil and gas is driven heavily by demand in the global market which in turn drives the utilization of pipelines. Additional consequences of this interdependency will be discussed in detail further in this report.

In Canada there are nearly 115,000 KM of pipeline, a majority of which is heavily concentrated in Alberta and Saskatchewan. Natural gas pipelines are approximately 72,000 KM in length and transport 14.6 billion cubic feet per day and liquid petroleum pipelines are



approximately 38,000 KM in length and transport 3.2 million barrels per day. In 2012 the industry contributed \$8.8 billion, out of \$1.8 trillion (Government of Canada, 2014), to Canada's GDP, \$27 billion in taxes, \$1.9 billion in labour income, and provided 25,000 full time equivalent (FTE) positions (Canadian Energy Pipeline Association, 2014). Table 1 provides a detailed breakdown by province from the Canadian Energy Pipeline Association (CEPA).

	<b>British Columbia</b>	<b>Alberta</b>	<b>Saskatchewan</b>	<b>Manitoba</b>	<b>Ontario</b>	<b>Quebec</b>	<b>Other</b>
<b>Pipelines Operated</b>	9,000 KM	56,000 KM	27,000 KM	5,000 KM	15,000 KM	1,000 KM	2,000 KM
<b>GDP Contribution</b>	\$645 M	\$3,936 M	\$1,639 M	\$736 M	\$1,383 M	\$259 M	\$228 M
<b>Labour Income</b>	\$174 M	\$772 M	\$370 M	\$132 M	\$379 M	\$80 M	\$96 M
<b>Number of FTE Positions</b>	2,915	7,591	5,037	1,858	5,360	1,467	791

*Table 1 (Angevine Economic Consulting Ltd., 2013)*

Figures 1 and 2, on the next page, show the locations of Canadian liquid petroleum and natural gas pipelines. The majority of the Canadian oil and gas industry is located in Alberta with the second largest presence being in Saskatchewan. It is also evident that these pipelines extend well into the United States of America. In the United States there are multiple hubs from coast to coast. The major hubs, pictured in Figure 3, are PADD II – East (in Minneapolis, Illinois, Indiana, Ohio, Kentucky, and Tennessee) and PADD III – Gulf Coast. These figures display an additional interdependency between the United States and Canada as oil and gas partners, but IPL does not have pipelines in the United States, therefore this report will mainly focus on the Canadian market.

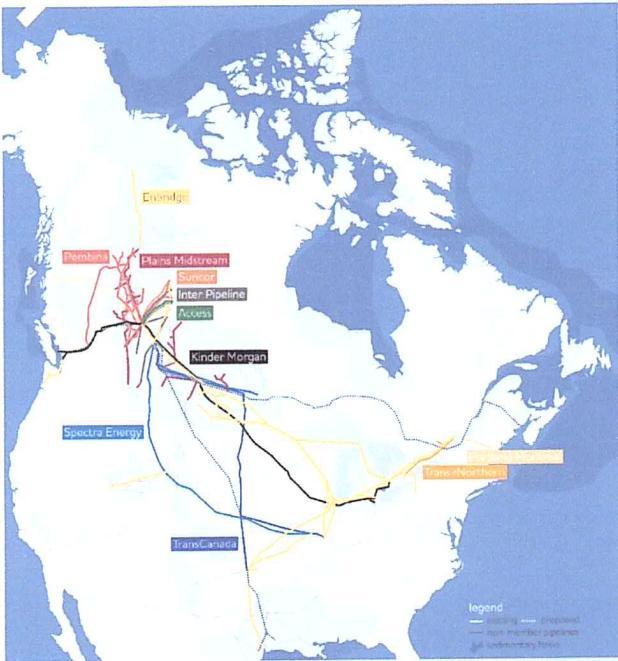


Figure 1 (Canadian Energy Pipeline Association, 2013)

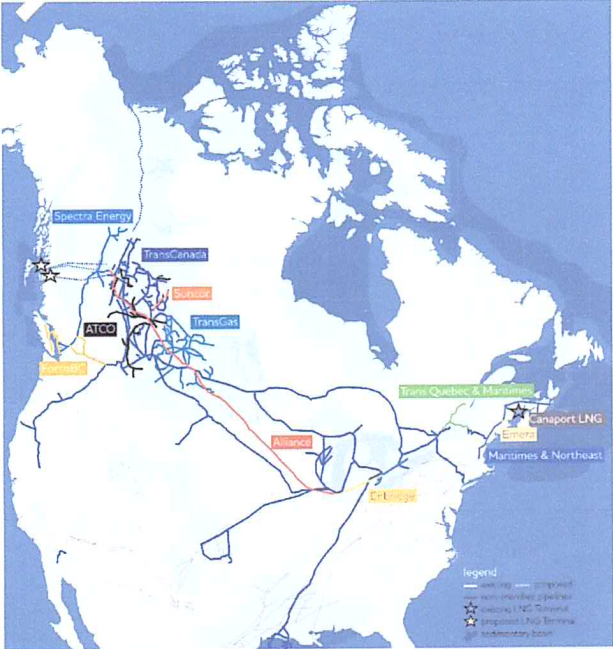


Figure 2 (Canadian Energy Pipeline Association, 2013)

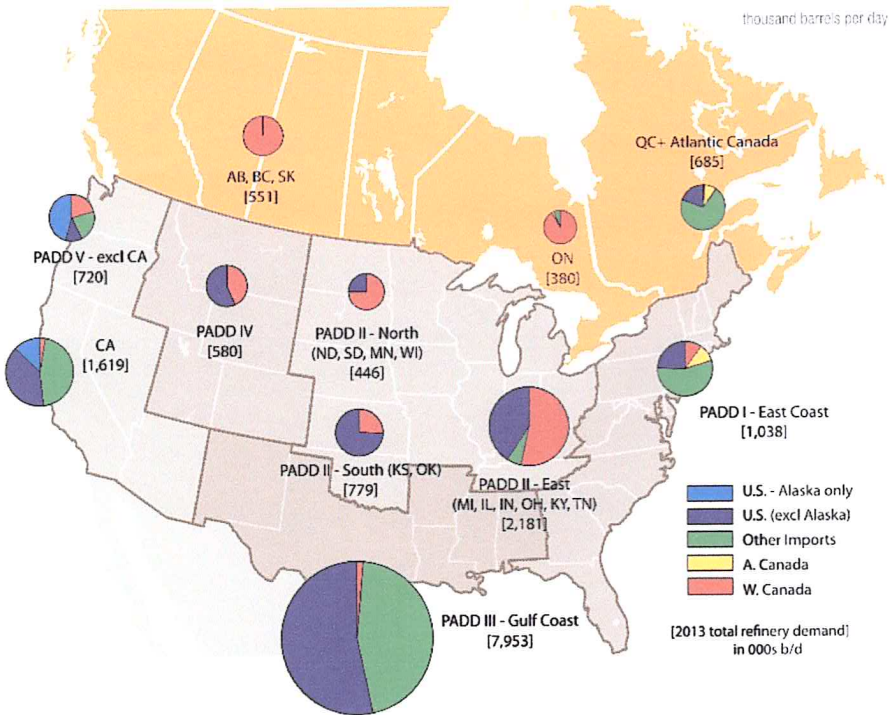


Figure 3 (Canadian Association of Petroleum Producers, 2014)

### **Pipeline Industry Services**

The main offering of the pipeline industry is the transportation service. Pipeline firms operate transport lines between producers, refineries, and end users. Within this network there are four main types of pipelines: gathering lines, feeder lines, transmission pipelines, and distribution pipelines. Gathering lines are short distance and move commodities from wells to processing facilities. Feeder lines act as a bridge between processing facilities and transmission pipelines. Transmission pipelines are extremely large scale and are the main transport route for commodities. Distribution pipelines stem from transmission pipelines and deliver commodities to local distributors (Canadian Energy Pipeline Association, 2014).

These four types of pipelines allow the industry to offer additional services. Gathering lines allow firms to gather commodities directly from wells, whereas normally the commodities would be brought to the transmission pipeline by the producer. Feeder lines allow for direct access from processing facilities but also for storage of commodities. Feeder lines also allow for processing to be carried out by the pipeline firm. A special form of processing, fractionation, utilizes separate facilities to separate natural gas liquids from natural gas. Fractionating is seeing a rise due to the favourable price of natural gas.

Before a firm is able to offer any services it must undergo the pipeline process which can be decomposed into three stages: design, construction, and operation. Design is the planning stage of the entire process. Engineering and environmental teams consult with other stakeholders to determine the pipeline's intended use, intended volumes, and proposed routes (Canadian Energy Pipeline Association, 2014). Two main factors considered are physical aspects, described earlier, and environmental aspects such as sensitive areas, proximity to communities, climate,



and geology (Canadian Energy Pipeline Association, 2014). This stage intends to maximize pipeline performance and safety while having a minimal negative impact on the environment and communities (Canadian Energy Pipeline Association, 2014).

The construction process involves three parts: pre-construction, construction, and post-construction. Pre-construction involves physical surveying and staking where sites are prepared for excavation as well as storage for construction personnel and materials. A right-of-way is then prepared by clearing trees along the designated pipeline path and a trench is dug for the placement of pipeline sections. Construction involves bending pipeline sections to fit the environment and welding them together. Anti-corrosion coats are added to the inside and outside of the pipes and the fixed pipeline is lowered into the trench. Valves and fittings are installed afterwards and the trench is backfilled with the soil removed initially during pre-construction. Post-construction involves testing of the pipeline's integrity for eight hours and a final clean-up to reclaim the environment (Canadian Energy Pipeline Association, 2014).

Transporting commodities from point A to point B involves very little work. Much of the operation stage is focused on surveillance and maintenance. Surveillance is carried out physically as well as through the use of Supervisory Control and Data Acquisition Systems to monitor the interior of pipelines. Tickets are used to track the actual commodities being transported. Tickets log identifying information such as the commodity, amount, origin, destination, and owner. Maintenance is carried out through routine inspections of surface level equipment. Pipelines are not dug up unless accidental damage has occurred due to unprepared digging or a natural disaster (Canadian Energy Pipeline Association, 2014).

Pipelines not only transport liquid petroleum and natural gas but also a large variety of liquid by-products. Typical commodities transported include crude oil, natural gas, natural gas

liquids, diluents, bitumen, carbon dioxide, gasoline, jet fuel, home heating oil, diesel fuel and highly volatile liquids (ethane, butane, and propane) (Association of Oil Pipelines, 2013). The sizes of pipelines directly depend on the commodity being transported and its destination. Refined products, such as gasoline, are transported in smaller lines across short distances. Crude oil is transported in large lines across long distances.

### **Other Methods of Transportation**

Besides pipelines there are three other methods to transport similar commodities. Trucks are used to transport commodities from pipeline hubs to the end user such as gas stations or smaller manufacturing plants. Water carriers, such as tankers, are used to transport commodities across oceans. Water carriers can also be used to transport commodities along the coastline of one continent, but this is an expensive task with limited capacity. These two methods should be considered as complements to pipelines, allowing commodities to reach areas where pipelines cannot or do not. Railways on the other hand can be considered as a legitimate substitute. Due to the industrial history of North America, and in fact the entire world, many railways and rail-hubs exist to this day, spanning large distances. With a stringent regulatory environment, railways are being used as an alternative to pipelines when expansions are difficult. A railway expansion in Bruderheim, Alberta is in development by Canexus Corporation, but it is the only project of its kind currently (Canexus Corporation, 2014). Railways are still not as widely used and only occupy 3% of all oil and gas transportation in the United States (Association of Oil Pipelines, 2013).

In contrast to the substitutes/complements above, pipelines have a large variety of advantages. They utilize low amounts of energy and as a consequence produce very little pollution. Canadian pipelines have a 99.9999% safety record and due to close surveillance, leaks



are quickly fixed (Canadian Energy Pipeline Association, 2014). Most importantly pipelines are cost efficient after their construction and as a result are the only feasible method for long-distance continental transport.

### **Firm Revenue and Cost Structure**

Due to the pipeline industry's interdependency on the oil and gas industry and the nature of its business the revenue and cost structure is easily determinable. Revenues are generated through the provision of collection, transportation and storage services. Revenues are divided into contracted and un-contracted capacity (Inter Pipeline Ltd., 2014). Contracts are take-or-pay, requiring payment for pipeline capacity regardless of use by the producer. This method of payment is unaffected by market fluctuations of oil and gas prices. Furthermore, rates charged by pipelines are federally regulated and adjusted for inflation, removing the relationship to oil and gas prices completely (Landis, 2009). It is important to note that while oil and gas prices do not influence rates charged by the pipeline industry they do affect supply and demand, which ultimately affects pipeline utilization. Un-contracted revenue is generated through one-time requests by producers.

Costs in the pipeline industry are similarly straight-forward. The largest cost involved is capital expenditure; the cost necessary to build pipelines and various connecting facilities. Many expansion projects alone, with existing capacity, exceed \$500 million. In comparison, operating expenses are small and are entirely covered by revenues (Inter Pipeline Ltd., 2014). An interesting fact to note is the increase of operating costs in relation to capital expenditure. In 2014 IPL spent approximately \$550 million on the expansion of a number of its facilities, yet operating expenses increased by only \$10 million (Inter Pipeline Ltd., 2014).

**Firm Strategy**

The pipeline industry is a utilization based business. Profits require the use of pipelines by producers and others in the field. No users would result in no utilization and ultimately no revenues for pipeline firms. This results in a single general strategy: service diversification. More specifically, firms must compete on the services they provide to attract users. This competition revolves around the following factors:

- Destinations offered by the pipelines
- Services offered in addition to transportation (e.g. gathering, processing, storage, etc.)
- Types of commodities transported
- Capacity of pipelines and daily volume potential

The combination of these factors results in a constant growth strategy by the pipeline industry. Many firms attempt to expand their current network of pipelines to offer more commodities or more destinations. Some firms choose to peg their strategies on a single commodity or production area. IPL is currently focused on growing along with the oil sands in Alberta.

Therefore its expansion involves liquid petroleum and diluent lines. An additional strategy in this industry is the acquisition of new technology and assets. The pipeline industry is capital intensive and an increase in assets is always a focus but an increase in advanced pipelines is more desirable (Inter Pipeline Ltd., 2014).

**Regulatory Environment**

Pipeline regulation in Canada falls under the National Energy Board (NEB) and in the United States under the Federal Energy Regulatory Commission (FERC). In Canada, provinces have independent regulatory bodies for pipelines within their borders. Additional regulatory bodies can also be involved depending on the location and impact of a pipeline (Canadian

Energy Pipeline Association, 2014). This results in a long approval process should a firm decide to expand or build a new pipeline. The NEB is responsible for interprovincial and international pipelines in Canada. Its main focus is the safety of communities and the environment as well as the regulation of tolls and tariffs by the pipeline industry (Government of Canada, 2013). The NEB is also involved in accident investigations, which is done alongside the Transportation Safety board (Government of Canada, 2014).

Common tools for regulators, regardless of location, include audits, before and after construction projects are completed, on-site inspections, compliance meetings, emergency response exercise evaluations, and incident investigations. Legislation is also very important, especially in the environmental aspect. Compliance and enforcement is publicly available and can be found on the NEB website (Government of Canada, 2014).

### **Inter Pipelines Ltd. Analysis**

#### **Business and Operations**

IPL is unique in the pipeline industry due to its holding of pipelines in Canada only. These holdings are primarily centred in Edmonton, Alberta and Hardisty, Alberta. Additionally, IPL has storage units in Europe operated by wholly owned entities Simon Storage Limited and Inter Terminals (Inter Pipeline Ltd., 2014). These storage units are located in the United Kingdom, Ireland, Germany, and Denmark.

IPL's pipeline business focuses on three areas: oil sands, conventional oil, and natural gas liquids extraction. These accounts for 88% of its EBITDA. All together IPL's pipelines cover 6,402 KM and have a capacity of 4.85 million barrels per day. Its oil sands pipelines account for 40% of its EBITDA and have secured approximately \$3.3 billion in contracts with an additional \$3 billion of capacity remaining. All three pipelines in the oil sands sector transport diluents to

oil sands firms and two of the pipelines transport bitumen to refineries. IPL has complete ownership of the Corridor and Polaris pipelines and 85% ownership of the Cold Lake pipeline. Figure 4 provides further details regarding oil sands pipelines.

Specifications				
System	Type	Length (km)	Storage Capacity (bbls)	2013 Throughput (b/d)
Cold Lake	Oil sands & condensate gathering system	1,101	376,000	478,200
Corridor	DilBit, diluent, feedstock & products pipeline	1,046	3,500,000	334,800
Polaris	Diluent transportation system	495	-	15,400

*Figure 4 (Inter Pipeline Ltd., 2014)*

IPL's conventional oil pipelines accounts for 24% of its EBITDA. All three pipelines are shorter feeder and gathering lines, with the exception of the Bow River line which is the longest (2,774 KM) in IPL's portfolio (Inter Pipeline Ltd., 2014). The conventional oil pipelines are connected to 135 producers in the Alberta and Saskatchewan area (Inter Pipeline Ltd., 2014). Figure 5 provides further details regarding conventional oil pipelines.



Specifications					
System	Type	Length (km)	Delivery Point	Storage Capacity (bbls)	2013 Throughput (b/d)
Bow River	Crude oil feeder pipeline & gathering system	2,774	Hardisty, AB Milk River, AB	464,500	97,700
Central Alberta	Crude oil feeder pipeline & gathering system	553	Edmonton, AB	113,700	35,400
Mid-Saskatchewan	Crude oil feeder pipeline & gathering system	433	Kerrobert, SK	397,600	53,500

*Figure 5 (Inter Pipeline Ltd., 2014)*

IPL's natural gas facilities focus on processing pipeline natural gas to remove natural gas liquids. IPL does not actually transport natural gas, though it has the capacity to do so. It has complete ownership of the Cochrane and Empress II plants and 50% ownership of Empress V. This aspect of its Canadian business accounts for 24% of its EBITDA. Figure 6 provides further details regarding NGL extraction plants.

Specifications			
Location	Facilities	Processing Capacity	2013 Throughput
Cochrane	Three turbo-expander cryogenic trains, lean oil plant, CO <sub>2</sub> liquefaction plant	2.5 bcf natural gas 100,000 b/d of NGL	Natural Gas: 1.7bcf/d Ethane: 47,500 b/d Propane Plus: 23,100 b/d
Empress II	Two turbo-expander cryogenic trains	2.6 bcf natural gas 65,000 b/d of NGL	Natural Gas: 0.1 bcf/d Ethane: 3,000 b/d Propane Plus: 1,700 b/d
Empress V	One turbo-expander cryogenic train	1.1 bcf natural gas 39,000 b/d of NGL	Natural Gas: 0.9 bcf/d Ethane: 24,200 b/d Propane Plus: 10,700 b/d

*Figure 6 (Inter Pipeline Ltd., 2014)*



In addition to current pipelines IPL is investing \$3.37 billion in 12 expansions of all pipelines. The expected EBITA benefit is \$471 million annually. Figure 7 provides further details regarding expansion.

Current Projects*			
	Revenue Start Date	Capital	Annual EBITDA
Cold Lake Pipeline: Kirby South Connection	Third Quarter 2013	\$95 million	\$35 million per year
Cold Lake Pipeline: West Leg Quarter Point Expansion	Third Quarter 2013	\$80 million	\$10 million per year
Polaris Pipeline: Husky Sunrise Connection	Fourth Quarter 2013	\$15 million	\$27 million per year
Polaris Pipeline: Suncor Diluent Connection	Third Quarter 2013	\$10 million	\$10 million per year
Polaris Pipeline: FCCL Foster Creek and Christina Lake Diluent Facilities	Third Quarter 2014	\$1.3 billion	\$120 million per year
Cold Lake Pipeline: Canexus Rail Loading Facility Connection	Third Quarter 2014	\$60 million	\$12 million per year
Cold Lake Pipeline: FCCL Foster Creek Bitumen Blend Facilities	First Quarter 2015	\$1.34 billion	\$160 million per year
Polaris Pipeline Imperial Kearn Phase 2 Expansion	Third Quarter 2015	\$45 million	\$19 million per year
Cold Lake and Polaris Pipeline FCCL Narrows Lake Diluent and Bitumen Blend Facilities	Second Half 2017	\$275 million	\$50 million per year
Polaris Pipeline: AOC Hangingstone Diluent Connection	First Quarter 2015	\$25 million	\$5 million per year
Polaris Pipeline: JACOS/Nexen Hangingstone Diluent Connection	Third Quarter 2016	\$25 million	undisclosed
Mid-Saskatchewan Pipeline: Major System Expansion	Second quarter 2015	\$100 million	≈\$25 million per year
Total		\$3.37 billion	\$471 million per year

Figure 7 (Inter Pipeline Ltd., 2014)

Despite the apparently large differences in contribution to EBITDA, all three Canadian segments generate the same net income (\$43 million) annually. The NGL extraction segment is

the highest grossing segment but has expenses that are more than double of the other two segments. A segment report can be found in the appendix.

In Europe, IPL is the fourth largest bulk storage firm with a capacity of over 19 million barrels. This segment accounts for 12% of EBITDA and is the lowest grossing and least profitable segment at \$45 million and \$13 million respectively (Inter Pipeline Ltd., 2014). This may be attributable to the low utilization rate of 77% (Inter Pipeline Ltd., 2014). Figure 8 provides further details regarding bulk storage in Europe.

Specifications		
Terminal	Description	Capacity
Immingham East/West, UK	On the deep water of the south bank of the River Humber - UK's largest multi purpose storage facility	628,000 m3 240 tanks
Seal Sands, UK	On the River Tees - provides access to petrochemical and industrial complexes in the north of England	220,000 m3 111 tanks
Riverside, UK	On the River Tees - within the heartland of the UK's chemical industry	65,000 m3 22 tanks
Tyne, UK	The only independent bulk liquid storage terminal on the River Tyne - provides links to north England and Scotland	57,000 m3 64 tanks
Shannon, Ireland	Located on the Shannon estuary - is one of the few deep water ports in Ireland	14,000 m3 13 tanks
TLG North/ South, Germany	Two terminals located on the River Rhine - integrated with regional petrochemical and petroleum industries	304,000 m3 134 tanks
Asnaes, Denmark	Located next to the Asnaes power plant owned by DONG Energy and the Statoil refinery on the west coast of Sealand, Denmark	430,000 m3 6 tanks
Ensted, Denmark	Located on the west coast of Sealand, Denmark - provides deep draft and the capability of accommodating Very Large Crude Carriers (VLCCs) – terminal currently used for fuel oil and vacuum gas oil storage	320,000 m3 4 tanks
Stigsnaes, Denmark	Located on the west coast of Sealand, Denmark - provides deep draft and the capability of accommodating VLCCs – terminal currently used for fuel oil and vacuum gas oil storage	406,000 m3 7 tanks
Gulfhavn, Denmark	Located on the west coast of Sealand, Denmark - currently stores jet fuel, gasoline, and diesel	630,000 m3 33 tanks

*Figure 8 (Inter Pipeline Ltd., 2014)*

### **IPL Management Team**

The intention of including a discussion of the management team is to use the discussion as part of the deciding factors for the recommendation. A management team plays an important role in steering a firm in the right direction. A poor management team, such as Blackberry's, can result in losses and downsizing. Therefore it is vital to discuss this aspect of a firm.

Richard Shaw is a former lawyer with McCarthy Tétrault LLP who joined IPL in 2010. Richard's position was as an independent director focusing on corporate governance as well as M&A and securities law. On January 1, 2014 Richard was appointed Chairman of the Board to replace retiring John Driscoll. Richard's legal expertise is mainly from Alberta therefore he can not only provide legal advice but geographically relevant legal advice.



David W. Fesyk has been with IPL since 1997 as President and CEO. His experience included other executive positions at different affiliates of Koch (Inter Pipeline's predecessor) and the Saskatchewan Pipeline Company. David's education is focused in science and business administration providing him with the ability to make educated but sound business decisions. David is now Executive Vice Chairman, promoted a long with Richard Shaw.



Christian P. Bayle, similarly to David W. Fesyk, has been with IPL since its predecessor Koch. He has had multiple roles in the company including Vice President, Operations, in 2002, Vice President, Corporate Development, in 2005, Senior Vice President, Corporate Development, in 2008, and Chief Operating Officer in 2011. Christian has been appointed as President and CEO in 2014, following the recent promotions of his coworkers. Christian has a Bachelor's of Mechanical Engineering as well as a Master's in Engineering Management. This assures shareholders that





decisions made are extremely educated and from the perspective of an engineer rather than a business person.

Brent Heagy is the current Chief Financial Officer. He joined IPL in 2014 after serving in financial roles in the oil and gas industry for 30 years. Brent's contribution lies in his knowledge of corporate financing. Specifically, Brent should be able to guide the management team in making the appropriate debt and equity decisions to finance expansions and construction projects. This is important due to the capital intensive nature of the pipeline industry.



Cory W. Neufeld is another original management team member from the days of Koch. He has held positions primarily in the operations and engineering areas. Currently he is Vice President, Oil Sands Pipeline Development. His education includes a Bachelor's of Science in Mechanical Engineering and a professional engineering designation. Oil sands are expected to vastly grow and IPL is planning to expand along with them. Therefore it is crucial that the executive in charge of Oil Sands Pipeline Development has an engineering background and experience in the industry, such as Cory.



Jeffery D. Marchant is the current Senior Vice President, Transportation. Jeffery was also with Koch and joined IPL in 1998. His experience lies in engineering and his education includes a Bachelor's of Chemical Engineering and a professional engineering designation. Transportation is an extremely important segment





within IPL due to the fact that it is the nature of the business. Jeffery's engineering background and experience with the pipeline industry ensures appropriate decisions will be made.

The remainder of the management team involves many auditors on the Board of Directors and legal counsel on the Officer Team (Inter Pipeline Ltd., 2014). Auditors are especially important in IPL due to many positions being dominated by engineers. The reason for this is that a strong firm will not only be knowledgeable and efficient in its industry but also proficient in the business world. For the pipeline industry it is extremely important to have corporate financing experience amongst other areas. Additionally, a strong legal counsel is important in any heavily regulated industry. The pipeline industry is one such example with a variety of external stakeholders all with separate legal concerns.

## Financial Analysis

IPL's Investor Presentation frequently states that the firm has a strong balance sheet (Inter Pipeline Ltd., 2014). Additionally, the nature of the pipeline industry sets expectations that cash flows are also strong due to the predictability. The author of this report is inclined to agree with both statements and a discussion of the most recent quarter's reports, Q1 2014, and the most recent annual reports, 2013, follows to show why this is the case. Full size versions of all financial statements<sup>1</sup> can be found in the appendix.

The strength of the balance sheet has been determined to be as such not due to exceptional performance but due to a lack of any adverse performance. Accounts payables are greater than accounts receivables by a ratio of 3:1, signifying trade credit. There is also a significant sum of cash that can cover all

### Interim Consolidated Balance Sheets

	As at March 31 2014	As at December 31 2013
(unaudited) (thousands of Canadian dollars)		
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents (note 18)	\$ 225,089	\$ 47,236
Accounts receivable	179,198	246,310
Derivative financial instruments (note 15)	4,102	5,051
Prepaid expenses and other deposits	27,519	41,302
Total Current Assets	436,908	339,899
Non-Current Assets		
Derivative financial instruments (note 15)	-	395
Property, plant and equipment (note 5)	7,249,776	6,699,702
Goodwill and intangible assets	620,973	617,704
Total Assets	\$ 8,307,657	\$ 7,657,700
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities		
Dividends payable (note 6)	\$ 33,310	\$ 32,980
Accounts payable and accrued liabilities (notes 8 and 9)	630,801	578,748
Current income taxes payable	-	31,232
Derivative financial instruments (note 15)	-	1,394
Deferred revenue	30,057	6,763
Convertible shares (note 10)	170,000	-
Current portion of long-term debt (note 7)	438,080	287,983
Commercial paper (note 7)	1,295,459	1,309,452
Total Current Liabilities	2,597,707	2,248,552
Non-Current Liabilities		
Long-term debt (note 7)	2,405,254	2,345,591
Convertible shares (note 10)	-	170,000
Long-term payable	-	395
Provisions (note 8)	64,247	65,102
Employee benefits (note 9)	9,123	11,886
Long-term deferred revenue and other liabilities	16,280	16,461
Deferred income taxes	428,305	415,446
Total Liabilities	5,520,896	5,273,433
Commitments (notes 5 and 13)		
Shareholders' Equity		
Shareholders' equity (note 10)	2,403,597	2,045,954
Total reserves (note 10)	86,848	54,296
Total Shareholders' Equity	2,490,445	2,100,250
Non-Controlling Interest (note 11)	296,316	284,017
Total Equity	2,786,761	2,384,267
Total Liabilities and Equity	\$ 8,307,657	\$ 7,657,700

of the receivables in the case that they are not recoverable. IPL is heavily leveraged as noted by its \$2.8 billion current portion of long term debt and long term debt line items and its \$1.3 billion commercial paper line item. Calculating the debt/equity ratio using the line items mentioned above (\$4.1 billion) as the debt line and total shareholder's equity (\$2.5 billion) as the equity line, reveals a ratio of 1.656 (Government of Canada, 2012). This is under the 2009 benchmark of 1.769, meaning IPL is not necessarily over-leveraged. The debt line items also did not

<sup>1</sup> All reports can be found at <http://www.interpipeline.com/investor/financial-reports.cfm> or in references list.

significantly increase since the previous quarter, further supporting that IPL is not over-leveraged.

The annual balance sheet provides further insight into the debt figure. It is clear that debt increased each year by a significant portion (approximately \$600 million per year) but it is in line with an increase in the property, plant and equipment (PPE) line item. It is important to note the PPE line item increased in 2013 by \$2 billion was funded jointly through debt and equity. This is a good sign that further supports the notion that IPL is not over-leveraged.

The annual income statement shows an unusual \$46 million loss for IPL. This is a result of management consolidation to prepare the firm for conversion to corporate form. The line item showing this is General Partner internalization at \$384 million. This expense was non-cash and performed

## Consolidated Balance Sheets

	December 31 2013	December 31 2012	As at January 1 2012
(thousands of Canadian dollars)		(restated – see note 27)	(restated – see note 27)
<b>ASSETS</b>			
Current Assets			
Cash and cash equivalents (note 23)	\$ 47,236	\$ 64,979	\$ 50,817
Accounts receivable	246,310	146,746	109,567
Derivative financial instruments (note 19)	5,051	20,816	5,167
Prepaid expenses and other deposits	41,302	31,279	11,142
Total Current Assets	339,899	263,820	176,693
Non-Current Assets			
Derivative financial instruments (note 19)	395	4,865	9,772
Property, plant and equipment (note 7)	6,699,702	4,793,508	4,154,324
Goodwill and intangible assets (note 8)	617,704	620,202	513,396
Total Assets	\$ 7,657,700	\$ 5,682,395	\$ 4,854,185
<b>LIABILITIES AND EQUITY</b>			
Current Liabilities			
Dividends payable (note 9)	\$ 32,980	\$ 25,452	\$ 23,114
Accounts payable and accrued liabilities (notes 11 and 12)	578,748	292,999	162,503
Current income taxes payable (note 13)	31,232	8,685	49,761
Derivative financial instruments (note 19)	1,394	8,336	25,746
Deferred revenue	6,763	6,143	4,606
Current portion of long-term debt (note 10)	287,983	–	90,989
Commercial paper (note 10)	1,309,452	1,351,132	1,464,369
Total Current Liabilities	2,248,552	1,692,747	1,821,088
Non-Current Liabilities			
Long-term debt (note 10)	2,345,591	1,760,902	1,102,288
Convertible common shares (note 5)	170,000	–	–
Long-term payable	395	4,865	9,772
Derivative financial instruments (note 19)	–	–	11,035
Provisions (note 11)	65,102	59,953	37,025
Employee benefits (note 12)	11,886	9,631	6,969
Long-term deferred revenue and other liabilities	16,461	16,958	17,452
Deferred income taxes (note 12)	415,446	384,531	342,474
Total Liabilities	5,273,433	3,929,587	3,348,323
Commitments (notes 7 and 11)			
Shareholders' Equity			
Shareholders' equity (note 14)	2,045,954	1,682,955	1,452,066
Total reserves (note 14)	54,296	(23,504)	(32,280)
Total Shareholders' Equity	2,100,250	1,659,451	1,419,786
Non-Controlling Interest (note 15)	284,017	93,357	86,076
Total Equity	2,384,267	1,752,808	1,505,862
Total Liabilities and Equity	\$ 7,657,700	\$ 5,682,395	\$ 4,854,185

## Consolidated Statements of Net (Loss) Income

	2013	2012
(thousands of Canadian dollars)		(restated – see note 27)
<b>REVENUES</b>		
Operating revenues	\$ 1,362,713	\$ 1,205,991
<b>EXPENSES</b>		
Shrinkage gas	235,652	206,325
Midstream product purchases	71,067	31,905
Operating (note 27)	351,405	300,806
Depreciation and amortization	126,686	124,593
Financing charges (note 21)	91,882	97,604
General and administrative (note 22)	77,070	64,046
Unrealized change in fair value of derivative financial instruments (note 19)	9,065	(44,363)
Acquisition fee to General Partner (note 16)	–	4,591
Management and incentive fees to General Partner (note 16)	7,971	13,832
General Partner internalization (note 5)	348,584	–
Loss on disposal of assets	3,729	175
	1,323,111	799,114
<b>INCOME BEFORE INCOME TAXES</b>	39,602	406,277
<b>Provision for income taxes (note 13)</b>		
Current	57,114	57,042
Deferred	29,483	32,253
	86,597	89,295
<b>NET (LOSS) INCOME</b>	\$ (46,995)	\$ 316,982
<b>Net (loss) income attributable to</b>		
Shareholders of Inter Pipeline Ltd.	\$ (58,095)	\$ 307,153
Non-controlling interest (note 15)	11,100	9,829
	\$ (46,995)	\$ 316,982
<b>Net (loss) income per share attributable to shareholders of Inter Pipeline Ltd. (note 14)</b>		
Basic and diluted	\$ (0.20)	\$ 1.14



through the issuance of new shares to the previous shareholders. Currently the firm is in corporate form and a single entity.

The quarterly income statement is a more accurate representation of IPL's current situation. Most important to note is the \$58 million increase in costs and the \$83 million increase in revenues. This is a good sign that the firm is operating at a profit. The per share values have also increased by \$0.03 (basic) and \$0.02 (diluted).

Due to the conversion to corporate form and purchases of PPE, IPL's 2013 statement of cash flows shows many negative values. These are offset by debt and equity issuance and funds from operations which help maintain a positive cash balance at the end of the year.

Unlike the annual report, the quarterly statement cash flows shows a large positive cash balance. But this

### Interim Consolidated Statements of Net Income

(unaudited) (thousands of Canadian dollars)		Three Months Ended March 31	
		2014	2013
<b>REVENUES</b>			
Operating revenues	\$	410,738	\$ 327,679
<b>EXPENSES</b>			
Shrinkage gas		90,455	61,594
Midstream product purchases		28,828	13,955
Operating		94,061	81,045
Depreciation and amortization		33,266	30,926
Financing charges (note 17)		20,833	23,878
General and administrative		25,421	16,248
Unrealized change in fair value of derivative financial instruments		(1,214)	716
Management and incentive fees to general partner (note 12)		-	4,182
(Gain) loss on disposal of assets		(860)	1,733
		290,790	234,217
<b>INCOME BEFORE INCOME TAXES</b>		119,948	93,402
<b>Provision for income taxes</b>			
Current		16,963	14,519
Deferred		13,363	6,651
		30,326	21,170
<b>NET INCOME</b>	\$	89,622	\$ 72,232
<b>Net income attributable to</b>			
Shareholders of Inter Pipeline Ltd.	\$	86,124	\$ 69,651
Non-controlling interest (note 11)		3,498	2,581
	\$	89,622	\$ 72,232
<b>Net income per share attributable to shareholders of Inter Pipeline Ltd. (note 10)</b>			
Basic	\$	0.28	\$ 0.25
Diluted	\$	0.27	\$ 0.25

### Consolidated Statements of Cash Flows

(thousands of Canadian dollars)		Years Ended December 31	
		2013	2012
			(restated – see note 27)
<b>OPERATING ACTIVITIES</b>			
Net (loss) income	\$	(46,995)	\$ 316,982
Items not involving cash:			
Depreciation and amortization		126,686	124,593
Loss on disposal of assets		3,729	175
Non-cash expense		2,004	4,236
Unrealized change in fair value of derivative financial instruments		9,065	(44,363)
General Partner internalization (note 5)		348,584	-
Deferred income tax expense		29,483	32,253
Funds from operations		472,556	433,876
Net change in non-cash operating working capital (note 23)		(3,882)	(48,343)
Cash provided by operating activities		468,674	385,533
<b>INVESTING ACTIVITIES</b>			
Expenditures on property, plant and equipment		(1,948,471)	(384,491)
Proceeds on sale of assets		1,790	360
Net change on amalgamation (note 5)		(218)	-
Acquisition of Inter Terminals (note 26)		-	(509,713)
Assumption of cash on acquisition of Inter Terminals (note 26)		-	48,293
Capital contributions received from Cold Lake non-controlling interest		191,425	7,237
Net change in non-cash investing working capital (note 23)		201,385	99,514
Cash used in investing activities		(1,554,089)	(738,800)
<b>FINANCING ACTIVITIES</b>			
Cash dividends paid to shareholders of Inter Pipeline Ltd. (note 9)		(91,493)	(16,264)
Cash distributions paid by Cold Lake to non-controlling interest		(11,865)	(9,785)
Increase in debt		833,119	455,402
Transaction costs on debt		(4,894)	(1,924)
Issuance of common shares		345,045	-
Share issue costs		(14,356)	-
Net change in non-cash financing working capital (note 23)		8,739	412
Cash provided by financing activities		1,064,295	367,841
Effect of foreign currency translation on foreign currency denominated cash		3,377	(412)
<b>(Decrease) increase in cash and cash equivalents</b>		(17,743)	14,162
<b>Cash and cash equivalents, beginning of year</b>		64,979	50,817
<b>Cash and cash equivalents, end of year</b>	\$	47,236	\$ 64,979
Cash taxes paid	\$	35,146	\$ 98,146
Cash interest paid	\$	105,517	\$ 97,416

is an inflated value through the use of debt and equity issuance, similar to the annual report. While the situation in 2013 warranted this strategy the situation in Q1 2014 (with no conversions and a smaller PPE expenses) does not. Removing the nearly \$282 million raised through debt and equity issuance IPL would have a negative cash balance of \$56 million. A good sign is that funds from operations is increasing and by the end of the year it can expected to be larger than in 2013.

## Interim Consolidated Statements of Cash Flows

		Three Months Ended March 31	
(unaudited) (thousands of Canadian dollars)		2014	2013
<b>OPERATING ACTIVITIES</b>			
Net income	\$	89,622	\$ 72,232
Items not involving cash:			
Depreciation and amortization		33,266	30,926
(Gain) loss on disposal of assets		(860)	1,733
Non-cash recovery		(2,447)	(2,902)
Unrealized change in fair value of derivative financial instruments		(1,214)	716
Deferred income tax expense		13,363	6,651
Funds from operations		131,730	109,356
Net change in non-cash operating working capital (note 18)		2,482	10,746
Cash provided by operating activities		134,212	120,102
<b>INVESTING ACTIVITIES</b>			
Expenditures on property, plant and equipment		(563,560)	(415,194)
Proceeds on sale of assets		1,386	8
Capital contributions received from Cold Lake non-controlling interest		12,892	3,528
Net change in non-cash investing working capital (note 18)		123,219	174,715
Cash used in investing activities		(416,063)	(236,943)
<b>FINANCING ACTIVITIES</b>			
Cash dividends paid to shareholders of Inter Pipeline Ltd. (note 6)		(19,524)	(22,405)
Cash distributions paid by Cold Lake to non-controlling interest		(4,091)	(2,896)
Increase in debt		194,827	118,877
Transaction costs on debt		10	(152)
Issuance of common shares		300,560	-
Share issue costs		(12,519)	-
Net change in non-cash financing working capital (note 18)		330	228
Cash provided by financing activities		469,593	93,652
Effect of foreign currency translation on foreign currency denominated cash		1,101	(437)
<b>Increase (decrease) in cash and cash equivalents</b>		<b>178,863</b>	<b>(23,626)</b>
<b>Cash and cash equivalents, beginning of period</b>		<b>47,236</b>	<b>64,979</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$</b>	<b>226,099</b>	<b>\$ 41,353</b>
Cash taxes paid	\$	48,292	\$ 8,514
Cash interest paid	\$	36,818	\$ 25,538

IPL's Free Cash Flow is a negative value of \$325 million<sup>2</sup> and Economic Value Added is also a negative value of \$460 million<sup>3</sup>. While this would be a red flag for many firms it important to understand that the pipeline industry and the oil and gas industry as a whole have high capital expenditures due to growth, which is required to compete and increase profit. Much of this capital expenditure is financed through debt and equity, leading to higher leverage ratios and lower cash from operations figures.

It is also prudent to recognize the pipeline industry's relationship to global markets. It has been stated already that the industry is not affected by market prices but by demand and supply as a result of market prices. This puts firms in the industry at risk of decreased revenue should utilization of pipelines slow down due to a decrease in demand for oil and gas. Take-or-pay

<sup>2</sup> Free Cash Flow = Funds From Operations – Capital Expenditure – Dividends.

<sup>3</sup> Economic Value Added = Net Operating Profits After Tax – (Capital \* Cost of Capital).



contracts do rectify this situation requiring payment from producers regardless of utilization, but un-contracted capacity will remain unutilized. The result is a potential default risk for debt.

## **Forecast**

### **Value Drivers**

All of IPL's business segments rely on the increasing demand in the oil and gas industry. The expected reaction to growing demand is a growth in production facilities and an increased necessity to transport large volumes of commodities quickly and inexpensively. IPL's specific value drivers include the global demand for oil and gas, the size of the oil and gas industry (signalling the necessity for larger volumes), and demand for storage in Europe. These value drivers are straightforward and are often predicted to grow positively in the future. Decrease in growth occurs during recessionary periods but this trend is not often sustained for a long period of time.

### **Forecast of Value Drivers**

Forecasts of oil demand growth are particularly favourable. The Gulf Coast, PADD III, in the United States is already closely tied to Western Canadian oil supply and there is another opportunity to increase supply by 400,000 barrels per day by 2020. PADD I and PADD V, also in the United States, are other potential targets. The majority of demand growth for oil is based internationally in quickly growing countries such as China and India. By 2030 it is expected that both countries will require a combined 18 million barrels per day (Canadian Association of Petroleum Producers, 2014). While the pipeline industry does not transport commodities overseas they benefit by connecting producers to ports. Figure 9 provides more detailed information regarding international oil demand in the future.

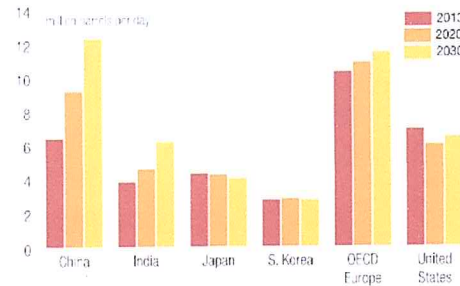


Figure 9 (Canadian Association of Petroleum Producers, 2014)

Canadian oil sands have the potential to provide 168 billion barrels of oil over 100 years (Canadian Association of Petroleum Producers, 2014). This production potential provides a positive forecast for the growth of oil sands, a specific value driver of IPL. This also supports the previous statements regarding worldwide growth by 2030 by proving there is ample supply to meet forecasted demand.

Global demands for natural gas and its liquids are expected to grow by 42 million barrels per day<sup>4</sup> (Canadian Association of Petroleum Producers, 2012) by 2035. Additionally, Canada is the third largest producer of natural gas in the world, capable of fulfilling domestic and international demands (Canadian Association of Petroleum Producers, 2012). Figure 10 provides more detailed information regarding international natural gas demand in the future.

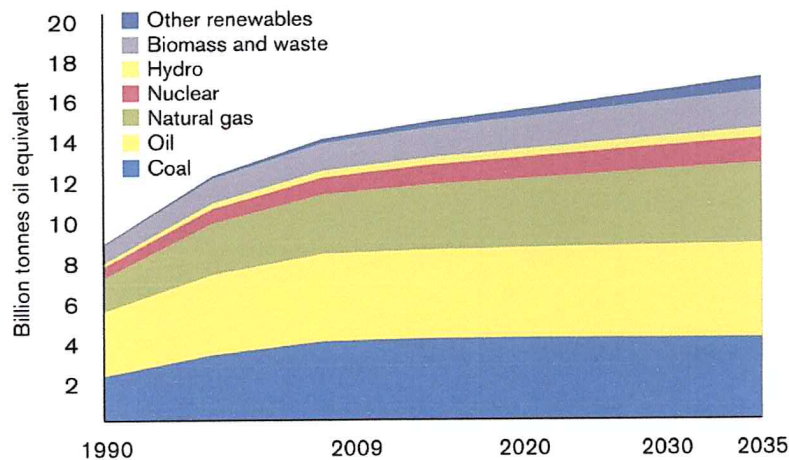


Figure 10 (Canadian Association of Petroleum Producers, 2012)

<sup>4</sup> 1 Barrel of Oil Equivalent = 1.4E-7 Million Tonnes of Oil Equivalent (the common measure for natural gas).

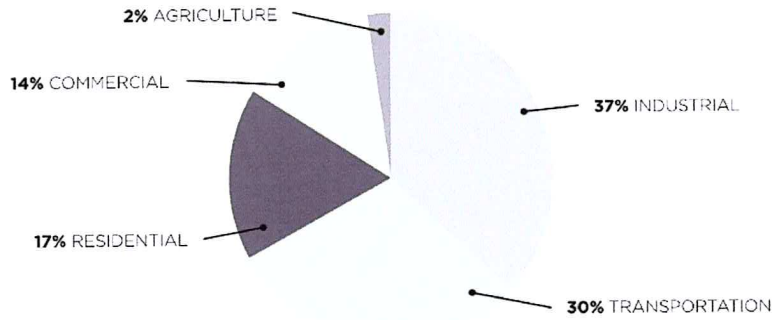


Additionally, the global increases in demand for oil and gas should result in an increase in demand for storage, positively affecting IPL's European bulk liquid storage segment. This is a logical assumption of a correlation between demand and storage, therefore it may not be correct.

The forecast for all value drivers is currently positive. As previously mentioned these forecasts are often positive due to their correlation with population growth. As populations increase the demand for direct energy or energy for manufacturing processes also increases. Therefore it would difficult to establish periods of time where absolute growth is negative. Fluctuations do occur during recessionary periods when consumers change their habits and lifestyles, but these are often for short periods of time and do not affect energy or manufacturing demand.

### **Factors that Could Undermine Forecast**

While the forecasts for IPL's value drivers are generally positive it is prudent to discuss factors that could, in theory, adversely affect these drivers. Besides a decrease in demand for oil and gas, two major factors could completely halt IPL's business. The first is a global financial crisis that heavily affects the use of oil by industries and consumers simultaneously. As previously mentioned, fluctuations in consumer demand are offset by the industrial demand, but should both demands decrease significantly 67% of oil use would disappear immediately (Canadian Association of Petroleum Producers, 2014). Chart 1 provides information on the oil use in Canada by sector in 2011.



*Chart 1 (Canadian Association of Petroleum Producers, 2014)*

The second major factor is a complete replacement of the oil and gas industry with renewable energy. While it is highly unlikely that this would occur in the near future and all at once, the possibility of such a situation is not unlikely itself. In the past we have seen trials of wind turbine power, biomass power, nuclear power, as well as alternative fuels for daily processes such as completely electric cars. Once again, this factor is completely hypothetical and will not occur in the near future but it may be the natural progression as oil and gas resources become more and more limited.

## **Valuation**

### **Approach**

To value IPL, five key areas were analyzed and equally weighted. The first area is the business and operations of IPL and the pipeline industry. This analysis focused on understanding the business environment and how it uniquely affects financial statements and other results. The second area is the management team of IPL. The focus here was to determine whether the current team had the proper inclination to manage a pipeline firm and if enough experience was available to mitigate unexpected situations. The third area is the financial statements of IPL. Annual statements are used to determine whether the firm typically generated gains or if losses were common. Annual statements are also used to determine if certain line items were unusual and not a common occurrence. Quarterly statements are used to determine the firm's performance and whether recent decisions have resulted in a positive impact. The fourth area is the forecast for IPL's value drivers. Is IPL's base business expected to profit or lose? Are negative externalities on the horizon and how will they affect IPL? These questions are the focus of this area. The fifth and final area focuses on technical analysis of multi-year charts and 50 and 200 day moving averages. The goal is to determine whether, on a technical basis, the firm's share price is favourable for an investor or not.

### **Application**

Looking at the business and operations of IPL and the pipeline industry it is clear that there is a strong interdependency between them and the oil and gas industry. IPL cannot exist without the oil and gas industry. In most cases this would be a negative factor considering reliance on another industry to generate revenues in your business is not logically sound. The other industry could undergo fluctuations or face slowdowns in their operations, affecting your



business. But through the analysis of value drivers and factors that could undermine the forecasts, it is clear that the entire oil and gas industry would need to disappear for the pipeline industry to fail. Rather the real issue in the interdependency is the spread from take-or-pay contracts and commodity demand. A decrease in the price of a contract or the quantity of a commodity demanded can affect IPL's revenues and underlying profit. In this analysis it was determined that this is not a strong risk and therefore the first area is acceptable.

The management team of IPL is a perfect combination of engineers, auditors, and legal counsel. It is an advantage to have as many engineers as IPL does in Officer positions while also maintaining an audit heavy Board of Directors and a significant sized legal counsel. This combination allows IPL to make educated operational decisions while maintaining a business mindset and navigating the regulatory environment with ease.

The financial statements of IPL are very promising. It is clear that IPL utilizes a large amount of debt and equity to fund its capital expenditure, but a closer look reveals that without expansion and financing the firm is able to profits above \$100 million. In comparison to the rest of the industry the debt/equity ratio is actually lower than the benchmark and there are no unexpected expenses outside of PPE expansion.

IPL's value drivers were the global demand for oil and gas, the size of the oil and gas industry, and demand for storage in Europe. All value drivers are forecasted to increase and IPL has planned related expansions in its pipelines. This provides assurance that IPL's business will not disappear overnight. Furthermore, factors that would undermine the forecasts are the worst case scenario and extremely unlikely to ever happen in the immediate future.

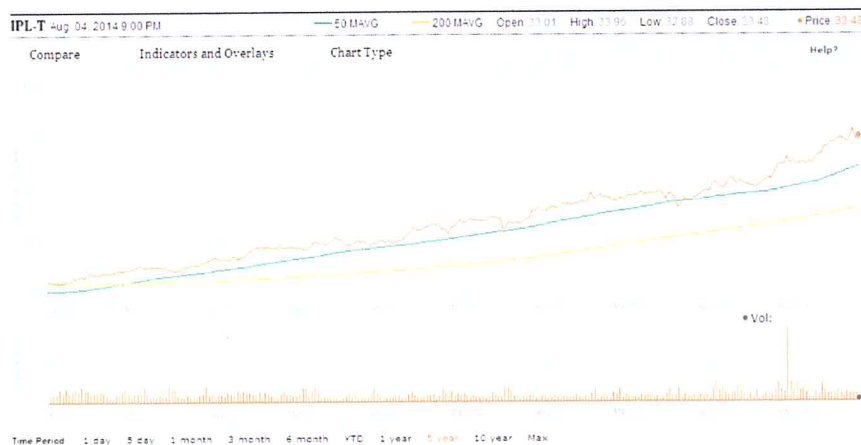
Finally, the remaining area is the technical analysis through the use of charts provided by The Globe and Mail. Chart 2 provides a 10 year historical outlook on the price of IPL stock.

Since the 2008 global financial crisis IPL stock price has been consistently increasing. It is interesting to note that during recent events in the Middle East and Europe the price has not fluctuated significantly. This is potentially a good sign of IPL's role as a transporter, which is necessary regardless of other prices and small fluctuations in demand.



*Chart 2 (The Globe and Mail, 2014)*

Chart 3 provides a 5 year historical outlook on IPL's stock price with the addition of 50 and 200 day moving averages. Using technical analysis theory, a buy signal is seen mid-2010 where the 50 day moving average crosses the 200 day moving average. The averages also appear to continue increasing, which is another signal that the stock is strong and the price will continue increasing as well.



*Chart 3 (The Globe and Mail, 2014)*

**Recommendation**

Based on the analysis of the five key areas, the recommendation of this report on Inter Pipeline Ltd. stock is to buy. To reiterate the reasoning behind this recommendation, IPL is in an industry where it is the most cost-efficient and only long distance continental method of transport for commodities. The value drivers of the business are forecast to increase and are never expected to drastically decrease. Finally, the financial position of IPL and its own business operations and management team are extremely favourable.



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## Appendix

## Quarterly balance sheet (Inter Pipeline Ltd., 2014).

	As at March 31 2014	As at December 31 2013
(unaudited) (thousands of Canadian dollars)		
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents (note 18)	\$ 226,089	\$ 47,236
Accounts receivable	179,198	246,310
Derivative financial instruments (note 15)	4,102	5,051
Prepaid expenses and other deposits	27,519	41,302
Total Current Assets	436,908	339,899
Non-Current Assets		
Derivative financial instruments (note 15)	-	395
Property, plant and equipment (note 5)	7,249,776	6,699,702
Goodwill and intangible assets	620,973	617,704
Total Assets	\$ 8,307,657	\$ 7,657,700
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities		
Dividends payable (note 6)	\$ 33,310	\$ 32,980
Accounts payable and accrued liabilities (notes 8 and 9)	630,801	578,748
Current income taxes payable	-	31,232
Derivative financial instruments (note 15)	-	1,394
Deferred revenue	30,057	6,763
Convertible shares (note 10)	170,000	-
Current portion of long-term debt (note 7)	438,080	287,983
Commercial paper (note 7)	1,295,459	1,309,452
Total Current Liabilities	2,597,707	2,248,552
Non-Current Liabilities		
Long-term debt (note 7)	2,405,254	2,345,591
Convertible shares (note 10)	-	170,000
Long-term payable	-	395
Provisions (note 8)	64,247	65,102
Employee benefits (note 9)	9,123	11,886
Long-term deferred revenue and other liabilities	16,260	16,461
Deferred income taxes	428,305	415,446
Total Liabilities	5,520,896	5,273,433
Commitments (notes 5 and 13)		
Shareholders' Equity		
Shareholders' equity (note 10)	2,403,597	2,045,954
Total reserves (note 10)	86,848	54,296
Total Shareholders' Equity	2,490,445	2,100,250
Non-Controlling Interest (note 11)	296,316	284,017
Total Equity	2,786,761	2,384,267
Total Liabilities and Equity	\$ 8,307,657	\$ 7,657,700

**Annual balance sheet (Inter Pipeline Ltd., 2013).**

	As at		
	December 31 2013	December 31 2012	January 1 2012
<i>(thousands of Canadian dollars)</i>		<i>(restated – see note 27)</i>	<i>(restated – see note 27)</i>
<b>ASSETS</b>			
Current Assets			
Cash and cash equivalents (note 23)	\$ 47,236	\$ 64,979	\$ 50,817
Accounts receivable	246,310	146,746	109,567
Derivative financial instruments (note 19)	5,051	20,816	5,167
Prepaid expenses and other deposits	41,302	31,279	11,142
Total Current Assets	339,899	263,820	176,693
Non-Current Assets			
Derivative financial instruments (note 19)	395	4,865	9,772
Property, plant and equipment (note 7)	6,699,702	4,793,508	4,154,324
Goodwill and intangible assets (note 8)	617,704	620,202	513,396
Total Assets	\$ 7,657,700	\$ 5,682,395	\$ 4,854,185
<b>LIABILITIES AND EQUITY</b>			
Current Liabilities			
Dividends payable (note 9)	\$ 32,980	\$ 25,452	\$ 23,114
Accounts payable and accrued liabilities (notes 11 and 12)	578,748	292,999	162,503
Current income taxes payable (note 13)	31,232	8,685	49,761
Derivative financial instruments (note 19)	1,394	8,336	25,746
Deferred revenue	6,763	6,143	4,606
Current portion of long-term debt (note 10)	287,983	–	90,989
Commercial paper (note 10)	1,309,452	1,351,132	1,464,369
Total Current Liabilities	2,248,552	1,692,747	1,821,088
Non-Current Liabilities			
Long-term debt (note 10)	2,345,591	1,760,902	1,102,288
Convertible common shares (note 5)	170,000	–	–
Long-term payable	395	4,865	9,772
Derivative financial instruments (note 19)	–	–	11,035
Provisions (note 11)	65,102	59,953	37,025
Employee benefits (note 12)	11,886	9,631	6,989
Long-term deferred revenue and other liabilities	16,461	16,958	17,652
Deferred income taxes (note 13)	415,446	384,531	342,474
Total Liabilities	5,273,433	3,929,587	3,348,323
Commitments (notes 7 and 17)			
Shareholders' Equity			
Shareholders' equity (note 14)	2,045,954	1,682,955	1,452,066
Total reserves (note 14)	54,296	(23,504)	(32,280)
Total Shareholders' Equity	2,100,250	1,659,451	1,419,786
Non-Controlling Interest (note 15)	284,017	93,357	86,076
Total Equity	2,384,267	1,752,808	1,505,862
Total Liabilities and Equity	\$ 7,657,700	\$ 5,682,395	\$ 4,854,185

**Annual income statement (Inter Pipeline Ltd., 2013).**

	Years Ended December 31	
(thousands of Canadian dollars)	2013	2012
		(restated – see note 27)
<b>REVENUES</b>		
Operating revenues	\$ 1,362,713	\$ 1,205,991
<b>EXPENSES</b>		
Shrinkage gas	235,652	206,525
Midstream product purchases	71,067	31,905
Operating (note 22)	351,405	300,806
Depreciation and amortization	126,686	124,593
Financing charges (note 21)	91,882	97,604
General and administrative (note 22)	77,070	64,046
Unrealized change in fair value of derivative financial instruments (note 19)	9,065	(44,363)
Acquisition fee to General Partner (note 16)	–	4,591
Management and incentive fees to General Partner (note 16)	7,971	13,832
General Partner internalization (note 5)	348,584	–
Loss on disposal of assets	3,729	175
	1,323,111	799,714
<b>INCOME BEFORE INCOME TAXES</b>	39,602	406,277
<b>Provision for income taxes</b> (note 13)		
Current	57,114	57,042
Deferred	29,483	32,253
	86,597	89,295
<b>NET (LOSS) INCOME</b>	\$ (46,995)	\$ 316,982
<b>Net (loss) income attributable to</b>		
Shareholders of Inter Pipeline Ltd.	\$ (58,095)	\$ 307,153
Non-controlling interest (note 15)	11,100	9,829
	\$ (46,995)	\$ 316,982
<b>Net (loss) income per share attributable to shareholders of Inter Pipeline Ltd.</b> (note 14)		
Basic and diluted	\$ (0.20)	\$ 1.14



**Quarterly income statement (Inter Pipeline Ltd., 2014).**

(unaudited) (thousands of Canadian dollars)	Three Months Ended March 31	
	2014	2013
<b>REVENUES</b>		
Operating revenues	\$ 410,738	\$ 327,679
<b>EXPENSES</b>		
Shrinkage gas	90,455	61,594
Midstream product purchases	28,828	13,955
Operating	94,061	81,045
Depreciation and amortization	33,266	30,926
Financing charges (note 17)	20,833	23,878
General and administrative	25,421	16,248
Unrealized change in fair value of derivative financial instruments	(1,214)	716
Management and incentive fees to general partner (note 12)	-	4,182
(Gain) loss on disposal of assets	(860)	1,733
	290,790	234,277
<b>INCOME BEFORE INCOME TAXES</b>	119,948	93,402
<b>Provision for income taxes</b>		
Current	16,963	14,519
Deferred	13,363	6,651
	30,326	21,170
<b>NET INCOME</b>	\$ 89,622	\$ 72,232
<b>Net income attributable to</b>		
Shareholders of Inter Pipeline Ltd.	\$ 86,124	\$ 69,651
Non-controlling interest (note 11)	3,498	2,581
	\$ 89,622	\$ 72,232
<b>Net income per share attributable to shareholders of Inter Pipeline Ltd. (note 10)</b>		
Basic	\$ 0.28	\$ 0.25
Diluted	\$ 0.27	\$ 0.25

**Annual statement of cash flows (Inter Pipeline Ltd., 2013).**

	Years Ended December 31	
(thousands of Canadian dollars)	2013	2012
		(restated – see note 27)
<b>OPERATING ACTIVITIES</b>		
Net (loss) income	\$ (46,995)	\$ 316,982
Items not involving cash:		
Depreciation and amortization	126,686	124,593
Loss on disposal of assets	3,729	175
Non-cash expense	2,004	4,236
Unrealized change in fair value of derivative financial instruments	9,065	(44,363)
General Partner internalization (note 5)	348,584	–
Deferred income tax expense	29,483	32,253
Funds from operations	472,556	433,876
Net change in non-cash operating working capital (note 23)	(3,882)	(48,343)
Cash provided by operating activities	468,674	385,533
<b>INVESTING ACTIVITIES</b>		
Expenditures on property, plant and equipment	(1,948,471)	(384,491)
Proceeds on sale of assets	1,790	360
Net change on amalgamation (note 5)	(218)	–
Acquisition of Inter Terminals (note 26)	–	(509,713)
Assumption of cash on acquisition of Inter Terminals (note 26)	–	48,293
Capital contributions received from Cold Lake non-controlling interest	191,425	7,237
Net change in non-cash investing working capital (note 23)	201,385	99,514
Cash used in investing activities	(1,554,089)	(738,800)
<b>FINANCING ACTIVITIES</b>		
Cash dividends paid to shareholders of Inter Pipeline Ltd. (note 7)	(91,493)	(76,264)
Cash distributions paid by Cold Lake to non-controlling interest	(11,865)	(9,785)
Increase in debt	833,119	455,402
Transaction costs on debt	(4,894)	(1,924)
Issuance of common shares	345,045	–
Share issue costs	(14,356)	–
Net change in non-cash financing working capital (note 23)	8,739	412
Cash provided by financing activities	1,064,295	367,841
Effect of foreign currency translation on foreign currency denominated cash	3,377	(412)
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(17,743)</b>	<b>14,162</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>64,979</b>	<b>50,817</b>
<b>Cash and cash equivalents, end of year</b>	<b>\$ 47,236</b>	<b>\$ 64,979</b>
Cash taxes paid	\$ 35,146	\$ 98,146
Cash interest paid	\$ 105,517	\$ 97,416

**Quarterly statement of cash flows (Inter Pipeline Ltd., 2014).**

(unaudited) (thousands of Canadian dollars)	Three Months Ended March 31	
	2014	2013
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 89,622	\$ 72,232
Items not involving cash:		
Depreciation and amortization	33,266	30,926
(Gain) loss on disposal of assets	(860)	1,733
Non-cash recovery	(2,447)	(2,902)
Unrealized change in fair value of derivative financial instruments	(1,214)	716
Deferred income tax expense	13,363	6,651
Funds from operations	131,730	109,356
Net change in non-cash operating working capital (note 18)	2,482	10,746
Cash provided by operating activities	134,212	120,102
<b>INVESTING ACTIVITIES</b>		
Expenditures on property, plant and equipment	(563,560)	(415,194)
Proceeds on sale of assets	1,386	8
Capital contributions received from Cold Lake non-controlling interest	12,892	3,528
Net change in non-cash investing working capital (note 18)	123,219	174,715
Cash used in investing activities	(416,063)	(236,943)
<b>FINANCING ACTIVITIES</b>		
Cash dividends paid to shareholders of Inter Pipeline Ltd. (note 6)	(19,524)	(22,405)
Cash distributions paid by Cold Lake to non-controlling interest	(4,091)	(2,896)
Increase in debt	194,827	118,877
Transaction costs on debt	10	(152)
Issuance of common shares	300,560	-
Share issue costs	(12,519)	-
Net change in non-cash financing working capital (note 18)	330	228
Cash provided by financing activities	469,593	93,652
Effect of foreign currency translation on foreign currency denominated cash	1,101	(437)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>178,853</b>	<b>(23,626)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>47,236</b>	<b>64,979</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 226,089</b>	<b>\$ 41,353</b>
Cash taxes paid	\$ 48,292	\$ 8,514
Cash interest paid	\$ 36,818	\$ 25,538

## Quarterly segment reporting (Inter Pipeline Ltd., 2014).

## 4. SEGMENT REPORTING

Inter Pipeline operates its business under the following principal business segments:

Three Months Ended March 31, 2014

	Canada					Europe		Total
	Oil Sands Transportation Business	Conventional Oil Pipelines Business	NGL Extraction Business	Corporate	Total Canadian Operations	Bulk Liquid Storage Business	Canadian and European Operations	
REVENUES	\$ 105,172	\$ 91,185	\$ 168,385	\$ -	\$ 364,742	\$ 45,996	\$ 410,738	
EXPENSES								
Shrinkage gas	-	-	90,455	-	90,455	-	90,455	
Midstream product purchases	-	28,828	-	-	28,828	-	28,828	
Operating	29,416	15,630	29,300	-	74,346	19,715	94,061	
Depreciation and amortization	12,352	2,613	7,640	773	23,378	9,888	33,266	
Financing charges	8,464	170	75	11,834	20,543	290	20,833	
General and administrative	2,497	-	-	20,598	23,095	2,326	25,421	
Unrealized change in fair value of derivative financial instruments	-	33	(1,247)	-	(1,214)	-	(1,214)	
Gain on disposal of assets	-	(7)	-	-	(7)	(853)	(860)	
INCOME (LOSS) BEFORE INCOME TAXES	52,729	47,287	126,223	33,205	259,424	31,366	290,790	
Provision for income taxes	52,443	43,978	42,162	(33,205)	105,318	14,630	119,948	
NET INCOME (LOSS)	\$ 9,139	\$ -	\$ -	\$ 20,141	\$ 29,280	\$ 1,046	\$ 30,326	
Items not involving cash:	\$ 43,304	\$ 43,918	\$ 42,162	\$ (53,346)	\$ 76,038	\$ 13,584	\$ 89,622	
Depreciation and amortization*	12,352	2,606	7,640	773	23,371	9,035	32,406	
Non-cash recovery	(232)	(556)	(74)	(1,263)	(2,145)	(302)	(2,447)	
Unrealized change in fair value of derivative financial instruments	-	33	(1,247)	-	(1,214)	-	(1,214)	
Deferred income tax expense (recovery)	7,966	-	-	6,087	14,053	(690)	13,363	
FUNDS FROM (USED IN) OPERATIONS	\$ 63,380	\$ 46,001	\$ 48,481	\$ (47,769)	\$ 110,103	\$ 21,627	\$ 131,730	
PROPERTY, PLANT AND EQUIPMENT ADDITIONS	\$ 536,857	\$ 6,700	\$ 1,763	\$ 1,176	\$ 546,496	\$ 4,416	\$ 550,912	
Property, plant and equipment - net book value	\$ 5,564,342	\$ 484,129	\$ 419,566	\$ 14,668	\$ 6,482,705	\$ 767,071	\$ 7,249,776	
Goodwill and intangible assets - net book value	\$ 224,693	\$ -	\$ 197,633	\$ -	\$ 422,326	\$ 198,647	\$ 620,973	
Other assets	\$ 84,191	\$ 233,521	\$ 61,945	\$ 504	\$ 380,161	\$ 56,747	\$ 436,908	
TOTAL ASSETS	\$ 5,873,226	\$ 717,650	\$ 679,144	\$ 15,172	\$ 7,285,192	\$ 1,022,465	\$ 8,307,657	
As at March 31, 2014								

As at March 31, 2014