1999 Dominion Bond Rating Service (DBRS) Report

Newfoundland Power Inc.

(formerly Newfoundland Light & Power Co. Limited)

Current Report: March 26, 1999
Previous Report: March 16, 1998

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Rating	Trend	Rating Action	Debt Rated
"A"	Stable	Confirmed	First Mortgage Bonds
Pfd-2	Stable	Confirmed	First Preference Shares – cum. redeemable

RATING HISTORY (as at Dec. 31)	Current	1998	1997	1996	1995	1994	1993	1992	1991
First Mortgage Bonds	A	A	A	A (high)	A (high)	A (high)	A (high)	A (high)	A (high)
First Preference Shares	Pfd-2	Pfd-2	Pfd-2	Pfd-2	Pfd-2	Pfd-2	Pfd-2	Pfd-2	-

RATING UPDATE

DBRS confirms the long-term debt and preferred share ratings of Newfoundland Power ("the Utility") based on the following considerations: (1) A comparatively strong balance sheet and favourable coverage ratios, given a regulatory deemed equity of 45%. (2) The island's geographic isolation and the unavailability of natural gas both limit competitive pressures. (3) The implementation of a formula-based mechanism to automatically adjust the approved ROE allows for better earnings predictability and should reduce regulatory lag. In addition, Newfoundland Power continues to focus on cost control efforts, which should help the Utility contend with potential competitive pressures as a result of current depressed oil prices. The Utility's primary challenge has been a weak provincial economy that has historically adversely affected earnings and electricity demand growth. However, progress on a number of energy related projects in the region continues in spite of weak oil prices. Over the longer-term, the regional economy is expected to benefit both from construction activity and the economic spill-over effects once the projects are up and running. These projects should be positive in terms of the Utility's future earnings outlook.

RATING CONSIDERATIONS

Strengths:

- Relatively strong balance sheet, 45% deemed equity
- Geographic isolation limits competitive pressures
- Implementation of formula-based ROE
- Weather variance account reduces s-t earnings volatility
- Power purchase costs passed through to customers

Challenges:

- Earnings sensitive to interest rates via approved ROEs
- Relative weak Provincial economy, but expected to improve over longer term
- High coupon debt not redeemable prior to maturity
- Low oil prices contributing to competitive pressures
- Unfunded pension liability

FINANCIAL INFORMATION

For years ended December 31st	1998	1997	1996	1995	1994	1993	1992	1991
Fixed Charges Coverage (times)	2.31	2.69	2.62	2.56	2.77	2.64	2.52	2.35
Cash Flow/Total Debt (times)	0.17	0.19	0.19	0.22	0.24	0.25	0.24	0.25
Cash Flow-Divid/Capital Expenditures (times)	0.64	0.85	0.55	1.20	0.69	1.16	0.93	0.85
Net Debt in Capital Structure	54.9%	53.2%	52.5%	50.3%	49.4%	48.1%	48.6%	48.7%
Average Coupon on L-T Debt	9.66%	10.26%	10.26%	10.54%	10.67%	10.67%	10.67%	11.10%
Approved ROE	9.25%	11.00%	11.00%	13.25%	13.25%	13.25%	13.25%	13.25%
Operating Income ($ millions)	63.5	72.3	68.4	64.1	70.5	70.3	67.0	64.2
Net Income (before extras.) ($ millions)	22.2	28.7	25.8	28.2	27.8	29.2	29.6	27.8
Operating Cash Flows ($ millions)	49.1	50.5	49.9	55.4	55.0	57.5	55.1	53.7
Electricity Sales - millions of kWh	4,440	4,438	4,425	4,382	4,371	4,286	4,244	4,196
Electricity Revenues (cents/kWh sold)	7.50	7.68	7.64	7.65	7.65	7.68	7.67	7.51
Variable Costs (cents/kWh sold)	5.50	5.51	5.58	5.61	5.48	5.51	5.59	5.49
Fixed Costs (cents/kWh sold)	1.20	1.17	1.14	1.18	1.17	1.15	1.12	1.10
Purchased Power (cents/net kWh purch)	4.75	4.72	4.78	4.80	4.74	4.79	4.61	4.59
Pre-tax Margin (cents/kWh sold)	0.80	1.00	0.92	0.86	0.99	1.01	0.95	0.92

COMPANY

Newfoundland Power Inc. distributes electricity throughout the island of Newfoundland. The Utility purchases the bulk of its electricity needs from government owned Newfoundland and Labrador Hydro and generates the balance from owned facilities. Newfoundland Power is a wholly owned subsidiary of Fortis Inc.

Regulation

Newfoundland Power Inc. is regulated by the Newfoundland & Labrador Board of Commissioners ("PUB"), based on a cost of service methodology. The PUB reduced the approved rate of return for 1998 and 1999 to 9.25% from 11.0% in 1997. In addition, effective 1999, the PUB established a formula based mechanism to adjust approved ROEs based on forecast long Canada bond yields. The key difference between this mechanism and that used in other jurisdictions is that rather than fluctuating every year with the movement in interest rates, ROEs will be adjusted only if they fall outside a specified range. The Utility's deemed equity component remains unchanged (40-45% common), and is slightly favourable compared to other regulated electric utilities in Canada. It is this capital structure which gives the Utility a comparatively strong balance sheet and favourable interest coverage ratios relative to other electric utilities.

Rating Considerations

Strengths: (1) Newfoundland Power has one of the strongest balance sheets in the industry. In addition, parent Fortis Inc. is available to potentially provide financial support should the need arise. Debt maturities are well staggered with no repayments required until 2005. (2) The geographic isolation of the island and the unavailability of natural gas limit competitive pressures. (3) The implementation of a formula-based mechanism to automatically adjust the approved ROE should contribute to better earnings predictability and reduced regulatory lag. (4) The Utility is permitted to maintain a weather normalization account to adjust for variances in weather and hydro-electric power availability against long term averages. Although the ultimate impact is small (less than 1.5% of revenues), it provides Newfoundland Power with a mechanism to stabilize earnings, particularly during periods of extreme weather conditions. (5) Newfoundland Power is permitted by the PUB to pass on any increase in power costs from Newfoundland and Labrador Hydro (N&L Hydro) to the consumer.

Challenges: (1) The earnings outlook will be strongly influenced by the provincial economy. Over the short term, completion of the construction phase of Hibernia, public sector restraint, changes in the Employment Insurance program and emigration will all contribute to relatively low economic growth. Over the longer term, the provincial economic outlook is more positive, given the commencement of Hibernia oil production, and the development of the Terra Nova and White Rose oil fields as well as other energy related projects in the region. (2) Earnings are sensitive to interest rates via the approved ROE. (3) The Utility has the highest average coupon on its outstanding long-term debt of all investor-owned utilities. This high debt cost is not likely to change in the near future as there are no debt maturities prior to 2005, and the mortgage bonds are not redeemable prior to maturity. (4) Depressed oil prices are contributing to competitive pressures. Revenues have been under some pressure in the space and water heating markets during the past few years, as oil prices declined (roughly 50% of total sales). New home penetration with electricity heating has dropped to 64%, but the incident reflects the competitive pressures that are beginning as the electric industry moves towards deregulation. (5) The Utility has a $5.1 million unfunded pension (actuarial) liability that will have to be addressed in the future. (6) In 1995, Revenue Canada issued a Notice of Reassessment disallowing certain deductions made by Newfoundland Power for tax purposes. The Utility is faced with a potential $38 million liability, but may have recourse to recover the costs through an application to the PUB. (7) Power costs from N&L Hydro are based on a blended rate produced from a mix of roughly 75% hydro and 25% thermal generated power. Rate increases, although not a cost consideration for Newfoundland Power since it is permitted to pass on the increase, are a concern from a market share perspective, as increases in electricity rates could reduce the competitive gap relative to oil in the home heating market.

Earnings

Earnings before extraordinary items were down sharply in 1998 as a result of a 175 basis point decline in the approved ROE (9.25% versus 11.0% in 1997), consistent with the trend in interest rates over the period. Electricity sales were relatively flat, with slightly lower residential sales offset by higher commercial sales.

Outlook: As the approved ROE for 1999 remains unchanged (9.25%), the earnings outlook will be largely influenced by the region's economic growth. Although the ongoing fishing moratorium and subsequent emigration are material constraints, the Provincial economic outlook appears more promising and should benefit from ongoing resource exploration and development. Other factors that will affect future earnings include (1) a continuing corporate focus on cost controls (positive over the longer term), and (2) potential competitive pressures from depressed oil prices (negative over the near term).

Financial Profile

Cash flows were relatively flat during 1998 with lower earnings offset by higher depreciation expenses following the commissioning of a new generating facility late in the year. The $13 million hydro plant largely accounted for the sharp increase in capital expenditures during 1998 relative to last year. Although dividends were reduced, net external financing increased to finance the project and balance sheet strength weakened slightly compared to 1997. The higher debt levels contributed to a weakening of coverage ratios, but ratios remain adequate given current credit ratings.

Outlook: The common equity component of the capital structure, currently at 43.2%, is below the allowed 45%. With capital expenditures dropping to more normal levels in the $30 million range, balance sheet strength could potentially improve over the next couple of years. Coverage ratios should improve accordingly, but are unlikely to return to historical highs given the current interest rate environment.

Bank Operating Lines of Credit Amounts - $285 million of uncommitted bank operating lines of credit.

Debt Maturities There are no debt maturities prior to 2005, although sinking fund requirements and installment payments amount to $3.055 million annually in each of the next five years.

Newfoundland Power Inc.

Balance Sheet
($ millions)

Assets:	1998	1997	1996	Liabilities & Equity:	1998	1997	1996
	As at December 31st				As at December 31st		
Cash + equivalents	0.0	0.0	0.0	S-T debt	5.0	30.6	19.9
Accounts rec	33.0	36.9	32.6	A/P + accr'd liab	55.0	57.6	56.9
Materials + supplies	3.7	3.7	4.3	LTD due in 1 year	3.1	2.6	2.6
Prepaids + stab acct	4.5	3.9	5.2	Current Liabilities	63.1	90.7	79.3
Current Assets	41.2	44.5	42.1	Def'd credits	15.0	17.1	19.4
Corp tax deposit	15.6	15.6	15.6	Long-term debt	283.2	236.3	238.8
Net fixed assets	507.4	491.8	489.6	Preferred shares	9.9	9.9	9.9
Deferred charges	36.5	29.6	26.3	Shlders' equity	229.5	227.5	226.2
Total	600.7	581.5	573.5	Total	600.7	581.5	573.5

Ratio Analysis	For years ended December 31st							
Liquidity Ratios	1998	1997	1996	1995	1994	1993	1992	1991
Current Ratio	0.65	0.49	0.53	0.49	0.60	0.77	0.86	0.45
Accumulated deprec/Gross fixed assets	41.7%	41.6%	40.3%	38.9%	37.0%	35.2%	33.5%	32.1%
Cash flow/Total debt	0.17	0.19	0.19	0.22	0.24	0.25	0.24	0.25
Cash flow/Capital expenditures	1.08	1.63	1.77	1.80	1.53	1.69	1.37	1.26
Cash flow-divid/Capital expenditures	0.64	0.85	0.55	1.20	0.69	1.16	0.93	0.85
Net debt in capital structure	54.9%	53.2%	52.5%	50.3%	49.4%	48.1%	48.6%	48.7%
Average coupon on l-t debt	9.66%	10.26%	10.26%	10.54%	10.67%	10.67%	10.67%	11.10%
Common equity in capital structure	43.2%	44.9%	45.5%	47.7%	48.1%	48.5%	45.7%	44.6%
Deemed equity	40-45%	40-45%	40-45%	40-45%	40-45%	40-45%	40-45%	40-45%
Preferred equity in capital structure	1.9%	2.0%	2.0%	2.0%	2.3%	2.3%	4.8%	6.7%
Common dividend payout (before extras.)	90.9%	84.0%	134.3%	65.0%	108.4%	59.2%	56.6%	60.2%
Coverage Ratios (1)								
Net interest coverage	2.46	2.87	2.82	2.79	3.03	3.07	3.04	2.90
EBITDA net interest coverage	3.55	3.93	3.90	4.04	4.24	4.25	4.22	4.01
Fixed charges coverage	2.31	2.69	2.62	2.56	2.77	2.64	2.52	2.35
Earnings Quality / Operating Efficiency								
Return on avg common equity (before extras.)	9.4%	12.4%	10.9%	12.0%	12.0%	12.6%	13.4%	13.2%
Approved ROE - mid point	9.25%	11.00%	11.00%	13.25%	13.25%	13.25%	13.25%	13.25%
Power purchases/Revenues	57.0%	55.5%	56.2%	56.4%	55.7%	55.8%	53.7%	54.6%
Operating margin	18.9%	21.0%	20.0%	18.9%	20.8%	21.1%	20.3%	20.1%
Gov't levies/Revenues	4.8%	5.4%	5.5%	3.9%	5.8%	5.6%	4.8%	4.7%
Net margin (before extras.)	6.6%	8.3%	7.5%	8.3%	8.2%	8.7%	9.0%	8.7%
Customers/Employee	303	301	262	253	255	248	210	205
Degree days - % normal	93%	103%	94%	101%	101%	107%	108%	107%
Rate base - $ millions	488	477	473	470	465	460	450	435
GWh sold/Employee	6.3	6.3	5.5	5.3	5.4	5.3	4.5	4.4
Generating Capacity								
Installed capacity - megawatts	148	147	147	147	147	147	147	147
Generated	429	424	423	423	420	420	417	417
Purchased	4,259	4,244	4,236	4,186	4,178	4,093	4,066	4,008
Gross power generated + rec'd	4,688	4,668	4,659	4,609	4,598	4,513	4,483	4,425
LESS: Transmission losses + internal use	248	230	234	227	227	227	239	229
Total sold - GWh	4,440	4,438	4,425	4,382	4,371	4,286	4,244	4,196
Energy lost + used/Energy gen + rec'd	5.3%	4.9%	5.0%	4.9%	4.9%	5.0%	5.3%	5.2%
Purchases/Energy gen + rec'd	90.8%	90.9%	90.9%	90.8%	90.9%	90.7%	90.7%	90.6%
Energy sales growth	0.0%	0.3%	1.0%	0.3%	2.0%	1.0%	1.1%	0.5%
Peak demand - megawatts	957	1,065	1,081	1,123	1,031	1,098	1,027	1,101

(1) Before capitalized interest / AFUDC.

Newfoundland Power Inc.

Income Statements ($ millions)	For years ended December 31st 1998	1997	1996	1995	1994	1993	1992	1991
Revenues:								
Residential	198.4	203.4	199.7	197.1	196.2	192.3		
General Service	134.5	137.3	138.2	138.2	138.0	136.7		
Electricity revenues	332.9	340.7	337.9	335.3	334.2	329.0	325.3	315.0
Other	2.9	3.0	3.6	3.6	4.1	4.5	4.9	4.1
Total revenues	335.8	343.7	341.6	338.9	338.4	333.6	330.2	319.1
Expenses:								
Operating + administration	52.6	53.9	54.6	54.8	51.2	50.1	59.9	55.9
Power purchased	191.5	190.6	192.1	191.1	188.4	186.1	177.4	174.4
Fuel	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.2
Depreciation	28.1	26.8	26.3	28.9	28.1	26.9	25.9	24.6
Total operating costs	272.3	271.4	273.2	274.8	267.8	263.2	263.3	255.0
Operating income	63.5	72.3	68.4	64.1	70.5	70.3	67.0	64.2
LESS: Interest expense	26.8	26.1	25.5	24.7	24.6	24.6	23.8	23.7
AFUDC	(0.6)	(0.2)	(0.3)	(0.3)	(0.3)	(0.4)	(0.4)	(0.7)
Interest income	(1.0)	(0.9)	(1.2)	(1.7)	(1.4)	(1.7)	(1.8)	(1.6)
Net interest costs	25.2	24.9	24.0	22.7	23.0	22.5	21.6	21.5
Net income before taxes	38.2	47.4	44.4	41.4	47.5	47.8	45.3	42.7
Income taxes	16.0	18.7	18.6	13.1	19.7	18.7	15.7	14.9
Net income before extras.	22.2	28.7	25.8	28.2	27.8	29.2	29.6	27.8
Extraordinary items	0.0	3.1	0.0	0.0	0.0	0.0	0.0	0.0
Net income	22.2	25.6	25.8	28.2	27.8	29.2	29.6	27.8
Operating Cash Flow	49.1	50.5	49.9	55.4	55.0	57.5	55.1	53.7
LESS: Dividends	20.2	24.2	34.4	18.6	30.1	17.9	17.6	17.7
Capital expenditures	45.4	30.9	28.2	30.8	36.0	34.1	40.3	42.5
Gross cash flow	(16.5)	(4.7)	(12.7)	6.1	(11.1)	5.5	(2.8)	(6.5)
Working capital	(0.6)	1.6	(10.1)	6.7	2.1	(7.6)	(5.5)	2.9
Free Cash Flow	(15.9)	(6.3)	(2.5)	(0.7)	(13.1)	13.2	2.7	(9.4)
Net Financing	46.6	(2.5)	37.3	(14.5)	(0.6)	(9.7)	18.4	35.1
Electricity Sold - Breakdown								
Residential	2,652	2,669	2,635	2,600	2,594	2,540	2,509	2,462
General Service	1,788	1,769	1,790	1,782	1,777	1,746	1,735	1,734
Total sold - GWh	4,440	4,438	4,425	4,382	4,371	4,286	4,244	4,196
Unit Revenues and Costs	(cents / kWh sold) (1)							
Revenues:								
Residential	7.48	7.62	7.58	7.58	7.56	7.57	0.00	0.00
Commercial	7.52	7.76	7.72	7.76	7.77	7.83	0.00	0.00
Average electricity revenues	7.50	7.68	7.64	7.65	7.65	7.68	7.67	7.51
Ancillary businesses	0.06	0.07	0.08	0.08	0.09	0.11	0.12	0.10
Average revenues	7.56	7.74	7.72	7.73	7.74	7.78	7.78	7.61
Costs:								
Operating & administration	1.19	1.21	1.23	1.25	1.17	1.17	1.41	1.33
Power purchases	4.31	4.29	4.34	4.36	4.31	4.34	4.18	4.16
Fuel	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Variable Costs	5.50	5.51	5.58	5.61	5.48	5.51	5.59	5.49
Net interest costs	0.58	0.57	0.55	0.52	0.53	0.53	0.52	0.53
Total Cash Costs	6.08	6.08	6.13	6.14	6.02	6.05	6.11	6.02
Cash Margin	1.48	1.67	1.59	1.60	1.73	1.73	1.67	1.59
Capitalized interest	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)	(0.02)
Depreciation	0.63	0.60	0.59	0.66	0.64	0.63	0.61	0.59
Pretax margin	0.86	1.07	1.00	0.94	1.09	1.12	1.07	1.02
Income taxes	0.36	0.42	0.42	0.30	0.45	0.44	0.37	0.35
Net margin	0.50	0.65	0.58	0.64	0.64	0.68	0.70	0.66
Variable Costs (excl inc taxes)	5.50	5.51	5.58	5.61	5.48	5.51	5.59	5.49
Fixed Costs (deprec, int + levies)	1.20	1.17	1.14	1.18	1.17	1.15	1.12	1.10
Total Costs	6.70	6.68	6.72	6.79	6.65	6.67	6.71	6.59
Purchased power cost/net kWh purchased	4.75	4.72	4.78	4.80	4.74	4.79	4.61	4.59

(1) Tables may not add due to rounding.