Standard & Poor's Rating Report

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Summary: Newfoundland Power Inc.

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Analyst: Damian DiPerna, Toronto (1) 416-956-4870; Jenny Catalfo, Toronto (1) 416-956-4870

Credit Rating: A-/Stable/--

Rationale

The ratings on Newfoundland Power Inc. reflect the following:

-- The rating on parent Fortis Inc., which holds the common stock of Maritime Electric Co. Ltd., Newfoundland Power, and Fortis US Energy, as well as equity interests in Belize Electricity, Canadian Niagara Power, and Caribbean Utilities Co. Ltd.

-- Newfoundland Power's cost of service-rate of return regulation with complete flow through of purchased power costs to customers. Like other Canadian regulated utilities, Newfoundland Power's approved ROE is adjusted in response to changes in long-term Government of Canada bond yields. Nevertheless, rather than fluctuating from year to year, the allowed rate of return is adjusted only when it falls outside a specified range. As a result, Newfoundland Power's earnings are less sensitive to interest rate movements than those of other regulated utilities.

-- Newfoundland Power's regulated capital structure ensures that financial leverage remains stable, reflecting a 45%-allowed equity component, the highest of all Canadian regulated utilities.

-- The utility's position as the principal distributor of electricity in the province of Newfoundland, serving 85% of all electricity customers, the vast majority of which are residential and small to midsize commercial and institutional customers. The company generates about 9% of its energy requirements and purchases the remaining 91% from provincially owned Newfoundland and Labrador Hydro.

-- In spite of strong real GDP growth in the past few years, and favorable economic growth forecasts for the next few years as a result of ongoing resource exploration and development in the region, Newfoundland Power's annual demand load forecast remains relatively low at about 1%, due to high unemployment, emigration, and public sector restraint. As a result, the company's rate base and revenue stream also will grow at a modest pace.

In 2000 Fortis' total debt to capital increased marginally to 64% and is currently above historical highs. Nevertheless, Fortis plans to reduce debt with surplus cash flow and the refinancing of its 2002 preferred shares over a longer term. The company's target debt to total capital is around 60% and is partially predicated on regulatory limits on its two largest subsidiaries, Newfoundland Power (45% deemed equity) and Maritime Electric (40% deemed equity). In the future, Fortis' funds from operations (FFO) interest coverage of 2.4 times and FFO to total debt of 11% should show modest improvements.

Outlook

Earnings and growth of the rate base will remain modest, with annual demand growth in the 1% area, but combined with cost controls and improved operating efficiencies, they should lead to a modest improvement in profitability. With good cash flows and moderate capital expenditure requirements, Newfoundland Power should continue to generate surplus cash flows that will be dividended up to parent Fortis, while a regulated capital structure ensures that financial leverage remains stable.