

**MANITOBA HYDRO
2010/11 & 2011/12 GENERAL RATE APPLICATION**

INTEGRATED FINANCIAL FORECAST & ECONOMIC OUTLOOK

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MANITOBA HYDRO
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INTEGRATED FINANCIAL FORECAST

5.0 OVERVIEW

Tab 5 discusses the Integrated Financial Forecast (IFF) and financial outlook of Manitoba Hydro.

Section 5.1 – 2009 Economic Outlook.

Section 5.2 – Integrated Financial Forecast, IFF09-1.

Section 5.3 – Financial Targets.

Appendix 5.1 – 2009 Economic Outlook.

Appendix 5.2 – Integrated Financial Forecast, IFF09-1.

5.1 ECONOMIC OUTLOOK

The Economic Outlook is prepared at the start of the annual forecasting cycle at Manitoba Hydro each year. It provides a forecast of economic variables that are used in other forecasts. Variables such as real gross domestic product (“RGDP”), and residential customer projections are inputs to the Load Forecast; interest, escalation and exchange rates are used in a number of component forecasts that are inputs to the Integrated Financial Forecast.

The Economic Outlook is prepared in the spring of each year. Weaker economic growth stemming from U.S. financial, housing and auto sectors in the latter part of 2008/09 continued to impact the views of forecasters in 2009. The 2009 Economic Outlook is provided in Appendix 5.1.

1 Due to uncertainty pertaining to the current economic situation key short term variables
 2 including escalation, interest rates and exchange rates impacting the IFF were reviewed
 3 in summer 2009 to ensure that current information was considered in the forecast.
 4

5 The value of the Canadian dollar continued to exhibit volatility relative to the US dollar
 6 throughout the summer of 2009. The Canadian dollar averaged \$1.26 in March 2009,
 7 \$1.12 in July 2009 and further appreciated to reach \$1.02 in mid-October 2009. The
 8 value of the Canadian dollar had appreciated over the summer due, in large part, to the
 9 US dollar depreciating relative to other currencies in response to ongoing concerns with
 10 U.S. trade and budgetary deficits. Due to this volatility, forecasts of exchange and interest
 11 rates were reviewed again in October 2009 to ensure the most current information was
 12 reflected in the IFF. The Manitoba Hydro short term and long term cost of debt, shown in
 13 the table below, incorporates the relevant credit spread and the provincial guarantee fee.
 14 As a result of these subsequent reviews, the values of certain variables that were used in
 15 the IFF differ from those in the 2009 Economic Outlook. The revised variables are as
 16 follows:
 17

	CPI % change	Short-Term Interest Rate		Long-Term Interest Rate		Cdn\$/US\$
		T- Bill %	MH Cost of Debt %	10 Yr+ %	MH Cost of Debt %	
2009/10	0.6	0.25	1.45	3.70	5.60	1.11
2010/11	1.9	1.20	2.40	4.00	5.65	1.07
2011/12	2.0*	3.40	4.60	4.60	6.20	1.09
2012/13	2.0*	4.10	5.30	5.10	6.70	1.07

18
 19 *Note: CPI was unchanged from 2009 Economic Outlook for 2011/12 and 2012/13.
 20

21 **5.2 INTEGRATED FINANCIAL FORECAST**

22
 23 The Integrated Financial Forecast IFF09-1 sets forth the projected financial results and
 24 financial position of Manitoba Hydro. Its purpose is to provide an indication of the
 25 Corporation's long-term financial direction and for use in sensitivity analysis evaluating
 26 strategic alternatives. The forecast IFF09-1 can be found in Appendix 5.2.
 27

28 This year's IFF reflects the impacts of the economic downturn on short-term financial
 29 results and the consequential impacts over the 10-year forecast period. A comparison of
 30 MH09-1 with MH08-1 in Table 5.1.1 shows a significant decline in net income due

1 mainly to the lower domestic revenues throughout the forecast and lower net export
 2 revenues in the early years of the forecast.

3
Table 5.1.1 - Comparison of Electrical Operations MH09-1 to MH08-1
Increase/(Decrease)
(millions of \$)

	2010 - 2012			2010 - 2019		
	MH09-1	MH08-1	Variance	MH09-1	MH08-1	Variance
General Consumers at projected rates	3,599	3,810	(212)	14,179	14,709	(530)
General Consumers at approved rates	3,496	3,563	(67)	12,178	12,400	(221)
Projected Rate Increases	102	247	(145)	2,001	2,310	(309)
Extraprovincial (net of Fuel & Power Purchased and Water Rentals)	528	546	(18)	2,360	2,149	212
Other	22	22	(0)	81	78	2
Total Revenues	4,149	4,378	(230)	16,620	16,936	(316)
Operating and Administrative	1,155	1,102	52	4,241	4,003	238
Finance Expense	1,297	1,318	(21)	5,228	5,169	59
Depreciation and Amortization	1,161	1,190	(30)	4,498	4,692	(194)
Capital and Other Taxes	226	220	7	927	893	34
Corporate Allocation	26	24	2	88	79	9
	3,864	3,854	11	14,982	14,836	145
Non-controlling Interest	1	2	(1)	(51)	(32)	(19)
Net Income	286	526	(241)	1,587	2,068	(480)

4
 5
 6 General Consumers Revenue is lower compared to MH08-1 due to lower projected load
 7 growth. Although lower projected Manitoba load growth increases the amount of export
 8 energy available, the increase in volume is significantly more than offset by lower export
 9 prices in the shorter term reflecting current market conditions. After a return to expected
 10 export prices in 2011/12, the additional available export energy results in increased net
 11 extraprovincial revenues in the longer term.

12
 13 Operating and administrative expenses over the IFF period are projected to increase by
 14 \$18 million from IFF08 net of the reclassification of the IFRS and Canadian Accounting
 15 Standard change provisions totalling \$220 million which was previously included in
 16 Depreciation and Amortization in MH08-1. The remaining increase is the result of
 17 higher wage and benefit settlements, higher pension costs and higher costs of maintaining
 18 aging generation, transmission and distribution infrastructure, largely offset by cost
 19 saving measures and productivity improvements.

20
 21 Finance expense is initially lower compared to MH08-1 due to lower projected interest
 22 rates and then higher over the remaining forecast period due to increased cash
 23 requirements and debt resulting from lower overall net income.

1 Depreciation and amortization expenses have increased \$26 million net of the MH08-1
2 IFRS and Canadian Accounting Standard change provision. This increase is primarily
3 attributable to the timing of expenditures and in-service dates of capital projects.
4

5 The Corporation is embarking on a period of major investment in generation and
6 transmission systems. During this time, it is projected that the debt/equity ratio will rise
7 above the target level within an acceptable range; however, a strong improvement to
8 financial ratios is anticipated following the period of investment. The proposed rate
9 increases of 2.9% effective April 1, 2010 and 2.9% effective April 1, 2011 maintain
10 ratios within a reasonable range and achieve an appropriate balance between customer
11 sensitivity and fiscal responsibility.
12

13 Only the rate increases proposed for 2010/11 and 2011/12 have been approved by the
14 Board of Manitoba Hydro-Electric Board. Proposed rate increases subsequent to 2011/12
15 may be changed in subsequent forecasts and are presented for illustrative purposes only.
16 Each year's revision to the Integrated Financial Forecast is based on the current year's
17 assumptions including energy supply and demand, projected interest and escalation rates,
18 projected prices for exported energy, operating and capital forecasts and other factors.
19 Changes in any of these assumptions will have an impact on the projected future results.
20 Actual rate applications made in future years will depend upon the circumstances and
21 outlook at that time and will be subject to the review and approval of the Manitoba
22 Hydro-Electric Board.
23

24 **5.3 FINANCIAL TARGETS**

25

26 Manitoba Hydro has the following financial targets for consolidated operations:
27

- 28 – Debt/Equity: Maintain a minimum debt/equity ratio of 75:25.
- 29
- 30 – Interest Coverage: Maintain a minimum annual gross interest coverage ratio of
31 greater than 1.20.
- 32
- 33 – Capital Coverage: Maintain a capital coverage ratio of greater than 1.20 (excepting
34 new major generation and transmission).
- 35

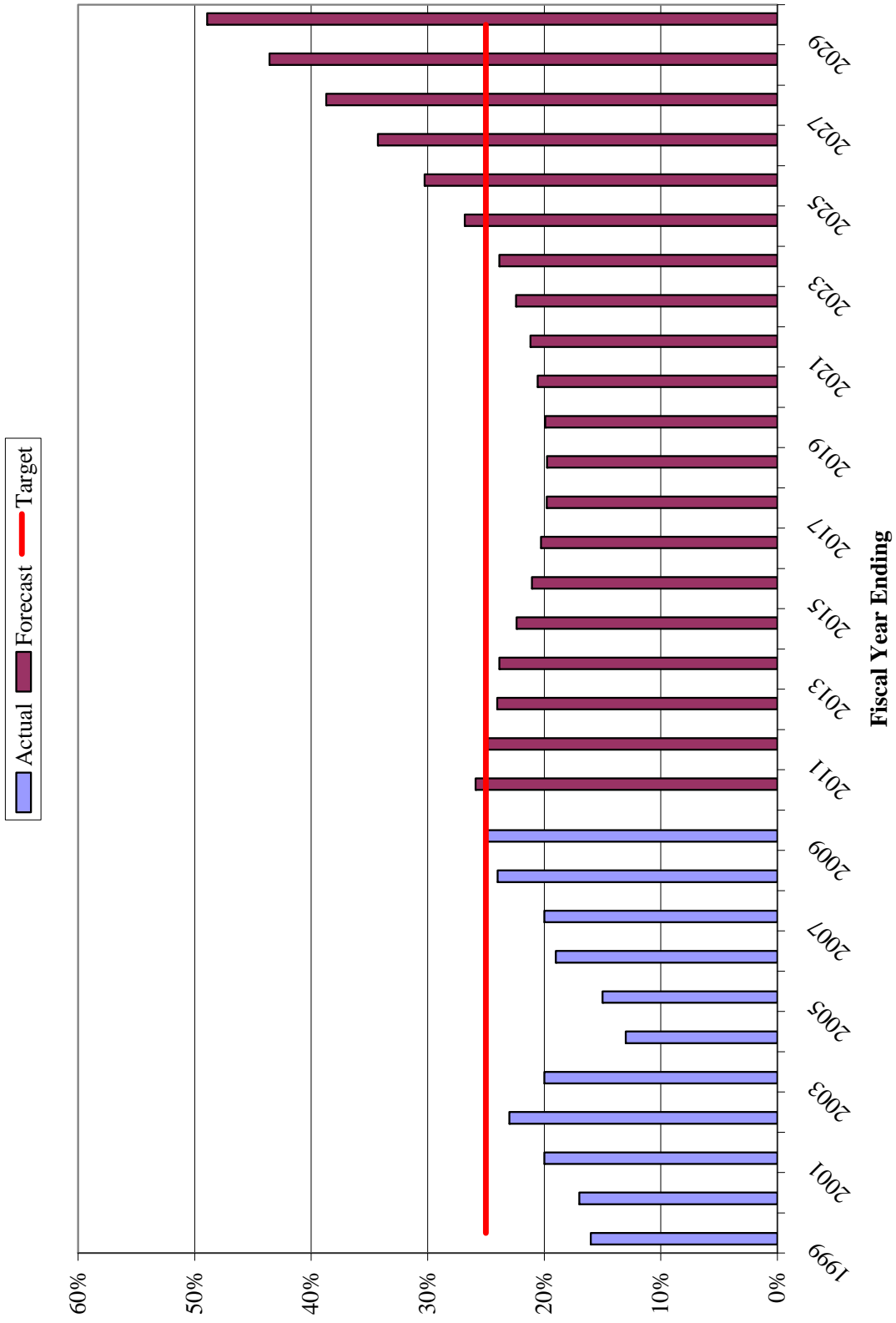
36 Note: Financial targets not be maintained during years of major investments in the
37 generation and transmission system.

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The following charts indicate the debt/equity, interest coverage and capital coverage ratios of recent years and the forecasts in the current Financial Outlook.

1

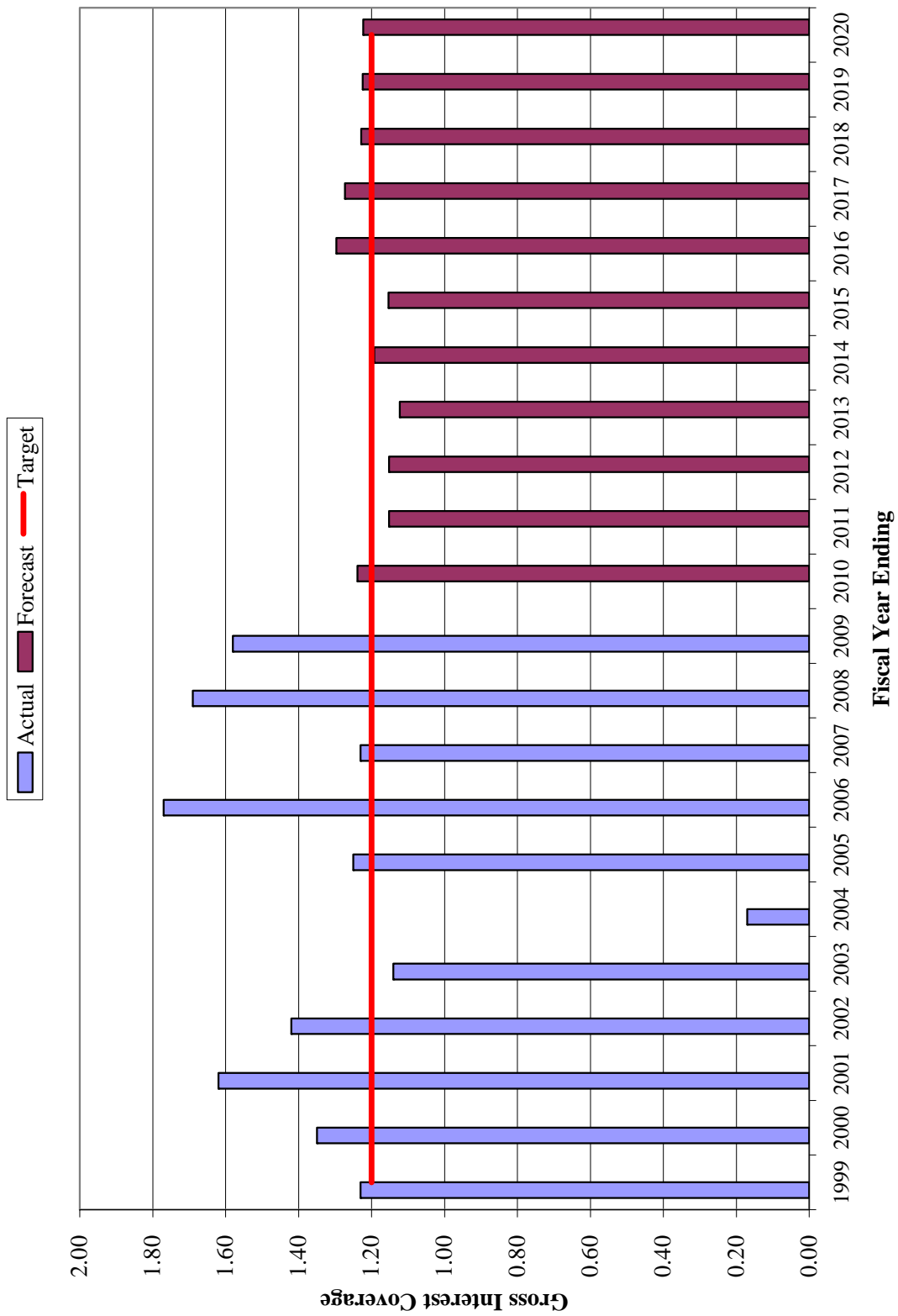
Figure 5.2.1 – Equity Ratio (Consolidated Operations)



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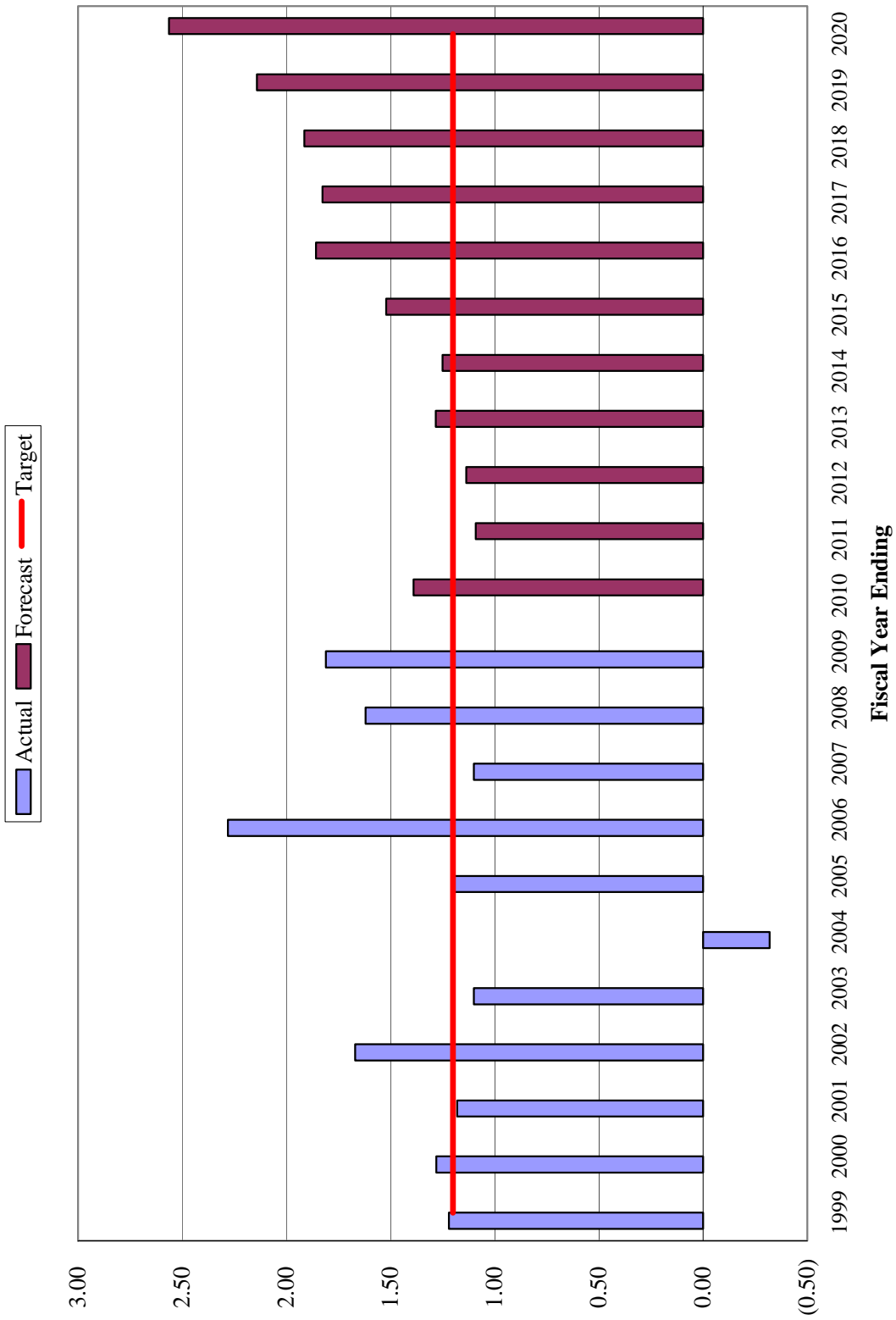
Figure 5.2.2 - Interest Coverage Ratio (Consolidated Operations)



3

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Figure 5.2.3 - Capital Coverage Ratio (Consolidated Operations)



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