

Ontario Electricity Financial Corporation Bulletin

August 30, 2002

2002 OEFC Annual Report Highlights

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Highlights in 2001-02

Ontario Electricity Financial Corporation (OEFC) accomplished its key objectives for 2001-02, namely:

Achieved cost-effective borrowing and debt management.

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Continued the necessary revisions to the non-utility generator (NUG) contracts to prepare for a competitive electricity market.

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Initiated the development of necessary infrastructure to manage the NUG contracts and related exposures in a competitive market, in a cost-effective and prudent manner.

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Concluded an agreement on the division and transfer of the assets and liabilities of the OEFC pension plan to the pension plans of the other successor corporations. Approval for the transfer of the assets was obtained from the Superintendent of Financial Services, with the transfer occurring on June 29, 2001.

2001-02 Borrowing Program

- OEFC's borrowing requirements for 2001-02 were \$3.4 billion, excluding rollovers of maturing short-term debt.
- OEFC completed \$1.8 billion of the borrowing program in long-term funding, all in the Canadian dollar domestic market, including pre-borrowing in 2000-01 of \$0.3 billion, and by using financial market transactions to fix interest rates on \$0.4 billion of short-term debt.
- The remaining borrowing requirement was funded by issuing \$1.6 billion in short-term debt. Total short-term debt outstanding increased by only \$1.4 billion through the fiscal year, as the \$0.4 billion in new fixing of interest rates on short-term debt was offset by \$0.6 billion in maturities of transactions of this nature.

2001-02 Financial Highlights

- As of March 31, 2002, total debt outstanding was \$29.4 billion, a decrease of \$1.2 billion from the previous fiscal year. Overall debt left by the former Ontario Hydro has been reduced by \$1.9 billion from its peak in 1999-2000.
- For the year ended March 31, 2002, revenues totalled \$3,544 million, while expenses totalled \$3,613 million, resulting in a deficiency of revenue over expense of \$69 million, a reduction of \$87 million from the prior year's excess of revenue over expense of \$18 million.
- This decrease reflects lower payments-in-lieu of taxes, primarily due to the decline in OPG's financial results for the first quarter of 2002, which included non-recurring costs for restructuring of \$210 million and recognition of unrealized losses on transition rate options of \$210 million. OPG's losses resulted in no electricity sector dedicated income transfer from the Province. This reduction was partially offset by an increase in the revenue pool residual as a result of the increase in wholesale electricity rates, effective June 1, 2001.

Risk Management

OEFC's foreign exchange and floating interest rate exposures remained within policy limits in 2001-02.

Foreign Exchange Exposure: The target for unhedged foreign currency exposure by the end of fiscal 2002-03 is five per cent of outstanding debt, although the policy limit is 20 per cent. When the OFA became responsible for the management of OEFC's debt portfolio, total debt exposed to fluctuations in foreign currencies was 14.5 per cent. The OFA reduced OEFC's exposure to 7.5 per cent as of March 31, 2002. The OFA will continue to reduce the level of exposure towards the five per cent target in a prudent manner.

Floating Interest Rate Exposure: The limit on OEFC's floating interest rate exposure (net of liquid reserves) is 20 per cent of outstanding debt. Actual floating interest rate exposure was 9.8 per cent as of March 31, 2002.

Management of Power Purchase Agreements

During 2001-02, OEFC completed the following initiatives:

- Continued to negotiate revisions to the NUG contracts to ensure that the contracts are consistent with the requirements of the transition to an open market.
- Facilitated the transition from Hydro One to UBS Warburg Energy (Canada) Ltd. (UBS) as settlement services manager of the power purchase agreements (PPAs) with the NUGs.
- Worked with UBS to establish systems and procedures for the administration of the PPAs in an open electricity market.
- In anticipation of OEFC's participation in Ontario's electricity market, the Board of Directors approved a policy framework addressing risks associated with the management of the NUG contracts.

OEFC Objectives in 2002-03

OEFC's activities for 2002-03 will be focused on the following corporate objectives:

- Provide borrowing, risk management, cash management, banking and accounting services as required to manage and retire the outstanding debt and derivatives portfolios of the former Ontario Hydro;
- Negotiate revisions to the NUG contracts to ensure that the contracts are consistent with the requirements of the open market. Manage the NUG contracts and related exposures within a competitive electricity market in a cost effective and prudent manner.

Debt Repayment Plan

Pursuant to the *Electricity Act, 1998* and consistent with the principles of electricity sector restructuring, the government has established a long-term plan to retire debt from within the electricity sector. The \$38.1 billion in obligations (as of April 1, 1999) is being repaid from the following sources:

- Notes receivable from the Province, OPG, Hydro One and the IMO;
- Payments-in-lieu (PILs) of corporate income, capital, and property taxes, made by OPG, Hydro One and municipal electric utilities (MEUs);
- A Debt Retirement Charge (DRC), paid by electricity consumers commencing on May 1, 2002, the day the electricity market opened to competition. The charge will end once the residual stranded debt is retired and will be administered by the Ministry of Finance on behalf of OEFC. Prior to May 1, 2002, OEFC received the residual of the revenue pool. This pool, managed by OPG, collected revenues from electricity consumers and allocated revenues to OPG, Hydro One and IMO, with the residual going to OEFC; and
- Electricity Sector Dedicated Income. Consistent with the government's commitment to keep electricity income in the electricity sector, the combined net incomes of OPG and Hydro One in excess of the Province's interest cost of its investment in its electricity subsidiaries is dedicated to the retirement of OEFC's debt.
- The long-term plan supports a current estimate that OEFC's obligation will likely be defeased in the year 2012.

2002-03 Financing Requirements

- Maturing debt and planned redemptions are \$2.7 billion in 2002-03.
- Total debt outstanding is projected to decrease to \$28.8 billion at March 31, 2003.

Additional Information

Ontario Electricity Financial Corporation (OEFC), an agency of the Province of Ontario, is a statutory, non-share capital corporation and the legal continuation of Ontario Hydro.

A full set of 2001-02 OEFC financial statements can be found in the 2002 OEFC Annual Report at www.oefc.on.ca

Contact (416) 325-8000 or email investor@oefc.on.ca to request a hard copy of the report.