NLH-171 PUB (Re: Page 6, lines 8-11)

Dr. Waverman states, “Thus, Hydro’s business risk is priced by Canadian capital markets and will be a normal part of Hydro’s regulated prices if regulated rates reflect its capital costs – i.e., its embedded cost of debt, and for shareholder’s equity (primarily retained earnings) the marginal cost of debt.” Please explain how Hydro’s business risk is priced separately from the other risks faced by holders of Newfoundland and Labrador bonds, given that Hydro’s bonds are guaranteed by the Province.

A. Hydro bondholders will expect, in the first instance, to be repaid out of Hydro’s cash flows, and will therefore take Hydro’s net income, cash flows and financial integrity into account when debt is raised by Hydro in bond markets. The Provincial guarantee, which acts as a “backstop” or secondary source of repayment, will also be factored in when capital is raised by Hydro in bond markets.