

1 **Q. Chairman's question of November 10, 2009 at page 94, line 16 et. seq.**

2  
3 **A. 1. General**

4  
5 The Chairman inquired as to (i) the forecast returns on equity and relative risk of Fortis  
6 Inc. ("Fortis") and Newfoundland Power and (ii) why Fortis wouldn't be included as a  
7 comparable company for cost of equity estimation purposes.

8  
9 In his question, the Chairman referred to (i) *The Blue Book of CBS Stock Reports*, August  
10 2009, and (ii) a *BMO Capital Markets* report on Fortis by Michael McGowan, dated June  
11 11, 2009. Both of these documents were attached with materials filed by the Consumer  
12 Advocate in relation to the cross-examination of Ms. McShane on October 19, 2009.  
13 Neither document was used in the cross-examination of Ms. McShane or any other  
14 witness.

15  
16 For convenience, a copy of the *Blue Book* report is Attachment A and a copy of the *BMO*  
17 *Capital Markets* report is Attachment B.

18  
19 Newfoundland Power's counsel undertook to provide a response to the Chairman's  
20 inquiry.

21  
22 **2. Book vs. Market Returns**

23  
24 Implicit in the Chairman's question was the inference that the return expected by  
25 investors in Fortis was less than that sought by Newfoundland Power in this proceeding.  
26 That inference is incorrect. In order to understand why this is so, it is necessary to  
27 understand the difference between a market return on an investment in a security (the  
28 share price) and a return on book equity.

29  
30 Newfoundland Power is entitled to the opportunity to earn a fair return. One element of  
31 the fair return is that it be commensurate with returns on investments of similar risk. In  
32 the determination of whether a return is commensurate with returns on investments of  
33 similar risk, the appropriate perspective is the *market* return on investments of similar  
34 risk. Market returns are consistent with the concept of opportunity cost.<sup>1</sup>

35  
36 In the *Blue Book* report, a return on equity of 8.3% was indicated for Fortis. In the *BMO*  
37 *Capital Markets* report, a 2010 estimated return on equity of 8.5% is indicated for Fortis.  
38 Both of these returns on equity refer to returns on *book* equity of Fortis. As such, the  
39 returns are accounting rates of return based upon book values as opposed to market  
40 returns.

---

<sup>1</sup> See McShane Evidence, Appendix A; and Booth Evidence, Appendix B.

1 But an investor in Fortis stock would expect to receive a *market* return on his or her  
2 investment in the stock.

3  
4 The difference between book returns and market returns can be observed from the *BMO*  
5 *Capital Markets* report. In that report, the analyst indicates a target price for Fortis stock  
6 of \$27.00 or \$1.95 higher than the June 11, 2009 price of \$25.05. This indicates  
7 estimated capital appreciation in Fortis' stock of 7.8% ( $\$1.95 / \$25.05 = 7.8\%$ ). In  
8 addition, the report indicates a dividend yield of \$1.04 or 4.2%. It is the combination of  
9 capital appreciation and dividend yield which represents the estimated *market* return on  
10 Fortis stock of approximately 12% indicated in the *BMO Capital Markets* report.<sup>2</sup> It is  
11 presumably this return which is the basis for the *BMO Capital Markets* stock rating of  
12 outperform.

13  
14 As a matter of North American regulatory practice, the return ultimately determined by  
15 the regulator to be just and reasonable is applied to a regulated utility's *book* equity.  
16 When the allowed return on a regulated utility's book equity is set, a market-derived cost  
17 of attracting capital (that is a *market* return) is converted to a fair return on equity.

18  
19 In the case of Newfoundland Power, it is entitled to the opportunity to earn a just and  
20 reasonable return on its book equity commensurate with the market return on investments  
21 of comparable risk. If Fortis was to be considered a comparable company to  
22 Newfoundland Power, the required return, based upon the views of *BMO Capital*  
23 *Markets*, would be in excess of 12%.<sup>3</sup> However, as indicated below, it is not appropriate  
24 to consider Fortis a comparable company to Newfoundland Power for the purpose of  
25 estimating a fair return.

### 26 27 **3. Comparisons of Fortis and Newfoundland Power**

#### 28 29 ***Relative Riskiness***

30  
31 Fortis is an unregulated utility holding company which holds interests in a number of  
32 regulated utilities in addition to other investments, some of which are unregulated. This  
33 diversity affects comparisons of the relative riskiness of Fortis and Newfoundland Power  
34 from an investor perspective.

35  
36 For example, Fortis indicates in its Management Discussion and Analysis that its key  
37 business risk is regulatory risk. However, it also indicates that "Although the receipt of  
38 an adverse regulatory decision may materially affect the ability of any utility to recover  
39 the cost of providing its services and achieving a reasonable rate of return, the impact on

---

<sup>2</sup> As at September 10, 2009, Mr. McGowan of BMO Capital Markets was indicating a target price for Fortis stock of \$29.00, or \$4.01 higher than the September 10, 2009 price of \$24.99. This indicates estimated capital appreciation in Fortis' stock of 16% ( $\$4.01 / \$24.99 = 16\%$ ). When combined with a dividend yield of \$1.04, or 4.2% at September 10, 2009, this indicates an estimated *market* return of 20.2%. See Attachment C.

<sup>3</sup> See footnote 2.

1 the Corporation as a whole is lessened due to the geographic and regulatory diversity of  
2 its operations.”<sup>4</sup>

3  
4 From an investor perspective, the combination of unregulated investment and overall  
5 diversity impacts any assessment of the relative riskiness of Fortis as compared to  
6 Newfoundland Power.

### 7 8 ***Credit Ratings*** 9

10 Fortis has a lower credit rating than many of its larger Canadian regulated utilities,  
11 including Newfoundland Power.<sup>5</sup> This is because Fortis’ credit requirements are  
12 different than those of Newfoundland Power.

13  
14 Fortis’ regulated subsidiaries operate on a standalone basis and raise debt on a standalone  
15 basis. This permits them to fund the ongoing capital expenditure required to discharge  
16 the regulatory obligation to serve. As an unregulated utility holding company, Fortis is  
17 not required to fund a continuing obligation to serve customers as Newfoundland Power  
18 is.

19  
20 Fortis’ assets predominantly consist of interests in other companies. Fortis has very  
21 limited physical assets. It does not issue secured financing as it has no physical assets to  
22 secure.<sup>6</sup> So, Fortis has never issued secured bonds or been subject to the same type of  
23 debt issue conditions such as the trust deed requirements that apply to Newfoundland  
24 Power.

25  
26 These differences affect the credit requirements of Fortis. In his question, the Chairman  
27 made reference to different coverage ratios between Fortis and Newfoundland Power.  
28 The observed differences in coverage ratios are simply one reflection of broader  
29 differences in credit requirements between Fortis, a holding company, and Newfoundland  
30 Power, an operating utility.

### 31 32 ***Fortis as a Comparable Company*** 33

34 For a regulated utility, returns are determined by a regulator. For this reason, estimating  
35 a regulated utility’s return by reference to the utility itself is, to a large degree, a  
36 projection of what returns the regulator will allow. This exercise has an inevitable  
37 element of circularity.<sup>7</sup>  
38

---

<sup>4</sup> See CA-NP-58, Attachment C, *Fortis 2008 Annual Report*, Page 25.

<sup>5</sup> Fortis has an A- long term corporate and unsecured debt credit rating from Standard & Poor’s and a BBB (high) unsecured debt credit rating from DBRS. See CA-NP-58, Attachment C, *Fortis 2008 Annual Report*, Page 50. Newfoundland Power has an A bond rating from DBRS and an issuer debt rating of Baa1 and an A2 bond rating from Moody’s Investor Services. See Exhibit 4 (1<sup>st</sup> Revision).

<sup>6</sup> See footnote 4.

<sup>7</sup> See, for example, McShane Evidence, Page 62, Lines 1569-1574.

1 Returns achieved by Fortis, to a large degree, reflect the returns allowed by Canadian  
2 regulators for its regulated utility subsidiaries, including Newfoundland Power.<sup>8</sup>  
3 Inevitably, therefore, comparisons of Fortis to Newfoundland Power for the purposes of  
4 estimating a fair return will also have a degree of circularity.  
5

6 For this reason, use of Fortis as a comparable company for the purposes of estimating a  
7 fair return for Newfoundland Power is conceptually problematic. No cost of capital  
8 expert in this proceeding indicated that Fortis was an appropriate comparator for the  
9 purposes of estimating a fair return for Newfoundland Power for 2010.

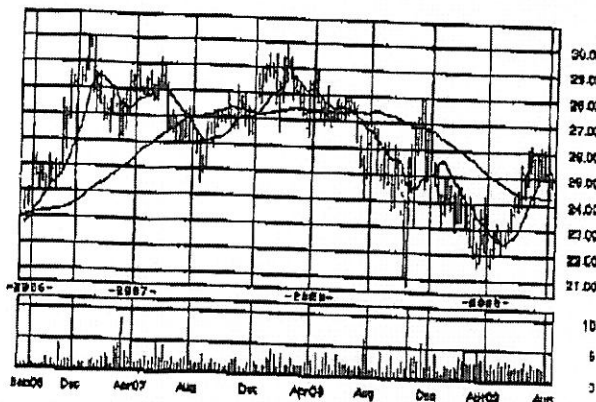
---

<sup>8</sup> See CA-NP-58, Attachment C, *Fortis 2008 Annual Report*, Page 28.

**Blue Book of CBS Stock Reports**  
**August 2009**

# FORTIS' BUSINESS (Gas & Electrical Utilities)

Fortis owns Newfoundland Power, Maritime Electric, Fortis US Energy, Canadian Niagara Power, Cornwall Electric, FortisAlberta/BC, Belize Electric, Fortis Turks & Caicos and Terasen Gas. Interests in Belize Electricity, 67%; Caribbean Utilities, 54%. Owns hotels and commercial real estate.



HEAD OFFICE 139 Water St.  
Suite 1201, P.O. Box 6837  
St. John's, NL A1B 9T2  
TEL: (709) 737-2800  
FAX: (709) 737-5007

Traded: TSX  
Trading volume: 123,645,000  
Avg. per month: 10,300,000  
Web site: www.fortis.com

## Marpep Multi-year performance analysis

Fiscal year ended Dec. 31	2008	2007	2006	2005	2004	2003
Selected figures from income and cash flow statements (\$ thousands) (p)						
Total revenues	3,905,000	2,722,000	1,478,000	1,447,240	1,151,430	643,080
Operating profit — EBITDA (p)	1,048,000	814,000	523,000	503,710	378,659	253,854
Operating profit — EBT	702,000	544,000	361,000	350,323	271,199	201,242
Income before income taxes	337,000	250,000	183,000	213,729	143,458	118,687
Income	259,000	199,000	148,000	137,097	80,655	77,582
Operating items	0	8,000	2,000	8,897	-1,384	0
Real dividends	176,000	134,000	75,000	62,368	43,828	40,372
Cash flow from operations	645,000	479,000	336,000	309,473	224,948	140,155
Free cash flow (p)	-435,000	-458,000	-238,000	-198,924	-102,551	99,783
Balance Sheet Information (\$ thousands) (p)						
Current assets	1,150,000	1,038,000	408,000	293,274	283,423	192,532
Current liabilities	1,897,000	1,804,000	558,000	412,298	538,258	238,056
Working capital	-547,000	-766,000	-150,000	-119,024	-254,835	-103,524
Net fixed assets	7,809,000	7,287,000	4,044,000	3,315,001	2,712,747	0
Total assets	11,178,000	10,273,000	5,441,000	4,587,104	3,938,018	2,163,797
Long-term debt	4,894,000	4,523,000	2,556,000	2,135,874	1,904,491	0
Total shareholders' equity	3,393,000	2,723,000	1,388,000	1,213,413	1,000,112	737,657
Financial data (\$ per common share) (p)						
Total revenues	24.81	19.78	14.27	14.22	13.59	12.18
Cash flow	4.10	3.48	3.24	3.04	2.65	2.02
Earnings before income taxes	2.14	1.82	1.82	2.10	1.69	1.73
Net earnings	1.56	1.40	1.42	1.35	1.07	1.06
EPS fully diluted	1.52	1.32	1.37	1.24	1.01	1.02
Dividend	1.00	0.82	0.67	0.59	0.55	0.53
Cash flow after dividend	3.10	2.66	2.57	2.45	2.11	-0.08
Shareholders' equity (book value)	18.00	16.72	12.26	11.78	10.47	8.84

## Key ratios we use to assess profitability

EBITDA as % of operating rev.	26.9	29.9	35.8	35.2	33.1	30.5
Net inc. as % of total rev. (net margin)	8.3	7.1	9.8	9.5	7.9	8.7
Return on assets	2.2	1.9	2.7	3.0	2.3	3.5
Return on common equity	8.3	7.6	12.2	12.0	8.5	12.8

## Ratios we use to assess risk

EBIT as % of total interest	1.86	1.75	2.03	2.20	2.08	2.47
Long-term debt to equity	1.44	1.70	1.83	1.78	1.90	0.00

## Valuation ratios, share prices and shares outstanding

Average price to net earnings (P/E)	16.2	18.5	17.7	15.8	14.9	13.0
Average price to cash flow	8.2	7.8	7.8	7.0	6.0	6.8
Average price to book	1.4	1.8	2.1	1.8	1.5	1.6
Price range \$ — Fiscal year high	29.84	30.00	30.00	25.64	17.75	15.24
Price range \$ — Fiscal year low	20.70	24.50	20.36	17.00	14.22	12.25
Price range \$ — Fiscal year range	157,400	137,500	103,578	101,750	84,731	69,236

## Statistical data as of Dec. 31 2008

Capitalization	\$ thousands	% of total
Long-term debt	4,894,000	58.6
Other liabilities	777,000	8.5
Deferred taxes	81,000	0.7
Shareholders' equity	3,393,000	37.2
Total (%)	8,115,000	100.0

# Fortis

TSX — FTS, \$25.12  
52 WEEK — High \$28.00 Low \$20.70

## Current news

Fortis Inc. announced in late July, the purchase of additional shares of Caribbean Utilities Company, Ltd. through its wholly-owned subsidiary. The company now indirectly owns 59.5 per cent of CUC shares which are being held for investment purposes and could increase or decrease depending on a number of factors. First-half financial results were released with slightly lower revenue but increased earnings compared to the similar period of the previous year. Fortis's results were boosted by its Canadian Regulated Utilities segment despite current economic conditions as well as one-time charges of about \$15 million in the second quarter related to Belize Electricity and FortisOntario.

## Operating performance

For the six months ended June 30, 2009, net income increased to \$154.0 million or \$0.83 a diluted share compared to \$120.0 million or \$0.75 a diluted share in the similar period of the previous year. Revenue decreased slightly by 2.0 per cent to \$2.0 billion while total expenses decreased by 3.0 per cent due to lower energy supply costs and decreased operating expenses. With expenses falling at a quicker pace than revenue, operating income subsequently increased by 2.8 per cent to \$367.0 million. First-half cash flow generated a net increase of \$71.0 million. Cash from operations excluding an increase in non-cash working capital, was not sufficient in funding capital expenditures in utility assets and dividend payouts. Financing for these activities was received from proceeds of long-term debt.

## Company outlook

The company's subsidiaries are focused on completing their 2009 capital projects which is estimated to total more than \$1 billion. These projects are primarily located in western Canada and the Caribbean. For the next five years, its capital program will reach \$5 billion with funding generated at the subsidiary level. Fortis Inc.'s common shares are still a buy.

## FOOTNOTES:

- At the time this report was prepared, consult The Investment Reporter weekly for changes in our opinion before the next update of this report.
- This is a compilation of brokerage surveys and rated: Buy, Sell, Hold.
- Marpep quality ratings (least risk to highest risk): Very Conservative; Conservative; Average; Higher Risk; Speculative.
- The MPE (Marpep Risk Index) is the p/e ratio divided by the dividend yield. Generally speaking, the lower the MPE, the better the value.
- The MGI (Marpep Growth Index), if above 1.0, it may be an undervalued stock.
- Earnings before interest, income taxes, depreciation and amortization.
- Certain figures provided by Global Interactive.
- Cash flow from operations after capital expenditures and dividends.
- Adjusted for US/Can exchange.
- Refers to previous calendar year on TSE.
- Not available/not applicable.

## Our Advice\*

Buy

## Consensus Advice\*

Hold

## Marpep quality ratings\*

Very Conservative

## Latest fiscal e.p.s.

\$1.56

## Marpep forecast e.p.s.

\$1.50

## Consensus e.p.s.

\$1.51

## Marpep forecast P/E ratio

16.7

## Consensus P/E ratio

16.6

## Current Dividend

\$1.04

## Current Yield

4.1 %

## Marpep Risk Index\*

4.0

## Marpep Growth Index\*

0.5

## Short-term outlook

Match sector

## Long-term outlook

Match sector

## STANDARD RATIOS

## Equity per common share

\$18.00

## Long-term debt to equity

1.44:1

## Working capital ratio

0.67:1

## Return on equity

8.3 %

## Return on assets

2.2 %

## EBITDA margin

26.9 %

## Net margin

6.3 %

## Report

140-006

VOL. 98, ISSUE 8

AUGUST, 2009

**BMO Capital Markets Report**  
**June 11, 2009**

# Fortis

(FTS-TSX)

June 11, 2009

Research Fact Sheet  
Gas & Electric Utilities

**Stock Rating:** Outperform  
**Industry Rating:** Market Perform

**Michael McGowan, CA, CFA**

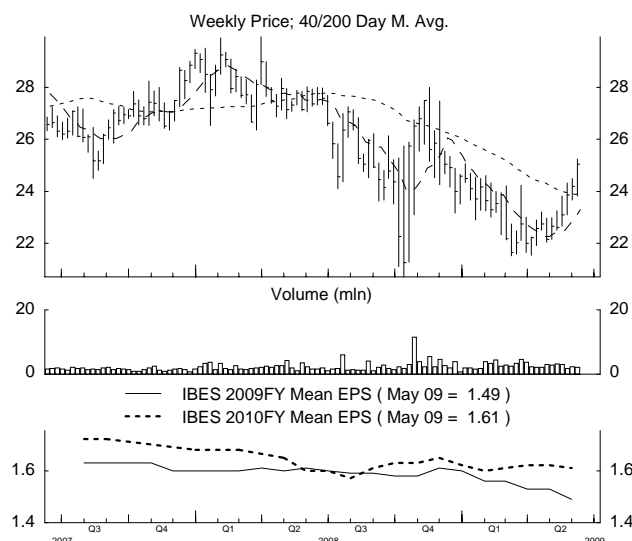
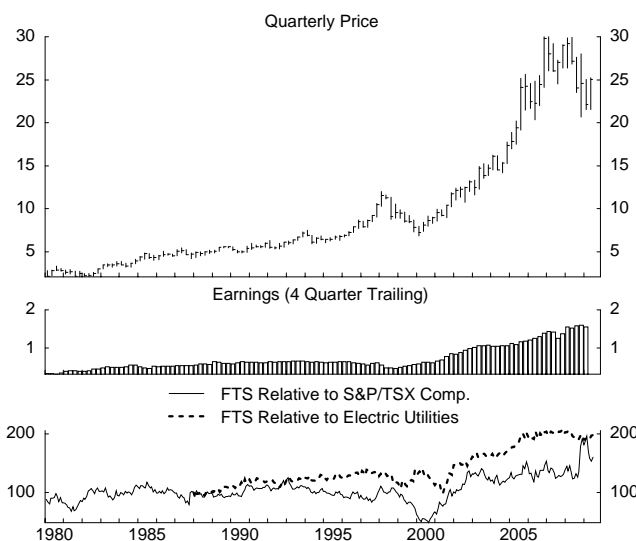
(416) 359-5807

Michael.McGowan@bmo.com

Price (11-Jun)	\$25.05	52-Week High	\$28.00	
Target Price	\$27.00	52-Week Low	\$20.70	
Dividend	\$1.04	Book Value	\$18.02	
Yield	4.2%	Price/Book	1.4x	
Shares O/S (mm)	169.2	Mkt. Cap (\$mm)	\$4,238	
Float O/S (mm)	169.2	Float Cap (\$mm)	\$4,238	
Wkly Vol (000s)	2,707	Wkly \$ Vol (mm)	\$66.1	
Net Debt (\$mm)	\$5,851	Next Rep. Date	5-Aug (E)	
Quarterly EPS	Q1	Q2	Q3	Q4
2007A	\$0.40	\$0.31	\$0.20	\$0.46
2008A	\$0.58	\$0.28	\$0.26	\$0.48
2009E	\$0.53 a	\$0.26	\$0.22	\$0.48

(FY-Dec.)	2007A	2008A	2009E	2010E
<b>EPS</b>	\$1.29	\$1.56	\$1.47	\$1.60
<b>P/E</b>			17.0x	15.7x
<b>CFPS</b>	\$2.71	\$4.21	\$3.76	\$4.13
<b>P/CFPS</b>			6.7x	6.1x
<b>Div.</b>	\$0.82	\$1.03	\$1.04	\$1.08
<b>EV (\$mm)</b>	\$10,012	\$10,534	\$11,158	\$11,364
<b>EBITDA (\$mm)</b>	\$810	\$1,034	\$1,161	\$1,289
<b>EV/EBITDA</b>	12.4x	10.2x	9.6x	8.8x
<b>ROE (%)</b>	7.2%	8.3%	8.1%	8.5%
<b>Book Value (\$)</b>	\$16.72	\$18.00	\$18.48	\$19.05
<b>D/Tot. Cap. (%)</b>	65.6%	67.6%	68.8%	68.7%
<b>Reg. ROE (%)</b>	na	na	na	na

**Notes:** EPS estimates are diluted; Quarterly numbers are basic **Disclosures:** 2, 3, 7, 9, 10AC



**Company Description** – Fortis is a publicly listed holding company with four key businesses: electric utility operations, regulated natural gas distribution, non-regulated electric power generation and non-utility property activities. Electric power operations include Newfoundland Power (100%, Newfoundland), Maritime Electric (100%, PEI), Fortis Ontario (100%, Ontario), Belize Electricity (70.1%, Belize), Caribbean Utilities (56%, Grand Cayman Island),

Turks and Caicos (100%, Turks and Caicos), FortisAlberta (100%, Alberta) and FortisBC (100%, British Columbia).  
*Website: fortisinc.com*

**Recent Results** – Fortis Inc. reported Q1/09 EPS of \$0.54 (basic). After adjusting for \$2 million of non-recurring income from Fortis Turks and Caicos, comparable EPS of \$0.53 were lower than our estimate of \$0.58 and the First Call Mean of \$0.57. The difference between expected and

This report was prepared by an Analyst employed by a Canadian affiliate, BMO Nesbitt Burns Inc., and who is not registered as a research analyst under FINRA rules. For disclosure statements, including the Analyst's Certification, please refer to pages 3 to 5.



actual results appears to be due to lower-than-expected income from the Caribbean utility companies (\$0.01/share); Fortis Properties (\$0.01/share); Terasen Inc. (\$0.01/share); Fortis Generation (\$0.01/share); and corporate costs that were (\$0.01/share) above our estimates.

**Corporate Developments** – 2009 will be an important year for regulatory applications. Rate applications are expected to be filed by Terasen Gas, Terasen Gas Vancouver Island, FortisAlberta and Newfoundland Power. We expect cost of capital reviews in British Columbia and possibly in Newfoundland in conjunction with these applications. In addition, provincial regulators in Alberta and Ontario are expected to conduct generic cost of capital proceedings.

On December 19, 2008, Fortis announced that it had completed the issuance of 11,700,000 common shares, priced at \$25.65/share, for gross proceeds of \$300.1 million. Approximately \$200 million from the issuance will be used

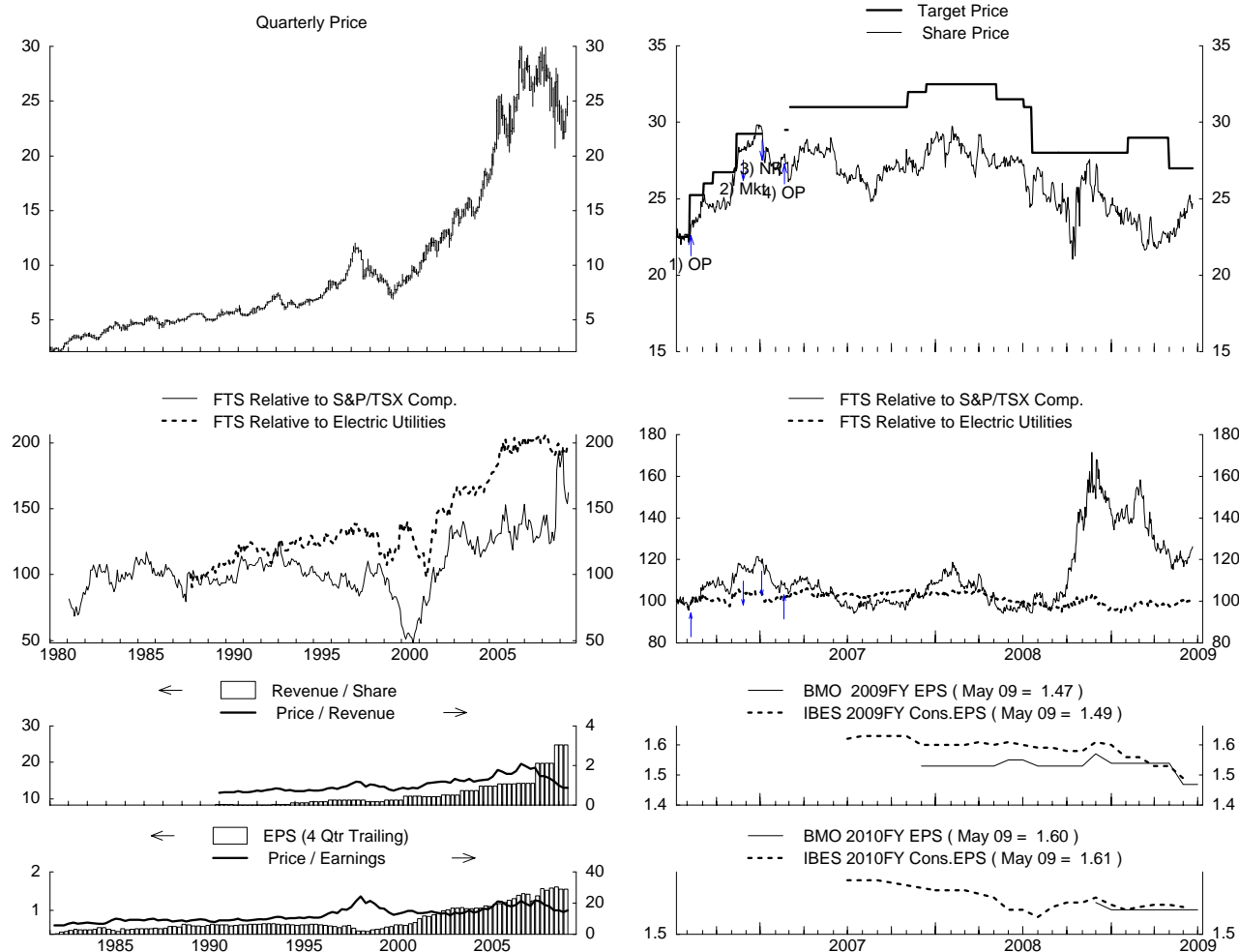
to repay debt incurred to temporarily finance the acquisition of Terasen Gas, which was completed in May 2007. The remaining proceeds will be used for general corporate purposes.

**Forecasts** – Our diluted EPS estimates are \$1.47 in 2009 and \$1.60 in 2010.

**Valuation** – Our target price of \$27 is based on a weighted valuation approach: 14x diluted 2010E EPS of \$1.60 (12.5%); 1.5x 2010E BVPS of \$19.05 (12.5%); and a target yield of 4.00%, assuming 2010E dividends per share of \$1.08.

**Recommendation** – We believe that Fortis' shares are attractively valued, considering the company's relatively low-risk, diversified business model. Our rating is Outperform. Member of Top 15 Income and Value stock selections.

## Fortis Inc. (FTS)



FYE (Dec.)	EPS \$	P/E	DPS \$	Yield %	Payout %	BV \$	P/B	ROE %
1987	0.52	9	0.31	6.5	60	3.92	1.2	13
1988	0.56	9	0.34	6.8	60	4.16	1.2	14
1989	0.59	10	0.36	6.3	60	4.45	1.3	14
1990	0.62	9	0.37	6.8	60	4.71	1.1	13
1991	0.60	10	0.37	6.2	61	5.01	1.2	12
1992	0.64	10	0.38	6.2	60	5.28	1.2	12
1993	0.64	11	0.40	5.6	63	5.53	1.3	12
1994	0.62	10	0.42	6.5	68	5.82	1.1	11
1995	0.63	11	0.43	6.3	68	6.05	1.1	11
1996	0.59	14	0.43	5.1	73	6.21	1.4	10
1997	0.60	18	0.44	4.2	74	6.40	1.6	9
1998	0.45	21	0.45	4.7	>100	6.63	1.4	7
1999	0.56	14	0.45	5.7	80	6.57	1.2	9
2000	0.60	15	0.46	5.1	77	6.97	1.3	9
2001	0.84	14	0.47	4.0	56	7.49	1.6	12
2002	0.96	13	0.49	3.7	50	8.50	1.5	12
2003	1.03	14	0.52	3.5	49	8.82	1.7	12
2004	0.99	16	0.54	3.1	51	10.45	1.7	10
2005	1.10	21	0.64	2.6	55	11.74	2.1	10
2006	1.33	22	0.76	2.6	55	12.19	2.4	11
2007	1.29	21	0.84	2.9	61	16.69	1.7	9
2008	1.56	15	1.00	4.1	62	20.05	1.2	8
Current*	1.55	15	1.04	4.3	67	18.02	1.3	9
Average:		14		4.9	64		1.4	10.8
Growth(%):								
5 Year:	8.3		14.0			15.4		
10 Year:	12.3		8.7			10.5		
20 Year:	4.6		5.7			7.6		

\* Current EPS is the 4 Quarter Trailing to Q1/2009.

FTS - Rating as of 10-Jul-06 = Mkt

Date	Rating Change	Share Price
1 8-Aug-06	Mkt to OP	\$23.24
2 24-Nov-06	OP to Mkt	\$28.20
3 3-Jan-07	Mkt to NR	\$29.51
4 19-Feb-07	NR to OP	\$27.94

Last Daily Data Point: June 18, 2009

### Company Risk Disclosure

In addition to the risks involved in investing in common stocks generally, we also highlight the following risks that pertain to this company. Operations are subject to complex regulation by a variety of provincial, state and federal (Canada, Cayman Islands & Belize) agencies. Changes in regulation may adversely affect performance.

Financial performance depends on the availability of installed generation and the production of electric power by third parties. Fortis Properties' cash flow is dependent on hotel room vacancy rates and commercial building occupancy levels. The company's operations in Belize may be disrupted and assets may be damaged by hurricanes and/or tropical storms.

### Analyst's Certification

I, Michael McGowan, CA, CFA, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities or issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### General Disclosure

The information and opinions in this report were prepared by both BMO Nesbitt Burns Inc. and BMO Nesbitt Burns Ltée./Ltd., collectively ("BMO NB") and BMO Capital Markets Limited (U.K.), ("BMO CM Ltd"). BMO NB and BMO CM Ltd. are not subject to U.S. rules with regard to the preparation of research reports and the independence of analysts. "BMO Capital Markets" is a trade name used by the BMO Investment Banking Group, which includes the wholesale arm of Bank of Montreal and its subsidiaries BMO NB in Canada, BMO Capital Markets Ltd. in the U.K. and BMO Capital Markets Corp. in the U.S. BMO Capital Markets Ltd. and BMO Capital Markets Corp. are affiliates of BMO NB. Bank of Montreal or its subsidiaries ("BMO Financial Group") has lending arrangements with, or provide other remunerated services to, many issuers covered by BMO NB research. A significant lending relationship may exist between BMO Financial Group and certain of the issuers mentioned herein. The opinions, estimates and projections contained in this report are those of BMO NB and BMO CM Ltd. as of the date of this report and are subject to change without notice. BMO NB and BMO CM Ltd. endeavour to ensure that the contents have been compiled or derived from sources that we believe are reliable and contain information and opinions that are accurate and complete. However, BMO NB and BMO CM Ltd. make no representation or warranty, express or implied, in respect thereof, takes no responsibility for any errors and omissions contained herein and accepts no liability whatsoever for any loss arising from any use of, or reliance on, this report or its contents. Information may be available to BMO NB, BMO CM Ltd or its affiliates that is not reflected in this report. The information in this report is not intended to be used as the primary basis of investment decisions, and because of individual client objectives, should not be construed as advice designed to meet the particular investment needs of any investor. This material is for information purposes only and is not an offer to sell or the solicitation of an offer to buy any security. The research analyst and/or associates who prepared this report are compensated based upon (among other factors) the overall profitability of BMO NB, BMO CM Ltd. and its affiliates, which includes the overall profitability of investment banking services. BMO NB, BMO CM Ltd., or its affiliates expect to receive or will seek compensation for investment banking services within the next 3 months from all issuers covered by BMO NB. BMO NB, BMO CM Ltd. or its affiliates will buy from or sell to customers the securities of issuers mentioned in this report on a principal basis. BMO NB, BMO CM Ltd. or its affiliates, officers, directors or employees may have a long or short position in the securities discussed herein, related securities or in options, futures or other derivative instruments based thereon. The reader should assume that BMO NB, BMO Capital Markets Ltd., BMO Capital Markets Corp., Bank of Montreal or their affiliates may have a conflict of interest and should not rely solely on this report in evaluating whether or not to buy or sell securities of issuers discussed herein.

### Company Specific Disclosure

Disclosure 2: BMO NB has undertaken an underwriting liability with respect to this issuer within the past 12 months.

Disclosure 3: BMO NB has provided investment banking services with respect to this issuer within the past 12 months.

Disclosure 7: BMO Capital Markets Corp. or an affiliate has received compensation for investment banking services from this issuer within the past 12 months.

Disclosure 9: BMO Capital Markets Corp. or an affiliate received compensation for products or services other than investment banking services within the past 12 months.

Disclosure 10: This issuer is a client (or was a client) of BMO NB, BMO Capital Markets Corp., BMO CM Ltd. or an affiliate within the past 12 months: Investment Banking Services & Non-Securities Related Services.

### Distribution of Ratings (June 11, 2009)

Rating Category	BMO Rating	BMO Universe	BMO I.B. Clients *	Starmine Universe **
--------------------	---------------	-----------------	-----------------------	-------------------------

Buy	Outperform	31%	46%	46%
Hold	Market Perform	57%	47%	46%
Sell	Underperform	12%	7%	8%

\* Reflects rating distribution of all companies where BMO Capital Markets has received compensation for Investment Banking services.

\*\* Reflects rating distribution of all North American equity research analysts.

### **Ratings Key**

We use the following ratings system definitions:

OP = Outperform - Forecast to outperform the market;

Mkt = Market Perform - Forecast to perform roughly in line with the market;

Und = Underperform - Forecast to underperform the market;

(S) = speculative investment;

NR = No rating at this time;

R = Restricted – Dissemination of research is currently restricted.

Market performance is measured by a benchmark index such as the S&P/TSX Composite Index, S&P 500, Nasdaq Composite, as appropriate for each company. Prior to September 1, 2003, a fourth rating tier—Top Pick—was used to designate those stocks we felt would be the best performers relative to the market. Our six Top 15 lists which guide investors to our best ideas according to six different objectives (large, small, growth, value, income and quantitative) have replaced the Top Pick rating.

### **Dissemination of Research**

Our research publications are available via our web site <http://bmocapitalmarkets.com>. Institutional clients may also receive our research via FIRST CALL Research Direct and Reuters. All of our research is made widely available at the same time to all BMO NB, BMO Capital Markets Ltd., BMO Capital Markets Corp. and BMO Nesbitt Burns Securities Ltd. client groups entitled to our research. Please contact your investment advisor or institutional salesperson for more information.

### **Conflict Statement**

A general description of how BMO Financial Group identifies and manages conflicts of interest is contained in our public facing policy for managing conflicts of interest in connection with investment research which is available at:  
[http://research-ca.bmocapitalmarkets.com/conflict\\_statement\\_public.asp](http://research-ca.bmocapitalmarkets.com/conflict_statement_public.asp)

### **Additional Matters**

TO U.S. RESIDENTS: BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd., affiliates of BMO NB, furnish this report to U.S. residents and accept responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd.

TO U.K. RESIDENTS: In the UK this document is published by BMO Capital Markets Limited which is authorised and regulated by the Financial Services Authority. The contents hereof are intended solely for the use of, and may only be issued or passed on to, (I) persons who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (II) high net worth entities falling within Article 49(2)(a) to (d) of the Order (all such persons together referred to as "relevant persons"). The contents hereof are not intended for the use of and may not be issued or passed on to, retail clients.

BMO Nesbitt Burns Inc. and BMO Nesbitt Burns Ltée/Ltd. are Members of CIPF. BMO Capital Markets Corp. and BMO Nesbitt Burns Securities Ltd. are Members of SIPC.

"BMO Capital Markets" is a trade-mark of Bank of Montreal, used under licence.

"BMO (M-Bar roundel symbol)" is a registered trade-mark of Bank of Montreal, used under licence.

**BMO Capital Markets Report**  
**September 10, 2009**

# Fortis

(FTS-TSX)

September 10, 2009

Research Fact Sheet

Gas &amp; Electric Utilities

**Stock Rating:** Outperform  
**Industry Rating:** Market Perform

**Michael McGowan, CA, CFA**

(416) 359-5807

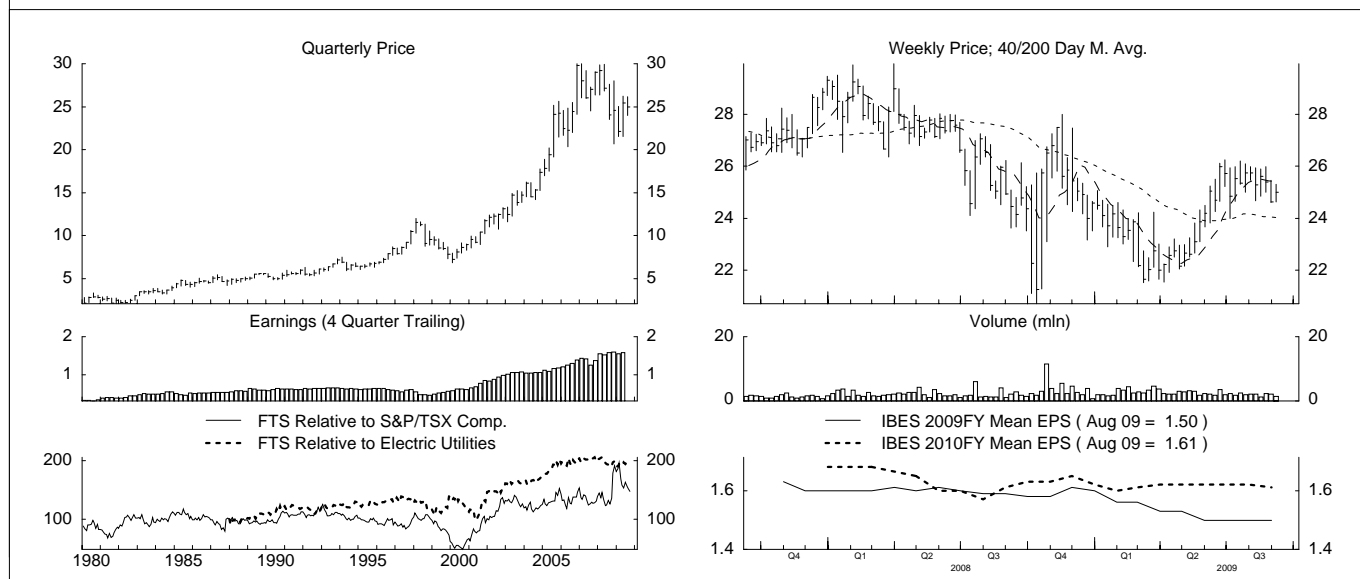
Michael.McGowan@bmo.com

Assoc: Mark Laing, CA

Price (10-Sep)	\$24.99	52-Week High	\$28.00	
Target Price	\$29.00	52-Week Low	\$20.70	
Dividend	\$1.04	Book Value	\$18.02	
Yield	4.2%	Price/Book	1.4x	
Shares O/S (mm)	169.2	Mkt. Cap (\$mm)	\$4,228	
Float O/S (mm)	169.2	Float Cap (\$mm)	\$4,228	
Wkly Vol (000s)	2,736	Wkly \$ Vol (mm)	\$66.1	
Net Debt (\$mm)	\$5,393	Next Rep. Date	05-Nov (E)	
Quarterly EPS	Q1	Q2	Q3	Q4
2007A	\$0.40	\$0.31	\$0.20	\$0.46
2008A	\$0.58	\$0.28	\$0.26	\$0.48
2009E	\$0.53 a	\$0.31 a	\$0.22	\$0.48

(FY-Dec.)	2007A	2008A	2009E	2010E
<b>EPS</b>	\$1.29	\$1.56	\$1.51	\$1.63
<b>P/E</b>			16.5x	15.3x
<b>CFPS</b>	\$2.71	\$4.21	\$3.81	\$4.28
<b>P/CFPS</b>			6.6x	5.8x
<b>Div.</b>	\$0.82	\$1.03	\$1.04	\$1.08
<b>EV (\$mm)</b>	\$10,012	\$10,534	\$11,407	\$11,899
<b>EBITDA (\$mm)</b>	\$810	\$1,034	\$1,195	\$1,313
<b>EV/EBITDA</b>	12.4x	10.2x	9.5x	9.1x
<b>ROE (%)</b>	7.2%	8.3%	8.3%	8.7%
<b>Book Value (\$)</b>	\$16.72	\$18.00	\$18.53	\$19.13
<b>D/Tot. Cap. (%)</b>	65.6%	62.6%	64.9%	65.8%
<b>Reg. ROE (%)</b>	na	na	na	na

**Notes:** EPS estimates are diluted; Quarterly numbers are basic **Disclosures:** 2, 3, 7, 9, 10AC



**Company Description** – Fortis is a publicly listed holding company with four key businesses: electric utility operations, regulated natural gas distribution, non-regulated electric power generation and non-utility property activities. Electric power operations include Newfoundland Power (100%, Newfoundland), Maritime Electric (100%, PEI), Fortis Ontario (100%, Ontario), Belize Electricity (70.1%, Belize), Caribbean Utilities (56%, Grand Cayman Island),

Turks and Caicos (100%, Turks and Caicos), FortisAlberta (100%, Alberta) and FortisBC (100%, British Columbia).  
**Website:** fortisinc.com

**Recent Results** – Fortis Inc. reported Q2/09 EPS of \$0.31 versus our estimate of \$0.26 and the First Call Mean of \$0.27. The difference between actual and expected results was due to strong earnings at Terasen Gas (\$0.03/share greater than our estimate) and FortisAlberta (\$0.03/share

This report was prepared by an Analyst employed by a Canadian affiliate, BMO Nesbitt Burns Inc., and who is not registered as a research analyst under FINRA rules. For disclosure statements, including the Analyst's Certification, please refer to pages 3 to 5.

greater than our estimate), both of which benefitted from lower-than-expected income tax expenses. Earnings from the remainder of the company's business segments were generally in line with expectations.

**Corporate Developments** – During Q2/09, FortisAlberta, the Terasen Companies and Newfoundland Power all filed rate applications with their respective regulators. In addition, all of these utilities are currently engaged in cost of capital reviews. Decisions on these applications and cost of capital proceedings are expected in late 2009 or early 2010.

Fortis has increased its capital expenditure estimate by \$500 million and the company is now planning to invest approximately \$5 billion during the next five years. Approximately 70% of the total relates to planned capital expenditures at the regulated electric utilities, 25% relates to

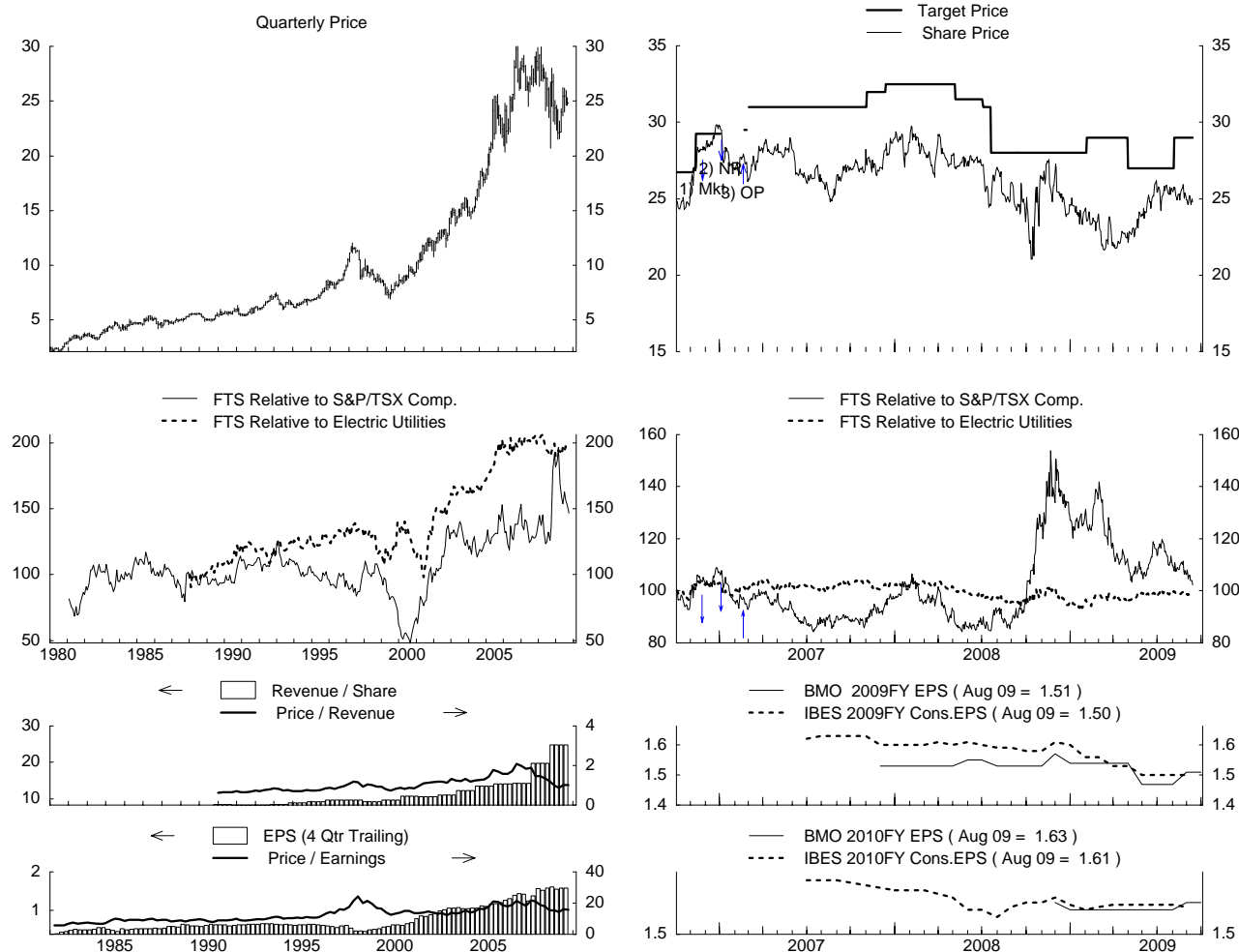
the Terasen Companies, and 5% relates to Forts' non-regulated businesses.

**Forecasts** – Our diluted EPS estimates are \$1.51 in 2009 and \$1.63 in 2010.

**Valuation** – Our target price of \$29 is based on a weighted valuation approach: 15x diluted 2010E EPS of \$1.63 (12.5%); 1.75x 2010E BVPS of \$19.13 (12.5%); and a target yield of 3.75%, assuming 2010E dividends per share of \$1.08.

**Recommendation** – We believe that Fortis's shares are attractively valued, considering the company's relatively low-risk, diversified business model. Our rating is Outperform. Member of Top 15 Income and Value stock selections.

## Fortis Inc. (FTS)



FYE (Dec.)	EPS \$	P/E	DPS \$	Yield %	Payout %	BV \$	P/B	ROE %
1987	0.52	9	0.31	6.5	60	3.92	1.2	13
1988	0.56	9	0.34	6.8	60	4.16	1.2	14
1989	0.59	10	0.36	6.3	60	4.45	1.3	14
1990	0.62	9	0.37	6.8	60	4.71	1.1	13
1991	0.60	10	0.37	6.2	61	5.01	1.2	12
1992	0.64	10	0.38	6.2	60	5.28	1.2	12
1993	0.64	11	0.40	5.6	63	5.53	1.3	12
1994	0.62	10	0.42	6.5	68	5.82	1.1	11
1995	0.63	11	0.43	6.3	68	6.05	1.1	11
1996	0.59	14	0.43	5.1	73	6.21	1.4	10
1997	0.60	18	0.44	4.2	74	6.40	1.6	9
1998	0.45	21	0.45	4.7	>100	6.63	1.4	7
1999	0.56	14	0.45	5.7	80	6.57	1.2	9
2000	0.60	15	0.46	5.1	77	6.97	1.3	9
2001	0.84	14	0.47	4.0	56	7.49	1.6	12
2002	0.96	13	0.49	3.7	50	8.50	1.5	12
2003	1.03	14	0.52	3.5	49	8.82	1.7	12
2004	0.99	16	0.54	3.1	51	10.45	1.7	10
2005	1.10	21	0.64	2.6	55	11.74	2.1	10
2006	1.33	22	0.76	2.6	55	12.19	2.4	11
2007	1.29	21	0.84	2.9	61	16.69	1.7	9
2008	1.56	15	1.00	4.1	62	20.05	1.2	8
Current*	1.58	16	1.04	4.2	66	18.02	1.4	9
Average:		14		4.9	64		1.4	10.8
Growth(%):								
5 Year:	8.6		14.0			15.4		
10 Year:	12.0		8.7			10.5		
20 Year:	4.8		5.7			7.6		

\* Current EPS is the 4 Quarter Trailing to Q2/2009.

FTS - Rating as of 3-Oct-06 = OP

Date	Rating Change	Share Price
1 24-Nov-06	OP to Mkt	\$28.20
2 3-Jan-07	Mkt to NR	\$29.51
3 19-Feb-07	NR to OP	\$27.94

Last Daily Data Point: September 11, 2009



### Company Risk Disclosure

In addition to the risks involved in investing in common stocks generally, we also highlight the following risks that pertain to this company. Operations are subject to complex regulation by a variety of provincial, state and federal (Canada, Cayman Islands & Belize) agencies. Changes in regulation may adversely affect performance.

Financial performance depends on the availability of installed generation and the production of electric power by third parties. Fortis Properties' cash flow is dependent on hotel room vacancy rates and commercial building occupancy levels. The company's operations in Belize may be disrupted and assets may be damaged by hurricanes and/or tropical storms.

### Analyst's Certification

I, Michael McGowan, CA, CFA, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities or issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

### General Disclosure

The information and opinions in this report were prepared by both BMO Nesbitt Burns Inc. and BMO Nesbitt Burns Ltée./Ltd., collectively ("BMO NB") and BMO Capital Markets Limited (U.K.), ("BMO CM Ltd"). BMO NB and BMO CM Ltd. are not subject to U.S. rules with regard to the preparation of research reports and the independence of analysts. "BMO Capital Markets" is a trade name used by the BMO Investment Banking Group, which includes the wholesale arm of Bank of Montreal and its subsidiaries BMO NB in Canada, BMO Capital Markets Ltd. in the U.K. and BMO Capital Markets Corp. in the U.S. BMO Capital Markets Ltd. and BMO Capital Markets Corp. are affiliates of BMO NB. Bank of Montreal or its subsidiaries ("BMO Financial Group") has lending arrangements with, or provide other remunerated services to, many issuers covered by BMO NB research. A significant lending relationship may exist between BMO Financial Group and certain of the issuers mentioned herein. The opinions, estimates and projections contained in this report are those of BMO NB and BMO CM Ltd. as of the date of this report and are subject to change without notice. BMO NB and BMO CM Ltd. endeavour to ensure that the contents have been compiled or derived from sources that we believe are reliable and contain information and opinions that are accurate and complete. However, BMO NB and BMO CM Ltd. make no representation or warranty, express or implied, in respect thereof, takes no responsibility for any errors and omissions contained herein and accepts no liability whatsoever for any loss arising from any use of, or reliance on, this report or its contents. Information may be available to BMO NB, BMO CM Ltd or its affiliates that is not reflected in this report. The information in this report is not intended to be used as the primary basis of investment decisions, and because of individual client objectives, should not be construed as advice designed to meet the particular investment needs of any investor. This material is for information purposes only and is not an offer to sell or the solicitation of an offer to buy any security. The research analyst and/or associates who prepared this report are compensated based upon (among other factors) the overall profitability of BMO NB, BMO CM Ltd. and its affiliates, which includes the overall profitability of investment banking services. BMO NB, BMO CM Ltd., or its affiliates expect to receive or will seek compensation for investment banking services within the next 3 months from all issuers covered by BMO NB. BMO NB, BMO CM Ltd. or its affiliates will buy from or sell to customers the securities of issuers mentioned in this report on a principal basis. BMO NB, BMO CM Ltd. or its affiliates, officers, directors or employees may have a long or short position in the securities discussed herein, related securities or in options, futures or other derivative instruments based thereon. The reader should assume that BMO NB, BMO Capital Markets Ltd., BMO Capital Markets Corp., Bank of Montreal or their affiliates may have a conflict of interest and should not rely solely on this report in evaluating whether or not to buy or sell securities of issuers discussed herein.

### Company Specific Disclosure

Disclosure 2: BMO NB has undertaken an underwriting liability with respect to this issuer within the past 12 months.

Disclosure 3: BMO NB has provided investment banking services with respect to this issuer within the past 12 months.

Disclosure 7: BMO Capital Markets Corp. or an affiliate has received compensation for investment banking services from this issuer within the past 12 months.

Disclosure 9: BMO Capital Markets Corp. or an affiliate received compensation for products or services other than investment banking services within the past 12 months.

Disclosure 10: This issuer is a client (or was a client) of BMO NB, BMO Capital Markets Corp., BMO CM Ltd. or an affiliate within the past 12 months: Investment Banking Services & Non-Securities Related Services.

### Distribution of Ratings (June 11, 2009)

<b>Rating</b>	<b>BMO</b>	<b>BMO</b>	<b>BMO</b>	<b>Starmine</b>
<b>Category</b>	<b>Rating</b>	<b>Universe</b>	<b>I.B. Clients *</b>	<b>Universe **</b>

Buy	Outperform	31%	46%	46%
Hold	Market Perform	57%	47%	46%
Sell	Underperform	12%	7%	8%

\* Reflects rating distribution of all companies where BMO Capital Markets has received compensation for Investment Banking services.

\*\* Reflects rating distribution of all North American equity research analysts.

### Ratings Key

We use the following ratings system definitions:

OP = Outperform - Forecast to outperform the market;

Mkt = Market Perform - Forecast to perform roughly in line with the market;

Und = Underperform - Forecast to underperform the market;

(S) = speculative investment;

NR = No rating at this time;

R = Restricted – Dissemination of research is currently restricted.

Market performance is measured by a benchmark index such as the S&P/TSX Composite Index, S&P 500, Nasdaq Composite, as appropriate for each company. Prior to September 1, 2003, a fourth rating tier—Top Pick—was used to designate those stocks we felt would be the best performers relative to the market. Our six Top 15 lists which guide investors to our best ideas according to six different objectives (large, small, growth, value, income and quantitative) have replaced the Top Pick rating.

### Dissemination of Research

Our research publications are available via our web site <http://bmocapitalmarkets.com>. Institutional clients may also receive our research via FIRST CALL Research Direct and Reuters. All of our research is made widely available at the same time to all BMO NB, BMO Capital Markets Ltd., BMO Capital Markets Corp. and BMO Nesbitt Burns Securities Ltd. client groups entitled to our research. Please contact your investment advisor or institutional salesperson for more information.

### Conflict Statement

A general description of how BMO Financial Group identifies and manages conflicts of interest is contained in our public facing policy for managing conflicts of interest in connection with investment research which is available at:  
[http://research-ca.bmocapitalmarkets.com/conflict\\_statement\\_public.asp](http://research-ca.bmocapitalmarkets.com/conflict_statement_public.asp)

### Additional Matters

TO U.S. RESIDENTS: BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd., affiliates of BMO NB, furnish this report to U.S. residents and accept responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd.

TO U.K. RESIDENTS: In the UK this document is published by BMO Capital Markets Limited which is authorised and regulated by the Financial Services Authority. The contents hereof are intended solely for the use of, and may only be issued or passed on to, (I) persons who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (II) high net worth entities falling within Article 49(2)(a) to (d) of the Order (all such persons together referred to as "relevant persons"). The contents hereof are not intended for the use of and may not be issued or passed on to, retail clients.

BMO Nesbitt Burns Inc. and BMO Nesbitt Burns Ltée/Ltd. are Members of CIPF. BMO Capital Markets Corp. and BMO Nesbitt Burns Securities Ltd. are Members of SIPC.

"BMO Capital Markets" is a trade-mark of Bank of Montreal, used under licence.

"BMO (M-Bar roundel symbol)" is a registered trade-mark of Bank of Montreal, used under licence.