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Ontario Power Generation Inc.

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Major Rating Factors

Strengths:

- Government ownership and financial support
- Dominant position in a strong market with a diversified economy
- Regulatory support for nuclear and the bulk of hydroelectric assets
- Diversified portfolio of generating assets
- Low-cost hydroelectric assets with river system diversity

Corporate Credit Rating

A-/Negative/--

Weaknesses:

- Significant financial risk profile, given low allowed returns on regulated operations, substantial debt-financed projects, and exposure to merchant electricity prices
- Uncertain profitability due to variability in assets' operating performance, river flows, and weather
- Nuclear technology that exposes the company to significant operating risk and potential for unexpected large capital expenditures

Rationale

The ratings on Ontario Power Generation Inc. (OPG), which the Province of Ontario owns, reflect Standard & Poor's Ratings Services' opinion of the regulatory oversight of the utility's baseload nuclear and hydroelectric assets; a diverse generation portfolio; and dominant market position in Ontario. Weak cash flow metrics and exposure to regulatory delay and cost overruns related to new construction and refurbishment of existing facilities offset the company's credit strengths, in our view. Exposure to merchant electricity prices and volume related to OPG's unregulated business further constrain the stand-alone credit profile (SACP). The company borrowed about 80% of its C\$4.9 billion reported consolidated debt as of Sept. 30, 2012, from the government shareholder, through Ontario Electricity Financial Corp. (OEFEC).

We base the 'A-' rating on OPG's SACP, which we assess at 'bbb-', and our opinion that the ratings on OPG and Ontario are linked. We assess that there is a "high" likelihood that the government shareholder would provide timely and sufficient extraordinary support in the event of financial distress. This reflects our views that OPG's role is "important" to Ontario, that the utility plays a major role in the government's energy policy; and that the link between the utility and the province is "very strong", reflecting ownership relationship, ongoing financial support from OEFEC, and the province's strong influence in the company's investment decisions.

In our view, OPG's business risk profile benefits from having about 77% of its EBITDA in 2011 supported by regulated sources. These sources include nuclear and baseload hydroelectric assets that the Ontario Energy Board (OEB) regulates, as well as regulated nuclear waste management. Assurance of cost recovery and a predictable, albeit moderate, return for these assets is a positive credit factor. Historically, although the OEB decisions have led to more moderate returns for OPG, given the discretion that the company has with respect to its capital expenditure and the resultant level of debt, it has been able to mitigate the impact of lower revenues. However, the company has reached

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an inflection point in its capital plans where significant expenditures for such things as the Darlington nuclear facility refurbishment and the Lower Mattagami project are required. We believe that these projects will put significant strain on credit metrics for the next two years. In particular, we forecast that the Darlington refurbishment and Lower Mattagami project will require approximately C\$1 billion in capital expenditures in each of the next two years. This is in addition to the other projects that OPG is working on, along with sustaining capital expenditure.

We view this capital expenditure in a regulatory context, which provides limited cash flow relief during construction for multiyear projects and a balanced-but measured-perspective on rate applications. Accordingly, the timing difference between the regulatory asset's development (with the consequential debt) and the start of cash flow in the regulatory environment (which has allowed moderate rate increases) could stress financial metrics.

The fuel diversity and large number of generating units in OPG's generation portfolio mitigate the risk of operational disruptions and enhance its business position, in our opinion. As of Sept. 30, 2012, the portfolio of assets that the company owns and operates includes:

- 6,606 megawatts (MW) of baseload regulated nuclear generation;
- 6,996 MW of predominantly run-of-the-river hydroelectric generation, of which 3,312 MW is regulated; and
- 5,447 MW of intermediate unregulated thermal generation.

We believe OPG has a strong competitive position. The company dominates the Ontario electricity market, producing 85 terawatt-hours (TWh; most of it baseload) of the 142 TWh of electricity consumption in the province in 2011. Its unregulated hydro assets typically enjoy a competitive advantage compared with higher marginal cost gas-fired alternatives.

Constraining OPG's unregulated cash flows, in our view, are the company's exposure to the wholesale electricity price and volume risk due to fluctuations in Ontario demand, the inherent uncertainty of available water flows, and competitively priced imports from neighboring markets. Wholesale electricity prices have struggled in 2012, with the weighted average Hourly Ontario Electricity Price at C\$24 per MW-hour (MWh) for the nine months ended Sept. 30, 2012, compared with the C\$32 per MWh in 2011.

Technical challenges associated with key components of nuclear facilities have the potential to expose the units to lengthy outages, hurting cash flow performance and increasing capital demands. OPG's nuclear liability risk-sharing agreement with Ontario limits the company's used nuclear fuel liabilities and partially mitigates the operating challenges.

In implementing its energy policy favoring renewable energy generation to replace the less eco-friendly coal-fired generation facilities, the province has directed OPG toward investments in projects on various occasions. It also required the utility to shut down the remaining coal-fired plants by 2014. Along with these directives, the government has provided ongoing support to OPG through loans from OEFC and long-term power purchase agreements with the Ontario Power Authority to support the company's other projects. It also provides OPG with a contingency support agreement to cover operating costs and a modest return on investments of the coal-fired facilities until complete closure in 2014. We regard these ongoing supports as important mitigating factors to the company's business risk profile.

We believe OPG's stand-alone financial risk profile is significant. We believe stand-alone cash flow metrics are generally weak, partially as a result of the material postretirement benefit adjustments and modest return on investments. Adjusted funds from operations (AFFO) interest coverage was 2.7x and FFO-to-total debt was 9.1% for the 12 months ended Sept. 30, 2012. AFFO, in our definition, deducts the contribution to nuclear waste and decommissioning funds, which we regard as a cost of ongoing operations. We expect any improving trend that might emerge in the next three years to be gradual. We forecast that AFFO will be approximately C\$800 million in each of the next two years. Based on the significant capital expenditure required, we believe that AFFO-to-debt could fall below 9% each year.

Liquidity

OPG's liquidity is adequate under our criteria, and should be sufficient to cover cash uses in the next 12 months. Standard & Poor's bases its liquidity assessment on the following factors and assumptions:

- We expect that the company's liquidity sources of about C\$2.9 billion in the next 12-18 months will exceed its uses by about 1.6x.
- Available cash resources include our expectation of annual cash flow from operations of about C\$900 million, and available credit facilities of C\$1.9 billion as of Sept. 30, 2012. The committed and available credit facilities comprise a C\$1 billion maturing May 2017, a C\$700 million bank credit facility to support initial construction of the Lower Mattagami project, and a C\$700 million OEFC facility for Lower Mattagami.
- Projected uses of cash in the next 12 months include a sizable capital expenditure of about C\$1.7 billion.

We expect that the utility will not pay out dividends in the foreseeable future and future debt maturities do not present a material concern, given the shareholder's practice of refinancing notes payable at their due dates.

Outlook

The negative outlook reflects our view of the 'bbb-' SACP, the high likelihood of provincial support, and the negative outlook on the province. Although we recognize that OPG's cash flow adequacy will be weaker in the next two years due to substantial capital expenditure on regulated and contracted projects, we could lower the SACP if we expect the company's AFFO-to-total debt to stay below 8% or AFFO interest coverage weakens to below 3.0x. This could result from unfavorable rate decisions, operational issues resulting in unexpected outages in its generation facilities, or a move toward a more aggressive financial policy (including extended significant debt financed capital expenditure). A decline in the SACP to 'bb+' would result in a downgrade on OPG.

For the SACP to move a notch higher, we believe OPG would need to improve significantly the level and stability of its overall cash flow strength comfortably above AFFO-to-total debt of 12%. This could result from an equity injection from the province, which we consider to be highly unlikely. It could also result from some form of additional regulatory cash flow support during the upcoming period of high capital spending on large projects that we have seen for other Canadian utilities in a similar position.

We link the ratings on the utility and those on the province through our enhanced government-related entity methodology. All else being equal, a one-notch downgrade to Ontario would result in a one-notch downgrade to OPG. An outlook revision to stable on the province could result in a similar outlook revision on the utility. A change in the

relationship with the government shareholder, which includes changes in ownership, could move the ratings in either direction.

Business Description

OPG is an electricity generator with both regulated (nuclear and hydroelectric) and unregulated (coal, hydroelectric, and oil- and gas-fired) assets, comprising 75 generation stations with total generating capacity of 19.1 gigawatts (GW) and 85 TWh generated in 2011. In addition to energy revenues, the company receives payments from Bruce Power L.P., which operates OPG's Bruce A and Bruce B nuclear stations under a long-term lease arrangement; and revenues from sales of radioactive isotopes for medical treatments. The company also has equity interests in two gas-fired generation stations: Portlands Energy Centre L.P. (550 MW, 50-50 joint venture with TransCanada Energy Ltd.) and Brighton Beach (580 MW, 50-50 joint venture with ATCO Resources Ltd.). OPG has a small energy trading operation, which has contributed to less than 1% of total revenue. The province wholly owns the company.

Government Support And Government-Related Entities Rating Methodology

We base the 'A-' rating on OPG on the company's SACP and our view that there is "high" likelihood that the province would provide timely and sufficient extraordinary support in the event of financial distress. We assess the company's SACP at 'bbb-'.

In accordance with our criteria for GREs, we base our view of a "high" likelihood of extraordinary government support on the following assessment:

- Within the context of our GRE methodology and scale for assessing the importance of a GRE's role to its government owner, we view OPG's role as "important" to Ontario. The company operates as a profit-seeking enterprise and its credit standing is important to the government because it provides an essential service. OPG's role is clear, important, and intertwined with the government's energy policy. As an example, the province's energy policy is directing the company to shut down its coal fired plants in an effort to meet provincial carbon dioxide emission reduction targets. Furthermore, although we do not believe that default or credit stress would disrupt OPG or Ontario's operations, it would affect the credibility of the province's electricity market and reputation.
- Within the context of our GRE methodology and scale for assessing strength and durability, we view the link between the utility and Ontario as "very strong." The government is a strong and stable shareholder, and it has a policy and track record of both constraining profitability and providing financial support to the generator. Government policy has a strong influence on the company's strategic and business plans. Ministerial directives instruct OPG where to invest. Management updates government staff on monthly financial and operational performance. Furthermore, the province appoints the utility's board of directors. Financial support is available through the Ontario Electricity Finance Corp. (OEF; senior unsecured debt rating: 'AA-'). The OEF is an established provincial agency with a legislated mandate "to provide financial assistance to the successor corporations of Ontario Hydro," of which OPG is one. Ontario provides OPG with both liquidity support and long-term financing (credit facilities and five-, 10-, and 30-year notes) at market rates for the company's existing operations and new investments. The government has also directed its agency, OPA, to negotiate long-term contracts with OPG for these projects that provide revenue certainty backed by a solid counterparty.

The Ontario government has contemplated at certain times selling Crown assets, which could include OPG, although it is not contemplating that now. In our view, any privatization could weaken its link with the government and the likelihood of extraordinary support in times of need. This could be the result of changes in OEFC's mandate toward OPG or reduced government influence in the company's business strategy and appointments to the board. We consider this an event risk and would reevaluate the likelihood of support when the government takes more concrete steps toward privatization.

For more information on our rating criteria, see "Rating Government-Related Entities: Methodology And Assumptions," published Dec. 9, 2010, on RatingsDirect on the Global Credit Portal.

Regulatory Support And Dominant Market Position Underpin Strong Business Risk Profile

OPG maintains a dominant market position in the Ontario power market. Total output from its regulated assets supports about 52% of its total capacity, which represents approximately 57% of provincial capacity. The regulated assets generated about 77% of the company's energy-related EBITDA in 2011. OPG is the only regulated generator in the province, which further supports its market position. Its regulated facilities include the Niagara River plants, the St. Lawrence River Saunders plant, the Pickering Nuclear Generating Stations (A and B), and the Darlington station. We do not expect OEB to regulate any new assets. Instead, electricity from new facilities would be sold to the Independent Electricity System Operator (IESO) with revenue top-ups from the OPA, ensuring, on average, a modest contracted return.

OEB is an independent, quasijudicial tribunal that reports to the Ontario legislature through the minister of energy, with a mandate to regulate the electricity and gas sectors in the public interest and to set reasonable rates. Although it operates independently from the government, it provides advice on energy matters that the minister refers to. As such, OEB has no jurisdiction over the utility's economic viability.

In our opinion, OEB regulation reduces uncertainty surrounding cost recovery of these regulated assets and supports OPG's strong business risk profile, although it does not fully alleviate volume risk linked to nuclear output and available hydrology. Furthermore, the company's nuclear segment is highly susceptible to poorer-than-targeted performance (aging assets) and cost overruns that we believe heighten regulatory risk. The timeliness of cash recovery of large, often unexpected costs related to nuclear output could be slow, given general reluctance to raise energy prices. There is a long history of regulated entities in Ontario being allowed to recoup unforeseen costs (regulatory assets) or having to refund the customer (regulatory liabilities) after the fact through rates. The cash recovery or repayment, however, is subject to a prudency review and regulatory approval. Furthermore, depending on the magnitude, the OEB may spread the recovery over several years to avoid rate shock.

Policy consideration could affect profitability and cash flow

Although regulations are generally balanced to facilitate cost recovery of regulated assets, the province's energy policy and political situation influences OPG's profitability. These factors in some cases weaken the company's ability to improve its profitability while in other cases provide it more revenue stability.

Rates OPG receives on its regulated assets (see table 1) reflect those effective March 1, 2011 to Dec. 31, 2012. The rates are based on a return on equity (ROE) of 9.43% for 2011 and 9.55% for 2012 and an equity layer of 47%. The company filed a rate application in September 2012 requesting approval to recover balances in the OEB's authorized regulatory variance and deferral accounts as of Dec. 31, 2012. We expect the final decision and order in spring 2013.

Table 1

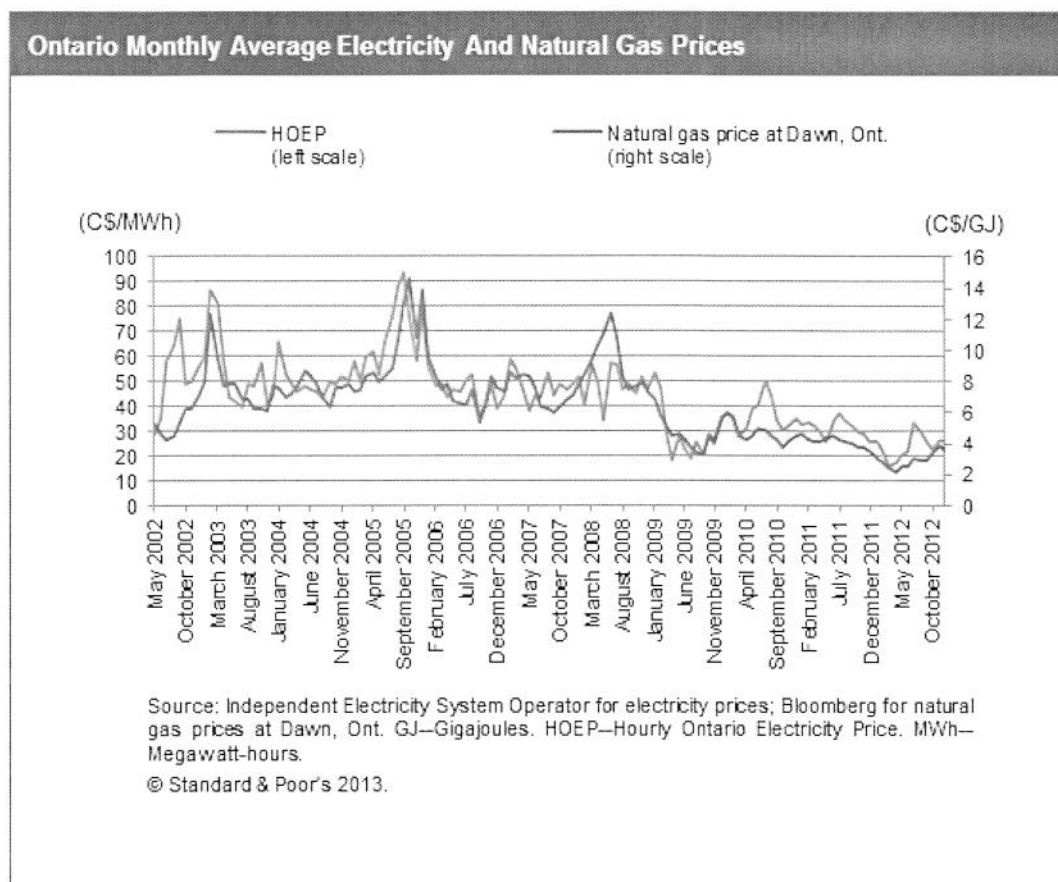
Ontario Power Generation Inc. (OPG)--Prices For Regulated Assets		
(C\$/MWh)	Regulated Prices up to March 2011	Regulated price effective April 2011
OPG regulated nuclear	54.98	55.85
OPG regulated hydro	36.66	34.13

MWh--Megawatt-hours.

In implementing the province's energy policy favoring renewable energy generation to replace the less ecofriendly coal-fired generation facilities, Ontario has directed OPG toward investments in hydroelectricity projects on various occasions. The province also required the company to shut down its coal-fired plants by 2014. Although the government has demonstrated a more active hand respect to OPG with these directives, it has also provided ongoing support to the company through loans from OEFC and long-term power purchase agreements (PPAs) with OPA to support the projects. It also provides OPG a contingency support agreement to cover operating costs and a modest return on investments of the coal-fired facilities until complete closure in 2014, thereby stabilizing cash flow from this segment. A further example of support with respect to this directive is the execution of the Atikokan Biomass Energy Supply Agreement between OPG and the OPA to convert the Atikokan generating station to biomass fuel. We regard these ongoing supports as important mitigating factors supporting the company's business risk profile.

Lower spot prices stress unregulated cash flow

Overall, lower hourly Ontario electricity prices (HOEP) continue to be weak in 2012 (C\$24 per MWh for the nine months ended Sept. 30, 2012, compared with C\$32 per MWh in 2011). This continues to place additional stress on OPG's unregulated cash flow. Typically, prices in Ontario have loosely tracked the same trends as natural gas prices, which were also low at the time of publication. We do not expect a material recovery in HOEP in the next two years, given that the economic recovery remains uncertain and that natural gas prices are still close to historical lows (see chart).



The lower wholesale electricity prices has affected the earnings and cash flow of OPG's unregulated segment in 2011, resulting in a 22% decline in segment EBITDA to C\$314 million in 2011. Total electricity consumption in Ontario increased marginally to 141.2 TWh in 2011 compared to 140.4 TWh in 2010. The relatively flat consumption reflects ongoing weakness in the provincial economy and mild weather. While the closure of coal-fired facilities will offset new generating capacity, we expect electricity demand growth to be flat-to-modest while recovery in manufacturing activities continues to be slow and because of the conservation and demand management effort. Therefore, we do not expect wholesale prices to rebound materially in the near-to-medium term.

We expect OPG to gradually increase the proportion of contracted businesses in the unregulated segments, which should help reduce its exposure to wholesale electricity prices. Examples include the contingency support agreement covering the company's coal-fired facilities until their closure and the PPAs supporting the Upper and Lower Mattagami projects and the recent agreement to redevelop the Atikokan facility to biomass.

Market dominance and cost competitiveness of baseload capacity are key strengths

OPG's strong competitive position in the Ontario wholesale electricity spot market reflects its market dominance and the low marginal operating costs of its hydroelectric and nuclear generating facilities. The company produced approximately 60% of the 141.2 TWh of electricity consumed in the province in 2011. The Ontario market is large, with a population of 12 million. Its economy is diversified, although the weaker North American economy has affected

its manufacturing base. Nevertheless, as residential and commercial sectors account for about two-thirds of electricity demand, the manufacturing sector's impact on Ontario's base electricity needs is relatively moderate. Therefore, we believe that even if the company were to lose its regulatory support, it would have little or very modest dispatch risk for these baseload assets.

We believe OPG's nuclear and hydroelectric generation capacities are significant, accounting for approximately 58% and 88% of the province's respective capacities as of Dec. 31, 2011. About 77% of the company's EBITDA comes from regulated plants, which have little dispatch risk or price risk exposures. The unregulated hydroelectric assets generally enjoy a competitive advantage over higher marginal cost gas-fired alternatives, ensuring high capacity use even in price-depressed markets.

In our view, hydroelectric imports from Quebec and Manitoba do not pose an immediate competitive threat to OPG, although they do give Ontario some added supply security. Imports from Quebec face transmission constraints and faster-than-expected growth in that province's domestic electricity demand. Furthermore, Ontario consumers must compete with generally higher-priced U.S. markets for Hydro-Quebec's available surplus generation. Interconnections to New York and Michigan also place the company's generation assets in a good competitive position against imports, in our opinion.

OPG's generation portfolio is well-diversified and hydroelectric operations are efficient

We believe OPG's generation portfolio is well-diversified, which mitigates cash flow exposure to hydrology and nuclear-related operating risks. Although fuel type diversification has marginally decreased as OPG's coal-fired facilities begin to close with final closure by 2014, the company still benefits from geographically diversified hydroelectricity assets, situated in numerous river systems. In addition, the conversion of coal-fired plants to biomass-fueled facilities has introduced a new fuel source, albeit a very small proportion of overall generation.

OPG's hydroelectric assets have lower operating risk than either the coal-fired or nuclear-fueled assets, with comparatively strong capability factors and low forced outage rates. The company has made substantial investment in its hydroelectric assets with the Niagara Tunnel, Lower Mattagami, and Upper Mattagami projects. We expect the company to continue investing C\$600 million-C\$800 million per year in its long-lived hydroelectric assets. Although the in-service dates of OPG's hydroelectric assets range from 1898-2009, its two largest hydroelectric facilities (representing about 37% of its total hydroelectric capacity) are among the youngest, at about 50 years old. Proposed changes to provincial dam safety regulations could require some one-time additional capital spending. We expect the spending to be manageable (in terms of time and cost) and that the company will recover a large portion eventually through regulated rates.

Two key assets on the Great Lakes, in addition to the benefits of run-of-the-river plants on numerous river systems throughout the province, reduce OPG's exposure to variable hydrology.

OPG's consistent production levels relative to that of peers during years of low water supports this view. In the past 20 years, its total hydroelectric energy production has fluctuated by plus 10% or minus 9% from 51-year average historical annual production of 34.7 TWh. Nevertheless, year-to-year fluctuations can be larger. Total production was about 7% below average in 2011, at 32.4 TWh, representing a partial rebound from 30.6 TWh in 2010 (which was a historically low hydrology year).

Material exposure to construction risks in redevelopment projects

OPG continues to face construction risk for its development projects. The company has experienced significant cost and delay issues with some of its recent development projects, including a 10.2-kilometer tunnel at its Sir Adam Beck facility to increase water flow and expand the Niagara Falls production.

We expect OPG to face significant construction risks as it proceeds with major refurbishments of Darlington nuclear facilities, work to extend operation at Pickering B by four-to-six years, and the Lower Mattagami redevelopment. We understand that the utility expects to spend more than C\$2 billion in each of the next two years in sustaining and committed capital expenditure. The company could face additional construction risk if it and Ontario decide to proceed with two new nuclear units at the Darlington site.

Improving the performance of its nuclear fleet is an ongoing challenge. OPG has been unable to meet targeted performances in its nuclear plants in the past several years, in part due to longer-than-expected maintenance and inspection outages. (see table 2). Performance reliability and output of the Pickering A station, which includes two refurbished operating units, is uncertain. Darlington, the newest of the three nuclear stations, has performed consistently better than Pickering A and B. The average age of nuclear units that OPG operates is 29 years (on a MW-weighted basis).

Table 2

Ontario Power Generation Inc.--Historical Nuclear Performance As Of Dec. 31, 2011										
Capability factor (%) [*]	--2011--		--2010--		--2009--		--2008--		--2007--	
	Target	Actual	Target	Actual	Target	Actual	Target	Actual	Target	Actual
Industry benchmark	N/A	82.3	N/A	79.3	N/A	81.5	N/A	83.5	N/A	91.2
Pickering A	82.7	67.9	73.7	62.4	79.5	64.2	79.0	71.8	83.7	41.3
Pickering B	81.2	76.2	76.1	76.3	87.3	84.0	86.6	71.4	86.0	75.0
Darlington	94.3	95.2	90.3	87.6	86.5	85.9	92.8	94.5	87.3	89.5

^{*}Capability factor represents the amount of electricity the station is actually capable of producing as a percent of its potential capacity.
N/A--Not applicable.

Dedicated funds and regulatory support cover sizable nuclear asset retirement obligations

The costs associated with retiring nuclear generation are material, but mitigating OPG's exposure is a segregated nuclear asset decommissioning and waste management fund, and regulatory support. In addition, the company has established a nuclear liability risk-sharing framework with the province.

Weaker profitability and cash flow mitigated by higher proportion of regulated assets

We compare OPG with four government owned electricity generation companies and utilities, which all benefit from material government or parent support (see table 3). Although the company and EDF Energy Inc. have a higher proportion of more stable regulated businesses, the larger scale and diversity of Vattenfall AB and Statkraft AS reduce impact of operating risks and market price volatility. As a result, OPG and its peers all share similar business risk profiles. The company's relatively high exposure to nuclear generation, which carries somewhat higher operating risk, also constrains its business risk profile, in our view.

OPG's cash flow (AFFO interest coverage and FFO-to-debt) and profitability (return on common equity) measures were weaker than those of several peers, partially because of a higher proportion of relatively modest, albeit more

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stable, regulated return (compared with that of DONG Energy AS, Vattenfall, and Statkraft), large postretirement debt adjustments, and poor returns from its aging thermal assets. The company's relatively weak cash flow measures largely contribute to its significant financial risk profile, along with EDF (which is more highly geared) and Statkraft (which is more exposed to price volatility, with only relatively small regulated EBITDA).

Table 3

Ontario Power Generation Inc.--Peer Comparison					
Industry Sector: Electric Utility					
	Ontario Power Generation Inc.	EDF Energy PLC	DONG Energy A/S	Vattenfall AB	Statkraft AS
Rating as of Feb. 1, 2013	A-/Negative/A-1	A/Negative/A-1	BBB+/Negative/A-2	A-/Stable/A-2	A-/Stable/A-2
--Average of past three fiscal years--					
Currency (mil.)	C\$	£	Dkr	kr	NOK
Revenues	5,349.7	5,557.2	53,573.3	200,006.3	25,766.3
Operating income	920.3	131.7	5,022.7	33,237.8	10,343.2
Net income from continuing operations	562.7	(26.8)	3,285.3	12,325.3	4,800.7
Funds from operations (FFO)	753.7	175.5	10,049.1	36,709.1	10,715.8
Capital expenditures	911.1	317.3	16,296.9	40,122.7	4,268.5
Free operating cash flow	(146.1)	82.8	(4,723.5)	(1,453.3)	6,601.6
Cash and short-term investments	331.0	1,351.9	1,037.3	3,473.3	9,668.3
Debt	7,518.9	2,280.6	38,715.9	192,037.2	41,301.5
Preferred stock	0.0	0.0	(4,285.7)	4,677.0	0.0
Equity	5,852.0	2,626.0	46,999.7	141,331.6	68,618.2
Debt and equity	13,371.0	4,906.6	85,715.6	333,368.8	109,919.7
Adjusted ratios					
EBIT interest coverage (x)	2.6	1.2	2.4	3.6	6.8
EBITDA interest coverage (x)	4.6	2.1	4.7	5.3	6.8
FFO interest coverage (X)	2.8	2.2	6.4	4.3	6.5
FFO/debt (%)	10.0	7.7	26.0	19.1	25.9
Free operating cash flow/debt (%)	(1.9)	3.6	(12.2)	(0.8)	16.0
Discretionary cash flow/debt (%)	(1.9)	(0.3)	(16.8)	(4.2)	(6.3)

Significant Financial Risk Profile

Financial policy

OPG does not have a publicly stated capital structure target and its reported debt-to-capital was 37% as of Sept. 30, 2012. With large capital expenditure in the next five years, we expect leverage to increase substantially. The company has a moderate dividend policy but has not paid any dividend since 2007 and we do not expect any in the next few years.

The utility has no access to the equity market and does not expect equity injections from the province in the foreseeable future. It borrows almost all its long-term from OEFC, which has a mandate to provide financial support to successor companies of Ontario Hydro.

Accounting

Since Jan. 1, 2012, OPG has prepared its consolidated financial statements in accordance with U.S. generally accepted accounting principles. We believe the accounting policies the company adopted in preparing its financial statements appear reasonable.

In assessing OPG's creditworthiness and overall financial risk profile, Standard & Poor's treats payments to nuclear waste and decommissioning funds as a cost of ongoing operations and deducts them from FFO before working capital, as presented in the company's financial statements.

We have not adjusted the company's balance sheet to reflect financial risk involved in trading activities because, given the company's limited risk exposure, the amount was not material. OPG engages primarily in asset-backed physical trades, bought and sold at the Ontario border. Typical commitments last less than a year. The utility's value-at-risk (VaR) was C\$500,000 or less during 2011, below its VaR limit of C\$5.0 million.

Our adjusted ratios reflect significant post retirement benefit obligations, operating leases and securitization. We added C\$4.1 billion to the company's reported debt of C\$4.9 billion in 2011 primarily for adjustments to post retirement benefit obligations. (see table 4).

Table 4

Reconciliation Of Ontario Power Generation Inc. Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. C\$)										
--Fiscal year ended Dec. 31, 2011--										
Ontario Power Generation Inc. reported amounts	Debt	Shareholders' equity	Revenues	EBITDA	Operating income	Interest expense	Cash flow from operations	Cash flow from operations	Dividends paid	Capital expenditures
Reported	4,907.0	8,389.0	5,061.0	1,307.0	584.0	174.0	990.0	990.0	0.0	1,145.0
Standard & Poor's adjustments										
Trade receivables sold or securitized	50.0	N/A	N/A	N/A	N/A	7.5	200.0	N/A	N/A	N/A
Operating leases	125.7	N/A	N/A	7.9	7.9	7.9	20.1	20.1	N/A	11.9
Postretirement benefit obligations	4,004.6	(3,293.3)	N/A	224.0	224.0	120.0	(18.0)	(18.0)	N/A	N/A
Capitalized interest	N/A	N/A	N/A	N/A	N/A	86.0	(86.0)	(86.0)	N/A	(86.0)
Non-operating income (expense)	N/A	N/A	N/A	N/A	9.0	N/A	N/A	N/A	N/A	N/A
Reverse changes in working-capital	N/A	N/A	N/A	N/A	N/A	N/A	N/A	27.0	N/A	N/A

Table 4

Reconciliation Of Ontario Power Generation Inc. Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. C\$) (cont.)										
Minority interests	N/A	4.0	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Total adjustments	4,180.3	(3,289.3)	0.0	231.9	240.9	221.4	116.1	(56.9)	0.0	(74.1)
Standard & Poor's adjusted amounts	Debt	Equity	Revenues	EBITDA	EBIT	Interest expense	Cash flow from operations	Funds from operations	Dividends paid	Capital expenditures
Adjusted	9,087.3	5,099.7	5,061.0	1,538.9	824.9	395.4	1,106.1	933.1	0.0	1,070.9

N/A--Not Applicable.

Weaker cash flow measures as low electricity prices affected unregulated segments

AFFO declined to C\$834.1 million on a rolling 12-month basis as of Sept. 30, 2012, from C\$933.0 million in 2011. We believe that the drop was the combined result of depressed HOEP due to weak electricity demand and low output at the unregulated hydro facilities. The increased adjusted debt and related interest expenses further weakened cash flow measures, because the company increased its borrowing to support capital expenditure. As a result, AFFO-to-debt was 10.3% in 2011 and 9.1% as of Sept. 30, 2012 on a rolling 12-month basis; rolling 12-month AFFO interest coverage fell to 2.7x from 3.0x in 2011. We consider these cash flow measures weak for the 'bbb-' SACP.

Operating cash flows in the next five years would depend largely on the regulator's approval of the proposed increase in rates and ROE in the current and subsequent applications, OPG's ability to maximize nuclear productions and to maintain operating cost control, favorable hydrology, and (to some extent) timing and speed of recovery of wholesale electricity prices. We expect material improvement in cash flow measures to be unlikely in the next five years, even under favorable business conditions, since the company would need to deploy the cash flow and increase its borrowing to support its sizable capital expenditure program during the period. In the event that rate decisions, cost control, or electricity prices for regulated segments are less favorable, the utility would need to scale down its capital program and related borrowing to avoid further deterioration in its cash flow measures and SACP.

Capital structure could weaken further with increasing borrowing

We estimate that total debt outstanding could possibly increase more than 50% in the next five years, given large spending on proposed and committed projects. If OPG proceeds with its planned capital expenditures, we expect the debt-to-capital ratio to increase towards 55% in the next five years from 37% in 2011.

We also expect that the OEFC will continue to provide financing for the construction of shareholder-directed projects, if required. Most company-level debts mature within the next 10 years. Approximately C\$1.7 billion of these debts are payable within the next five. Nevertheless, refinancing risk is not a concern, given the company's relationship with shareholder and because OEFC has consistently refinanced these debts at maturity.

Almost all of the company's debt is at fixed rates in Canadian currency, limiting interest rate and foreign exchange exposure related to debt-financing. The generator mitigates interest rate risk related to new financing through swap agreements.

OPG must, by law, contribute cash annually to funds covering the cost of nuclear used-fuel management,

decommissioning, and management of other nuclear waste. We expect that the OEB will recognize contributions to these funds, estimated to average C\$165 million per year in the next three years, as a prudent cost of operations and should be recovered through rates. Because the bulk of its staff works in the regulated nuclear division, we also expect that the company could recover most pension costs through regulated rates.

Financial flexibility derived mainly from parental support

The keystone to OPG's average financial flexibility is its supportive owner. There has been demonstrated ongoing support, with previous willingness to refinance maturing debts and current willingness to forgo dividend payments. We believe the province would also support the company's short-term liquidity, if only by allowing the deferral of various payments OPG makes to the province. Based on past experience, access to additional debt financing from the province is likely, should it be required. Further, but less timely, flexibility comes from the regulatory framework that includes an ability to recoup unexpected costs if approved by the regulator.

Financial flexibility is somewhat restricted, given limited discretionary capital spending once most new projects are committed. There is no indication of additional equity injections forthcoming from the shareholder and we expect that there are likely political constraints on the sale of assets.

Ratings Detail (As Of February 8, 2013)

Ontario Power Generation Inc.

Corporate Credit Rating A-/Negative/--

Commercial Paper

Canadian CP Rating Scale

A-1(LOW)

Corporate Credit Ratings History

27-Nov-2012

A-/Negative/--

13-Aug-2008

A-/Stable/--

27-Sep-2005

BBB+/Positive/--

Business Risk Profile

Strong

Financial Risk Profile

Significant

Related Entities

Hydro One Inc.

Issuer Credit Rating

A+/Negative/A-1

Commercial Paper

Local Currency

A-1

Canadian CP Rating Scale

A-1(MID)

Senior Unsecured

A+

Ontario (Province of)

Issuer Credit Rating

AA-/Negative/A-1+

Commercial Paper

Foreign Currency

A-1+

Senior Unsecured

AA-

UMH Energy Partnership

Senior Secured

A/Stable

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Ontario Power Generation Inc.

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