Management's Discussion and Analysis

Introduction

Management's discussion and analysis reviews the financial and operational results for the fiscal year ended March 31, 2016, relative to the previous year. This section should be read in conjunction with the Consolidated Financial Statements and the accompanying notes.

Contents of Management's Discussion and Analysis

Topic	Purpose
Financial and operating performance factors	Identifies and explains the effect of factors contributing to variability in earnings
Financial performance summary	Provides a summary of the year's key financial results
Significant events	Highlights significant events impacting the statement of financial position and earnings results in the past year
Year over year financial results	Explains the financial results for 2015/16 including a year-over-year variance analysis
Regulatory deferrals	Explains the impact of the regulatory deferrals
Financial instruments	Explains how financial instruments impact financial results
Liquidity and capital resources	Identifies and explains changes to liquidity and capital resources
Capital management	Identifies and explains debt reduction objective and strategy
Critical accounting policies	Describes changes in accounting policies and their impact on the consolidated financial statements
Significant accounting estimates	Explains the estimates made and how they impact earnings

Financial and Operating Performance Factors

Introduction

This explains why the NB Power earnings are subject to significant variability under normal operations.

Impact of Financial and Operating Performance Factors

There are many factors that impact earnings that are outside the control of management. These factors result in significant swings in year-over-year results because they affect the cost of generation or price competitiveness in export markets.

Factors that Affect Financial and Operating Performance

These are the major factors that have historically affected NB Power's variability in earnings. This table explains how each factor can affect the variability of revenue and expenses.

Factor	Description
Short-term energy purchases	Represents • approximately 30 to 40 per cent of total supply requirements, and • approximately 55 to 60 per cent of total fuel and purchased power costs. Depending on world oil prices, lower cost energy is purchased to displace internal oil-fired generation. Typically, NB Power enters into forward purchase contracts for energy to supply forecasted requirements.
Nuclear based generation	Nuclear generation represents up to 26 per cent of total production through the Point Lepreau Generating Station, of which effective operation is essential for NB Power's positive financial performance. Represents • approximately 25 to 30 per cent of total supply requirements, and • approximately 0 to 5 per cent of total fuel and purchased power costs. Reliability risks are being addressed through the Point Lepreau Generation Station's excellence plan which focuses on leadership, process, equipment, safety, and operational excellence.
Purchased power contracts based on natural gas	Represents • approximately 7 to 10 per cent of total supply, and • approximately 15 to 20 per cent of the total fuel and purchased power costs. A portion of the price of NB Power's purchased power contracts is based on natural gas prices. When possible, NB Power manages this exposure by entering into forward purchase contracts for natural gas.
Coal/petcoke based generation	Represents • approximately 10 to 15 per cent of total supply, and • approximately 10 to 15 per cent of the fuel and purchased power costs Coal is normally purchased through tendered contracts. As a mixture of coal types are blended and burned, coal is procured from a number of counterparties, at indexed or firm fixed prices. Petcoke is also normally purchased through tendered contracts. A floating price component is typically built into petcoke contracts in which the purchase price is reflective of an index price at the time the petcoke is delivered.

<table>
<tr><th>Factor (Con't)</th><th>Description</th></tr>
<tr><td>Hydro based generation</td><td>Represents NB Power's lowest-cost fuel for generating electricity. It typically represents
• 15 to 20 per cent of total production.

The table below describes how hydro flows can increase or decrease generation costs.

<table><tr><th>If hydro flows are</th><th>then NB Power</th></tr><tr><td>below anticipated levels</td><td>uses other more expensive fuel to make up the shortfall and increases its generation costs</td></tr><tr><td>higher than anticipated</td><td>reduces the use of expensive fuels and decreases its generation costs</td></tr></table>
Hydro net generation as a percentage of the long-term average over the past 10 years has ranged from 95 to 143 per cent.</td></tr>
<tr><td>Heavy fuel oil based generation</td><td>Heavy fuel oil subject to market price fluctuations represents
• approximately 0 to 5 per cent of total supply, and
• 5 to 10 per cent of fuel and purchased power costs.

To minimize short- to medium-term heavy fuel oil price exposure, NB Power typically enters into forward purchase contracts for its forecasted in-province and firm export heavy fuel oil requirements.</td></tr>
<tr><td>Out-of-province margins</td><td>NB Power is a price-taker in regional energy markets. Market prices in the surrounding regions are typically driven by the cost of natural gas generation.

In the normal course of business, the lowest cost or must-take energy is directed to in-province use and any remaining energy is available for out-of-province sales.

Subject to operating conditions, NB Power enters into forward electricity sales contracts which provides for more predictable out-of-province margins.</td></tr>
<tr><td>Exchange rates</td><td>NB Power is exposed to foreign exchange risk when purchases of fuel and purchased power in US dollars are not offset by the revenue received in US dollars. NB Power typically enters into forward purchase contracts for US dollar requirements net of expected US dollar revenue.

There was a fair amount of volatility in the Canadian dollar during the past year. The value of the Canadian dollar, against the US dollar, varied between $1.20 and $1.46 at different times of the year.</td></tr>
</table>

Financial Performance

Introduction

This provides an overview of NB Power's financial performance for the year.

Key Measures of Financial Performance

Financial Performance (in millions)	2015/16	2014/15
Earnings before depreciation, finance costs, investment income, and changes in regulatory balances	$471	$510
Net earnings	$12	$100
Operating cash flows	$183	$365
Net expenditures on property, plant and equipment	$231	$264
Total net debt at end of year	4,913	4,915
(Decrease) increase in net debt	($2)	($103)

Financial Ratios and Percentages

Financial Ratios and Percentages	2015/16	2014/15
Gross margin	51.3%	52.0%
Operating cash flow/capital expenditures	0.79	1.38
Operating cash flow/total debt	0.04	0.07
Capital expenditures/carrying amount of property, plant and equipment	5%	6%
Per cent of debt in capital structure	96%	94%

Highlights

International Financial Reporting Standards (IFRS)

The current year balances are in accordance with IFRS and prior year balances have been restated to be in accordance with IFRS. As a result of the transition to IFRS, retained earnings and accumulated other comprehensive income (AOCI) were adjusted. Neither cash nor debt balances were impacted by the transition to IFRS. The major variances related to change in discount rate of the decommissioning liabilities and the fair-value measurement of post-employment benefits.

Change in Net Debt

Change in net debt was $2 million in 2015/16, a decrease of $101 million compared to 2014/15. The primary reasons for the decrease were higher fuel inventory, lower gross margin, higher OM&A, and higher nuclear investment fund withdrawals partially offset by decreased capital expenditures. (see Liquidity and Capital Resources section for more detail)

Financial Overview

NB Power's net earnings were $12 million for the year ended March 31, 2016, compared to $100 million in the prior year. The decrease in net earnings of $88 million was largely attributable to increases in expenses related to unplanned outages and improvement initiatives at the Point Lepreau Generating Station, warmer weather, and lower nuclear investment funds earnings.

Electricity Operations

NB Power incurred earnings before depreciation, finance costs, investment income, and changes in regulatory balances of $471 million for the year compared to $510 million for the prior year.

Revenue from electricity sales within New Brunswick totaled $1,336 million for the year, which was $38 million or 3% lower than the prior year. The decrease was primarily attributed to the warmer temperatures partially offset by the change in rates in October 2014 and October 2015. Out-of-province revenues of $370 million were $24 million or 7% higher than the prior year reflecting higher out-of-province export prices due to market conditions.

Expenses attributed to electricity operations were $1,279 million for the year, an increase of $35 million or 2.8% higher than the prior year. Higher supply costs were partially offset by higher hydro and lower volumes. Operations, maintenance and administration (OM&A) costs were $30 million higher mainly due to higher costs associated with unplanned outages and improvement initiatives at the Point Lepreau Generating Station.

Other Expenses

Other expenses (depreciation, and finance costs less investment income) have the potential for variability due to changes in market values, discount rates, and interest rates.

In 2015/16 other expenses were $53 million higher than the prior year. This was as a result of finance costs less investment income increasing $57 million or 35% compared to the prior year, primarily due to lower realized gains and higher unrealized losses on investments. This increase was partially offset by lower depreciation expense of $4 million.

- (see Year-over-Year Results section for more detail)

Significant Events

The following significant events impacted NB Power's financial results.

Point Lepreau Generating Station

Equipment challenges on the non-nuclear side of the station impacted performance at the Point Lepreau Generating Station during the year. The Station was brought safely offline for equipment issues with its fuel handling machine and heat transport system, repairs to a reheater in the turbine, and repairs to the standby safety system. During the outages New Brunswick Energy Marketing Corporation purchased energy to replace the lost production.

International Financial Reporting Standards (IFRS)

NB Power transitioned from Canadian GAAP (CGAAP) to IFRS for the fiscal year ended March 31, 2016. The prior year numbers have been restated.

Rate Increase

NB Power applied for a 2% rate increase to begin July 1st, 2015. A rate increase of 1.6% beginning October 1st, 2015 was granted by the Energy Utilities Board (EUB).

Revised Investment Strategy for Nuclear Funds

In 2015/16 NB Power completed its revision to the investment strategy that began in 2014/15. The 2015/16 year included investment gains of $30 million incurred on the transition of investments. The investment portfolio was transitioned to a more diversified asset mix to provide better inflation protection and reduce future expected contributions over the long term.

Life Extensions at Coleson Cove and Belledune Generating Stations

NB Power extended the useful lives of both the Coleson Cove and Belledune Generating Stations. This extension was due to new engineering studies that align with the Integrated Resource Plan. The impact in-year was reduced depreciation of $20 million and reduced amortization savings in the regulatory deferral.

Year-Over-Year Results - Electricity Operations

NB Power incurred earnings before depreciation, finance costs, investment income, and changes in regulatory balances of $471 million for the year compared to $510 million for the prior year. The following discusses the contributing factors that impacted electricity operations in 2015/16 compared to the prior year.

Revenues

Introduction

This provides an overview of NB Power's revenues for the year and compares them with previous years.

Revenue Overview

Revenue Overview (in millions)	2015/16	2014/15
Sales of power		
In-province	$1,336	$1,374
Out-of-province	370	346
Miscellaneous	85	71
Total revenues	1,791	$1,791
Per cent (decrease) increase year-over-year	(-%)	(-%)

IN-PROVINCE SALES OF POWER

In-province sales of power (in millions)	2015/16	2014/15
Residential	$601	$635
Industrial	322	318
General service	280	285
Wholesale	109	112
Street lights	24	24
Total	$1,336	$1,374
Per cent (decrease) increase year-over-year	(3%)	3%
GWh	13,209	13,648
Per cent (decrease) increase year-over-year	(3%)	2%

Major contributors to year-over-year in-province sales variance

In-province sales of power totaled $1,336 million in 2015/16, representing a $38 million or three per cent decrease compared to 2014/15. The main contributors to the year-over-year variance were as follows

Revenues	By this amount	Due to
Contributing factors		
decreased	$60 million	warmer weather in 2015/16
decreased	$6 million	interruptible sales
decreased	$2 million	weather adjusted load (decreased residential partially offset by increased industrial transmission)
(increased)	($30 million)	October 2014 and 2015 rate increases

OUT-OF-PROVINCE SALES OF POWER

Out-of-province sales of power (in millions)	2015/16	2014/15
Revenue	$370	$346
Per cent (decrease) increase	6.9%	11.5%
MWh	4,533	4,575
Per cent (decrease) increase year-over-year	(0.9%)	(8%)

Major contributors to year-over-year out-of-province sales variance

In 2015/16, out-of-province sales of power increased by $24 million or 6.9 per cent compared to 2014/15. The main contributors to the year-over-year variance were:

Revenues	By this amount	Due to
Contributing factors		
increased	$27 million	higher market prices
(decreased)	($3 million)	lower volumes mainly due to loss of some export contracts and less opportunity sales to US

MISCELLANEOUS REVENUE

Miscellaneous revenue consists primarily of

- efficiency programs
- water heater rentals
- pole attachment fees
- point-to-point tariff
- net transmission revenue and expense
- generation by-products

Major contributors to miscellaneous revenue variance

Miscellaneous revenue was $85 million in 2015/16, an increase of $14 million compared to 2014/15. This increase was mainly due to efficiency program revenue (offset in OM&A) and sale of LED streetlights (mainly offset in OM&A).

Year-Over-Year Results - Electricity Operations

Expenses

Introduction

This provides an overview of NB Power's expenses associated with electricity operations for 2015/16 compared to the prior year.

Expenses Overview

Expenses (in millions)		**2015/16**		**2014/15**
	$	%	$	%
Fuel and purchased power	$830	47%	$825	49%
Operations, maintenance & administration	449	25	419	25
Depreciation and amortization	226	13	230	14
Taxes	41	2	37	2
Finance costs	286	16	327	19
Sinking funds and other investment income	(67)	(3)	(123)	(7)
Mark-to-market losses (gains) of fair value through profit or loss investments	1	-	(41)	(2)-
Total	$1,763	100%	$1,674	100%
Per cent (decrease) increase year-over-year		5%		(4%)

Major contributors to year-over-year expense variance

Total expenses increased by $89 million to $1,763 million in 2015/16. The variances are included in the following tables:

FUEL AND PURCHASED POWER

Fuel and Purchased Power (in millions)		**2015/16**		**2014/15**
	$	%	$	%
Hydro	$0	0	$0	0
Nuclear	29	3	21	3
Thermal	114	14	253	30
Purchases	687	83	551	67
Total	$830	100%	$825	100%
Per cent (decrease) increase year-over-year		(-%)		(1%)

Major contributors to year-over-year fuel and purchased power expense variance

The cost of fuel and purchased power was $830 million in 2015/16, an increase of $5 million from 2014/15.

The year-over-year increase in fuel and purchased power costs was mainly attributable to:

Fuel and purchased power expenses	**By this amount**	**Due to**
Contributing factors		
increased	$37 million	higher supply costs (purchased power prices)
(decreased)	($22 million)	lower overall volumes required
(decreased)	($10 million)	higher hydro flows

OPERATIONS, MAINTENANCE AND ADMINISTRATION

The table below shows the operations, maintenance and administration expenses compared with previous year.

Operations, maintenance and administration (in millions)	2015/16	2014/15
Operations, maintenance and administration expenses	$449	$419
Per cent increase (decrease) year-over-year	7%	(4%)

Major contributors to year-over-year operations, maintenance and administration variance

Operations, maintenance and administration costs were $449 million in 2015/16, a $30 million or seven per cent increase compared to 2014/15. The significant changes were:

Operations, maintenance and administration expenses	By this amount	Due to
Contributing factors		
increased	$25 million	higher costs associated with PLGS unplanned outages and improvement initiatives
increased	$24 million	higher costs associated with Efficiency NB Merger (offset in miscellaneous revenue), contract amendments, professional services, computer and office equipment and union raises, and LED street light sales (offset in miscellaneous revenue)
(decreased)	($19 million)	higher costs associated with storms in 2014/15

Year over Year Results – Other Expenses

Introduction

This provides an overview of NB Power's other expenses (finance costs less investment income, and depreciation and amortization) for the year and compares them with previous years. These expenses have the potential for variability due to changes in market values, discount rates, and interest rates.

FINANCE COSTS LESS INVESTMENT INCOME

Finance Costs Less Investment Income (in millions)	2015/16	2014/15
Finance costs	$286	$327
Sinking funds and other investment income	(67)	(123)
Mark-to-market of held for trading investments	1	(41)
Finance costs less investment income	$220	$163
Per cent increase year-over-year	35%	19%

Contributing factors to changes in finance costs less investment income

Finance costs less investment income were $220 million in 2015/16 a $57 million or 35 per cent increase from 2014/15. This was mainly due to:

Finance charges less investment income	By this amount	Due to
Contributing factors		
increased	$57 million	lower realized gains and higher unrealized mark-to-market losses on investment funds due to changes in market conditions partially offset by lower interest expense due to lower interest rates

DEPRECIATION AND AMORTIZATION

Depreciation and amortization (in millions)	2015/16	2014/15
Depreciation and amortization	$226	$230
Per cent increase year-over-year	(2%)	-%

Contributing factors to changes in depreciation and amortization

Depreciation and amortization costs were $226 million in 2015/16, a $4 million or two per cent decrease compared to 2014/15. The significant changes were:

Depreciation and amortization expenses	By this amount	Due to
Contributing factors		
decreased	$20 million	life extension at Coleson Cove and Belledune generating stations
(increased)	($16 million)	additional outage costs and shortened life of defective nuclear closure plugs

Regulatory Balances

Regulatory Balance – Point Lepreau Generating Station Refurbishment

Background

A legislated regulatory balance[1] was created for non-capital costs incurred during the refurbishment period of the Point Lepreau Generating Station (March 28, 2008 through November 23, 2012). The refurbishment of the Point Lepreau Generating Station enables electricity to be provided to future generations of customers. The deferral and amortization of these costs over the life of the Station provides for inter-generational equity. The regulatory balance consists of the period costs of the nuclear division, net of any revenues, and the additional costs to supply energy during the period of refurbishment.

Impact on earnings

These amounts are to be recovered over the operating life of the refurbished Point Lepreau Generating Station and are to be reflected in the charges, rates and tolls charged to customers.

During 2015/16, $20 million in changes to regulatory balances were made to earnings ($70 million amortization of deferral offset by $50 million interest on deferral).

Regulatory Balance – Lawsuit Settlement with Petroleos de Venezuela S.A. (PDVSA)

Background

On August 23, 2007, the Energy and Utilities Board approved a regulatory balance for the purpose of returning the benefit of the lawsuit settlement with PDVSA to customers in a levelized manner. The levelized benefit is being paid to customers over 17 years (eight years remaining as of March 31, 2016). NB Power is recovering the depreciation and interest savings over the life of the Coleson Cove Generating Station.

Impact on earnings

During 2015/16, ($7) million in changes to regulatory balances were made as follows:

- $23 million of a levelized benefit to customers
- $3 million of interest charges
  partially offset by
- $19 million in amortization and interest savings resulting from the lawsuit settlement

Net Earnings Adjusted to Remove Effects of Regulatory Accounting

As a rate regulated entity NB Power applies regulatory accounting. If NB Power did not apply regulatory accounting then net earnings would be as follows:

	2015/16	2014/15
Net earnings	$12	$100
Remove impact of changes in regulatory balances on earnings	13	17
Net earnings adjusted to remove the effects of regulatory accounting	$25	$117

[1] *Section 139 of the Electricity Act provides for the establishment of this regulatory deferral related to the refurbishment of the Point Lepreau Generating Station.*

Financial Instruments

NB Power enters into forward contracts for commodities. The accounting impacts of these financial instruments can be found in Note 27 of the Financial Statements.

Liquidity and Capital Resources

Introduction

This provides an overview of NB Power's liquidity and capital resources. The two main items which impact NB Power's net debt are capital expenditures and cash flow from operating activities.

Total Net Debt

Total Net Debt (in millions)	**2015/16**	**2014/15**
Long-term debt	$4,124	$4,025
Current portion of long-term debt	400	580
Short-term indebtedness	855	784
Sinking fund receivable	(464)	(471)
Cash	(2)	(3)
Total net debt	$4,913	$4,915

Year-over-Year Change to Total Debt Level

Total net debt decreased by $2 million in 2015/16 due to the following:

CHANGE IN NET DEBT

Decrease (increase) in net debt (in millions)	**2015/16**	**2014/15**
Cash flow from operating activities	$183	$365
Add back non-cash component of net debt	23	20
Capital expenditures less proceeds on disposal	(231)	(264)
Nuclear fuel investment fund withdrawals (deposits)	40	(7)
Cash expenditures on decommissioning	(13)	(11)
Decrease in net debt	$2	$103

Contributing factors to change in net debt

Change in net debt was $2 million in 2015/16, a decrease of $101 million compared to 2014/15. The primary reasons for the decrease were higher fuel inventory, lower gross margin, higher OM&A, and higher nuclear investment fund withdrawals partially offset by decreased capital expenditures.

Contributing factors to changes in investing activities

Investing activities were $204 million in 2015/16. This year-over-year decrease of $78 million or 28 per cent resulted primarily from the following:

Investing activities	By this amount	Due to
Contributing factors		
decreased	$62 million	decreased spending on safety and regulatory projects at Lepreau and Transmission projects
decreased	$47 million	withdrawal from nuclear funds
(increased)	($30 million)	increased spending on Generation projects including Mactaquac

Capital Management

NB Power has a statutory goal established through the *Electricity Act* to achieve a debt/equity ratio of at least 80/20 and is mandated to do so by fiscal year 2020/21. NB Power plans to achieve this goal through low and stable rate increases and debt reduction as a result of continuous improvement, cost management, and new revenue streams. This will provide NB Power with some flexibility to respond to changing markets and technologies and to better prepare for future investment requirements. The percentage of net debt in capital structure is as follows:

	2015/16	2014/15
Total net debt	$4,913	$4,915
Retained earnings	420	408
Accumulated other comprehensive income (AOCI)	(213)	(72)
Total capital	$5,120	$5,251
Percentage of net debt in capital structure	96%	94%
Percentage of net debt in capital structure (excluding AOCI)	92%	92%

Critical Accounting Policy Changes

Introduction

This provides an overview of NB Power's accounting policies that have changed.

Topic	Purpose
Change in accounting policies for fiscal 2016	Describes changes required by the Corporation related to adopting IFRS.
Future change	Describes future changes required by the Corporation related to IFRS.

Changes in Accounting Policies

In February 2013, the Accounting Standards Board (AcSB) confirmed that all rate regulated enterprises in Canada must report under IFRS effective for fiscal years beginning after January 1, 2015. As such the current year financial statements and comparatives have been prepared in accordance with IFRS and IFRS 1 *first-time application of IFRS* has been applied. For further details refer to notes 30 and 31 of the financial statements.

Future Changes

New standards to be implemented include: IFRS9 *Financial Instruments* which will be effective for fiscal years beginning after January 1, 2017, IFRS15 *Revenue from Contracts with Customers* which will be effective for fiscal years beginning after January 1, 2018, IFRS16 *Leases*, which will be effective for fiscal years beginning after April 1, 2019.

Significant Accounting Estimates

Please refer to note 2(b) of the Financial Statements for a listing of NB Power's significant accounting estimates.