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## **2004 Management's Discussion and Analysis**

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## INTRODUCTION

In December 2003, the Canadian securities regulators released National Instrument 51-102, "Continuous Disclosure Obligations". The management discussion and analysis ("MD&A") of Brascan Power Inc. (the "Company") for December 31, 2004 has been prepared to comply with the requirements of regulation 51-102. The purpose of this discussion and analysis is intended to provide a framework for understanding our competitive advantages, the long-term growth trends of our business and the ability of our assets to deliver strong and stable cash flows. In addition, this discussion and analysis is intended to complement and supplement the Company's financial statements. It should be read in conjunction with the audited consolidated financial statements. Additional information relating to Brascan Power Inc. can also be found on the Company's website at [www.brascanpower.com](http://www.brascanpower.com) and on the SEDAR website. Unless expressly indicated otherwise, all dollar amounts reflected are Canadian.

*The following management discussion and analysis is the responsibility of management. The Board of Directors carries out its responsibility for review of this disclosure principally through its Audit Committee. The Audit Committee reviews this disclosure and recommends its approval to the Board of Directors.*

## OVERVIEW OF THE BUSINESS

The Company owns or operates<sup>1</sup> 117 hydroelectric power generating stations located on 35 river systems and 3 cogeneration plants with an installed capacity of 2,622 MW, capable of generating in excess of 10,000 GWh of electricity annually.

The Company has power generating operations in the regionally interconnected markets of Ontario, Quebec, New England, New York, as well as British Columbia, Louisiana and Brazil, and a regulated transmission and distribution business in Ontario. The transmission and distribution business consists of approximately 726 km of 44kv to 230kv transmission lines and includes a low voltage distribution system consisting of approximately 1,700km of low voltage lines and 11 distribution stations that service approximately 11,500 customers. Some of the Company's assets are owned through Great Lakes Hydro Income Fund (the "Fund"), a publicly traded reporting issuer on the Toronto Stock Exchange (symbol: GLH.UN) of which the Company owns a 50.1% interest. The Company is not listed on any stock exchange but it is a reporting issuer with publicly held debt. The Company is a wholly-owned subsidiary of Brascan Corporation ("Brascan"). Brascan is an asset management company listed on the Toronto Stock Exchange (symbol: BNN.LV.A) and New York Stock Exchange (symbol: BNN), focused on the real estate and power generation sectors. Financial results have historically been reported in Canadian dollars, although the Company plans to adopt the US dollar as its functional currency in 2005.

The Company is focused on delivering long-term sustainable cash flows through the operation of low-cost hydroelectric power generating facilities. The Company strives to maximize the stability and predictability of power generating revenues through the use of fixed price contracts which serve to minimize the impact of price fluctuations, and through diversification of watersheds and water storage reservoirs to manage fluctuation in generation levels. Approximately 40% of the Company's generation is sold under long-term fixed-price power purchase agreements, with an average term of over 13 years. The remaining generation is dispatched in competitive electricity markets in Ontario, Quebec, New England and New York, where the Company is one of the lowest cost suppliers. Prices in those markets are a function of instantaneous supply and demand that fluctuates on an hourly basis. The Company manages those fluctuations by entering into short-term financial contracts, when appropriate and within the limits of its risk management policy, to limit its exposure to price fluctuations and optimize overall returns. The Company conducts all of its energy marketing through its wholly owned subsidiary, Brascan Energy Marketing Inc ("BEMI"). BEMI operates in the wholesale energy markets in both Canada and the United States. The Company's strategy is to increase its annual generation sold under power purchase agreements ("PPAs") to approximately 60% when the market price of power is at a level which the Company believes is sustainable.

## PERFORMANCE MEASUREMENT

The Company focuses principally on net operating income for performance measurement because it is tangible and reflects the value of our assets. Net operating income consists of revenues from the Company's power operations, net of operating and maintenance costs, fuel purchases for its cogeneration plants, power purchases, marketing and administration expenses and municipal and other generation taxes on its facilities. Net operating income is a non-GAAP basis of performance measurement. Interest and financing fees, depreciation and amortization, non-controlling interests and provision for income taxes are deducted from net operating income to obtain net income.

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<sup>1</sup> The Brazil common shares are owned by Brascan Corporation. The Company has an investment in preferred shares in these facilities and manages the operations. Results are not included in the Company's consolidated financial statements.  
BRASCAN POWER INC. 2004 – MANAGEMENT'S DISCUSSION AND ANALYSIS

## SELECTED CONSOLIDATED ANNUAL RESULTS

<i>CDN \$ millions (except otherwise noted)</i>	<b>2004</b>	2003	2002
Power generated (GWh)	7,806	6,237	5,584
Power revenues	687	448	340
Net operating income	327	218	232
Net income	134	97	167
Diluted net income per share	0.85	0.77	1.32
Power generating assets	3,195	2,130	2,155
Long-term financial liabilities	2,480	1,582	1,491
Dividend per common share	0.64	0.64	0.64

The increase in power revenues, net operating income and net income from 2003 to 2004 is primarily the result of additional generation from acquisitions or start up of new facilities in 2003 and 2004, a return to more normal hydrology conditions and enhancement initiatives in our operations and marketing activities. The acquisitions of Pontook, Errol and Brassua in New England in the fourth quarter of 2003 contributed \$7 million in net operating income in 2004 compared to \$1 million in the prior year. In 2003, the Pingston facility in British Columbia commenced operations with two units, which contributed a full year of generation in 2004. As well, in May 2004, a third unit in Pingston was added. The Pingston facilities contributed \$4 million to net operating income in 2004, compared to \$3 million in 2003. The White Mountain Energy cogeneration facilities located in Berlin, New Hampshire commenced operations in April 2004 and contributed a further \$5 million to 2004 net operating income. On September 28, 2004, the Company acquired 71 power generating stations in New York State from Reliant Energy Inc. These assets were operational for the last quarter of the year, generating 688 GWh and contributing \$23 million to net operating income.

The Company's net operating income and net income decrease in 2003 from 2002 was the result of lower than average generation levels resulting from water flows much below long-term average and moderate summer temperatures impacting the average price realized on uncommitted power and the demand for ancillary services.

### OVERALL OPERATING RESULTS

Financial results for the year ended December 31, 2004 compared to 2003 are shown in the following table:

<i>millions</i>	<b>2004</b>	2003
Revenue	<b>\$ 687</b>	\$ 448
Net operating income		
Power generation	<b>302</b>	192
Transmission and distribution	<b>25</b>	26
	<b>327</b>	218
Investment income and other	<b>84</b>	89
Non-operating expenses	<b>277</b>	210
Net income	<b>\$ 134</b>	\$ 97
Basic net income per share	<b>\$ 0.97</b>	\$ 0.81
Diluted net income per share	<b>\$ 0.85</b>	\$ 0.77

### NET OPERATING INCOME

Net operating income increased to \$327 million in 2004 from \$218 million in 2003. Revenue for the year totaled \$687 million compared with \$448 million in 2003, an increase of 53% or \$239 million. The return to more normal generation levels in all our operations added approximately \$35 million to our revenues in 2004. The acquisition of the assets in New York State in September 2004, a full year of contribution from the assets acquired in 2003 and the contribution of projects that started operations in 2004 added approximately \$70 million to our revenues. Operating and marketing enhancement initiatives such as re-marketing of power contracts, resale of Lake Superior gas, optimization of our generation profile, ancillary revenues and price management also positively impacted our revenue for the year by adding approximately \$74 million. Power sold to an affiliate for a full year in 2004 compared to only seven months in 2003 added \$60 million over 2003 revenue and totaled \$154 million. Power purchases to supply this contract during the year totaled \$178 million compared to \$95 million in the prior year, net of an amount of \$17 million for profit/loss sharing. The contract with the affiliate expires in May 2005.

Operating and maintenance costs totaled \$80 million compared with \$58 million in 2003, an increase of \$22 million. Water rental and property taxes totaled \$36 million compared with \$22 million in 2003, an increase of \$14 million. Selling, marketing and administration expenses for the year totaled \$31 million, compared to \$22 million in prior year. Increases are a result of the addition of new facilities in 2003 and 2004 and the return to normal hydrology levels in 2004.

Fuel purchases consist of the cost of natural gas required for the cogeneration plants. Fuel purchases for the operation of our cogeneration plants remained relatively stable in 2004 at \$35 million compared to \$34 million in 2003. The slight increase is due to annual rate increases across suppliers for transportation.

The Company expects cash operating expenses from existing operations in 2005 to remain relatively consistent with 2004.

## BUSINESS SEGMENT PERFORMANCE

<b>Power Generated</b> (gigawatt hours)	<b>2004</b>	2003	Long-term average <sup>3</sup>
Ontario	<b>3,190</b>	3,069	3,262
Québec	<b>1,661</b>	1,461	1,628
British Columbia	<b>387</b>	328	356
New England	<b>1,056</b>	710	1,194
New York <sup>1</sup>	<b>688</b>	-	2,933
Other <sup>2</sup>	<b>824</b>	669	677
<b>Total</b>	<b>7,806</b>	6,237	10,050

1. Full year long-term average. Generation in 2004 includes September 28 to December 31, 2004.

2. Excludes power produced by Brazilian assets operated by the Company but owned by Brascan Corporation.

3. Long-term average is the simulated annual generation, based on observed historical inflows and current asset bases.

<b>Revenue (\$ millions)</b>	<b>2004</b>	2003
Ontario	<b>\$ 229</b>	\$ 178
Québec	<b>90</b>	63
British Columbia	<b>15</b>	12
New England	<b>63</b>	39
New York	<b>50</b>	-
Other <sup>4</sup>	<b>240</b>	156
	<b>\$ 687</b>	\$ 448

4. Includes the Company's Transmission and Distribution business and contract sales to an affiliate

### Revenue by Segment

#### Ontario

Revenues from Ontario operations increased by 29% to \$229 million. This is due to a 4% increase in power generated by these operations, from 3,069 GWh to 3,190 GWh in 2004, the resale of the Lake Superior gas, re-marketing of power contracts, the optimal use of our reservoirs and flexibility to obtain better than average pricing and other marketing, hedging and financial activities.

#### Québec

Revenue from our operations in Québec totaled \$90 million during the year, representing an increase of 43%, or \$27 million, as compared to 2003. Power generated by the Company's operations in Québec increased by approximately 14% to 1,661 GWh. Our Québec facilities were affected by a favorable first-half of the year, resulting in above average water inflows. The maximization of the value of the power produced by the Lièvre river system, by using our Québec/Ontario interconnection and the execution of other marketing activities also contributed to the revenue increase.

#### British Columbia

Generation in British Columbia totaled 387 GWh in 2004, 18% above the 328 GWh generated in 2003, partially due to the commissioning of the Pingston third unit in 2004 and the benefit of the first two units commissioned in 2003 for the full year. Revenue from our British Columbia operations totaled \$15 million in 2004, representing an increase of 25% over 2003.

#### New England

Power generated by the Company's operations in New England increased by 49% from 710 GWh in 2003 to 1,056 GWh in 2004, reflecting a full year of generation from the assets acquired in November 2003 and the commercial operation of our cogeneration facility in Berlin, New Hampshire, in April 2004. In addition, a return to more normal hydrology also contributed to increased revenues. In total, our New England operations contributed approximately \$63 million to our revenue in 2004 compared to \$39 million in 2003.

#### New York

On September 28, 2004, the Company acquired 71 hydroelectric power generating plants and a 105 megawatt cogeneration facility from Reliant Energy Inc. During the last 95 days of the year, the New York operations generated 688 GWh and contributed \$50 million to revenues.

#### Other

Power generated by the Louisiana facilities increased from 669 GWh in 2003 to 824 GWh in 2004, which resulted in a higher equity pick-up totaling \$36 million (2003 - \$18 million) from our 75% ownership in these facilities. Our Transmission and Distribution business contributed \$38 million to our revenues, consistent with the prior year.

Revenues from other power operations also includes power sold to an affiliate in the amount of \$154 million for a full year in 2004, compared to \$95 million in the previous year representing only seven months of sales. The contract with the affiliate expires in May 2005.

## NET INCOME AND EARNINGS PER SHARE

The Company's net income in 2004 totaled \$134 million, an increase of \$37 million or 28% from 2003. The increase in net income and earnings per share is a result of higher net operating income, partially offset by higher depreciation expenses and an increase in the provision for income taxes.

The Company's basic earnings per share increased from \$0.81 in 2003 to \$0.97 in 2004, representing an increase of \$0.16 or 20%. The Company's weighted average outstanding common shares for the year ended December 31, 2004 is consistent with 2003.

## INVESTMENT AND OTHER INCOME

Investment and other income for 2004 was \$84 million compared with \$89 million in 2003. Investment and other income consist of dividend income from long-term investments and the Company's securities portfolio, interest on cash and cash equivalents, swap recouping income and gains or losses on foreign exchange. The decrease in investment and other income is attributed to the redemption or sale of securities and long-term investments during the year, resulting in lower dividend income. This decrease was partially offset by higher interest income earned during the year as a result of overall higher cash on deposit with Brascan Corporation.

## INTEREST AND FINANCING FEES

Years ended December 31

<i>millions</i>	<b>2004</b>	2003
Ontario	<b>\$ 40</b>	\$ 31
Québec	<b>14</b>	14
British Columbia	<b>3</b>	3
New England	<b>10</b>	10
New York	<b>8</b>	-
Other <sup>1</sup>	<b>36</b>	44
<b>Total</b>	<b>\$ 111</b>	\$ 102

1. Other interest and financing fees includes \$30 million (2003 - \$39 million) of corporate debenture interest.

Interest and financing fees were \$111 million in 2004 compared to \$102 million in 2003. Interest and financing fees in New York relates to the US \$500 million bridge financing for the acquisition of the New York assets. The increase in interest and financing fees in Ontario results from the refinancing of the Mississagi bridge facility from a floating \$150 million mortgage loan to fixed rate \$175 million senior bonds and the refinancing of the Great Lakes Power Limited ("GLPL") bonds in June 2003. The repayment of the US \$175 million term debentures positively impacted other interest and financing fees.

## DEPRECIATION AND AMORTIZATION

Depreciation in 2004 was \$76 million compared to \$55 million in 2003. The increase is due to the assets acquired or put into service in 2003 and 2004 and the write-off of some transmission assets resulting from the transmission reinforcement project.

## NON-CONTROLLING INTERESTS

Non-controlling interests consists of the allocation of income associated with the non-controlling interests in the Company's consolidated entities. The increase of \$4 million in 2004 is related to the higher earnings recorded by the Fund, which is 49.9% owned by other investors.

## PROVISION FOR INCOME TAXES

The provision for taxes increased to \$64 million in 2004 compared with \$31 million in 2003. The increase in the provision for taxes is primarily related to provisions for federal and provincial income taxes on higher taxable income in 2004. Taxes are accounted for under the asset and liability method.

## BALANCE SHEET

### POWER GENERATING ASSETS

Power generating assets as at December 31, 2004 totaled \$3,195 million, compared to \$2,130 million in the prior year. This increase is primarily attributable to the purchase of the New York assets, which amounted to approximately \$1,058 million. There were \$163 million in additional capital investments made during the year, the most significant relating to the investment in Brazil (\$40 million), the transmission reinforcement project in Northern Ontario (\$27 million), the Weldon conversion project in Maine (\$7 million), the Cedar Dam project on the Lièvre River in Québec (\$11 million), the cogeneration facility in Berlin, New Hampshire (\$4 million) and the installation of a third unit at Pingston generating station in British Columbia (\$3 million). The Company also invested an amount of \$12 million to rebuild the Shikwamka dam. All of these projects will contribute positively to our results in 2005.

## CAPITAL STRUCTURE AND FINANCING

The Company has investment grade issuer ratings from DBRS (BBB High), Standard and Poors ("S & P") (BBB) and Moody's (BAA3). The Company maintains a prudent level of low-cost asset level financing and modest levels of corporate debt. The long-life nature of its assets allows the Company to finance its assets with non-recourse debt with minimal near-term maturities.

At December 31, 2004, the Company's total debt was as follows:

<i>millions</i>	Maturity	2004	2003	Interest Rates	Rating	Agency
Great Lakes Power Ltd.						
First Mortgage Bonds						
Series 1	2023	\$ 384	\$ 384	6.60% <sup>1</sup>	A Low	DBRS
Subordinated debt	2023	115	115	7.80%	BBB	DBRS
Great Lakes Power Trust						
First Mortgage Bonds						
Series 1	2005	50	50	7.33%	BBB+	S & P
Series 2	2010	25	25	7.55%	BBB+	S & P
Series 3	2015	25	25	7.78%	BBB+	S & P
Powell River	2009	39	39	6.40%	A Low	DBRS
Lake Superior Power mortgage loan	-	-	13	9.41%	-	-
Lake Superior Power senior secured bonds	2009	73	-	4.39%	BBB High	DBRS
Pontiac Power	2020	59	60	10.52%	Not rated	N/A
Valerie Falls	2042	32	32	6.84%	Not rated	N/A
Mississagi Power	2020	175	175	6.92%	A Low	DBRS
GLHA Senior secured notes (US \$125)	2014	150	-	5.60%	Not rated	N/A
GLHA bridge facility (US \$11)	2006	13	177	US Prime + 150bps	Not rated	N/A
New York bridge financing (US \$500)	2006	600	-	LIBOR + 100 bps	A Low	DBRS
		<b>1,740</b>	1,095			
US Corporate debentures (Series 1)	2004	-	227	9.00%	-	-
US Corporate debentures (Series 3) (US \$200)	2005	240	260	8.30% <sup>1</sup>	BBB High BBB BAA3	DBRS S & P Moody's
CDN Corporate debentures (Series 1)	2009	400	-	4.65%	BBB High BBB	DBRS S & P
CDN Corporate debentures (Series 2)	2006	100	-	CDOR + 68 bps	BBB High BBB	DBRS S & P
		<b>740</b>	487			
		<b>\$2,480</b>	\$1,582			

1. The Company has entered into interest rate swaps for these First Mortgage Bonds and debentures.

At December 31, 2004, the Company's weighted average interest rate and term to maturity for long-term debt are 5.4% and 8.1 years respectively.

The change in our capital structure in 2004 compared to 2003 is due to the increase in property specific borrowings relating to the New York acquisition and the issuance of corporate term debentures in December 2004. These new borrowings are discussed below.

<b>CAPITAL STRUCTURE</b> (composition of total structure)	As at December 31, 2004	As at December 31, 2003
Credit facilities	1%	1%
Property specific borrowings and corporate term debentures	52%	46%
Deferred credits	4%	4%
Non-controlling interests	7%	9%
Shareholders' equity	36%	40%
Total	100%	100%

In 2004, the Company refinanced US\$125 million of the New England bridge facility with senior secured notes. The notes are secured by a first ranking lien on all New England assets, bear an annual average interest rate of 5.60% payable quarterly, and mature on May 28, 2014. The remaining US\$11 million of the New England bridge facility rests with Brascan Corporation, bears an annual interest rate of US prime plus 150 basis points payable monthly and matures on January 29, 2006.

Additionally, the Company completed the issuance of \$77 million of senior secured bonds with an annual interest rate of 4.39%. These bonds mature on September 23, 2009 and are secured by a first ranking lien on the Lake Superior Power assets.

The Company also obtained bridge financing of US \$500 million for the acquisition of the New York assets. The agreement is secured by a first ranking lien on all Erie Boulevard Hydro Power LP assets, bears an annual interest rate of LIBOR plus 100 basis points and matures on September 28, 2006.

Furthermore, we completed the issuance of \$400 million Series 1 and \$100 million Series 2 Canadian debentures. The Series 1 debentures bear interest at 4.65% and are due December 16, 2009. The Series 2 debentures bear interest at Canadian Deposit Offering Rate ("CDOR") plus 68 basis points and are due December 18, 2006.

The US \$175 million Series 1 corporate debentures were repaid upon maturity in August 2004 and the US \$200 million Series 3 Corporate debentures will be repaid in the first quarter of 2005.

We have access to \$271 million of committed credit facilities, which ensures that we have adequate liquidity to fund our operations. At December 31, 2004, \$32 million was drawn against these facilities and \$79 million was drawn in the form of letters of credit.

The composition of our short-term facilities is as follows:

Years ended December 31					
<i>millions</i>	Available	Drawn		Letters of credit	
		2004	2003	2004	2003
Credit facilities					
Great Lakes Power Trust	\$ 50	\$ 32	\$ 21	\$ 6	\$ -
Powell River Energy Inc.	3	-	-	1	-
Commercial paper <sup>1</sup>	100	-	-	-	-
Unsecured general facility	118	-	-	72	73
	\$ 271	\$ 32	\$ 21	\$ 79	\$ 73

1. The Company has a \$100 million US credit facility backing the commercial paper program.

We provided covenants to certain of our lenders as do most borrowers. The Company is in compliance with all covenants that would have a material adverse effect on its business.

#### SHAREHOLDERS' EQUITY

The Company's capital base at December 31, 2004 of \$1,710 million was comprised of common equity with a book value of \$362 million and \$1,348 million of subordinated convertible debentures. During the year, the Company restructured the capital base through the issuance of \$1,100 million of subordinated convertible debentures and the payment of a dividend of \$800 million, resulting in an increase in equity of \$300 million. Principal on all debentures may be paid in the form of common shares at a fixed price at the option of the Company, while interest may also be paid by way of common shares at a variable rate. As such, the debentures are included as part of the Company's capital base.

The composition of the Company's capital base at December 31, 2004 and 2003 is summarized in the following table:

<i>millions</i>	2004	2003
Subordinated convertible debentures	\$ 1,348	\$ 248
Common shares, retained earnings and cumulative translation adjustment	362	1,134
	\$ 1,710	\$ 1,382

The Company had 101,383,135 common shares issued and outstanding as at December 31, 2004, consistent with prior year.

Regular dividends paid on the Company's common shares and interest paid on the subordinated convertible debentures were \$121 million in 2004 and \$80 million in 2003.

The Company's policy is to distribute surplus operating cash flows not required for investment in power generating facilities to its common shareholders in the form of regular quarterly and special dividend payments.

## LIQUIDITY AND CAPITAL RESOURCES

Given the nature of our operations, the industry in which we operate and our contractual arrangements, our cash margin is stable and provides a strong credit profile. In addition to the risk of variable hydrology conditions, our risk with respect to liquidity arises from the financing required for acquisitions and significant capital projects.

We have access to the following sources from which to fund our capital program:

- Existing cash reserves;
- Strong cash flow from operations; and
- Additional available credit facilities.

The Company continues to have a strong balance sheet and healthy financial ratios. As at December 31, 2004, we maintained a current cash and cash equivalents balance of \$556 million. These factors, combined with the additional available resources noted above, make liquidity for the Company a negligible risk factor.

## CONTRACTUAL OBLIGATIONS

The following table summarizes our significant contractual obligations as of December 31, 2004:

<i>\$ in millions</i>	Total	In years 2005-2009	In years 2010-2014	In years 2015-2019	Beyond 2020
Long-term debt (CDN)	\$1,508	\$ 706	\$ 45	\$51	\$706
Long-term debt (USD)	\$ 836	\$ 711	\$ 125	\$ -	\$ -
Capital projects (CDN)	\$ 53	\$ 53	\$ -	\$ -	\$ -
Purchase obligations (USD)	\$ 82	\$ 82	\$ -	\$ -	\$ -

## PURCHASE OBLIGATIONS

The Company has entered into a 50/50 joint venture agreement with Emera Inc. to acquire Bear Swamp, a 589 megawatt pumped storage hydro-electric facility in northern Massachusetts. The total purchase price of this acquisition is US \$92 million, of which our share is US \$46 million.

Additionally, the Company has entered into a 50/50 joint venture agreement with Emera Inc. to lease a 49 megawatt hydroelectric generating facility, located in Vermont. The total payments to lease this facility for up to 74 years are US \$72 million. The Company's payments relating to this agreement will be up to US \$36 million.

Given our historical profitability and our ability to manage expenses, we believe that our current resources are adequate to meet our requirements for working capital and capital expenditures through the foreseeable future.

## OFF-BALANCE SHEET ARRANGEMENTS

### Guarantees

In the normal course of operations, the Company and its consolidated subsidiaries execute agreements that provide for indemnification and guarantees to third parties in transactions such as business dispositions, business acquisitions, sales of assets and sales of services. The Company has also agreed to indemnify its directors and certain of its officers and employees. The nature of substantially all of the indemnification undertakings prevents the Company from making a reasonable estimate of the maximum potential amount that the Company could be required to pay third parties as the agreements do not specify a maximum amount and the amounts are dependent upon the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, neither the Company nor its consolidated subsidiaries have made significant payments under such indemnification agreements.

The Company has guaranteed various debt and other obligations for certain subsidiaries. The Company would be required to perform on these guarantees in the event of default by the guaranteed parties. No material loss is anticipated by reason of such agreements and guarantees. Note 23 to the consolidated financial statements provides detailed information regarding the nature and potential maximum exposure for these guarantees.

### Derivative Instruments

The Company uses derivative financial instruments including commodity swaps, interest rate swaps, and commodity and foreign exchange forward contracts to manage risk. Derivative financial instruments involve credit and market risk. Credit risk arises from the potential for a counterparty to default on its contractual obligations and is limited to those contracts where the Company would incur a loss in replacing the defaulted transaction. The Company minimizes credit risk through the selection, monitoring and diversification of counterparties, use of the International Swaps and Derivatives Association (ISDA) documentation, collateral and other credit risk mitigation techniques. These risks are reviewed on a regular basis and the Company believes the exposures are manageable and not material in relation to its overall business operations.



a) Commodity derivative instruments

As at December 31, 2004, the energy and gas derivative contracts were comprised of contracts with deferred unrealized losses in excess of that recorded in the Company's accounts of \$84 million (2003 - \$36 million) as well as contracts with deferred unrealized gains in excess of that recorded in the Company's accounts of \$76 million (2003 - \$30 million).

b) Interest rate derivative instruments

The Company designates its interest rate swap agreements as hedges of the underlying debt. Interest expense is adjusted to include the payments made or received under the interest rate swaps. The total notional amount of principal underlying interest rate swap contracts in 2004 was \$524 million (2003 - \$772 million). These contracts have maturities varying from one to nineteen years, and have unrealized deferred gains in excess of that recorded in the Company's accounts of \$1 million (2003 - \$6 million) and unrealized deferred losses of \$7 million (2003 - \$16 million) in excess of that recorded in the Company's accounts.

c) Foreign exchange derivative instruments

At December 31, 2004, the Company held foreign exchange contracts with a notional amount of \$377 million at an average exchange rate of 1.214, of which \$US 200 million was designated as a hedge of the net investments in foreign operations. At year end, these contracts had unrealized deferred gains in excess of that recorded in the Company's accounts of \$4 million. At December 31, 2003, the Company did not hold any foreign exchange contracts. All of the foreign exchange contracts held at December 31, 2004 had a maturity of less than one year.

The Company's derivative financial instruments are discussed more fully in note 21 to the consolidated financial statements.

## RELATED PARTY TRANSACTIONS

The Company carried out various transactions with related parties during the year. The nature of these transactions are consistent with prior year and include energy sales, physical gas sales and receipt and payment of interest on deposits. All transactions are in the normal course of operations and are settled at prevailing market rates. Related party transactions are described in note 3 to the consolidated financial statements. The following table summarizes all significant year-to-date related party transactions:

<i>millions</i>	<b>2004</b>	2003
<b>Revenues</b>		
Sale of power to Noranda Aluminum Inc.	<b>\$ 154</b>	\$ 95
Physical gas sales to Noranda Inc.	<b>13</b>	16
Sale of power and financial transactions with Brookfield Properties Corporation	<b>14</b>	18
Sale of power to Katahdin Paper Company	<b>29</b>	17
Sale of power and tolling agreement with Fraser New Hampshire	<b>13</b>	8
	<b>223</b>	154
<b>Investment income and other</b>		
Interest earned on demand deposits with Brascan Corporation	<b>6</b>	(1)
Income from securities with affiliated companies	<b>27</b>	34
Income from investments with affiliated companies	<b>36</b>	44
	<b>\$ 69</b>	\$ 77
<b>Expenses</b>		
Profit/loss sharing with Noranda Aluminum Inc. <sup>1</sup>	<b>\$ (17)</b>	\$ 3
Income on interest rate swaps with Brascan Corporation	<b>(7)</b>	(3)
Interest expense on bridge facility with Brascan Corporation	<b>5</b>	10
	<b>\$ (19)</b>	\$ 10

*1. Included in power purchases*

As a result, the following balance is receivable at December 31:

<i>millions</i>	<b>2004</b>	2003
Noranda Inc.	<b>\$ 14</b>	\$ 15
Brookfield Properties Corporation	-	2
Katahdin Paper Company	<b>5</b>	5
Fraser New Hampshire	<b>1</b>	1
	<b>\$ 20</b>	\$ 23

## **OPERATING STRATEGY AND OUTLOOK**

The Company is committed to expanding its power generation base by strategically acquiring existing hydroelectric assets and developing renewable energy products such as small hydroelectric facilities and wind farms. Furthermore, the Company is committed to reinvesting in its regulated transmission and distribution system in Ontario. During the year, the Company increased generating capacity by 674 megawatts through the acquisition of the New York facilities. As a result, our total power generation base has increased to over 2,600 megawatt hours. Our acquisitions in the past few years have allowed the Company to establish a geographic presence in several regions, including the regionally interconnected markets of Ontario, Quebec, New England, and New York. The Company will continue to identify new opportunities to optimize the performance of its portfolio and expand and continue its diversification strategy in 2005 and beyond.

As at December 31, 2004, the majority of our reservoirs were at expected seasonal levels. As such, long-term average continues to be the best estimate for anticipated generation in 2005.

The Company will continue to preserve and enhance the value and reliability of its operations through capital additions and major maintenance work. In 2005, we expect to invest more than \$243 million to that effect. The completion of the reinforcement of the transmission system (\$45 million), Shikwamka earth dam repairs (\$84 million), the completion of the Cedar Dam project (\$11 million) and the conversion of Weldon from a 40 to 60HZ station (\$11 million) are estimated to account for approximately \$151 million of the total 2005 capital program spending.

The Company expects to liquidate over time the investment portfolio, comprised of securities and long-term investments, with the proceeds used to fund acquisitions and capital expenditures. The monetization of the investment portfolio will be executed in such a manner as to ensure the existing credit profile of the Company is maintained.

The Company has entered into an agreement to acquire two hydroelectric generating facilities with 48 megawatts of capacity from Reliant Energy Inc. The total purchase price is US \$42 million. The Piney station is a 28 megawatt facility located in Pennsylvania and the Deep Creek station is 20 megawatt facility located on the Youghiogheny River in Maryland.

The Company has also entered into an agreement to acquire leasehold interests in two hydroelectric generating facilities from Delta Power LLC. Hydro-Kennebec is a 15.4 megawatt facility located on the Kennebec River in Winslow, Maine. West Delaware is a 7.5 megawatt facility located in Grahamsville, New York. The total purchase price is US \$31 million, with approximately \$12 million assumed in debt and the balance paid in cash.

These transactions will increase our ability to optimize our New England generation portfolio and strengthen our geographic presence in the northeastern United States, in line with our objective of geographic penetration. These transactions are expected to close during the 2005 fiscal year, subject to regulatory approval and have been disclosed in note 24 to the consolidated financial statements.

In keeping with the emerging Ontario Securities Commission requirements, the Company plans to continue reviewing and documenting its controls and procedures for annual certification of the financial statements.

## **CRITICAL ACCOUNTING POLICIES**

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles, which require the use of estimates and judgment in reporting assets, liabilities, revenues, expenses and contingencies. In the judgment of management, none of the estimates outlined in Note 1 (Summary of Accounting Policies) of the 2004 consolidated financial statements are considered critical accounting estimates as defined in regulation 51-102. Key estimates for the Company include determination of accruals, purchase price allocations, useful lives, asset impairment testing and those relevant to the defined benefit pension and non-pension benefit plans. Estimates are based on historical experience, current trends and various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from those estimates.

## **CHANGES IN ACCOUNTING POLICIES**

Effective January 1, 2004, the Company adopted CICA Handbook section 3110, "Asset Retirement Obligations". Section 3110 addresses the recognition and re-measurement of obligations associated with the retirement of a tangible long-lived asset. This standard provides that obligations associated with the retirement of tangible long-lived assets be recorded as liabilities when those obligations are incurred, with the amount of the liability initially measured at fair value. These obligations are capitalized to the book value of the related long-lived assets and are depreciated over the useful life of the related asset. The Company does have asset retirement obligations associated with certain generating stations. The retirement date for these generating stations cannot be reasonably estimated and therefore the fair value of the associated liability cannot be estimated at this time. As a result, no liability has been accrued in these financial statements.

Effective January 1, 2004, the Company adopted Accounting Guideline 13, "Hedging Relationships" (AcG 13), the new accounting guideline issued by the CICA which increases the documentation, designation and effectiveness criteria to achieve hedge accounting. The guideline requires the discontinuance of hedge accounting for hedging relationships previously established that do not meet the criteria at the date it is first applied. AcG 13 does not change the method of accounting for derivatives in hedging relationships, but EIC 128, "Accounting for Trading, Speculative or Non-Hedging Derivative Financial Instruments", effective when AcG 13 is adopted, requires fair value accounting for derivatives that do not qualify for hedge accounting. Realized and unrealized gains and losses on derivative financial instruments designated as hedges of financial risks are included in income in the same period as when the underlying asset, liability or anticipated transaction affects income.

## **RECENTLY ISSUED STANDARDS**

In June 2003, the CICA issued Accounting Guideline 15, "Consolidation of Variable Interest Entities" (AcG 15), effective for years beginning on or after November 1, 2004. AcG 15 provides guidance for applying the principles in Section 1590, "Subsidiaries", to those entities (defined as Variable Interest Entities (VIEs)), in which either the equity at risk is not sufficient to permit that entity to finance its activities without additional subordinated financial support from other parties, or equity investors lack any of voting control, an obligation to absorb expected losses, or the right to share expected residual returns. AcG15 requires consolidation of VIEs by the Primary Beneficiary, which is defined as the party which has exposure to the majority of a VIEs expected losses and/or expected residual returns. The Company is in the process of assessing the impact of the standard on the consolidated financial statements, and believes that the most significant impact will be the consolidation of Louisiana Hydroelectric Power which is currently accounted for under the equity method.

In January 2004, the CICA issued amendments to CICA Handbook Section 3860, "Financial Instruments - Presentation and Disclosure" ("Section 3860"), to require obligations that may be settled, at the issuer's option, by a variable number of the issuer's own equity instruments to be presented as liabilities. Thus, securities issued by an enterprise that give the issuer unrestricted rights to settle the principal amount in cash or in the equivalent value of its own equity instruments will no longer be presented as equity. The amendments to Section 3860 are applicable to the Company beginning January 1, 2005 on a retroactive basis. Adoption of these amendments may require reclassification of a portion of the subordinated convertible debentures.

## **BUSINESS RISKS**

The following represents a summary of the most relevant risk factors relating to the Company's business. This summary contains only certain risk factors and is not all-inclusive.

### **Hydrology**

The revenues generated by the power systems are proportional to the amount of electricity generated. The amount of electricity generated by the hydroelectric power systems is dependent upon available water flows. Accordingly, revenues and cash flows may be affected by low and high water flows in the watersheds. There can be no assurance that the long-term historical water availability will remain unchanged or that no material hydrologic event will impact the hydrologic conditions that exist within the watershed. Annual deviations from the long-term average can be significant. The Company strives to mitigate the risk of variable hydrology conditions by acquiring and operating a portfolio of geographically diverse facilities. The diversified locations of our power generating assets assist in balancing the impact of generation fluctuations in any one geographic region. We also have access to hydrology insurance.

### **Equipment Failure**

There is a risk of equipment failure due to wear and tear, latent defect, design error or operator error, among other things, which could adversely affect revenues and cash flows. Although the power systems have operated in accordance with expectations, there can be no assurance that they will continue to do so. Nevertheless, this risk is substantially mitigated by the proven nature of hydroelectric technology, the design of the plants, the power systems' capital programs, adherence to prudent maintenance programs, comprehensive insurance and significant operational flexibility as a result of having generating units which can operate independently.

## Foreign Exchange

The price paid for energy produced by our US operations is denominated in US dollars and, therefore, results may be affected by the fluctuations of the Canadian/US dollar exchange rate over time. A material increase in the value of the Canadian dollar may negatively impact the Company's cash flows. The US operations' operating expenses and financing costs incurred are also denominated in US dollars, thus providing a natural hedge. In addition, we may manage the risk associated with foreign exchange rate fluctuations by entering, from time to time, into forward foreign exchange contracts and engaging in other hedging strategies. To the extent that we engage in risk management activities related to foreign exchange rates, it will then be subject to credit risks associated with the counterparties with which it contracts.

## Energy Price Fluctuations

A significant portion of the Company's revenue is tied, either directly or indirectly, to the spot market price for electricity. Electricity price volatility could have a material adverse effect on the Company's business, operating results, financial condition or prospects.

Through its wholly-owned subsidiary BEMI, the Company actively manages its energy production and sales, partly through physical and financial contracts, minimizing the impact of price volatility. The Company's objective is to derive its revenues primarily from PPAs and regulated rate base arrangements and to reduce the amount of non-contracted power by entering short-term financial contracts. For the next two years, approximately 70% of the Company's generation is contracted under PPA and short term financial contracts. The remaining power is sold on a wholesale basis. Due to the low variable cost of hydroelectric power and the ability to concentrate generation during peak pricing periods, the Company is able to generate attractive margins on uncommitted capacity. The Company's PPAs have an average term of 13 years and counterparties are almost exclusively customers with long-standing credit history or investment grade ratings. Our policy is to use financial contracts which typically have a term of less than two years to lock in the future price of uncommitted power we are reasonably certain to generate. This approach provides an appropriate level of revenue stability, without exposure to undue risk of contractual shortfalls, and provides the flexibility to enhance profitability through the production of power during peak price periods. These activities are closely monitored through risk management policies. However, there is a transaction risk associated with these activities that could result in losses in extraordinary circumstances. From time-to-time, BEMI may take advantage of very short-term arbitrage opportunities when hourly prices diverge between interconnected markets in its area of operation.

## QUARTERLY ANALYSIS OF RESULTS

### OVERALL OPERATING RESULTS

Financial results for the quarter ended December 31, 2004 compared to 2003 are shown in the following table:

<i>millions</i>	<i>Three months ended December 31</i>	
	<b>2004</b>	2003
Revenue	<b>\$ 183</b>	\$ 142
Net operating income		
Power generation	<b>71</b>	62
Transmission and distribution	<b>4</b>	6
	<b>75</b>	68
Investment income and other	<b>22</b>	29
Non-operating expenses	<b>86</b>	78
Net income	<b>\$ 11</b>	\$ 19
Diluted net income per share	<b>\$ (0.11)</b>	\$ 0.15

### NET OPERATING INCOME

Net operating income increased to \$75 million in the fourth quarter of 2004 from \$68 million in the same quarter of 2003, an increase of \$7 million. Revenue for the quarter totaled \$183 million compared with \$142 million in 2003, an increase of 29% or \$41 million. The decrease in generation for the fourth quarter negatively impacted our revenues by approximately \$21 million. The acquisition of the assets in New York State in September 2004, along with the contribution from the projects that started operations in 2004 added approximately \$52 million to our revenues. Operating and marketing enhancement initiatives such as re-marketing of power contracts, resale of Lake Superior gas, optimization of our generation profile, ancillary revenues and price management also positively impacted our revenue for the quarter by adding approximately \$13 million. Power sold to an affiliate for the fourth quarter was lower by \$3 million over 2003.

Operating and maintenance costs totaled \$37 million compared with \$18 million in 2003, an increase of \$19 million. Water rental and property taxes totaled \$15 million compared with \$7 million in 2003, an increase of \$8 million. Selling, marketing and administration expenses totaled \$8 million compared to \$5 million in the same quarter in the prior year. Increases are mostly a result of the addition of the New York facilities in September 2004.

Fuel purchases during the quarter remained stable compared to 2003 at \$9 million.

Power purchases during the quarter totaled \$39 million compared to \$35 million in the same quarter in the prior year. This increase is a result of a higher volume of power purchases and increases in the average price.

## BUSINESS SEGMENT PERFORMANCE

### GENERATION

<i>Gigawatt hours</i>	<i>Three months ended December 31</i>			<i>Twelve months ended December 31</i>		
	<b>2004</b>	<i>2003</i>	<i>Long-term average</i>	<b>2004</b>	<i>2003</i>	<i>Long-term average</i>
Ontario	<b>635</b>	817	774	<b>3,190</b>	3,069	3,262
Québec	<b>281</b>	530	382	<b>1,661</b>	1,461	1,628
British Columbia	<b>92</b>	76	73	<b>387</b>	328	356
New England	<b>245</b>	253	297	<b>1,056</b>	710	1,194
New York	<b>673</b>	-	765	<b>688</b>	-	2,933
Other	<b>199</b>	117	109	<b>824</b>	669	677
	<b>2,125</b>	1,793	2,400	<b>7,806</b>	6,237	10,050

### REVENUE

<i>CDN\$ millions</i>	<i>Three months ended December 31</i>		<i>Twelve months ended December 31</i>	
	<b>2004</b>	<i>2003</i>	<b>2004</b>	<i>2003</i>
Ontario	<b>\$ 46</b>	\$ 55	<b>\$ 229</b>	\$ 178
Québec	<b>13</b>	24	<b>90</b>	63
British Columbia	<b>3</b>	2	<b>15</b>	12
New England	<b>13</b>	15	<b>63</b>	39
New York	<b>49</b>	-	<b>50</b>	-
Other	<b>59</b>	46	<b>240</b>	156
	<b>\$ 183</b>	\$ 142	<b>\$ 687</b>	\$ 448

### Revenue by Segment

#### Ontario

In Ontario, generation was 635 GWh, a decrease of 22% from the same quarter in 2003. The Ontario region was the most affected by below average water inflows in the fourth quarter. Power generation contributed \$46 million of revenues during the fourth quarter compared to \$55 million in the fourth quarter of 2003.

#### Québec

In Québec, generation for both power systems during the fourth quarter was 281 GWh compared to 530 GWh for the same period last year. This decrease is the result of lower water inflows during the quarter in comparison to prior year, as well as management's decision to preserve water for the January and February periods when prices tend to be higher. As a result, revenues decreased from \$24 million in the fourth quarter of 2003 to \$13 million for the same quarter this year.

#### British Columbia

The Company's share of the quarterly generation in British Columbia was 92 GWh, an increase of 21% in production from the same period last year. This is due to above average inflows compared to prior year and the addition of the Pingston third unit. Revenues of \$3 million for the fourth quarter of 2004 increased by \$1 million over the same quarter of 2003.

#### New England

In New England, power generation contributed \$13 million of revenues compared to \$15 million for the same period last year. Overall, generation during the fourth quarter remains consistent with 2003. Generation from our co-generator, which commenced operations in the current year, offset decreases in generation from our other New England facilities. The decrease in revenues by \$2 million is attributable to a lower price per gigawatt hour for our co-generator compared to our other New England facilities. The decrease is also attributable to the strengthening Canadian dollar in 2004.

#### New York

In New York, the acquisition of 71 hydroelectric power generating plants and 1 co-generation facility on September 28, 2004 contributed \$49 million of revenues for the quarter. Generation for the fourth quarter was 673 GWh.

#### Other

Other power operations include our share of net income for Louisiana HydroElectric Power and the net result of power sales to an affiliate. The revenues increased by \$13 million to \$59 million primarily due to an increase in our other revenues resulting from the sale of a receivable which had been provided for in the first quarter of 2004.

### NET INCOME AND EARNINGS PER SHARE

The Company's net income for the fourth quarter totaled \$11 million, a decrease of \$8 million from the same quarter in the prior year. The decrease in net income is a result of a higher depreciation expense and lower investment income, which was partially offset by higher operating income.

The components of basic and diluted earnings per share are summarized below:

<i>millions</i>	<b>2004</b>	2003
Net income	\$ <b>11</b>	\$ 19
Convertible debenture interest	<b>(35)</b>	(4)
Tax effect of convertible debenture interest	<b>13</b>	-
Net income available to common shareholders - basic	\$ <b>(12)</b>	\$ 15
Dilutive effect of convertible debentures	-	4
Net income available to common shareholders- diluted	\$ <b>(12)</b>	\$ 19
Weighted average outstanding common shares - basic	<b>101.4</b>	101.4
Dilutive effect of the conversion of debentures	-	24.8
Common shares and common share equivalents - diluted	<b>101.4</b>	126.2
Basic earnings per share	\$ <b>(0.11)</b>	\$0.15
Diluted earnings per share	\$ <b>(0.11)</b>	\$0.15

#### INVESTMENT AND OTHER INCOME

Investment and other income decreased by \$7 million primarily due to the sale of investments during the year, resulting in lower dividend receipts compared to the same period in 2003.

#### INTEREST AND FINANCING FEES

<i>millions</i>	<b>2004</b>	2003
Ontario	\$ <b>8</b>	\$ 10
Québec	<b>3</b>	4
British Columbia	<b>1</b>	1
New England	<b>3</b>	2
New York	<b>8</b>	-
Other	<b>7</b>	15
Total	\$ <b>30</b>	\$ 32

#### DEPRECIATION AND AMORTIZATION

Depreciation in the fourth quarter of 2004 was \$31 million compared to \$15 million for the same period in 2003. The increase is due to the assets acquired or put into service in 2003 and 2004 and the write-off of some transmission assets resulting from the transmission reinforcement project.

#### NON-CONTROLLING INTERESTS

Non-controlling interests consists of the allocation of income associated with the non-controlling interests in the Company's consolidated entities. The decrease by \$10 million in the fourth quarter of 2004 is related to lower net income for the Fund in the fourth quarter resulting from below average hydrology conditions.

#### PROVISION FOR INCOME TAXES

The provision for taxes decreased to \$23 million in 2004 compared with \$27 million in 2003. The decrease in the provision for taxes is primarily related to provisions for federal and provincial income taxes on lower taxable income in the fourth quarter of 2004.

#### CONSOLIDATED QUARTERLY RESULTS

Variations in quarterly results are correlated with the amount of electricity generated in any given quarter, which is in turn dependent on available water inflows. Other marketing and asset enhancement initiatives also impact the quarterly results.

CDN \$ <i>millions (except otherwise noted)</i>	<b>2004</b>				2003			
	<i>Q4</i>	<i>Q3</i>	<i>Q2</i>	<i>Q1</i>	<i>Q4</i>	<i>Q3</i>	<i>Q2</i>	<i>Q1</i>
Power generated (GWh)	<b>2,125</b>	<b>1,647</b>	<b>1,986</b>	<b>2,048</b>	1,793	1,492	1,589	1,363
Power revenues	<b>183</b>	<b>154</b>	<b>170</b>	<b>180</b>	142	126	106	74
Net operating income	<b>75</b>	<b>70</b>	<b>84</b>	<b>98</b>	68	47	61	42
Net income	<b>11</b>	<b>36</b>	<b>35</b>	<b>52</b>	19	24	31	23
Diluted income per share	<b>(0.11)</b>	<b>0.24</b>	<b>0.28</b>	<b>0.41</b>	0.15	0.19	0.24	0.19

## **ANNUAL INFORMATION FORM**

The Company prepares an Annual Information Form which can be accessed on SEDAR at [www.sedar.com](http://www.sedar.com).

## **CERTIFICATION OF INTERIM FILINGS**

Form 52-109F1 – Certification of Annual Filings is attached to this document.

## **FORWARD-LOOKING STATEMENTS**

The Company's financial analysis and review contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The words "believe", "expect", "anticipate", "intend", "estimate" and other expressions which are predictions of or indicate future events and trends and which do not relate to historical matters identify forward-looking statements. Reliance should not be placed on forward-looking statements because they involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance or achievements of the Company to differ materially from anticipated future results, performance or achievements expressed or implied by such forward-looking statements. Factors that could cause actual results to differ materially from those set forth in the forward-looking statements include general economic conditions, weather conditions, interest rates, availability of equity and debt financing and other risks. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

A handwritten signature in black ink, appearing to be 'Donald Tremblay', written over a horizontal line.

Donald Tremblay  
Senior Vice President and Chief Financial Officer  
February 16<sup>th</sup>, 2004