

Hydro One announces third quarter net income

Toronto, October 28, 2004 - Hydro One Inc. today released its third quarter results with net income of \$312 million and revenues of \$3,079 million for the nine months ended September 30, 2004.

Net income increased by \$40 million, or 43%, in the third quarter and decreased by \$5 million, or 2%, in the first nine months compared to 2003 results. The increase in quarterly net income primarily reflects lower operations, maintenance and administration costs. These costs were lower due to the reassignment of resources to support a larger capital work program. Results for the quarter also reflect a one-time impact of recognizing a regulatory asset related to distribution pension costs that were expensed during the first two quarters of 2004. For the nine-month period, the impact of lower operations, maintenance and administration costs was more than offset by higher depreciation charges, consistent with the investments made in our electricity delivery system, and lower transmission revenues. Capital expenditures of \$538 million for the first nine months of 2004 increased by \$156 million, or 41%, compared to 2003 levels, primarily due to projects to expand and reinforce the electricity system. These projects address the impact of growing loads and the closure of the Lakeview Generating Station on the electricity network and increase the performance and capability of the distribution system.

For the nine months to September 30, 2004, total revenues increased by \$30 million, or 1%, compared to last year, primarily due to higher distribution revenues from the recovery of increased purchased power costs, partially offset by lower transmission revenues reflecting milder winter and cooler spring temperatures. Net cash from operations was \$748 million for the first nine months of 2004. During this period, the Company paid \$203 million in dividends to the Government of Ontario and invested \$538 million in capital expenditures, primarily in the transmission and distribution systems.

“Our record of consistent financial performance is, in large part, due to a highly-skilled, experienced and dedicated workforce who maintain and optimize the performance of Ontario’s electricity system. However, sometimes it takes an unfortunate situation like the recent hurricane damage in Florida to truly appreciate their dedication and expertise”, said Tom Parkinson, President and Chief Executive Officer of Hydro One. “Almost 500 of our workers volunteered to go to Florida, at the request and expense of Florida Power & Light, to assist in the restoration of their electricity system. We have received numerous messages from Florida residents thanking the Hydro One line crews for their extraordinary efforts in such trying circumstances. These workers are indicative of the dedication and expertise that our customers rely on daily.”

RECENT DEVELOPMENTS

- The Ontario Energy Board (OEB) has initiated a process to establish rates for electricity distributors reflecting updated revenue requirements based on cost-of-service, with the intent that these new distribution rates will be effective on May 1, 2006.
- Effective April 1, 2004, interim rates have been in place allowing us to commence recovery of certain regulatory assets in the amount of approximately \$160 million over four years. A decision by the OEB with respect to recoverability of these regulatory assets is anticipated by year-end.

CONSOLIDATED FINANCIAL HIGHLIGHTS AND STATISTICS

<i>(Canadian dollars in millions) (except as otherwise noted)</i>	Three months ended September 30		Nine months ended September 30	
	2004	2003	2004	2003
Revenues	1,018	949	3,079	3,049
Purchased power	470	409	1,465	1,409
Operating costs	279	318	913	910
Net income	133	93	312	317
Net cash from operations	264	355	748	857
Transmission – units transmitted (TWh) ¹	37.9	37.2	114.6	113.8
Distribution – units distributed (TWh) ¹	6.6	6.4	21.2	20.7
Average Ontario 60-minute peak demand (MW) ¹	23,015	22,589	22,403	22,557

¹ System-related statistics are preliminary

Hydro One Inc. is a holding company that operates through its subsidiaries in the electricity transmission and distribution and telecom businesses. One of its subsidiaries, Hydro One Networks Inc., operates one of the largest transmission and distribution systems in North America. Hydro One Inc. is wholly owned by the Ontario government.

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HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS

RESULTS OF OPERATIONS

As used in this section, references to increases and decreases, whether in terms of amounts or percentages, are made by comparison of the three and nine months ended September 30, 2004 to the three and nine months ended September 30, 2003.

Revenues

<i>(Canadian dollars in millions)</i>	Three months ended September 30				Nine months ended September 30			
	2004	2003	\$ Change	% Change	2004	2003	\$ Change	% Change
Transmission	327	325	2	1	945	983	(38)	(4)
Distribution	687	619	68	11	2,122	2,046	76	4
Other	4	5	(1)	(20)	12	20	(8)	(40)
	1,018	949	69	7	3,079	3,049	30	1
Transmission - units transmitted (<i>TWh</i>) ¹	37.9	37.2	0.7	2	114.6	113.8	0.8	1
Distribution - units distributed (<i>TWh</i>) ¹	6.6	6.4	0.2	3	21.2	20.7	0.5	2
Average Ontario 60-minute peak demand (<i>MW</i>) ¹	23,015	22,589	426	2	22,403	22,557	(154)	(1)

¹ System-related statistics are preliminary

The demand for electricity generally follows normal weather-related variations and therefore, our energy-related revenues tend to be higher in the first and third quarters than in the second and fourth quarters.

Transmission revenues consist predominantly of our transmission tariff, which is based on the monthly peak demand for electricity across our high-voltage network. The level of peak demand is primarily influenced by weather conditions. The average peak demand was higher in both July and September, but lower in August, resulting in marginally higher transmission tariff revenues in the quarter compared to 2003. On a year-to-date basis, the average peak demand was lower in all but four months of this year, reflecting milder winter and cooler spring temperatures. As a result, our transmission tariff revenues were lower than last year for the same period. Ancillary transmission revenues were also lower this year during the first nine months compared to last year.

Distribution revenues include our distribution tariff, which is based on Ontario Energy Board (OEB) approved rates, recovery of the cost of purchased power used by our customers, and ancillary distribution services revenue. Accordingly, distribution revenues are primarily influenced by our distribution rates, the amount of electricity we distribute, and the cost of purchased power.

Distribution revenues increased in the third quarter and in the first nine months of 2004 compared to the same periods last year, primarily due to the recovery of higher purchased power costs of \$61 million and \$56 million, respectively. These increased recoveries primarily reflect the implementation of the interim pricing structure on April 1, 2004, partially offset in the year-to-date period by a lower average Hourly Ontario Energy Price (HOEP) as described below under "Purchased Power". The remaining increase in both periods relates principally to marginally higher distribution tariff revenues from increased electricity consumption and higher ancillary revenues, partially offset by the deferral of revenues related to the interim recovery of certain regulatory assets, pending a decision by the OEB on the prudence of the related expenditures.

Other revenue decreased both in the third quarter and on a year-to-date basis compared to 2003 results, primarily due to lower sales of dark fibre partially offset by increased sales in other areas of our telecommunications business.

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Purchased Power

Purchased power costs incurred by our distribution business represent the cost of electricity delivered to customers within our distribution service area and consist of the wholesale commodity cost of energy, the Independent Electricity Market Operator's (IMO) wholesale market service charges, and transmission charges levied by the IMO. For certain low volume and designated customers, the wholesale commodity price of energy had been fixed at 4.3 cents per kWh. On April 1, 2004, this fixed price was replaced by an interim pricing structure of 4.7 cents per kWh for the first 750 kWhs consumed per month and 5.5 cents per kWh for any additional consumption. Customers who are not eligible for the interim pricing structure pay the wholesale commodity price of energy, which is based on the HOEP established by the IMO spot market.

Purchased power costs increased by \$61 million, or 15%, to \$470 million in the third quarter and by \$56 million, or 4%, to \$1,465 million in the nine-month period as compared to last year. These increases primarily reflect higher commodity prices of \$45 million and \$39 million, respectively, which were largely attributable to the implementation of the interim pricing structure. While the average monthly weighted-average HOEP for the quarter was essentially unchanged from the same period last year at 4.82 cents per kWh, it declined by 0.74 cents per kWh to 5.18 cents per kWh over the nine-month period, partially offsetting the impact of the implementation of the interim pricing structure on a year-to-date basis. The remaining increase in purchased power costs for both the quarter and year-to-date periods reflects higher energy consumption.

Operation, Maintenance and Administration

Our operation, maintenance and administration costs are comprised primarily of labour, material, equipment and purchased services in support of the transmission and distribution systems. These costs also include property taxes and payments in lieu thereof on our transmission and distribution lines, stations and buildings.

As a result of an actuarial valuation filed with the Financial Services Commission of Ontario on September 22, 2004, we are required to contribute approximately \$80 million to our pension plan in each year over the period 2004 through to 2006. Such pension contribution costs are attributed to labour and are charged to operation, maintenance and administration expense or are capitalized as part of the cost of fixed assets. In response to our pension application, which was filed on June 1, 2004, the OEB issued an order on July 14, 2004 approving the establishment of a regulatory deferral account to record the expensed portion of distribution-related pension contributions, as well as interest thereon. Given the OEB's order, we have determined that it is appropriate to recognize as a regulatory asset approximately \$16 million of distribution pension costs previously charged to operation, maintenance and administration expense during the first two quarters of 2004. In addition, ongoing distribution-related pension contributions that, in the absence of the OEB order, would be charged to operation, maintenance and administration, will also be recorded in the regulatory asset account.

Operation, maintenance and administration costs for each of our three business segments were as follows:

	Three months ended September 30				Nine months ended September 30			
	2004	2003	Change	%	2004	2003	Change	%
<i>(Canadian dollars in millions)</i>								
Transmission	79	99	(20)	(20)	267	288	(21)	(7)
Distribution	77	101	(24)	(24)	287	282	5	2
Other	6	5	1	20	16	19	(3)	(16)
	162	205	(43)	(21)	570	589	(19)	(3)

Transmission operation, maintenance and administration expenditures necessary to sustain our high-voltage system were lower by \$20 million in the third quarter and by \$21 million for the first nine months compared to the same periods last year. On both a quarterly and year-to-date basis, these reductions were primarily attributable to the reassignment of resources to support the larger transmission capital work program. During both the quarter and the year-to-date periods, the impact of these reductions was partially offset by the impact of the funding requirements for our pension plan and our higher planned and corrective maintenance expenditures to ensure the continued reliability of our transmission stations. During the quarter, we also incurred lower information management costs than last year, primarily related to infrastructure and software applications.

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MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Distribution operation, maintenance and administration costs declined by \$24 million in the third quarter compared to 2003, primarily as a result of the one-time impact of recognizing a regulatory asset related to distribution pension costs that were expensed during the first two quarters of 2004. Operation, maintenance and administration costs increased by \$5 million in the first nine months compared to the same period last year, reflecting increased forestry expenditures. The enhanced level of tree and brush clearing on our rights of way will allow us to maintain reliability and reduce vegetation-caused power outages on our system. We have also experienced higher customer care costs, necessary to implement the Government's electricity policy, and higher costs related to higher ancillary revenues. These increases were partially offset by the impact of the reassignment of resources to support a larger capital work program.

Other operation, maintenance and administration costs were reasonably consistent with the comparative periods and primarily reflect costs associated with fibre-optic cable and reduced sales of dark fibre.

Depreciation and Amortization

Depreciation and amortization expense increased by \$4 million, or 4%, to \$117 million in the third quarter and by \$22 million, or 7%, to \$343 million in the first nine months from the same periods last year. These increases primarily result from higher depreciation charges associated with our fixed assets in service, consistent with the investments made in our electricity delivery network. These overall increases were partially offset by a reduction, effective April 1, 2004, in amortization expense charged on certain regulatory assets pending a decision by the OEB on the prudence of the related expenditures.

Financing Charges

Financing charges decreased by \$5 million, or 6%, to \$81 million in the third quarter and by \$11 million, or 4%, to \$249 million in the first nine months compared to the respective periods last year. For the quarter, the reduction reflects the refinancing of our debt at lower average interest rates compared to the effective rates on the maturing debt, as well as the impact of lower average levels of debt outstanding in 2004 than in the comparative period. For the year-to-date period, the reduction is largely attributable to lower average interest rates compared to 2003.

Provision for Payments in Lieu of Corporate Income Taxes

The provision for payments in lieu of corporate income taxes increased by \$12 million, or 28%, to \$55 million in the third quarter compared to the same period last year, reflecting a proportionate increase in the level of income before taxes. Over the first nine months, compared to 2003, corporate income taxes decreased by \$13 million, or 8%, to \$140 million. This decrease is associated with lower year-to-date income before taxes, as well as the impact of a reduction in the statutory tax rate from 36.62% to 36.12%.

Net Income

Net income increased by \$40 million, or 43%, to \$133 million in the third quarter and decreased by \$5 million, or 2%, to \$312 million in the first nine months compared to last year. These results primarily reflect the impact of lower operations, maintenance and administration costs. While core work program expenditures were higher, our operations, maintenance and administration costs reflect the impact of the reassignment of resources to support a larger capital work program. Results for the quarter also reflect the one-time impact of recognizing a regulatory asset related to distribution pension costs that were expensed during the first two quarters of 2004. For the nine-month period, the impact of lower operations, maintenance and administration costs was more than offset by higher depreciation charges consistent with the investments made in our electricity delivery system and lower transmission revenues.

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth unaudited quarterly information for each of the eight quarters ended December 31, 2002 through September 30, 2004. This information has been derived from our unaudited interim Consolidated Financial Statements which, in the opinion of our management, have been prepared on a basis consistent with the audited annual Consolidated Financial Statements and which include all adjustments, consisting only of normal recurring adjustments,

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

necessary for fair presentation of our financial position and results of operations for those periods. These operating results are not necessarily indicative of results for any future period and should not be relied upon to predict our future performance.

<i>(Canadian dollars in millions)</i>	2004				2003			2002
Quarter ended	Sep. 30	Jun. 30¹	Mar. 31¹	Dec. 31	Sep. 30	Jun. 30	Mar. 31	Dec. 31
Total revenue	1,018	960	1,101	1,009	949	953	1,147	999
Net income	133	59	120	79	93	85	139	27
Net income to common shareholder	129	55	115	75	88	81	134	23

¹ Both the revenue and net income amounts reported in the first and second quarters of 2004 have been reduced by \$5 million and \$6 million, respectively, to reflect a change in interperiod allocations.

The demand for electricity generally follows normal weather-related variations and, therefore, our energy-related revenues and net income, all other things being equal, tend to be higher in the first and third quarters than in the second and fourth quarters.

LIQUIDITY AND CAPITAL RESOURCES

Our primary sources of liquidity and capital resources are funds generated from operations, debt capital market borrowings and bank financing. These sources will be used to satisfy our capital resource requirements, which continue to include capital expenditures, servicing and repayment of our debt, and payments related to our outsourcing arrangements, investing activities, and dividends.

Summary of Sources and Uses of Cash

<i>(Canadian dollars in millions)</i>	Three months ended September 30		Nine months ended September 30	
	2004	2003	2004	2003
Operating activities	264	355	748	857
Investing activities				
Capital expenditures	(193)	(148)	(538)	(382)
Financing activities				
Long-term debt issued	130	-	500	1,250
Long-term debt retired	-	-	(472)	(651)
Short-term notes payable	(142)	(285)	(25)	(579)
Dividends paid	(61)	(59)	(203)	(184)
Other investing and financing activities	(1)	4	14	8
Net change in cash and cash equivalents	(3)	(133)	24	319

Operating Activities

Net cash generated from operations was lower by \$91 million in the third quarter and was lower by \$109 million in the first nine months compared to 2003 results. These reductions primarily reflect higher working capital requirements. Weather-driven revenue variances, changing market prices and the introduction of the interim pricing structure affected our accounts receivable and accounts payable balances. Other factors, such as the timing of installment payments for corporate taxes and the \$55 million pension plan funding contribution made in September, contributed to the changes in working capital. These increases in our working capital requirements were partially offset by increased net income in the quarter and by increased adjustments not requiring cash resources, such as depreciation expense.

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Investing Activities

Cash used for investing activities primarily represents capital expenditures for each of our three business segments as follows:

	Three months ended September 30				Nine months ended September 30			
	2004	2003	\$ Change	% Change	2004	2003	\$ Change	% Change
<i>(Canadian dollars in millions)</i>								
Transmission	123	66	57	86	321	178	143	80
Distribution	69	80	(11)	(14)	212	194	18	9
Other	1	2	(1)	(50)	5	10	(5)	(50)
	193	148	45	30	538	382	156	41

Transmission capital expenditures increased by \$57 million in the third quarter and by \$143 million on a year-to-date basis compared to the same periods last year. Capital expenditures to expand and reinforce our transmission system increased by \$65 million in the quarter and by \$135 million in the first nine months. These expansion and reinforcement projects will primarily address growing loads and the closure of the Lakeview Generating Station, and include the new Parkway transformer station. We also incurred marginally higher capital expenditures to ensure the reliability of our existing transmission stations, lines and equipment and to support our transmission operations. These increases were more than offset in the quarter and partially offset on a year-to-date basis by a combination of lower spending on transport and work equipment and the substantial completion of our integrated operating facility, the Ontario Grid Control Centre. This facility was placed in service early in the third quarter and is expected to achieve cost efficiencies, improve customer response and provide advanced monitoring and analysis capabilities. The funding requirements associated with our pension plan also contributed to the overall increases in our capital expenditures.

Distribution capital expenditures decreased by \$11 million this quarter and increased by \$18 million on a year-to-date basis compared to the same periods in 2003. Expenditures to enhance our distribution system to accommodate increased loads, improve performance and mitigate risks increased by \$9 million in the quarter and by \$35 million in the first nine months compared to 2003. These increased expenditures reflect the effects of the OEB's Distribution System Code, which has resulted in our company funding a greater proportion of customer-shared new connection and system upgrade costs than last year. We also experienced marginal increases in storm and trouble call work and we incurred increased expenditures to replace existing distribution station components compared to last year. In the quarter, these increases were more than offset, and for the first nine months were partially offset, by reduced capital work on our distribution lines and reduced spending on transport and work equipment. The funding requirements associated with our pension plan also contributed to the year-over-year increase in our capital expenditures for the year-to-date period.

Other capital expenditures decreased by \$1 million in the third quarter and by \$5 million in the first nine months compared to 2003. These reductions reflect the completion of our fibre-optic network last year. The 2004 capital program reflects ongoing equipment upgrades commensurate with demand.

Financing Activities

Short-term liquidity is provided through funds from operations and our commercial paper program, under which we are able to issue up to \$750 million in short-term notes with a term to maturity of less than 365 days. This program is supported by a committed revolving credit facility with a syndicate of banks. Following our August 13, 2004 amendment of our credit agreement, primarily to cancel a \$250 million 5-year facility, this facility amounts to \$750 million. At September 30, 2004, we had no short-term notes outstanding. The available short-term liquidity under this program and anticipated levels of funding from operations should be sufficient to fund our normal operating requirements. Long-term financing is provided by our access to the debt markets, including through our medium-term note program. After considering our two debt issues in August 2004, we have approximately a \$1 billion principal amount issuable and available until July 2005 under this program. Our notes and debentures mature between 2005 and 2043. We currently plan to refinance maturing debt principally through our medium-term note program.

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Rating Agency	Rating	
	Short-term Debt	Long-term Debt
Standard & Poor's Rating Services Inc.	A-2	A
Dominion Bond Rating Service Inc.	R-1 (low)	A
Moody's Investor Services Inc.	Prime-1	A2

During the third quarter of 2004, we issued \$130 million in long-term debt under our medium-term note program and we repaid all of the \$142 million in short-term notes outstanding at June 30, 2004. In comparison, during the third quarter of 2003, we reduced our short-term notes payable by \$285 million, while no long-term debt was issued or retired. On a year-to-date basis, we issued \$500 million and retired \$472 million in long-term debt compared to issuances of \$1,250 million and retirements of \$651 million in 2003. Year-to-date reductions in short-term notes totaled \$25 million compared to reductions of \$579 million last year.

In the third quarter of 2004, we paid dividends to the Government of Ontario in the amount of \$61 million, consisting of \$57 million in common dividends and \$4 million in preferred dividends. In the comparative period, we paid common dividends of \$55 million and preferred dividends of \$4 million. Year-to-date, we have paid common and preferred dividends totaling \$203 million, compared to \$184 million in 2003.

Summary of Contractual Obligations and Other Commercial Commitments

The following table presents a summary of our debt and other major contractual obligations as well as other major commercial commitments.

September 30, 2004

(Canadian dollars in millions)	Total	2004 ¹	2005/2006	2007/2008	After 2008
Contractual Obligations (due by year):					
Short-term notes payable	-	-	-	-	-
Long-term debt	5,192	-	1,237	855	3,100
Operating lease commitments	20	2	9	6	3
Inergi LP outsourcing agreement	739	28	212	204	295
Total Contractual Obligations	5,951	30	1,458	1,065	3,398
Other Commercial Commitments (by year of expiry)					
Bank line ²	750	-	750	-	-
Letters of credit ³	90	72	18	-	-
Guarantees ³	275	275	-	-	-
Pension ⁴	188	26	162	-	-
Total Other Commercial Commitments	1,303	373	930	-	-

¹ The amounts disclosed represent the balances due over the period October 1, 2004 to December 31, 2004.

² As a backstop to our commercial paper program, we have a \$750 million, 364-day revolving standby credit facility with a syndicate of banks maturing in August 2005 with a two-year term out option. On August 13, 2004, we amended our credit agreement primarily to cancel a \$250 million 5-year facility.

³ We currently have bank letters of credit of \$69 million outstanding relating to retirement compensation arrangements. We have also provided prudential support to the IMO as required by the Market Rules, using a combination of bank letters of credit of \$16 million and parental guarantees of \$275 million. The amount of prudential support that we provide in the form of bank letters of credit to the IMO is dependent on our long-term credit ratings from major Canadian and U.S. rating agencies. The amount of bank letters of credit provided would need to increase if our credit ratings deteriorated. The remaining letters of credit pertain to operating letters of credit and to surety bonds.

⁴ Contributions after 2006 will be based on an actuarial valuation as at December 31, 2006 and will depend on future investment returns, changes in benefits or actuarial assumptions. Should financial market conditions improve significantly before December 31, 2006, we have the option to file an earlier actuarial valuation.

The amounts in the above table under short-term notes payable and long-term debt are not charged to our results of operations, but are reflected on our balance sheet and statement of cash flows. Interest associated with this debt is recorded under financing charges on our statement of operations or within our capital expenditures, but these financing charges are not reflected in the above table. Payments in respect of operating leases and our outsourcing agreement with Inergi LP are recorded under operation, maintenance and administration costs on our statement of operations or within our capital expenditures.

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

RECENT DEVELOPMENTS

2006 Electricity Distribution Rates

The OEB has initiated a process to establish rates for electricity distributors reflecting updated revenue requirements based on cost-of-service, with the intent that these new distribution rates will be effective on May 1, 2006. We anticipate that electricity distributors will be required to file individual applications in mid-2005 for May 1, 2006 implementation. The OEB has commenced a policy development process to develop generic guidelines for the rate-setting methodology. Generic guidelines will be developed by working groups established by the OEB staff. We will be an active participant in this process.

Phase II of Regulatory Assets Recovery Proceeding

Effective April 1, 2004, interim rates have been in place allowing us to commence recovery of certain regulatory assets in the amount of approximately \$160 million over four years. However, as directed by the OEB, amounts collected have since been accumulated in a regulatory liability account, pending the outcome of their prudence review, which commenced on September 13, 2004. A decision by the OEB with respect to recoverability of these regulatory assets is anticipated by year-end.

Electricity Distribution Licence

On September 29, 2004, the OEB renewed our electricity distribution licence, which is now valid until September 28, 2024. The distribution licence authorizes us to own and operate a distribution system in specified service areas, and to retail electricity and act as a wholesaler, as specifically permitted under the *Electricity Act, 1998*. Our transmission licence was previously renewed on December 3, 2003 and is valid until December 2, 2023.

Bill 100, Electricity Restructuring Act

On June 15, 2004, the Minister of Energy introduced Bill 100 to amend the *Electricity Act, 1998* and the *Ontario Energy Board Act, 1998*. Its focus is on the structure of the electricity industry, introducing a new Ontario Power Authority, a new Conservation Bureau and redefining the role of the IMO. Measures have been proposed to address the long-term supply of electricity, encourage electricity conservation and renewable energy and facilitate electricity demand management. We are continuing to assess the impact of the proposed legislation as further information becomes available, but expect the proposals to have minor implications for our regulated businesses. Additionally, we anticipate transmission and distribution to be reviewed by the Minister of Energy later this year.

SELECTED FINANCIAL HIGHLIGHTS AND RATIOS

<i>(Canadian dollars in millions) (except as otherwise noted)</i>	Three months ended		Nine months ended	
	September 30		September 30	
	2004	2003	2004	2003
Net income	133	93	312	317
Net cash from operations	264	355	748	857
Capital expenditures	193	148	538	382
Earnings per common share <i>(Canadian dollars)</i>	1,289	890	2,989	3,039
Earnings coverage ratio ¹			2.42	2.27
Net asset coverage on long-term debt ²			1.86	1.86
Total debt to capitalization ³			54%	54%

¹The earnings coverage ratio has been presented for the twelve months ended September 30, 2004 and September 30, 2003, respectively and has been calculated as the sum of net income, provision for payments in lieu of corporate income taxes and financing charges divided by the sum of financing charges, capitalized interest and cumulative preferred dividends.

²The net asset coverage on long-term debt ratio has been presented as at September 30, 2004 and December 31, 2003 and has been calculated as total assets minus total liabilities excluding long-term debt (including current portion) divided by long-term debt including current portion.

³Total debt to capitalization ratio has been presented as at September 30, 2004 and December 31, 2003 and has been calculated as total debt divided by total debt plus total shareholder's equity.

HYDRO ONE INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

FORWARD LOOKING STATEMENTS AND INFORMATION

We have included forward looking statements in this report that are subject to risks, uncertainties and assumptions. Such information represents our current views based on information as at the date of this report. We do not intend to update this information and disclaim any legal obligation to the contrary.

This management's discussion and analysis is dated as at October 28, 2004. Additional information about our company, including our annual information form, is available on SEDAR at www.sedar.com.

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

<i>(Canadian dollars in millions)</i>	Three months ended		Nine months ended	
	September 30		September 30	
	2004	2003	2004	2003
Revenues				
Transmission	327	325	945	983
Distribution	687	619	2,122	2,046
Other	4	5	12	20
	1,018	949	3,079	3,049
Costs				
Purchased power	470	409	1,465	1,409
Operation, maintenance and administration <i>(Note 2)</i>	162	205	570	589
Depreciation and amortization	117	113	343	321
	749	727	2,378	2,319
Income before financing charges and provision for payments in lieu of corporate income taxes	269	222	701	730
Financing charges	81	86	249	260
Income before provision for payments in lieu of corporate income taxes	188	136	452	470
Provision for payments in lieu of corporate income taxes	55	43	140	153
Net income	133	93	312	317
Basic and fully diluted earnings per common share (Canadian dollars)	1,289	890	2,989	3,039

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (unaudited)

<i>(Canadian dollars in millions)</i>	Three months ended		Nine months ended	
	September 30		September 30	
	2004	2003	2004	2003
Retained earnings, beginning of period	691	601	654	502
Net income	133	93	312	317
Dividends <i>(Note 3)</i>	(61)	(59)	(203)	(184)
Retained earnings, end of period	763	635	763	635

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED BALANCE SHEETS

<i>(Canadian dollars in millions)</i>	September 30, 2004	December 31, 2003
	(unaudited)	
Assets		
Current assets		
Accounts receivable (net of allowance for doubtful accounts)	631	616
Materials and supplies	48	45
	679	661
Fixed assets		
Fixed assets in service	14,694	14,362
Less: accumulated depreciation	5,403	5,175
	9,291	9,187
Construction in progress	435	278
	9,726	9,465
Other long-term assets		
Deferred pension asset	546	584
Regulatory assets (Note 2)	389	421
Goodwill	133	133
Long-term accounts receivable and other assets	15	20
Deferred debt costs	23	22
	1,106	1,180
Total assets	11,511	11,306
Liabilities		
Current liabilities		
Bank indebtedness	13	37
Accounts payable and accrued charges	578	620
Accrued interest	96	38
Short-term notes payable	-	25
Long-term debt payable within one year	200	472
	887	1,192
Long-term debt (Note 4)	4,897	4,539
Other long-term liabilities		
Regulatory liabilities	584	584
Employee future benefits other than pension (Note 5)	640	597
Environmental liabilities	62	69
Long-term accounts payable and accrued charges	41	34
	1,327	1,284
Total liabilities	7,111	7,015
Shareholder's equity		
Preferred shares (authorized: unlimited; issued: 12,920,000)	323	323
Common shares (authorized: unlimited; issued: 100,000)	3,314	3,314
Retained earnings	763	654
Total shareholder's equity	4,400	4,291
Total liabilities and shareholder's equity	11,511	11,306

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

<i>(Canadian dollars in millions)</i>	Three months ended		Nine months ended	
	September 30		September 30	
	2004	2003	2004	2003
Operating activities				
Net income	133	93	312	317
Adjustments for non-cash items:				
Depreciation and amortization (net of removal costs)	109	104	317	297
Amortization of discount	15	17	48	42
Retail settlement variance accounts	4	3	20	17
	261	217	697	673
Changes in non-cash balances related to operations	3	138	51	184
Net cash from operations	264	355	748	857
Investing activities				
Fixed assets	(193)	(148)	(538)	(382)
Other assets	(10)	4	7	25
Net cash used in investing activities	(203)	(144)	(531)	(357)
Financing activities				
Long-term debt issued	130	-	500	1,250
Long-term debt retired	-	-	(472)	(651)
Termination of forward sale	-	-	-	(12)
Short-term notes payable	(142)	(285)	(25)	(579)
Dividends paid	(61)	(59)	(203)	(184)
Other	9	-	7	(5)
Net cash used in financing activities	(64)	(344)	(193)	(181)
Net change in cash and cash equivalents	(3)	(133)	24	319
Cash and cash equivalents, beginning of period	(10)	417	(37)	(35)
Cash and cash equivalents, end of period	(13)	284	(13)	284

See accompanying notes to Consolidated Financial Statements.

HYDRO ONE INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1. BASIS OF PRESENTATION

The Consolidated Financial Statements of Hydro One Inc. (Hydro One or the Company) which are presented herein have been prepared in accordance with the accounting policies described in the Consolidated Financial Statements for the years ended December 31, 2003 and December 31, 2002, and should be read in conjunction with those financial statements.

In the opinion of management, the unaudited interim Consolidated Financial Statements reflect all of the adjustments, which consist only of normal and recurring adjustments, necessary to present fairly the financial position as at September 30, 2004 and the results of operations and cash flows for the three and nine months ended September 30, 2004 and 2003.

2. OPERATION, MAINTENANCE AND ADMINISTRATION

In response to the Company's pension application which was filed on June 1, 2004, the Ontario Energy Board (OEB) issued an order on July 14, 2004 approving the establishment of a regulatory deferral account to record Distribution-related pension contributions, as well as interest thereon. The OEB noted in its decision that it would not rule on the prudence of these costs at this time, but that prudently incurred costs of this type are normally recoverable as part of a general rate adjustment application. Given the OEB's order, the Company has determined that it is appropriate to recognize approximately \$16 million of distribution pension costs that were previously expensed during the first two quarters of 2004, as a regulatory asset. In addition, ongoing Distribution-related pension contributions that, in the absence of the OEB order, would be charged to operation, maintenance and administration expense, will also be recorded in the regulatory asset account.

3. DIVIDENDS

During the three months ended September 30, 2004, preferred dividends in the amount of \$4 million (2003 - \$4 million) and common dividends in the amount of \$57 million (2003 - \$55 million) were declared. During the nine months ended September 30, 2004, preferred dividends in the amount of \$13 million (2003 - \$13 million) and common dividends in the amount of \$190 million (2003 - \$171 million) were declared.

4. LONG-TERM DEBT

During the nine months ended September 30, 2004, Hydro One issued the following notes under its medium term note program:

Date of Issuance	Principal Amount <i>(Canadian dollars in millions)</i>	Coupon Rate <i>(Per cent)</i>	Maturity Date
February 19, 2004	250	3.95	February 24, 2009
June 22, 2004	120	6.35	January 31, 2034
August 17, 2004	65	6.59	April 22, 2043
August 19, 2004	65	6.35	January 31, 2034

HYDRO ONE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (continued)

5. EMPLOYEE FUTURE BENEFITS

Employee future benefits provided by Hydro One include pension, group life insurance, health care, workers' compensation and long-term disability.

Total benefit costs are as follows:

<i>(Canadian dollars in millions)</i>	Three months ended September 30		Nine months ended September 30	
	2004	2003	2004	2003
Pension				
Net period benefit costs ¹	16	-	70	-
Less: Portion attributable to labour and capitalized as part of the cost of fixed assets	6	-	29	-
Portion attributable to regulatory assets <i>(Note 2)</i>	5	-	21 ²	-
Charged to results of operations	5	-	20	-
Employee Future Benefits Other than Pension				
Net period benefit cost	25	23	72	67
Less: Portion attributable to labour and capitalized as part of fixed assets	9	9	27	27
Charged to results of operations	16	14	45	40

¹ In accordance with the OEB's rate orders, Hydro One recognizes pension costs in the year contributions are paid to the pension fund. No contributions were paid in 2002.

² The regulatory asset pertaining to pension was \$25 million as at September 30, 2004 (2003 - \$nil) as an additional \$4 million (2003 - \$nil) has been recorded relating to pension costs associated with former Hydro One employees.

6. SEGMENTED REPORTING

Hydro One has three reportable segments:

- I. The transmission business, which comprises the core business of providing transportation and connection services, is responsible for transmitting electricity throughout the Ontario electricity grid;
- II. The distribution business, which comprises the core business of delivering and selling electricity to customers; and
- III. The "other" segment, which primarily consists of telecommunications.

The designation of segments is based on a combination of regulatory status and the nature of the products and services provided. Segment information on the above basis is as follows:

<i>Three months ended September 30 (Canadian dollars in millions)</i>	Transmission	Distribution	Other	Consolidated
2004				
Segment profit				
Revenues	327	687	4	1,018
Purchased power	-	470	-	470
Operation, maintenance and administration	79	77	6	162
Depreciation and amortization	63	53	1	117
Income (loss) before financing charges and provision for payments in lieu of corporate income taxes	185	87	(3)	269
Financing charges				81
Income before provision for payments in lieu of corporate income taxes				188
Capital expenditures	123	69	1	193

HYDRO ONE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (continued)

<i>Three months ended September 30 (Canadian dollars in millions)</i>	Transmission	Distribution	Other	Consolidated
2003				
Segment profit				
Revenues	325	619	5	949
Purchased power	-	409	-	409
Operation, maintenance and administration	99	101	5	205
Depreciation and amortization	58	54	1	113
Income (loss) before financing charges and provision for payments in lieu of corporate income taxes	168	55	(1)	222
Financing charges				86
Income before provision for payments in lieu of corporate income taxes				136
Capital expenditures	66	80	2	148

Nine months ended September 30 (Canadian dollars in millions)

2004				
Segment profit				
Revenues	945	2,122	12	3,079
Purchased power	-	1,465	-	1,465
Operation, maintenance and administration	267	287	16	570
Depreciation and amortization	178	162	3	343
Income (loss) before financing charges and provision for payments in lieu of corporate income taxes	500	208	(7)	701
Financing charges				249
Income before provision for payments in lieu of corporate income taxes				452
Capital expenditures	321	212	5	538

2003

Segment profit				
Revenues	983	2,046	20	3,049
Purchased power	-	1,409	-	1,409
Operation, maintenance and administration	288	282	19	589
Depreciation and amortization	166	153	2	321
Income (loss) before financing charges and provision for payments in lieu of corporate income taxes	529	202	(1)	730
Financing charges				260
Income before provision for payments in lieu of corporate income taxes				470
Capital expenditures	178	194	10	382

(Canadian dollars in millions)

	September 30, 2004	December 31, 2003
Total assets		
Transmission	6,708	6,589
Distribution	4,708	4,623
Other	95	94
	11,511	11,306

All revenues, costs and assets, as the case may be, are earned, incurred or held in Canada.

7. COMPARATIVE FIGURES

The comparative Consolidated Financial Statements have been reclassified from statements previously presented to conform to the presentation of the September 30, 2004 Consolidated Financial Statements.