



Quarterly Report

Second Quarter 2019

Message from the Chair of the Board and the President and Chief Executive Officer

Second quarter

Hydro-Québec posted **net income** of \$264 million for the second quarter of 2019, compared to \$623 million in the same period last year.

It is worth remembering that, in June 2018, the company recorded a \$277-million gain on the sale of an equity interest in its subsidiary TM4. Excluding this non-recurring item, net income for the second quarter of 2019 decreased by \$82 million compared to the corresponding period in 2018.

The difference is due to two main factors. First, Hydro-Québec recognized a \$46-million charge in 2019 resulting from the writeoff of certain costs related to the Northern Pass Transmission (NPT) project. This project, which involved the construction of a transmission line in New Hampshire to export electricity to Massachusetts, was permanently shelved by the company's U.S. partner. Instead, Massachusetts chose another Hydro-Québec project, New England Clean Energy Connect (NECEC), which runs through Maine.

Second, Hydro-Québec Production's net electricity exports decreased by \$59 million, mainly because of lower demand on export markets due to temperature variances.

Summary of results for the first six months

For the six months ended June 30, 2019, Hydro-Québec recorded **net income** of \$2,038 million, or \$229 million less than the \$2,267 million posted a year earlier. Excluding the non-recurring gain related to the partial sale of TM4, net income for the first six months was \$48 million higher than in 2018. This is the second consecutive year that net income has exceeded the \$2-billion mark for the first half of the year. It is also worth noting that, through careful management, the company was able to lower its operational expenditure by \$18 million.

On the Québec market, electricity supplies provided by Hydro-Québec Production to Hydro-Québec Distribution increased by \$119 million compared to the same period in 2018. This growth is due to higher baseload demand across all customer segments as well as the impact of temperatures, which were colder in winter 2019 than in the previous winter.

On markets outside Québec, Hydro-Québec Production's net electricity exports decreased by \$30 million to \$805 million, primarily because demand was lower on export markets during the second quarter as a result of temperature variances. Net export volume therefore totaled 16.4 TWh for the first six months of 2019, or 2.3 TWh less than the record set in 2018. It has nonetheless remained above 16 TWh for a third consecutive year. The impact of the volume decrease was mitigated by an increase in the average price obtained, mainly on account of the positive impact of the company's risk management strategy.

Overall, greater needs in Québec propelled Hydro-Québec's net sales volume across all its markets to a historic high for the first six months, namely 109.5 TWh, an increase of 0.7 TWh over the previous record, set in 2015.

Consolidated results for the first six months

Revenue totaled \$7,572 million, compared to \$7,798 million in the first half of 2018. Revenue from ordinary activities was \$7,597 million, an increase of \$225 million resulting from a \$280-million rise in electricity sales. In Québec, these amounted to \$6,693 million, or \$353 million more than in 2018, partly on account of temperature variances, which led to an increase of 2.2 TWh or \$183 million, as well as higher baseload demand across all customer segments. Revenue from electricity sales on markets outside Québec was \$831 million, compared to \$904 million a year earlier. Revenue from other activities decreased by \$451 million, mainly because of the impact of the recognition, in 2018, of the non-recurring gain related to the partial sale of TM4.

Total expenditure amounted to \$4,207 million, compared to \$4,219 million in the same period in 2018. This \$12-million decrease is partly the result of careful management and tight control of operational expenditure, which made it possible to completely absorb the higher costs related to inflation and salary indexing.

Financial expenses totaled \$1,327 million in 2019, which is comparable to the \$1,312 million recorded a year earlier.

Segmented results for the first six months

Generation

Hydro-Québec Production posted net income of \$1,281 million, a \$95-million increase compared to \$1,186 million in the first half of 2018. Electricity supplies provided to Hydro-Québec Distribution rose by \$119 million because of the higher volume of electricity sales in Québec. Net electricity exports decreased by \$30 million, primarily on account of the 2.3-TWh reduction in volume.

Transmission

Hydro-Québec TransÉnergie's net income was \$342 million, comparable to the \$345 million posted in the first six months of 2018.

Distribution

Hydro-Québec Distribution recorded net income of \$442 million, compared to \$475 million in the same period in 2018. On the one hand, revenue grew by \$137 million over last year. This growth is largely due to an increase in revenue from electricity sales in Québec, which itself is the result of colder temperatures in winter 2019 and higher baseload demand across all customer segments. On the other hand, electricity purchases and the related transmission costs increased by \$205 million. More specifically, supplies from Hydro-Québec Production rose by \$119 million, while electricity purchases from third parties rose by \$55 million, essentially because of an increase in wind power purchases. Depreciation and amortization expense decreased by \$47 million.

Construction

The Construction segment includes activities related to the design and execution of construction and refurbishment projects involving power generation and transmission facilities, essentially for Hydro-Québec Production and Hydro-Québec TransÉnergie. These projects are carried out by Hydro-Québec Innovation, équipement et services partagés and by Société d'énergie de la Baie James (SEBJ).

The volume of activity in this segment totaled \$878 million, compared to \$858 million a year earlier. Projects under way for Hydro-Québec Production include ongoing construction of the Romaine hydroelectric complex and the refurbishment of various structures at Robert-Bourassa generating station. Work in progress for Hydro-Québec TransÉnergie includes numerous projects stemming from continued investment in asset reliability and sustainment. In addition, Hydro-Québec Innovation, équipement et services partagés completed the 735-kV Chamouchouane–Bout-de-l'Île project in the second quarter of 2019.

Investment

During the first six months of 2019, Hydro-Québec invested \$1,513 million in property, plant and equipment and intangible assets, compared to \$1,509 million in the same period last year.

A large part of Hydro-Québec Production's investments was allotted to ongoing work at the Romaine-4 jobsite, in the Minganie region. At the same time, the division continued investing to ensure the long-term operability of its facilities and optimize their output. For instance, refurbishment is under way at Robert-Bourassa and Beauharnois generating stations.

Hydro-Québec TransÉnergie allocated part of its investments to erecting transmission lines, in particular 420 km of lines to connect Chamouchouane substation, in the Saguenay–Lac-Saint-Jean region, to the Montréal metropolitan loop as part of the 735-kV Chamouchouane–Bout-de-l'Île project. This project will allow the division to meet growing demand in southern Québec while ensuring the reliability of the entire grid. The facilities, most of which were commissioned during the second quarter, were inaugurated in July 2019. In addition, the division continued work to bring the Romaine complex onto the grid and to build Patriotes substation in the Basses-Laurentides region. It also pursued upgrading and modernization projects to ensure the reliability and long-term operability of its assets and enhance service quality. Some examples of this include replacing the transmission grid control and special protection systems, as well as ongoing work on the architecture development plan for the 315-kV system on the island of Montréal.

Hydro-Québec Distribution made further investments to better meet customer needs, including connecting the Côte-Nord communities of La Romaine and Unamen Shipu, currently served by an off-grid system. The division is also pursuing projects to maintain and improve the quality of its facilities, such as replacing the distribution grid control systems.

Financing

During the second quarter, Hydro-Québec made two fixed-rate bond issues on the Canadian capital market, at an average cost of 2.68%. These bonds, which will mature in 2055, raised \$1.3 billion.

Since the beginning of 2019, financing activities have generated \$1.9 billion. The proceeds were used to support part of the investment program and to refinance maturing debt.

Jacynthe Côté

Chair of the Board

August 27, 2019

Éric Martel

**President and
Chief Executive Officer**

CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

CONSOLIDATED STATEMENTS OF OPERATIONS

In millions of Canadian dollars (unaudited)		Three months ended June 30		Six months ended June 30	
	Notes	2019	2018	2019	2018
Revenue	11	2,932	3,291	7,572	7,798
Expenditure					
Operations		702	705	1,396	1,414
Other components of employee future benefit cost	8	(140)	(85)	(279)	(170)
Electricity and fuel purchases		505	496	1,192	1,122
Depreciation and amortization	4	686	654	1,323	1,304
Taxes		250	244	575	549
		2,003	2,014	4,207	4,219
Income before financial expenses		929	1,277	3,365	3,579
Financial expenses	5	665	654	1,327	1,312
Net income		264	623	2,038	2,267

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

In millions of Canadian dollars (unaudited)		Three months ended June 30		Six months ended June 30	
	Notes	2019	2018	2019	2018
Net income		264	623	2,038	2,267
Other comprehensive income	9				
Net change in items designated as cash flow hedges	6	157	(120)	25	70
Net change in employee future benefits		11	29	23	59
Translation differences in financial statements of foreign operations		–	1	(1)	2
		168	(90)	47	131
Comprehensive income		432	533	2,085	2,398

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

In millions of Canadian dollars (unaudited)	Notes	As at June 30, 2019	As at December 31, 2018
ASSETS			
Current assets			
Cash and cash equivalents		4,526	1,335
Short-term investments		1,737	884
Accounts receivable and other receivables		2,498	2,713
Derivative instruments	6	119	72
Regulatory assets		276	203
Materials, fuel and supplies		269	264
		9,425	5,471
Property, plant and equipment		65,224	64,966
Intangible assets		889	877
Investments		1,031	1,022
Derivative instruments	6	35	121
Regulatory assets		3,773	3,863
Other assets		887	669
		81,264	76,989
LIABILITIES			
Current liabilities			
Borrowings		3,764	8
Accounts payable and accrued liabilities		2,151	2,135
Dividend payable		–	2,394
Accrued interest		918	914
Asset retirement obligations		65	62
Derivative instruments	6	36	80
Regulatory liabilities		511	80
Current portion of long-term debt	6	2,273	3,151
		9,718	8,824
Long-term debt	6	44,562	42,910
Asset retirement obligations		812	811
Derivative instruments	6	6	28
Regulatory liabilities		410	714
Other liabilities		2,189	2,219
Perpetual debt	6	263	274
		57,960	55,780
EQUITY			
Share capital		4,374	4,374
Retained earnings		20,789	18,741
Accumulated other comprehensive income	9	(1,859)	(1,906)
		23,304	21,209
		81,264	76,989
Contingencies	10		

The accompanying notes are an integral part of the consolidated financial statements.

On behalf of the Board of Directors,

/s/ Geneviève Brouillette
Chair of the Audit Committee

/s/ Jacynthe Côté
Chair of the Board

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

In millions of Canadian dollars
(unaudited)

Six months ended
June 30

	Notes	Share capital	Retained earnings	Accumulated other comprehensive income	Total equity
Balance as at December 31, 2018		4,374	18,741	(1,906)	21,209
Adjustments related to a change in accounting policy	2	–	10	–	10
Net income		–	2,038	–	2,038
Other comprehensive income	9	–	–	47	47
Balance as at June 30, 2019		4,374	20,789	(1,859)	23,304
Balance as at December 31, 2017		4,374	17,972	(2,591)	19,755
Adjustments related to a change in accounting policy		–	(29)	(2)	(31)
Net income		–	2,267	–	2,267
Other comprehensive income	9	–	–	131	131
Balance as at June 30, 2018		4,374	20,210	(2,462)	22,122

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

In millions of Canadian dollars (unaudited)		Three months ended June 30		Six months ended June 30	
	Notes	2019	2018	2019	2018
Operating activities					
Net income		264	623	2,038	2,267
Adjustments to determine net cash flows from operating activities					
Depreciation and amortization	4	686	654	1,323	1,304
Amortization of premiums, discounts and issue expenses related to debt securities		51	49	104	99
Deficit of net cost recognized with respect to amounts paid for employee future benefits		(111)	(45)	(223)	(87)
Gain on partial sale of a subsidiary		–	(277)	–	(277)
Other		128	105	109	106
Regulatory assets and liabilities		(49)	(133)	6	(201)
Change in non-cash working capital items	7	1,365	1,062	110	(268)
		2,334	2,038	3,467	2,943
Investing activities					
Additions to property, plant and equipment		(919)	(786)	(1,449)	(1,459)
Additions to intangible assets		(28)	(26)	(64)	(50)
Partial sale of a subsidiary, net of cash transferred		–	160	–	160
Net change in short-term investments and sinking fund		(825)	(316)	(834)	294
Other		2	7	4	12
		(1,770)	(961)	(2,343)	(1,043)
Financing activities					
Issuance of long-term debt		1,284	(23)	1,771	590
Repayment of long-term debt		(577)	(13)	(1,062)	(43)
Cash receipts arising from credit risk management		704	967	1,474	1,932
Cash payments arising from credit risk management		(761)	(776)	(1,539)	(1,686)
Net change in borrowings		74	(180)	3,818	1,441
Dividend paid		–	–	(2,394)	(2,135)
Other		–	1	10	11
		724	(24)	2,078	110
Foreign currency effect on cash and cash equivalents		(9)	1	(11)	8
Net change in cash and cash equivalents		1,279	1,054	3,191	2,018
Cash and cash equivalents, beginning of period		3,247	1,501	1,335	537
Cash and cash equivalents, end of period		4,526	2,555	4,526	2,555
Supplementary cash flow information	7				

The accompanying notes are an integral part of the consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

For the three- and six-month periods ended June 30, 2019 and 2018

Amounts in tables are in millions of Canadian dollars, unless otherwise indicated.

Note 1 Basis of Presentation

Hydro-Québec's consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP").

These quarterly consolidated financial statements, including these notes, do not contain all the required information regarding annual consolidated financial statements and should therefore be read in conjunction with the consolidated financial statements and accompanying notes in Hydro-Québec's *Annual Report 2018*.

The accounting policies used to prepare the quarterly consolidated financial statements are consistent with those presented in Hydro-Québec's *Annual Report 2018*, except for the recent changes as presented in Note 2, Changes to Accounting Policies.

Management is of the opinion that these quarterly consolidated financial statements present fairly, in all material respects, the consolidated financial position of Hydro-Québec.

Hydro-Québec's quarterly results are not necessarily indicative of results for the year on account of seasonal temperature fluctuations. Because of higher electricity demand during winter months, revenue from electricity sales in Québec is higher during the first and fourth quarters.

Management has reviewed events occurring until August 27, 2019, the date of approval of these quarterly consolidated financial statements by the Board of Directors, to determine whether circumstances warranted consideration of events subsequent to the balance sheet date.

Note 2 Changes to Accounting Policies

RECENT CHANGES

Leases

On January 1, 2019, Hydro-Québec adopted Accounting Standards Codification ("ASC") 842, *Leases*, issued by the Financial Accounting Standards Board (the "FASB") to replace ASC 840, *Leases*. The new standard provides guidance on lease definition, recognition, measurement, presentation and disclosure, and requires, in particular, the recognition of assets and liabilities by lessees for all operating and finance leases with a term of more than 12 months.

ASC 842 was applied on a modified retrospective basis to leases in effect on January 1, 2019. Hydro-Québec opted for the transition method allowing the cumulative effect of initially applying ASC 842 to be recognized as an adjustment to the opening balance of retained earnings as at the adoption date of the standard, without restatement of comparative data. It also applied the three practical expedients to not reassess the existence and classification of leases, nor the treatment of capitalized initial direct costs, as well as the practical expedient to not evaluate easement agreements that were not previously accounted for as leases. As at January 1, 2019, the adoption of ASC 842 led to the recognition of operating lease assets and liabilities on the balance sheet, which translated into an increase of \$200 million in other assets, of \$27 million in accounts payable and accrued liabilities, and of \$173 million in other liabilities. It also led to a \$10-million decrease in regulatory liabilities and a \$10-million increase in retained earnings, corresponding to the reversal of a deferred gain on a sale and leaseback transaction, as required by the ASC 842 transitional provisions.

STANDARDS ISSUED BUT NOT YET ADOPTED

Financial instruments

In June 2016, the FASB issued Accounting Standards Update ("ASU") 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. This ASU provides new guidance on the impairment of financial assets that are not accounted for at fair value through net income. It will be applied on a modified retrospective basis to the financial statements for interim and annual periods beginning on or after January 1, 2021. Hydro-Québec is currently examining the impact of this ASU on its consolidated financial statements.

Note 3 Regulation

DISTRIBUTION

In decisions D-2019-027 of March 5, 2019, and D-2019-037 of March 22, 2019, the Régie de l'énergie (the "Régie") authorized an increase of 0.9% in all Hydro-Québec electricity rates except Rate L, for which the increase was set at 0.3%. The new rates are effective as of April 1, 2019. The authorized return on the rate base was set at 7.13%, assuming a capitalization with 35% equity.

The Régie also allowed the Distributor to reduce the amortization period to two years for revenue variances related to climate conditions.

In addition, the Régie approved the amortization terms and conditions related to the variance account for the \$18-million total gain from the disposal of a property in a sale and leaseback transaction in 2018, which was recognized as a regulatory liability as at December 31, 2018. More specifically, it authorized the Distributor to include in its 2019–2020 rates an amount of \$8 million for the gain realized on the disposal of the property, and to recognize a \$10-million deferred gain in retained earnings as at January 1, 2019, in accordance with the ASC 842 transitional provisions for sale and leaseback transactions.

Lastly, the Régie authorized the Distributor to create a non-rate-base, interest-bearing variance account to record the impact of the 2018 revision of the useful life of overhead transformers, and to include the total \$31-million credit balance of this account in its 2019–2020 rates.

TRANSMISSION

In decisions D-2019-047 of April 12, 2019, and D-2019-058 of May 14, 2019, the Régie set Hydro-Québec's power transmission rates for 2019. The authorized return on the rate base was set at 7.05%, assuming a capitalization with 30% equity.

PROJECT INVOLVING THE REPLACEMENT OF POWER GRID CONTROL SYSTEMS

In decision D-2019-042 of April 2, 2019, the Régie authorized the Transmission Provider and the Distributor to each create a provisional, non-rate-base, interest-bearing variance account to record certain costs incurred during the draft designs for replacing power transmission and distribution grid control systems. As at June 30, 2019, no amount had been recognized in this account by the Transmission Provider or the Distributor.

Note 4 Depreciation and Amortization

	Three months ended June 30		Six months ended June 30	
	2019	2018	2019	2018
Property, plant and equipment	583	581	1,164	1,156
Intangible assets	26	27	51	60
Regulatory assets and liabilities	30	41	59	83
Retirement of capital assets	47	5	49	5
	686	654	1,323	1,304

Note 5 Financial Expenses

	Three months ended June 30		Six months ended June 30	
	2019	2018	2019	2018
Interest on debt securities	682	666	1,354	1,320
Net exchange loss (gain)	4	(4)	7	(6)
Guarantee fees related to debt securities ^a	55	53	110	107
	741	715	1,471	1,421
Less				
Capitalized financial expenses	46	44	89	79
Net investment income	30	17	55	30
	76	61	144	109
	665	654	1,327	1,312

a) Guarantee fees related to debt securities are charged at a rate of 0.5% and are paid to the Québec government.

Note 6 Financial Instruments

In the course of its operations, Hydro-Québec carries out transactions that expose it to certain financial risks, such as market, liquidity and credit risk. Exposure to such risks and the impact on results are reduced through careful monitoring and implementation of strategies that include the use of derivative instruments.

MARKET RISK

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market prices. Hydro-Québec is exposed to three main types of market risk: currency risk, interest rate risk and risk associated with energy and aluminum prices. Active integrated management of these three types of risk aims to limit exposure to each risk and reduce their overall impact on results.

MANAGEMENT OF LONG-TERM RISK

Management of risk associated with debt

Currency risk and interest rate risk – Hydro-Québec uses forward contracts and currency swaps to manage the currency risk associated with long-term debt and perpetual debt, as well as forward contracts and interest rate swaps to modify long-term exposure to interest rate risk. When designated as hedging items, these derivative instruments are recognized as cash flow hedges or fair value hedges, depending on the risk hedged. The impact on results of foreign currency hedging transactions and those associated with debt interest rates is recognized in Financial expenses.

The following table shows the notional amounts, expressed in Canadian dollars and foreign currencies, of forward contracts and swaps used to manage long-term risk:

	As at June 30, 2019 ^a	As at December 31, 2018 ^a
Forward contracts		
Canadian dollars	(1,350)	(1,000)
U.S. dollars	204	204
Swaps		
Canadian dollars	(6,917)	(6,844)
U.S. dollars	5,730	5,730

a) Figures in parentheses represent amounts to be paid.

Note 6 Financial Instruments (continued)

MANAGEMENT OF SHORT-TERM RISK

Currency risk – Hydro-Québec uses forward contracts to manage its foreign currency risk exposure over the short term. When designated as hedging items, these derivative instruments are recognized as cash flow hedges. The impact of currency risk hedging transactions on results is recognized in the line items affected by the hedged item, namely Revenue, Electricity and fuel purchases, or Financial expenses. In this context, Hydro-Québec has traded foreign currency sales and purchase contracts for which open positions as at June 30, 2019, totaled a notional amount of US\$1,226 million and US\$2,861 million, respectively (US\$1,800 million for sales contracts and nil for purchase contracts as at December 31, 2018).

Interest rate risk – Hydro-Québec uses forward contracts and interest rate swaps to manage short-term interest rate risk. When designated as hedging items, these derivative instruments are recognized as cash flow hedges. The impact on results of transactions to hedge short-term interest rate risk is recognized in the line item affected by the hedged item, namely Financial expenses.

Price risk – Hydro-Québec uses mainly commodity futures and swaps to manage risk resulting from fluctuations in energy and aluminum prices. When designated as hedging items, these derivative instruments are recognized as cash flow hedges. The impact on results of transactions to hedge the risk related to energy and aluminum prices is recognized in the line items affected by the hedged item, namely Revenue or Electricity and fuel purchases. In this context, Hydro-Québec has traded electricity futures and swaps for which open positions as at June 30, 2019, totaled 24.4 TWh (23.2 TWh as at December 31, 2018), natural gas futures for which open positions as at June 30, 2019, totaled 1.0 million MMBtu (0.4 million MMBtu as at December 31, 2018), petroleum product swaps for which open positions as at June 30, 2019, totaled 4.3 million litres (9.1 million litres as at December 31, 2018), as well as aluminum swaps for which open positions as at June 30, 2019, totaled 100,900 tonnes (240,825 tonnes as at December 31, 2018).

FAIR VALUE

FAIR VALUE OF DERIVATIVE INSTRUMENTS

The following tables present the fair value of derivative instruments by type and depending on whether they are designated as fair value hedges or cash flow hedges, or not designated as hedges:

	As at June 30, 2019			
	Derivatives designated as fair value hedges	Derivatives designated as cash flow hedges	Derivatives not designated as hedges ^a	Gross amounts of derivatives recognized ^b
Assets				
Contracts – Currency risk	–	1,052	9	1,061
Contracts – Interest rate risk	484	–	–	484
Contracts – Price risk	–	150	92	242
	484	1,202	101	1,787
Liabilities				
Contracts – Currency risk	–	(142)	(288)	(430)
Contracts – Interest rate risk	–	(76)	–	(76)
Contracts – Price risk	–	(7)	(22)	(29)
	–	(225)	(310)	(535)
Total	484	977	(209)	1,252

Note 6 Financial Instruments (continued)

	As at December 31, 2018			
	Derivatives designated as fair value hedges	Derivatives designated as cash flow hedges	Derivatives not designated as hedges ^a	Gross amounts of derivatives recognized ^b
Assets				
Contracts – Currency risk	–	1,280	14	1,294
Contracts – Interest rate risk	372	2	–	374
Contracts – Price risk	–	159	49	208
	372	1,441	63	1,876
Liabilities				
Contracts – Currency risk	–	(162)	(116)	(278)
Contracts – Interest rate risk	–	(55)	–	(55)
Contracts – Price risk	–	(104)	(13)	(117)
	–	(321)	(129)	(450)
Total	372	1,120	(66)	1,426

a) These derivative instruments are mainly traded as part of Hydro-Québec's risk management. As at June 30, 2019, \$(189) million was in consideration of amounts received or disbursed [\$116 million as at December 31, 2018] with respect to agreements to limit the market value of the main portfolios of derivative instruments. These agreements arise from frameworks applied by Hydro-Québec to reduce its credit risk exposure and limit risk concentration.

b) Fair value measurements of derivative instruments are Level 2 measurements. These measurements are obtained by discounting future cash flows, which are estimated on the basis of the spot rates, forward rates or forward prices (foreign exchange rates, interest rates, and energy or aluminum prices) in effect on the balance sheet date and take into account the credit risk assessment. The valuation techniques make use of observable market data.

The impact of offsetting derivative instruments is presented in the table below:

	As at June 30, 2019				As at December 31, 2018			
	Gross amounts of derivatives recognized	Gross amounts offset ^a	Cash (received) paid as collateral ^b	Net amounts presented on the balance sheet	Gross amounts of derivatives recognized	Gross amounts offset ^a	Cash (received) paid as collateral ^b	Net amounts presented on the balance sheet
Assets								
Current	233	(77)	(37)	119	217	(97)	(48)	72
Long-term	1,554	(383)	(1,136)	35	1,659	(215)	(1,323)	121
	1,787	(460)	(1,173)	154	1,876	(312)	(1,371)	193
Liabilities								
Current	(391)	322	33	(36)	(350)	240	30	(80)
Long-term	(144)	138	–	(6)	(100)	72	–	(28)
	(535)	460	33	(42)	(450)	312	30	(108)
Total	1,252	–	(1,140)	112	1,426	–	(1,341)	85

a) The gross amounts of derivatives offset are related to contracts traded according to International Swaps and Derivatives Association ("ISDA") guidelines and constituting enforceable master netting arrangements. Such master netting arrangements apply to all derivative instrument contracts traded over the counter.

b) Cash amounts offset are amounts received or paid under collateral exchange agreements signed in compliance with ISDA guidelines.

Moreover, although certain derivatives cannot be offset for lack of enforceable master netting arrangements, margin calls may result in amounts received from or paid to clearing agents, based on the fair value of the instruments concerned. As at June 30, 2019, no amount receivable from clearing agents in consideration of net cash payments was included in Accounts receivable and other receivables (\$129 million as at December 31, 2018), while \$85 million payable to clearing agents in consideration of net cash receipts was included in Accounts payable and accrued liabilities (\$10 million as at December 31, 2018).

Note 6 Financial Instruments (continued)

The impact of derivative instruments on results and other comprehensive income is presented in the tables below. It should be noted that most derivative instruments traded are designated as cash flow hedges or fair value hedges and therefore reduce the volatility of results. Derivative instruments which are not designated as hedges, but which nonetheless provide an economic hedge for at-risk opposite positions, also reduce the volatility of results. The sensitivity of results is thus limited to net exposure to unhedged risks.

	Three months ended June 30, 2019			
	Losses (gains) on derivatives designated as fair value hedges	Losses (gains) on derivatives designated as cash flow hedges		Losses (gains) on derivatives not designated as hedges
	Recognized in results	Recognized in Other comprehensive income	Reclassified from Other comprehensive income to results	Recognized in results
Contracts – Currency risk	–	22	167 ^a	65
Contracts – Interest rate risk	(40)	79	1 ^b	–
Contracts – Price risk	–	(149)	(59) ^c	(30)
	(40)^{b, d}	(48)	109^d	35^{d, e}
Impact of hedged items on results	41		(109)	(75)

	Three months ended June 30, 2018			
	Losses (gains) on derivatives designated as fair value hedges	Losses (gains) on derivatives designated as cash flow hedges		Losses (gains) on derivatives not designated as hedges
	Recognized in results	Recognized in Other comprehensive income	Reclassified from Other comprehensive income to results	Recognized in results
Contracts – Currency risk	–	(123)	(137) ^a	(38)
Contracts – Interest rate risk	16	5	1 ^b	1
Contracts – Price risk	–	125	23 ^c	20
	16^{b, d}	7	(113)^d	(17)^{d, e}
Impact of hedged items on results	(15)		117	39

a) In 2019, \$15 million was recognized in Revenue (\$3 million in 2018), and \$152 million in Financial expenses [\$(140) million in 2018].

b) These amounts were recognized in Financial expenses.

c) These amounts were recognized in Revenue.

d) In 2019, the line items Revenue, Electricity and fuel purchases, and Financial expenses totaled \$2,932 million, \$505 million and \$665 million, respectively (\$3,291 million, \$496 million and \$654 million in 2018).

e) These instruments are essentially related to integrated risk management transactions. Their impact on results is recognized in the line items affected by the managed risk. Therefore, in 2019, \$(33) million was recognized in Revenue (\$31 million in 2018), \$1 million in Electricity and fuel purchases [\$(7) million in 2018], and \$67 million in Financial expenses [\$(41) million in 2018].

Note 6 Financial Instruments (continued)

	Six months ended June 30, 2019			
	Losses (gains) on derivatives designated as fair value hedges	Losses (gains) on derivatives designated as cash flow hedges		Losses (gains) on derivatives not designated as hedges
	Recognized in results	Recognized in Other comprehensive income	Reclassified from Other comprehensive income to results	Recognized in results
Contracts – Currency risk	–	237	334 ^a	60
Contracts – Interest rate risk	(113)	153	2 ^b	2
Contracts – Price risk	–	(225)	(146) ^c	(32)
	(113)^{b, d}	165	190^d	30^{d, e}
Impact of hedged items on results	115		(207)	(74)

	Six months ended June 30, 2018			
	Losses (gains) on derivatives designated as fair value hedges	Losses (gains) on derivatives designated as cash flow hedges		Losses (gains) on derivatives not designated as hedges
	Recognized in results	Recognized in Other comprehensive income	Reclassified from Other comprehensive income to results	Recognized in results
Contracts – Currency risk	–	(246)	(371) ^a	(92)
Contracts – Interest rate risk	38	23	2 ^b	2
Contracts – Price risk	–	(99)	117 ^c	–
	38^{b, d}	(322)	(252)^d	(90)^{d, e}
Impact of hedged items on results	(35)		263	92

a) In 2019, \$21 million was recognized in Revenue [\$(10) million in 2018], and \$313 million in Financial expenses [\$(361) million in 2018].

b) These amounts were recognized in Financial expenses.

c) These amounts were recognized in Revenue.

d) In 2019, the line items Revenue, Electricity and fuel purchases, and Financial expenses totaled \$7,572 million, \$1,192 million and \$1,327 million, respectively (\$7,798 million, \$1,122 million and \$1,312 million in 2018).

e) These instruments are essentially related to integrated risk management transactions. Their impact on results is recognized in the line items affected by the managed risk. Therefore, in 2019, \$(38) million was recognized in Revenue (\$16 million in 2018), \$4 million in Electricity and fuel purchases [\$(12) million in 2018], and \$64 million in Financial expenses [\$(94) million in 2018].

Note 6 Financial Instruments (continued)

During the first six months of 2019, Hydro-Québec reclassified a net gain of \$17 million from Accumulated other comprehensive income to results after having discontinued cash flow hedges (net loss of \$11 million for the first six months of 2018).

As at June 30, 2019, the net gain presented in Accumulated other comprehensive income that would be reclassified to results in the next 12 months was estimated at \$100 million (net loss of \$61 million as at June 30, 2018).

As at June 30, 2019 and 2018, the maximum period during which Hydro-Québec hedged its exposure to the variability of cash flows related to anticipated transactions was three years.

FAIR VALUE OF OTHER FINANCIAL INSTRUMENTS

Fair value measurements for other financial instruments are Level 2 measurements. Fair value is obtained by discounting future cash flows, based on rates observed on the balance sheet date for similar instruments traded on capital markets.

The fair value of cash equivalents, receivables – accounts receivable, other receivables and financial liabilities approximates their carrying amount because of the short-term nature of these financial instruments, except in the case of the items presented in the table below:

	As at June 30, 2019		As at December 31, 2018	
	Carrying amount	Fair value	Carrying amount	Fair value
Long-term debt ^a	46,835 ^b	65,776	46,061 ^b	59,876
Perpetual debt	263	248	274	252

a) Including the current portion.

b) Including an amount of \$1,999 million as at June 30, 2019 (\$2,000 million as at December 31, 2018) for debts subject to a fair value hedge, which resulted in an adjustment of \$462 million (\$350 million as at December 31, 2018) in connection with the hedged risk for existing hedging relationships and of \$(91) million [\$(94) million as at December 31, 2018] for discontinued relationships.

ACCOUNTS RECEIVABLE AND OTHER RECEIVABLES

As at June 30, 2019, accounts receivable and other receivables included \$1,922 million (\$2,124 million as at December 31, 2018) from contracts with customers, of which unbilled electricity deliveries totaled \$755 million (\$1,390 million as at December 31, 2018).

Note 7 Supplementary Cash Flow Information

	Three months ended June 30		Six months ended June 30	
	2019	2018	2019	2018
Change in non-cash working capital items				
Accounts receivable and other receivables	1,002	833	200	140
Materials, fuel and supplies	–	(1)	(5)	(12)
Accounts payable and accrued liabilities	(47)	(175)	(66)	(386)
Accrued interest	410	405	(19)	(10)
	1,365	1,062	110	(268)
Activities not affecting cash				
Increase in property, plant and equipment and intangible assets	16	15	29	32
Increase in operating lease assets and liabilities	1	–	24	–
	17	15	53	32
Interest paid	147	158	1,092	1,095

Note 8 Employee Future Benefits

	Three months ended June 30			
	Pension Plan		Other plans	
	2019	2018	2019	2018
Current service cost	108	126	11	12
Other components of employee future benefit cost				
Interest on obligations	226	209	13	13
Expected return on plan assets	(406)	(383)	–	(1)
Amortization of net actuarial loss	22	69	4	8
Amortization of past service costs (credits)	2	1	(1)	(1)
	(156)	(104)	16	19
Net (credit) cost recognized	(48)	22	27	31

	Six months ended June 30			
	Pension Plan		Other plans	
	2019	2018	2019	2018
Current service cost	215	252	22	24
Other components of employee future benefit cost				
Interest on obligations	453	418	26	26
Expected return on plan assets	(812)	(766)	(1)	(2)
Amortization of net actuarial loss	45	138	8	15
Amortization of past service costs (credits)	4	3	(2)	(2)
	(310)	(207)	31	37
Net (credit) cost recognized	(95)	45	53	61

Note 9 Accumulated Other Comprehensive Income

	Six months ended June 30, 2019			
	Cash flow hedges	Employee future benefits	Translation differences	Accumulated other comprehensive income
Balance as at December 31, 2018	(193)	(1,717)	4	(1,906)
Other comprehensive income before reclassifications	(165)	–	(1)	(166)
Amounts reclassified to results	190	23	–	213
Other comprehensive income	25	23 ^a	(1)	47
Balance as at June 30, 2019	(168)	(1,694)	3	(1,859)

	Six months ended June 30, 2018			
	Cash flow hedges	Employee future benefits	Translation differences	Accumulated other comprehensive income
Balance as at December 31, 2017	(406)	(2,186)	1	(2,591)
Adjustments related to the adoption of a change in accounting policy	(2)	–	–	(2)
	(408)	(2,186)	1	(2,593)
Other comprehensive income before reclassifications	322	–	2	324
Amounts reclassified to results	(252)	59	–	(193)
Other comprehensive income	70	59 ^a	2	131
Balance as at June 30, 2018	(338)	(2,127)	3	(2,462)

a) Other comprehensive income includes the change in the employee future benefit regulatory asset, which totaled \$(32) million as at June 30, 2019 [\$(95) million as at June 30, 2018].

Note 10 Contingencies

GUARANTEES

In accordance with the terms and conditions of certain debt securities issued outside Canada, Hydro-Québec has undertaken to increase the amount of interest paid to non-residents in the event of changes to Canadian tax legislation governing the taxation of non-residents' income. Hydro-Québec cannot estimate the maximum amount it might have to pay under such circumstances. Should an amount become payable, Hydro-Québec has the option of redeeming most of the securities in question. As at June 30, 2019, the amortized cost of the long-term debts concerned was \$3,304 million (\$3,314 million as at December 31, 2018).

LITIGATION

In the normal course of its development and operating activities, Hydro-Québec is sometimes party to claims and legal proceedings. Management is of the opinion that an adequate provision has been made for these legal actions. Consequently, it does not foresee any significant adverse effect of such contingent liabilities on Hydro-Québec's consolidated results or financial position.

Among other ongoing actions, some Indigenous communities have instituted proceedings against the governments of Canada and Québec, as well as against Hydro-Québec, based on demands concerning their ancestral rights. In particular, the Innus of Uashat mak Mani-Utenam are demanding \$1.5 billion in damages resulting from various activities carried out on land they claim as their own. Hydro-Québec is challenging the legitimacy of these claims.

As well, in November 2006, the Innus of Pessamit reactivated a case instituted in 1998 aimed at obtaining, among other things, the recognition of ancestral rights related to Québec lands on which certain hydroelectric generating facilities belonging to the Manic-Outardes complex are located. This community is claiming \$500 million. Hydro-Québec is challenging the legitimacy of this claim.

Note 11 Segmented Information

The following tables present information on segment results and assets:

	Three months ended June 30, 2019						
	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	342	21	2,567	–	2	–	2,932^a
Intersegment customers	1,040	836	21	546	466	(2,909)	–
Net income (loss)	245	150	(124)	–	(7)	–	264

	Three months ended June 30, 2018						
	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	391	40	2,566	–	294	–	3,291^a
Intersegment customers	1,008	844	20	517	463	(2,852)	–
Net income (loss)	282	168	(112)	–	285	–	623

a) Including \$(8) million from sources other than contracts with customers (\$313 million in 2018), of which \$(1) million relates to alternative revenue programs involving certain regulatory assets and liabilities [(13) million in 2018].

Note 11 Segmented Information (continued)

	Six months ended June 30, 2019						
	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	922	30	6,613	–	7	–	7,572^a
Intersegment customers	2,711	1,718	42	878	900	(6,249)	–
Net income (loss)	1,281	342	442	–	(27)	–	2,038
Total assets as at June 30, 2019	33,319	23,449	13,961	40	10,655	(160)	81,264

	Six months ended June 30, 2018						
	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	945	73	6,477	–	303	–	7,798^a
Intersegment customers	2,591	1,694	41	858	897	(6,081)	–
Net income	1,186	345	475	–	261	–	2,267
Total assets as at June 30, 2018	32,978	22,942	13,617	42	8,432	(157)	77,854

a) Including \$(25) million from sources other than contracts with customers (\$426 million in 2018), of which \$(11) million relates to alternative revenue programs involving certain regulatory assets and liabilities (\$28 million in 2018).

Note 12 Comparative Information

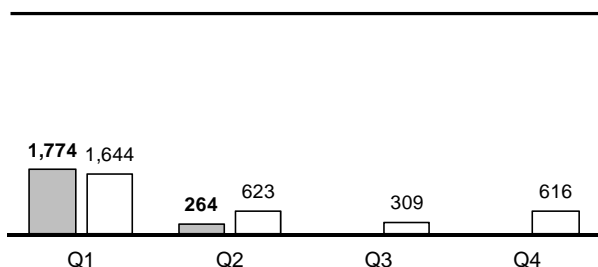
Some corresponding period data of the prior year have been reclassified to conform to the presentation adopted in the current periods.

CONSOLIDATED FINANCIAL HIGHLIGHTS (UNAUDITED)

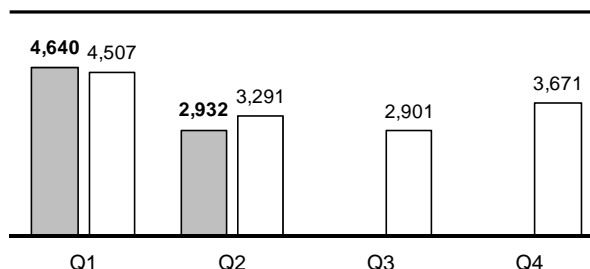
Amounts shown in tables are in millions of Canadian dollars.

Summary of Results	Three months ended June 30				Six months ended June 30			
	2019	2018	Change (%)		2019	2018	Change (%)	
Revenue	2,932	3,291	10.9	↓	7,572	7,798	2.9	↓
Expenditure	2,003	2,014	0.5	↓	4,207	4,219	0.3	↓
Financial expenses	665	654	1.7	↑	1,327	1,312	1.1	↑
Net income	264	623	57.6	↓	2,038	2,267	10.1	↓

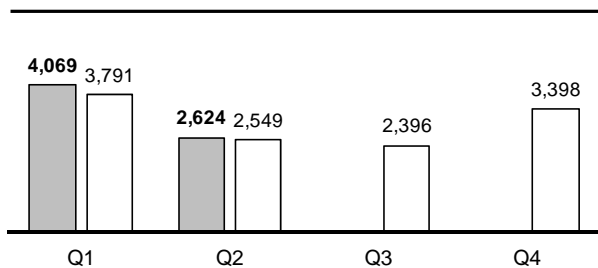
Net Income



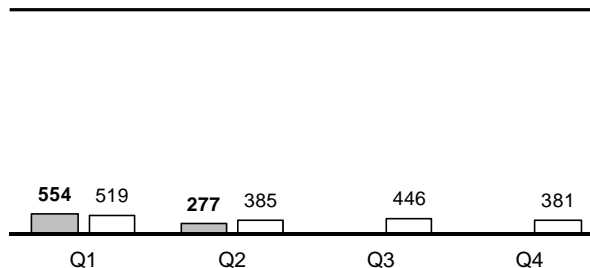
Revenue



Revenue from Electricity Sales in Québec



Revenue from Electricity Sales Outside Québec



■ 2019 □ 2018

