

Exhibit to Agenda Item #2

Discuss the monitoring report for Strategic Direction SD-3, Access to Credit Markets.

Board Policy Committee and Special SMUD Board of Directors Meeting

Wednesday, February 19, 2025, immediately following the Board Energy Resources & Customer Services Committee and Special SMUD Board of Directors meeting scheduled to begin at 6:00 p.m.

SMUD Headquarters Building, Auditorium

Strategic Direction SD-3

Access to Credit Markets

Maintaining access to credit markets is a core value of SMUD.

Therefore:

- For SMUD's annual budgets, the Board establishes a minimum target of cash coverage of all debt service payments (fixed charge ratio) of 1.50x
- When making resource decisions, SMUD shall weigh the impacts of long-term revenue requirements, debt, financial risk and flexibility
- SMUD's goal is to maintain at least an "A" rating with credit rating agencies

2024 Accomplishments

1. Credit ratings remain strong
 - “AA” by Fitch and Standard & Poor’s (“S&P”)
 - **Moody’s upgraded SMUD from Aa3 to Aa2 (AA equivalent)**
2. Fixed Charge Coverage ratio exceeded 1.50x minimum
 - 2.82x in 2024 and 2.60x in 2023
3. Successfully issued \$650 million in refunding and revenue bonds
 - \$628 million of which were green bonds
 - Refunded 2009 Series V bonds and 2010 Series W bonds with green refunding bonds
 - Refunded existing commercial paper with fixed rate green bonds and restored commercial paper capacity
 - Cash flow savings of \$24 million over 12 years
4. Successfully issued \$678 million in commodity prepay bonds
 - Refunded and extended the Northern California Energy Authority 2018 Series A commodity prepay bonds
 - Commodity cash-flow savings of \$34 million over 6 years
5. Successfully renewed property and casualty insurance coverage programs
 - Critical for financial recovery from major events like wildfire or a plant outage
 - Settled the final outstanding claim for the Consumnes Power Plant outage

Why Do Credit Ratings Matter?

- Higher credit ratings = lower borrowing cost
 - If SMUD's ratings were to fall from AA to A, the impact at today's rates would be approximately \$150k/yr. for every \$100 million borrowed.
 - ✓ Impact grows in higher rate environments or when credit is tight
- Enhances our position as strong counterparty
 - ✓ Lower cost for commodity procurement function
 - ✓ Reduced collateral posting
- Events over the past 5 years make access to credit and financial risk mitigation imperative
 - Cash on hand, commercial paper, and credit line provide liquidity
 - Business interruption insurance provides recovery from higher costs
 - ✓ Both support and enhance SMUD financial strength and our AA ratings

Credit Strengths and Concerns

➤ Credit Strengths:

- Strong financial liquidity
- Strong management planning and operation
- Proactive risk management and hedging practices
- Rate setting record
- Very competitive rates
- Diverse power supply with more than 60% carbon free in 2024

➤ Credit Concerns:

- Wildfire risk exposure given California's inverse condemnation laws
- We operate in complex and volatile California energy markets
- Increased capital forecast and heavier reliance on cash could put pressure on key metrics leading to higher borrowing

Recommendation

Staff recommends accepting the Strategic Direction-3 Report as evidence of compliance with Strategic Direction-3, Access to Credit Markets