Exhibit to Agenda Item #2

Board Policy Committee and Special SMUD Board of Directors Meeting
Wednesday, February 12, 2020, scheduled to begin at 5:30 p.m.
Auditorium, SMUD Headquarters Building
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 revenue coverage of all debt service payments (fixed charge ratio) of 1.50 times

• When making resource decisions, SMUD shall weigh the impacts on long-term revenue requirements, debt, financial risk and flexibility

• SMUD’s goal is to maintain at least an “A” rating with credit rating agencies
Evidence of Compliance

• Credit ratings remain very strong
  Aa3 Moody’s · AA S&P · AA Fitch

• Fixed Charge coverage exceeded minimum 1.50x target
  - 2.09 times 2019
  - 2.27 times 2018

• Increased the Commercial Paper program to $400 million providing flexibility

• Raised Days Cash on Hand target to 150 days to strengthen liquidity

• Defeased the remaining CVFA and SCA outstanding debt totaling $18 million one and two years early

• Successful $392 million Refunding and New Money Transaction:
  - Refunded all outstanding Commercial Paper
  - **Issued $75 million as SMUD’s 1st Green Bonds for HQ Renovation**
  - Locked in all in debt service costs of 1.81 percent
Why Do Credit Ratings Matter? The ABCs

Access to credit markets
• Ability to borrow and availability of Letters of Credit and other services with more competitive pricing and favorable terms

Borrowing Costs
• Stronger credit = lower interest rates
  • Our AA ratings provide meaningful savings to SMUD and its customers

Collateral Posting
• Commodity and interest rate hedging agreements receive better pricing, terms and conditions and collateral requirements supporting liquidity
Ratings Criteria and SMUD Report Card

- Financial Ratios/Metrics ✓ Positive
- Governance Structure ✓ Strong Positive
- Rate Competitiveness ✓ Strong Positive
- Resource Portfolio (cost) ✓ Neutral
- Risk Management ✓ Strong Positive
- Service Area (demographics) ✓ Neutral
- Regulatory Factors ✓ Negative
Credit Strengths

• Strong fixed charge coverage
• Very strong unrestricted cash reserves
• Governance structure - autonomous rate setting and no intra-government revenue transfers
• Management’s planning capability and measured approach to industry transition changes
• Proactive risk management practices
• Significant non-carbon resource portfolio and planned expansion
• Reduced reliance on debt for capital needs
• Diverse service territory, improving local economy
Credit Weaknesses / Concerns

• Legal and financial risk from Inverse Condemnation statute interpretation as it relates to potential wildfire liability (new in 2019)
• Increased capital forecast and heavier reliance on cash could put pressure on key metrics leading to higher borrowing
• Lower demand growth due to energy efficiency, distributed generation and potentially, battery storage
• Impact of state environmental energy policies
• Significant adjusted net pension liability obligation
• Commodity price risk
• Exposure to collateral posting requirements
Requested Action

It is recommended that the Board accept the Monitoring Report for SD-3, Access to Credit Markets.