Exhibit to Agenda Item #2
Accept the monitoring report for Strategic Direction SD-3, Access to Credit Markets.

Board Policy Committee and Special SMUD Board of Directors Meeting
Wednesday, February 9, 2022, scheduled to begin at 5:30 p.m.
Virtual Meeting (online)
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 1.50x
• 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
Evidence of Compliance

1. Credit ratings remains strong
   • “AA” Fitch – “Aa3” Moody’s – “AA” S&P

2. Fixed Charge Coverage ratio exceeded minimum 1.50x target
   • 2.42x in 2021 and 2.17x in 2020

3. Successfully issued $107 million in refunding bonds at 1.16% cost of funds
   • Refunded 2011 Series X bonds
   • Transaction resulted in $3 million annual savings through 2028
   • Total net present value savings of $23 million

4. Received strong offers to restructure $400 million Letter/Line of Credit Program
   • Lower fees than existing program will save SMUD $500k annually through 2025
   • Increases program liquidity adding $100 million emergency line of credit

5. Successfully renewed property and casualty insurance coverage programs
   • Maintained $800 million property program and $250 million wildfire program; and
   • Expanded cyber insurance program to $60 million, at or below market rates & within budgets
Why Do Credit Ratings Matter?

➢ Higher credit ratings translate into lower borrowing costs, which will be critical as the Federal Reserve enters a tightening cycle
  • If SMUD’s ratings were to fall from AA to A, the impact at today’s rates would be approximately $200k/yr. for every $100 million borrowed
    ✓ Impact grows in higher rate environments

➢ When credit markets freeze from events such as the 2007 Financial Crisis or Covid-19 in 2020, credit ratings matter
  • In March 2020, credit markets froze; SMUD was one of the first utilities able to enter the market because of our strong AA credit ratings
    ✓ Many “A” or lower rated utilities had to wait as investors were not lending to them
Credit Strengths

- Strong financial performance
- Governance structure – autonomous rate setting and no intra-government revenue transfers
- Proactive planning and hedging strategies
- Diverse resource portfolio
- Favorable debt and liabilities profile
- Strong wildfire mitigation program
- Diverse service territory, strong governmental presence
Credit Concerns

- Legal and financial risks from Inverse Condemnation statute interpretation as it relates to potential wildfire liability
- 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 potential for battery storage
- Prioritizing environmental goals or rate affordability over preservation of the financial profile
- Significant net pension liability obligation
Rating Criteria and SMUD Report Card

Financial Ratios: Positive
Governance Structure: Strong Positive
Rate Competitiveness: Strong Positive
Resource Portfolio (cost): Neutral
Risk Management Practices: Strong Positive
Service Area (demographics): Neutral
Regulatory Factors: Negative
Recommendation

Staff recommends accepting the SD-3 Report as evidence of compliance with Strategic Direction-3, Access to Credit Markets
Questions & Discussion?