



CONSTRUCTIVE PAY DOWN OF DEBT & OTHER FINANCE INITIATIVES

INTRODUCTION BY:

Cory Kuchinsky

Interim VP, Finance

PRESENTED BY:

Shannon R. Albert

Sr. Director, Capital Markets & Cash Mgmt.

November 12, 2018

Approval Requested

AGENDA

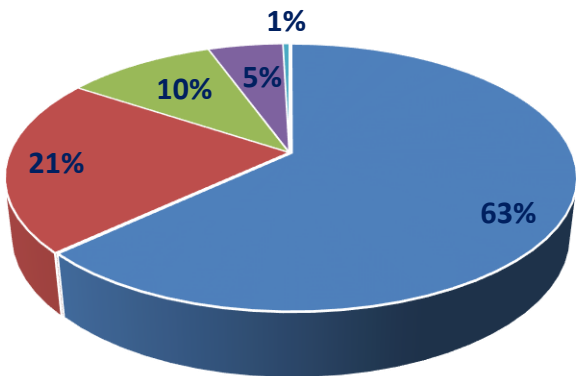


- **DEBT OVERVIEW**
- **UPCOMING OPPORTUNITIES**
 - **CONSTRUCTIVE PAY DOWN OF DEBT**
 - **FLEXIBLE RATE REVOLVING NOTE (FRRN) RENEWAL & INCREASE**
- **RECAP OF VOTING ITEMS**

DEBT OVERVIEW



Portfolio by Debt Type



<u>Debt Type</u>	<u>Par Outstanding ⁽¹⁾</u>	<u>% of Total</u>	
■ Sr. Lien Fixed	\$3,661,315	63.1%	} \$4.9B, 84% Fixed
■ Jr. Lien Fixed	1,233,545	21.2%	
<hr style="border-top: 1px dashed green;"/>			
■ Jr. Lien Variable Rate	590,115	10.2%	} \$900M, 16% Variable
■ Commercial Paper	295,000	5.1%	
■ Flex Rate Revolving Note	25,200	0.4%	
Total Portfolio	\$5,805,175	100%	

Note: Data as of August 1, 2018.
(1) \$s in thousands.

PREVIEW OF BOARD REQUESTS



Description	Required or Proposed	Estimated Amount	New \$	Existing \$	Anticipated Execution	CPS Energy Board Approval	City Council Approval	Commentary
Constructive Pay Down of Debt	Proposed	Up to \$130M	Up to \$130M		Dec. 2018 or Jan. 2019	Nov. 12, 2018	N/A	<ul style="list-style-type: none"> - Options to pay down existing Bonds or Commercial Paper or FRRN (or combination) - Effective use of cash - Improves metrics - Takes debt off balance sheet
Flex Rate Revolving Note (FRRN) Program	Proposed	\$100M	\$74.8M ⁽¹⁾	\$25.2M	Dec. 2018	Nov. 12, 2018	N/A	<ul style="list-style-type: none"> - Serves as back-up source of emergency liquidity - Improves liquidity metrics

(1) Current authorization of \$26M requesting increase to program limit of \$100M for future flexibility.

CONSTRUCTIVE PAY DOWN OF DEBT



- 1) Pay Down of Existing Bonds⁽¹⁾, or
- 2) Pay Down of Commercial Paper or FRRN, or
- 3) Combination of Options 1 & 2

We will evaluate & determine the most optimal combination of pay downs for the debt portfolio.

(1)-Referred to as a defeasance in required Board Resolution.

CONSTRUCTIVE PAY DOWN OF DEBT



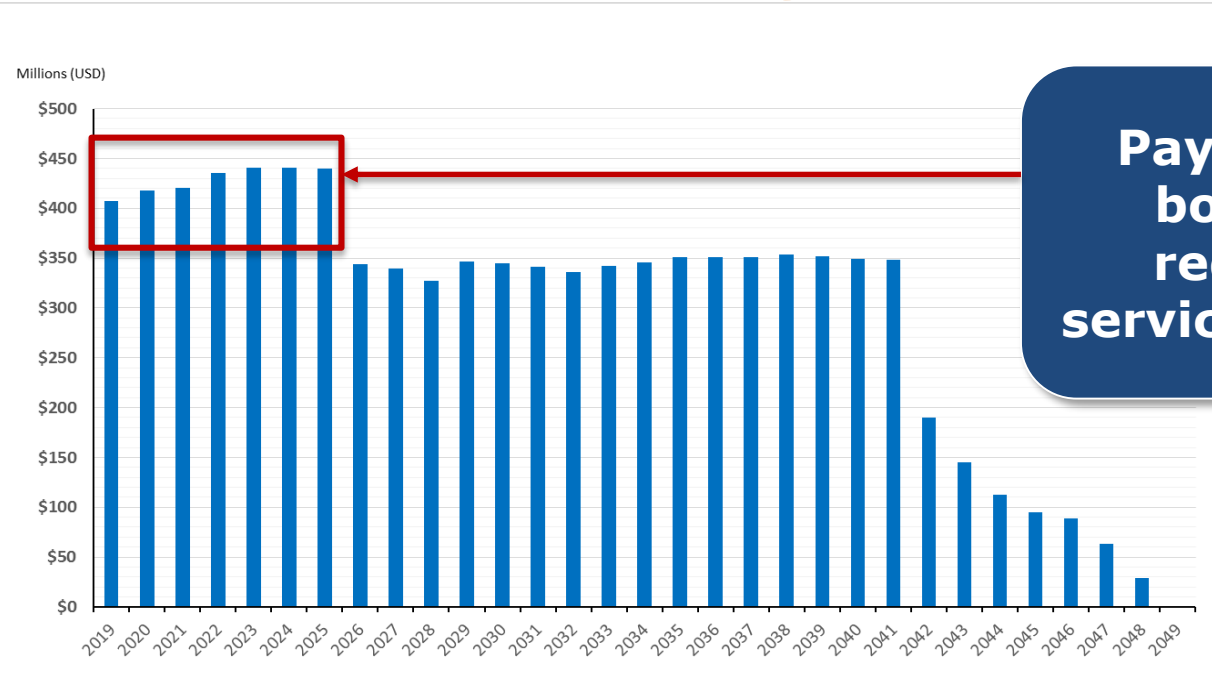
WHY CONSIDER NOW?

- ✓ Wholesale revenues are strong, providing additional cash
- ✓ Effective use of cash
- ✓ Provides debt service savings
- ✓ Strengthens metrics in targeted year

CONSTRUCTIVE PAY DOWN OF DEBT



DEBT SERVICE REQUIREMENTS



Paying down existing bonds allows us to reduce yearly debt service in targeted years.

Principal & Interest Due by Fiscal Year (Sr. Lien & Jr. Lien)

Note: Data as of August 1, 2018.

BOARD REQUEST:

CONSTRUCTIVE PAY DOWN OF DEBT

NOVEMBER 12, 2018 REQUEST OF THE BOARD

Approve a resolution that gives authority to the President & CEO to execute the defeasance of bonds & related documents:

- Up to \$130M
- At the Sr. Lien or Jr. Lien level
- Through January 31, 2019

FRRN PROGRAM

BACKGROUND



The FRRN Program provides quick access to capital at a manageable cost. We propose making the Program Limit (\$100M) the new authorized limit.

Transaction Description	Current Balance	Internal Authorized Limit	Program Limit	Anticipated Execution	CPS Energy Board Resolution	City Council Ordinance
Flex Rate Revolving Note (FRRN) Program	\$25.2M	\$26.0M	\$100.0M	Dec. 2018	✓	N/A

Established in 2009, in response to the financial credit crisis, to provide a form of emergency liquidity, portfolio diversification & flexibility at a manageable cost.

- The notes expire each year & require annual renewal & approval by the Board
- Final Termination Date of Program: 11/1/2028

FRRN PROGRAM

INCREASE LIMIT



WHY CONSIDER NOW?

- ✓ Provides additional flexibility
- ✓ Unused capacity noted by Ratings Agencies
- ✓ Improves Days Liquidity on Hand by ~19 days
- ✓ Additional source of liquidity at a manageable cost

BOARD REQUEST: FRRN RENEWAL & INCREASE



NOVEMBER 12, 2018 REQUEST OF THE BOARD

Approve a resolution to:

- Renew the FRRN Program for a 1-year term, &
- At an increased program limit of \$100M.

PROJECTED RESULTS



This strategy will provide debt service savings in future years. Additionally, we will maintain metrics at or above internal targets.

Metric	Internal Target	FY19 Forecast ⁽¹⁾
Adjusted Debt Service Coverage (ADSC)	> 1.60x	1.86x
Days Cash on Hand (DCOH)	> 170 days	222
Days Liquidity on Hand (DLOH)	> 250 days	327
Debt-to-Equity Ratio	62.2% ⁽²⁾	61.5%

(1) – Based on September 2018 Latest Estimate (LE).

(2) – Based on Board approved FY19 Budget.

RECAP OF VOTING ITEMS



Description of Requests	CPS Energy Board Resolution
Approval of Cash Defeasance Transaction (Constructive Pay Down of Debt) up to \$130M until January 31, 2019	✓
Approval of FRRN Extension for a 1-year term & increase of Authorized Limit to \$100M (Program Limit)	✓



Thank You



Appendix

CASH DEFEASANCE MECHANICS



- CPS Energy identifies specific bonds to be paid down
- With cash, we bid out & fund an escrow that will invest in US Treasuries / Agencies, sufficient to pay for principal & interest to the maturity date
- The escrows, once funded & executed, are irrevocable in nature & the cash cannot be used for any other purpose
- Bond counsel will provide a defeasance opinion as part of legal documentation, at which point the bonds will be removed from CPS Energy's obligations

GLOSSARY



Business Term	Acronym (if applicable)	Definition				
Adjusted Debt Service Coverage	ADSC	<p>The debt service coverage measures how many times debt service is covered from available revenues, net of operating expenses and city payment. (Also known as the Fixed Coverage Ratio or Adjusted Debt Service Coverage Ratio when inclusive of city payment).</p> <p>Adj. Gross Revenues – Operating Expenses = Cash from Operations</p> <p>ADSC = Cash from Operations / Debt Service Costs</p>				
Agency Security		<p>Debt issued by either Ginnie Mae, Fannie Mae, Freddie Mac, or the Federal Home Loan Banks. These securities are backed by mortgage loans and are sponsored by the U.S. government. They are also simply known as 'Agencies.' As a result of U.S. Government sponsorship, they enjoy credit protection based on either an explicit guarantee (Ginnie Mae) or implicit guarantee, ensuring high credit ratings.</p>				
Basis Point	bps	<p>Basis point (BPS) refers to a common unit of measure for interest rates and other percentages in finance. One basis point is equal to 1/100th of 1%, or 0.01%, or 0.0001, and is used to denote the percentage change in a financial instrument. The relationship between percentage changes and basis points can be summarized as follows: 1% change = 100 basis points, and 0.01% = 1 basis point.</p>				
Days Cash on Hand	DCOH	<p>Represents the number of days of operating expenses an organization can pay with its current cash available. It is a measure used in the financial community to measure liquidity. Liquidity is the amount of cash and cash conversion ability, an organization has available to meet operating expenses.</p> <table border="1" data-bbox="595 838 1787 915"> <tr> <td data-bbox="595 838 948 915">Days Cash on Hand</td> <td data-bbox="948 838 1619 915">= $\frac{\text{(General Fund Balance + R\&R Fund Balance)}}{\text{(Annual Operating Expenses - Depreciation)}}$</td> <td data-bbox="1619 838 1696 915">x</td> <td data-bbox="1696 838 1787 915">365</td> </tr> </table>	Days Cash on Hand	= $\frac{\text{(General Fund Balance + R\&R Fund Balance)}}{\text{(Annual Operating Expenses - Depreciation)}}$	x	365
Days Cash on Hand	= $\frac{\text{(General Fund Balance + R\&R Fund Balance)}}{\text{(Annual Operating Expenses - Depreciation)}}$	x	365			
Days Liquidity on Hand	DLOH	<table border="1" data-bbox="595 929 1787 991"> <tr> <td data-bbox="595 929 948 991">Adjusted Days Liquidity on Hand</td> <td data-bbox="948 929 1682 991">= $\frac{\text{(General Fund Balance + R\&R Fund Balance + Availabl CP + Available LOC)}}{\text{(Annual Operating Expenses - Depreciation)}}$</td> <td data-bbox="1682 929 1787 991">x 365</td> </tr> </table>	Adjusted Days Liquidity on Hand	= $\frac{\text{(General Fund Balance + R\&R Fund Balance + Availabl CP + Available LOC)}}{\text{(Annual Operating Expenses - Depreciation)}}$	x 365	
Adjusted Days Liquidity on Hand	= $\frac{\text{(General Fund Balance + R\&R Fund Balance + Availabl CP + Available LOC)}}{\text{(Annual Operating Expenses - Depreciation)}}$	x 365				

GLOSSARY



Business Term	Acronym (if applicable)	Definition
Defeasance		A financing tool that voids a bond when the issuer sets aside cash or bonds sufficient enough to service the debt as the bonds come due, thereby instantly removing the debt from the issuer's balance sheet.
Fed Funds		The federal funds rate is the interest rate at which depository institutions (banks and credit unions) lend reserve balances to other depository institutions overnight, on an uncollateralized basis.
Liquidity		The degree to which an asset or security can be quickly bought or sold in the market without affecting the asset's price.
Municipal Market Data	MMD	The yield curve of the highest-rated (AAA) municipal bonds as published by Thomson Reuters on a daily basis.
US Treasury Security	UST	A marketable, fixed-interest U.S. government debt security that is issued by the U.S. Department of the Treasury to finance government spending. They are also simply known as 'Treasuries.' Interest payments are paid semiannually, and are known in the market as primarily risk-free as they are backed by the full faith and credit of the U.S. Government.