PENNICHUCK

Pennichuck Corporation

Quarterly Report to the

Sole Shareholder
(City of Nashua Board of Aldermen)

Quarter Ended September 30, 2017

Executive Summary

- Revenues for the third quarter of 2017 were 12.4% lower than the prior year ($12.7 million for 2017 versus $14.5 million for 2016). Revenues on a year-to-date basis were 8.0% lower than last year ($31.2 million for the nine months in 2017 versus $33.9 million in 2016). These decreases are primarily due to lower consumption in 2017 versus 2016, as the drought that started in late summer of 2015, and persisted throughout 2016, finally abated in the late spring of this year. Additionally, the service company experienced decreased unplanned revenue activities, which are cost-plus activities performed on a "needs" basis.

- Operating Income for the third quarter of 2017 was 32.7% lower than the prior year ($3.7 million for 2017 versus $5.5 million for 2016). Operating Income on a year-to-date basis was 42.2% lower than the prior year ($4.8 million for 2017 versus $8.3 million for 2016). Both of these variances are almost exclusively attributable to the lower revenue levels year-over-year.

- Pre-Tax Income for the third quarter of 2017 was $1.0 million versus $2.8 million for 2016. On a year-to-date basis, the pre-tax loss was $3.3 million for 2017 versus pre-tax income of $1.1 million for 2016.

- Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) for the third quarter of 2017 was 22.2% lower than the prior year ($5.6 million in 2017 versus $7.2 million for 2016). On a year-to-date basis, EBITDA was $10.6 million for 2017 versus $14.0 million for 2016.

- During the quarter, the Company paid $2.1 million to the City in principal, interest and dividends to fund the City Acquisition Debt. Year-to-date, the Company has paid $6.4 million to the City in principal, interest and dividends to fund the City Acquisition Debt.

- Capital expenditures for the third quarter of 2017 were $2.7 million compared to $6.4 million in the third quarter of 2016. On a year-to-date basis, capital expenditures for 2017 were $5.0 million compared to $12.7 million in 2016. The decrease in activity year-over-year can be attributed to the timing of certain capital projects as well as the deferral of individual projects, such as the Locke Lake groundwater project and the PWW/PEU interconnection, due to permitting and delays in the ability to site new sources of supply for the Locke Lake project.

We remain focused on the Company's primary mission, in that we continue to provide clean water and excellent service to our customers and operate within the confines of the budgeted and planned levels of operating and capital expenditures.

Unaudited Financial Highlights

Financial highlights on a Generally Accepted Accounting Principles ("GAAP") basis for the third quarter of 2017 as compared to the third quarter of 2016, and the nine months of 2017 as compared to the nine months of 2016, are as follows:

	(000's)			
	Quarter Ended		Year-to-Date	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Revenues				
Regulated Utilities	$ 11,915	$ 13,572	$ 28,743	$ 31,175
Other	794	933	2,502	2,734
Total	$ 12,709	$ 14,505	$ 31,245	$ 33,909
Operating Expenses				
Regulated Utilities	$ 8,209	$ 8,126	$ 23,880	$ 22,889
Other	789	866	2,557	2,766
Total	$ 8,998	$ 8,992	$ 26,437	$ 25,655
Operating Income	$ 3,711	$ 5,513	$ 4,808	$ 8,254
Non-Operational Income (Expense)	(1)	27	(3)	857
Net Interest Expense	(2,744)	(2,747)	(8,126)	(8,033)
Pre-Tax Income (Loss)	$ 966	$ 2,793	$ (3,321)	$ 1,078
Income Tax Benefit (Expense)	(537)	(466)	427	(210)
Net Income (Loss)	$ 429	$ 2,327	$ (2,894)	$ 868
Earnings Before Interest, Taxes, Depreciation and Amortization	$ 5,646	$ 7,169	$ 10,608	$ 14,043

Revenues from the water utility operations decreased 12.5% in the quarter and 8.0% on an annual basis versus last year. Revenues include actual billed amounts through and including the September billing cycles, plus an accrual of unbilled amounts through the end of that month (based upon trailing consumption patterns). Revenues from the unregulated water service business have decreased 14.9% in the third quarter as compared to the second quarter of last year, primarily due to a reduction in "cost plus" contract work from unplanned maintenance activities. On a year-to-date basis, the unregulated water service revenues are down by 7.4%, for the same reason.

Operating Expenses have increased approximately 0.1% in the third quarter and 3.0% on a year-to-year basis. The increase is mainly attributable to increased direct operating costs associated with the increases in real estate taxes, labor costs and health insurance costs.

Operating Income has decreased year-over-year as a result of the variation in revenue and operating expense levels recognized for the quarter and year-to-date.

Interest Expense has decreased slightly in the third quarter by 0.1% over the third quarter of last year; year-to-date versus last year it has increased 1.2% resulting from the interest costs associated with the additional financed amounts for capital projects which have been incurred for ongoing infrastructure replacement, in conformity with the Company's key mission objectives.

The third quarter pre-tax income and year-to-date pre-tax loss for 2017 compare negatively to the pre-tax levels for 2016 due to the revenue and expense variations discussed above.

The year-to-date income tax benefit in the current year reflects the treatment for the Municipal Acquisition Regulatory Asset, which is not deductible for tax purposes. Therefore, the tax benefit is 12.9% versus the statutory rate benefit of 39.4% on a year-to-date basis.

Earnings before interest, taxes, depreciation and amortization (EBITDA) are lower than EBITDA for the same periods last year due to increased operating costs, coupled with lower revenue levels and lower non-operational income related to the sale of the Will Street Operations Facility in June 2016.

Balance Sheet

	(000's) As of September 30, 2017 (Unaudited)	As of December 31, 2016 (Audited)
Assets		
Property, Plant & Equipment, Net	$ 206,606	$ 201,698
Current Assets:		
Cash	728	2,446
Restricted Cash	6,967	6,530
Restricted Cash – 2014 and 2015 Bond Project Funds	-	7,568
Accounts Receivable Note 1	6,720	6,086
Inventory	592	666
Other Current Assets Note 2	1,328	2,047
Total Current Assets	16,335	25,343
Other Assets:		
Acquisition Premium	73,707	75,144
Other Assets	12,156	12,410
Total Other Assets	85,863	87,554
TOTAL ASSETS	$ 308,804	$ 314,595
Shareholder's Equity and Liabilities		
Shareholder's Equity	$ 17,496	$ 20,578
Bonds, Notes and Mortgages	197,805	200,758
Current Liabilities:		
Current Portion of Long-Term Debt	5,430	5,162
Other Current Liabilities Notes 3 and 4	6,167	9,798
Total Current Liabilities	11,597	14,960
Other Long-Term Liabilities:		
CIAC, net	44,609	40,364
Deferred Income Taxes	20,498	20,869
Accrued Pension Liability Note 5	8,818	9,010
Other Long-Term Liabilities	7,981	8,056
Total Other Long-Term Liabilities	81,906	78,299
TOTAL SHAREHOLDER'S EQUITY AND LIABILITIES	$ 308,804	$ 314,595

Notes to Balance Sheet

Note 1 (Accounts Receivable) – At December 31, 2016, approximately $1,250,000 of this balance was comprised of PFOA reimbursable costs from Saint-Gobain Performance Plastics Corporation, for design and expansion of public water to residents in the Town of Litchfield. The balance in accounts receivable for these reimbursable costs incurred during the third quarter, as of September 30, 2017 is $587,000.

Note 2 (Other Current Assets) – At December 31, 2016, approximately $1,163,000 of this balance was comprised of prepaid property taxes, which were expensed in the first quarter of 2017, relating to taxes paid in November and December of 2016 for the second half of the property tax year ended March 31, 2017. The balance of prepaid property taxes as of September 30, 2017 is zero, as we are fully into the second half of the property tax year for accrual accounting purposes.

Note 3 (Other Current Liabilities) – At December 31, 2016, approximately $6,300,000 of this balance was comprised of accounts payable, as well as PFOA reimbursable costs from Saint-Gobain Performance Plastics Corporation, for design and expansion of public water to residents in the Town of Litchfield. The accounts payable balance remaining, inclusive of these reimbursable costs as of September 30, 2017 is $690,000, as it relates to activities that were performed in the third quarter.

Note 4 (Other Current Liabilities) – At December 31, 2016, approximately $1,700,000 of this balance was comprised of accrued interest. These interest costs are associated with the financed amounts for capital projects which have been incurred for ongoing infrastructure replacement, in conformity with the Company's key mission objectives. The balance in accrued interest for these financed amounts as of September 30, 2017 is $818,000.

Note 5 (Accrued Pension Liability) – During the nine months of 2017, $936,000 was contributed into the Pension Plan, while approximately $497,000 in benefit payments were made to participants and approximately $1,844,000 of investment income and appreciation was earned in the plan.

Unaudited Cash Flow Statement

Cash Flow on a GAAP basis for the third quarter of 2017 as compared to the third quarter of 2016, and the year-to-date 2017 versus 2016, are as follows:

	(000's)			
	Quarter Ended		Year-to-Date	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Operating Activities:				
Net Income (Loss)	$ 429	$ 2,327	$ (2,894)	$ 868
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:				
Depreciation and Amortization	1,937	1,726	5,804	5,149
Provision for Deferred Taxes	550	480	(386)	251
Other	(10)	(48)	(55)	(107)
Changes in Assets and Liabilities:				
(Increase) Decrease in Accounts Receivable	(753)	(1,137)	(634)	(2,588)
(Increase) Decrease in Inventory	62	61	74	30
(Increase) Decrease in Other Assets	977	1,264	1,101	2,001
Increase (Decrease) in Accounts Payable	151	899	(2,542)	1,260
Increase (Decrease) in Other Liabilities	295	1,275	(1,483)	774
Net Cash Provided by (Used in) Operating Activities	3,638	6,847	(1,015)	7,638
Investing Activities:				
Purchases of Property, Plant & Equipment, including the Debt Component of AFUDC	(2,460)	(6,964)	(5,075)	(13,843)
Proceeds from Sale of Property, Plant & Equipment	-	(67)	37	635
(Increase) Decrease in Restricted Cash	(679)	2,016	7,130	(6,358)
Sale of Investment Securities	-	2,257	-	17,236
Change in Deferred Land Costs	-	3	-	7
Net Cash Provided by (Used in) Investing Activities	(3,139)	(2,755)	2,092	(2,323)
Financing Activities:				
Borrowings (Repayments) on Line of Credit	278	-	278	-
Payments on Long-term Debt	(778)	(720)	(4,406)	(3,490)
Contributions in Aid of Construction	-	4	18	25
Proceeds from Long-term Borrowings	64	1,172	1,503	2,605
Debt Issuance Costs	6	0	21	(57)
Dividends Paid	(70)	(70)	(209)	(210)
Net Cash Provided by (Used in) Financing Activities	(500)	386	(2,795)	(1,127)
Increase (Decrease) in Cash and Cash Equivalents	(1)	4,478	(1,718)	4,188
Cash and Cash Equivalents at Beginning of Period	729	956	2,446	1,246
Cash and Cash Equivalents at End of Period	$ 728	$ 5,434	$ 728	$ 5,434

Financial information is available on the Company's website (www.Pennichuck.com).

Capital Expenditures

Capital Expenditures in the third quarter of 2017 were $2.7 million as compared to $6.4 million in the third quarter of 2016. Capital Expenditures for the year-to-date were $5.0 million as compared to $12.7 million in 2016.

Major expenditures in the nine months of 2017 included:

Main Street, Nashua – Main Improvements	$ 431,000
PWW – PEU Interconnection Design Evaluation	$ 354,000
Asset Management, GIS, Data Presentation System	$ 332,000
PWW – Meter Replacements	$ 287,000
Temple Street, Nashua – Main Improvements	$ 139,000
PEU – Meter Replacements	$ 132,000

Rate Case – Pennichuck Water Works, Inc.

On September 23, 2016, Pennichuck Water Works, Inc. (PWW) filed a request with the New Hampshire Public Utilities Commission (NHPUC) for a rate increase of 17.21% over its current rates for the test year 2015, for which 7.86% was related to a permanent rate increase, and 9.35% was related to a prospective step increase (associated with capital investments and other allowable expenditures in the twelve months following the test year). The overall rate increase is subject to the normal regulatory filing process with the NHPUC, as followed for all prior rate case filings, and as such, the final permanent rate increase granted will be effective retroactive back to the filing date, once approved by the NHPUC. The step increase, once approved and granted, would be earned on a forward looking basis, as of the date of the order granting such increase. In addition, PWW requested that a temporary rate increase of 6.21% be granted as a subset of the final permanent rate increase, with the intention that this temporary rate increase would be approved very early in 2017. The Company, NHPUC Staff and the Office of Consumer Advocate agreed to a temporary rate increase at “current rates,” and as such, there was no impact on ratepayers for any temporary rate increases.

The request for the overall permanent rate increase was based upon increases in PWW’s operating costs since the last allowed rate increase in 2010/2011 (for the 2009 test year), as well as revenues needed to pay the debt service on over $40 million of infrastructure replacements made since the last rate case, with those dollars being invested in its real property assets, distribution and treatment systems, and other necessary capital items, to ensure continued compliance with the Safe Drinking Water Act and prudent ongoing replacement of aging infrastructure to properly maintain the company’s operating systems.

On November 7, 2017, the PUC issued Order No. 26,070 approving a permanent rate increase of 3.12% and a 7.69% step increase for its customers. The permanent rate increase is effective on a bills-rendered basis on and after December 7, 2016. The step increase is effective the date of the order, November 7, 2017

Rate Case - Pennichuck East Utility, Inc.

On October 18, 2017, Pennichuck East Utility, Inc. (PEU) filed a request with the New Hampshire Public Utilities Commission (NHPUC) for a rate increase of 21.24% over its current rates for the test year 2016, for which 20.08% of this increase is related to a permanent rate increase and 1.16% is related to a prospective step increase (associated with capital investments and other allowable expenditures in the twelve months following the test year). The overall rate increase is subject to the normal regulatory filing process with the NHPUC, as followed for all prior rate case filings, and as such, the final permanent rate increase granted will be effective retroactive back to the filing date, once approved by the NHPUC. The step increase, once approved and granted, would be earned on a forward looking basis, as of the date of the order granting such increase. In addition, PEU requested that a temporary rate increase of 13.70% be granted as a subset of the final permanent rate increase, with the intention that this temporary rate increase would be approved in early 2018, and with permanent rates being set in the summer or fall of 2018.

The last general rate increase for PEU was in 2014, based upon 2012 as a test year. Since then, PEU's operating expenses have increased ratably, and for some items like local property taxes, well above the rate of inflation. Additionally, since the beginning of 2013, the Company has borrowed and invested over $7.5 million in new capital assets to serve its customers through ongoing investments in infrastructure replacements and system improvements. The rate increase being requested will allow PEU to pay the debt service attributable to these new capital investments, pay its necessary operating costs, and continue to meet the needs of its customers now and into the future.

Water Infrastructure and Conservation Adjustment (WICA)

On January 31, 2017, Pennichuck Water Works, Inc. (PWW) filed a petition with the New Hampshire Public Utilities Commission (NHPUC) to approve a Water Infrastructure and Conservation Adjustment (WICA) surcharge to be effective June 1, 2017, approve proposed 2017 WICA projects, and preliminarily approve proposed 2018 WICA projects. This petition process was in a "suspended" state, pending the results of the PWW Rate Case, if approved per the Settlement Agreement, which would terminate the WICA program and replace it with a new program inclusive in those rates. The new program would be analogous to the WICA program, but would be eligible for all capital improvement projects and expenditures, not just certain main replacement projects.

On November 7, 2017, included in the NHPUC issued Order No. 26,070 which approved new permanent rates for PWW, the current WICA program is being replaced with an annual Qualified Capital Project Adjustment Charge (QCPAC) surcharge program, which will allow for annual surcharges between rate case filings. This annual surcharge will be based upon the debt service and property taxes associated with all of the capital projects undertaken and completed by PWW in the preceding year.

As a part of the approval in Order No. 26,070, within 15 days of the issuance of this approved order, PWW must file an interim QCPAC submission with the Commission, which will include the current forecast of the 2017 QCPAC eligible projects as well as a forecast of capital project expenditures for fiscal years 2018 and 2019.

Financing

On June 8, 2017, Pennichuck East Utility, Inc. completed a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water Revolving Loan Fund in the amount of $2,400,000 for a 20-year term at an interest rate of 1.96%. The loan will fund the installation of a Merrimack River crossing interconnection pipeline connecting the distribution main owned by Pennichuck Water Works, Inc. in the Town of Merrimack to the existing Pennichuck East Utility, Inc. distribution system in the Town of Litchfield.

On June 8, 2017, Pennichuck East Utility, Inc. completed a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water Revolving Loan Fund in the amount of $570,000 for a 30-year term at an interest rate of 1.96%. The loan will fund the replacement of approximately 2,400 linear feet of water main on Brady Avenue in the Maple Hills Community Water System in Derry, NH.

On June 8, 2017, Pennichuck East Utility, Inc. completed a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water Revolving Loan Fund in the amount of $245,000 for a 20-year term at an interest rate of 1.96%. The loan will fund the replacement of approximately 1,200 linear feet of water main on Hillcrest Road in Litchfield, NH.

On October 19, 2017, Pennichuck East Utility, Inc. filed a petition with the New Hampshire Public Utilities Commission relative to debt financings, to be serviced by CoBank ACB, as well as the refinance of intercompany loans with Pennichuck Corporation. Pennichuck East Utility, Inc. seeks approval for (1) a term loan of up to $500,000 to fund 2017 capital projects not funded by SRF loans, (2) a 3-year $3.0 million Fixed Asset Line of Credit to provide for short-term financing of capital projects, and (3) the refinance of two Intercompany Loans with Pennichuck Corporation, in the amount of $1,701,516, for a new term of 30 years. If approved, it is anticipated to close on these financings in late December 2017 or early January 2018.