PENNICHUCK

Pennichuck Corporation

Quarterly Report to the
Sole Shareholder
(City of Nashua Board of Aldermen)

Quarter Ended June 30, 2018

Executive Summary

- Revenues for the second quarter of 2018 were 19.8% higher than the prior year ($11.5 million for 2018 versus $9.6 million for 2017). Revenues on a year-to-date basis were also 12.1% higher when compared to the prior year ($20.8 million for the six months in 2018 versus $18.5 million in 2017). Both are primarily due to an overall 10.81% rate increase approved by the New Hampshire Public Utilities Commission in late 2017 for the Company's Pennichuck Water Works, Inc. subsidiary, coupled with a slight uptick in overall water consumption over the prior year, as well as increased revenues earned by the unregulated service company.

- Operating Income for the second quarter of 2018 was 125.0% above the prior year ($1.8 million for 2018 versus $0.8 million for 2017). Operating Income on a year-to-date basis is 81.8% higher than the prior year ($2.0 million for 2018 versus $1.1 million for 2017). Both of which are primarily attributed to the increased revenue levels year over year.

- Pre-Tax Loss for the second quarter of 2018 was $1.0 million versus the pre-tax loss of $1.9 million for 2017. On a year-to-date basis, the pre-tax loss was $3.4 million for 2018 versus $4.3 million for 2017.

- Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) for the second quarter of 2018 was 32.1% higher than the prior year ($3.7 million in 2018 versus $2.8 million for 2017). On a year-to-date basis, EBITDA was $6.0 million for 2018 versus $5.0 million for 2017.

- 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 $4.2 million to the City in principal, interest and dividends to fund the City Acquisition Debt.

- Capital expenditures for the second quarter of 2018 were $1.7 million compared to $1.2 million in the second quarter of 2017. On a year-to-date basis, capital expenditures for 2018 were $2.2 million compared to $2.3 million in 2017.

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 second quarter of 2018 as compared to the second quarter of 2017, and the six months of 2018 as compared to the six months of 2017, are as follows:

(000's)

	Quarter Ended		Year-to-Date	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Revenues				
Regulated Utilities	$ 10,440	$ 8,775	$ 18,836	$ 16,828
Other	1,006	888	1,947	1,708
Total	$ 11,446	$ 9,663	$ 20,783	$ 18,536
Operating Expenses				
Regulated Utilities	$ 8,700	$ 7,909	$ 16,861	$ 15,671
Other	1,000	920	1,927	1,768
Total	$ 9,700	$ 8,829	$ 18,788	$ 17,439
Operating Income	$ 1,746	$ 834	$ 1,995	$ 1,097
Non-Operational Income (Expense)	(2)	(1)	(3)	(2)
Net Interest Expense	(2,730)	(2,722)	(5,358)	(5,382)
Pre-Tax Income (Loss)	$ (986)	$ (1,889)	$ (3,366)	$ (4,287)
Income Tax Benefit (Expense)	145	(33)	1,011	964
Net Income (Loss)	$ (841)	$ (1,922)	$ (2,355)	$ (3,323)
Earnings Before Interest, Taxes, Depreciation and Amortization	$ 3,766	$ 2,766	$ 6,016	$ 4,962

Revenues from water utility operations increased 19.0% in the quarter and 11.9% on a year-to-date basis, versus last year, as discussed in the "*Executive Summary*." Revenues include actual billed amounts through and including the June billing cycles, plus an accrual of unbilled amounts through the end of the month (based upon trailing consumption patterns). Revenues from the unregulated water service business have increased 13.4% in the second quarter as compared to the second quarter of last year, primarily due to scheduled increases for their planned revenue contracts coupled with an increase in "cost plus" contract work from unplanned maintenance activities. On a year-to-date basis, the unregulated water service revenues are up by 14.1%, for the same reason.

Operating Expenses have increased approximately 9.9% in the second quarter and 7.7% on a year-to-year basis. The increase is mainly attributable to increased direct operating costs associated with increases in real estate taxes, labor and health insurance costs.

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

Interest Expense increased slightly in the second quarter by approximately .3% over the second quarter of last year; and, year-to-date versus last year it has decreased .4%, resulting from the interest costs 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 second quarter pre-tax loss and year-to-date pre-tax loss for 2018 are both lower than the pre-tax levels for 2017 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 30.0% versus the statutory rate benefit of 27.24% on a year-to-date basis.

Earnings before interest, taxes, depreciation and amortization (EBITDA) are higher than EBITDA for the same periods last year due to increased revenues, coupled with slightly lower interest expense levels than 2017.

Balance Sheet

	(000's) As of June 30, 2018 (Unaudited)	(000's) As of December 31, 2017 (Audited)
Assets		
Property, Plant & Equipment, Net	$ 209,964	$ 210,498
Current Assets:		
Cash	728	994
Restricted Cash	3,416	4,953
Restricted Cash – Bond Project Funds	34	3,288
Accounts Receivable	6,796	5,699
Inventory	578	604
Other Current Assets Note 1	2,362	2,257
Total Current Assets	13,914	17,795
Other Assets:		
Acquisition Premium	72,249	73,227
Other Assets	13,078	13,271
Total Other Assets	85,327	86,498
TOTAL ASSETS	$ 309,205	$ 314,791
Shareholders' Equity and Liabilities		
Shareholders' Equity	$ 11,491	$ 13,905
Bonds, Notes and Mortgages	200,173	197,905
Current Liabilities:		
Line of Credit Note 2	720	5,574
Current Portion of Long-Term Debt	5,882	5,575
Other Current Liabilities Notes 3 and 4	4,148	4,292
Total Current Liabilities	10,750	15,441
Other Long-Term Liabilities:		
CIAC, net	47,697	47,458
Deferred Income Taxes	11,912	12,847
Accrued Pension Liability Note 5	9,771	9,792
Other Long-Term Liabilities	17,411	17,443
Total Other Long-Term Liabilities	86,791	87,540
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	$ 309,205	$ 314,791

Notes to Balance Sheet

Note 1 (Other Current Assets) – At December 31, 2017, approximately $1,143,000 of this balance was comprised of prepaid property taxes, which were expensed in the first quarter of 2018, relating to taxes paid in November and December of 2017 for the second half of the property tax year ended March 31, 2018. The balance of prepaid property taxes as of June 30, 2018 is $1,139,000.

Note 2 (Line of Credit) – As of December 31, 2017, approximately $5,574,000 was borrowed and outstanding under the Company's Line of Credit in existence at that date. That balance was completely paid off on April 4, 2018 as a result of the proceeds brought into the Company by the issuance of bonds by Pennichuck Water Works, Inc. This was reimbursement of capital expenditures funded during 2017. That Line of Credit, which had a $6 million capacity for borrowings was replaced by a new $4 million Working Capital Line of Credit, and two new Fixed Asset Lines of Credit for Pennichuck Water Works, Inc. ($10 million FALOC) and Pennichuck East Utility, Inc. ($3 million FALOC), to be used to fund Construction Work in Progress on capital projects which will be refinanced into long term debt obligations or bond indebtedness annually. The balance outstanding under the Company's new Working Capital Line of Credit at June 30, 2018 was $0, whereas borrowing under the PWW FALOC was approximately $720,000 as of that date.

Note 3 (Other Current Liabilities) – At June 30, 2018, approximately $2,805,000 of this balance is comprised of accounts payable which relates to activities that were performed in the second quarter of 2018.

Note 4 (Other Current Liabilities) – At June 30, 2018, approximately $160,000 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.

Note 5 (Accrued Pension Liability) – During the six months of 2018, $514,000 was contributed into the Pension Plan, while approximately $319,000 in benefit payments were made to participants and approximately $46,000 of investment income and appreciation was earned in the plan.

Unaudited Cash Flow Statement

Cash Flow on a GAAP basis for the second quarter of 2018 as compared to the second quarter of 2017, and the year-to-date 2018 versus 2017, are as follows:

	(000's)			
	Quarter Ended		Year-to-Date	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Operating Activities:				
Net Income (Loss)	$ (841)	$ (1,922)	$ (2,355)	$ (3,323)
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:				
Depreciation and Amortization	2,018	1,934	4,020	3,867
Provision for Deferred Taxes	(136)	48	(994)	(936)
Other	(8)	(6)	(19)	(45)
Changes in Assets and Liabilities:				
(Increase) Decrease in Accounts Receivable	(1,580)	(1,708)	(1,097)	119
(Increase) Decrease in Inventory	80	54	26	12
(Increase) Decrease in Other Assets	(1,707)	(1,073)	(509)	124
Increase (Decrease) in Accounts Payable	1,700	1,676	1,291	(2,693)
Increase (Decrease) in Other Liabilities	(730)	(1,074)	(1,394)	(1,778)
Net Cash Provided by (Used in) Operating Activities	(1,204)	(2,071)	(1,031)	(4,653)
Investing Activities:				
Purchases of Property, Plant & Equipment, including the Debt Component of AFUDC	(1,875)	(1,252)	(2,368)	(2,615)
Proceeds from Sale of Property, Plant & Equipment	-	-	-	37
(Increase) Decrease in Restricted Cash	-	2,863	-	7,809
Sale of Investment Securities	-	-	-	-
Change in Deferred Land Costs	(5)	-	(16)	-
Net Cash Provided by (Used in) Investing Activities	(1,880)	1,611	(2,384)	5,231
Financing Activities:				
Borrowings (Repayments) on Lines of Credit	(5,025)	-	(4,854)	-
Payments on Long-term Debt	(858)	(768)	(3,853)	(3,628)
Contributions in Aid of Construction	80	17	81	18
Proceeds from Long-term Borrowings	6,685	393	6,697	1,439
Debt Issuance Costs	426	15	426	15
Dividends Paid	(70)	(69)	(140)	(139)
Net Cash Provided by (Used in) Financing Activities	1,238	(412)	(1,643)	(2,295)
Increase (Decrease) in Cash and Cash Equivalents	(1,846)	(872)	(5,058)	(1,717)
Cash and Cash Equivalents at Beginning of Period	6,024	1,601	9,236	2,446
Cash and Cash Equivalents at End of Period	$ 4,178	$ 729	$ 4,178	$ 729

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

Capital Expenditures

Capital Expenditures in the second quarter of 2018 were $1.7 million as compared to $1.2 million in the second quarter of 2017. Capital Expenditures for the year-to-date were $2.2 million as compared to $2.3 million in 2017.

Major expenditures in the first half of 2018 included:

PWW – PEU Interconnection	$ 809,000
Meter Replacements	$ 222,000
Asset Management and GIS System	$ 177,000
Rolling Stock Replacement	$ 97,000
Click Mobile Upgrade	$ 86,000
Merrimack River Intake	$ 72,000

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 20.78% over its current rates for the test year 2016, for which 19.36% of this increase is related to a permanent rate increase and 1.42% 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. As a part of this overall rate setting process, PEU entered into a settlement agreement with the NHPUC staff and the OCA staff, requesting a temporary rate increase of 12.24% 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.

On May 31, 2018, the NHPUC issued Order No. 26,136 approving the requested 12.24% increase in temporary rates effective on a bills-rendered basis as of January 8, 2018, until permanent rates are approved sometime in the fall of 2018.

Qualified Capital Project Adjustment Charge (QCPAC)

On November 7, 2017, the NHPUC issued Order No. 26,070 which approved replacement of the Pennichuck Water Works, Inc. (PWW) current WICA program with an annual QCPAC, which will apply an annual surcharge between rate cases. This surcharge will be based on essentially all of the capital projects undertaken and completed by PWW each year. The QCPAC is stipulated to include the full debt service (principal and interest), as well as the incremental property taxes, for annual additions to capital assets. At this juncture, the final order approving the QCPAC surcharge for 2017 capital improvements is imminent, with the surcharge to be implemented in the second half of 2018, at a rate not to exceed 1.58% of current permanent rates.

Financing

On April 4, 2018, the Company's Pennichuck Water Works, Inc. subsidiary issued $5.5 million of tax-exempt and taxable bonds through the NH Business Finance Authority to fund capital improvements for PWW's water supply, distribution and support systems. The bond issuance was approved by the Pennichuck Board of Directors and the Sole Shareholder. And, on February 2, 2018, the NHPUC approved an order, allowing for the issuance of up to $32.5 million in bonds, for multiple year issuances of bonds for the years 2018-2021. The bonds issued on April 4, 2018 represent the first series of bonds issued under this overall approval by the Company's Board and Shareholder, as well as the NHPUC and NH Governor and Council.

On April 25, 2018, the Company's Pennichuck East Utility, Inc. subsidiary completed financing transactions with CoBank, ACB of: (1) a 3-year $3.0 million Fixed Asset Line of Credit to provide for short-term financing of capital projects, and (2) a $350,078, 25-year fully amortizing term loan at an interest rate of 5.33% to reimburse 2017 capital projects which were not funded by SRF loans.

On April 27, 2018, Pennichuck Corporation completed a financing transaction with TD Bank, N.A. on a $4.0 million Working Capital Line of Credit, which expires on August 31, 2019 (amended from an original working capital and fixed asset $10 million Line of Credit, which was set to expire on April 30, 2018).

On May 1, 2018, the Company's Pennichuck East Utility, Inc. subsidiary completed the refinance of its three intercompany loans with Pennichuck Corporation into two new intercompany loans: (1) a 30-year $1,157,403 loan at an interest rate of 3.20%, and (2) a 30-year $1,701,516 loan at an interest rate of 3.20%. The two new intercompany loans are fully amortizing, whereas the pre-existing loans were a combination of fully amortizing and balloon maturity debt obligations.

On May 1, 2018, the Company's Pittsfield Aqueduct Company, Inc. subsidiary completed the refinance of its $776,850 balloon maturity intercompany loan with Pennichuck Corporation, which was set to expire on May 1, 2018, as well as the conversion of $409,150 of short-term intercompany obligations from Pittsfield Aqueduct Company to Pennichuck Corporation, to a new 30-year $1,186,000 fully amortizing loan at an interest rate of 3.20%.

On May 2, 2018, the Company's Pennichuck Water Works, Inc. subsidiary completed a financing transaction with TD Bank, N.A. on a new $10.0 million Fixed Asset Line of Credit which expires on August 31, 2020. As a requirement to securing this financing, on April 20, 2018, the NHPUC approved the Fixed Asset Line of Credit in order to provide for short-term financing of capital projects on an annual basis.

Subsequent Events

Pennichuck Water Works, Inc. will be filing a petition with the New Hampshire Public Utilities Commission (NHPUC) for approval to borrow $3,375,000 for a 30-year term from the State of New Hampshire's Drinking Water and Groundwater Trust Fund, to be used to finance the cost of the Pennichuck Core Water Main Replacement project. The financing has been approved by the Pennichuck Corporation and the Pennichuck Water Works, Inc. Boards of Directors. The loan is also subject to approval by the City of Nashua, as sole shareholder of Pennichuck Corporation.

Pennichuck East Utility, Inc. will be filing a petition with the New Hampshire Public Utilities Commission for approval to borrow $4,240,000 for a 30-year term from the State of New Hampshire's Drinking Water Revolving Loan Fund Program, to be used to finance the cost of the Locke Lake New Groundwater Source project in Barnstead, NH. The financing has been approved by the Pennichuck Corporation and the Pennichuck East Utility, Inc. Boards of Directors. The loan is also subject to approval by the City of Nashua, as sole shareholder of Pennichuck Corporation.