



Pennichuck Corporation

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

Quarter Ended June 30, 2019

Executive Summary

- Revenues for the second quarter of 2019 were 7.8% lower than the prior year (\$10.6 million for 2019 versus \$11.5 million for 2018). Revenues on a year-to-date basis were also 3.8% lower when compared to the prior year (\$20.0 million for the six months in 2019 versus \$20.8 million in 2018). Both are primarily due to lower consumption in 2018 versus 2017, as the regulated utilities were negatively impacted by higher-than-normal precipitation in the spring of this year.
- Operating Income for the second quarter of 2019 was 55.6% lower than the prior year (\$0.8 million for 2019 versus \$1.8 million for 2018). Operating Income on a year-to-date basis is 45.0% lower than the prior year (\$1.1 million for 2019 versus \$2.0 million for 2018). Both of which are primarily attributed to the lower revenue levels year-over-year.
- Pre-Tax Loss for the second quarter of 2019 was \$2.0 million versus the pre-tax loss of \$1.0 million for 2018. On a year-to-date basis, the pre-tax loss was \$4.3 million for 2019 versus \$3.4 million for 2018.
- Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) for the second quarter of 2019 was 24.3% lower than the prior year (\$2.8 million in 2019 versus \$3.7 million for 2018). On a year-to-date basis, EBITDA was 10.0% lower than the prior year (\$5.4 million for 2019 versus \$6.0 million for 2018).
- 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 2019 were \$1.9 million compared to \$1.7 million in the second quarter of 2018. On a year-to-date basis, capital expenditures for 2019 were \$2.5 million compared to \$2.2 million in 2018.

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 2019 as compared to the second quarter of 2018, and the six months of 2019 as compared to the six months of 2018, are as follows:

	(000’s)			
	<u>Quarter Ended</u>		<u>Year-to-Date</u>	
	<u>June 30, 2019</u>	<u>June 30, 2018</u>	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Revenues				
Regulated Utilities	\$ 9,764	\$ 10,440	\$ 18,547	\$ 18,836
Other	<u>842</u>	<u>1,006</u>	<u>1,487</u>	<u>1,947</u>
Total	\$ 10,606	\$ 11,446	\$ 20,034	\$ 20,783
Operating Expenses				
Regulated Utilities	\$ 9,087	\$ 8,700	\$ 17,500	\$ 16,861
Other	<u>747</u>	<u>1,000</u>	<u>1,387</u>	<u>1,927</u>
Total	\$ 9,834	\$ 9,700	\$ 18,887	\$ 18,788
Operating Income	\$ 772	\$ 1,746	\$ 1,147	\$ 1,995
Non-Operational Income (Expense)	(9)	(2)	16	(3)
Net Interest Expense	<u>(2,786)</u>	<u>(2,730)</u>	<u>(5,497)</u>	<u>(5,358)</u>
Pre-Tax Income (Loss)	\$ (2,023)	\$ (986)	\$ (4,334)	\$ (3,366)
Income Tax Benefit (Expense)	<u>91</u>	<u>145</u>	<u>184</u>	<u>1,011</u>
Net Income (Loss)	\$ <u>(1,932)</u>	\$ <u>(841)</u>	\$ <u>(4,150)</u>	\$ <u>(2,355)</u>
Earnings Before Interest, Taxes, Depreciation and Amortization	\$ <u>2,871</u>	\$ <u>3,766</u>	\$ <u>5,359</u>	\$ <u>6,016</u>

Revenues from water utility operations decreased 6.5% in the quarter and 1.5% 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 also decreased 16.5% in the second quarter as compared to the second quarter of last year, primarily due to the termination and non-renewal of one major operating contract in July of 2018. On a year-to-date basis, the unregulated water service revenues are down by 23.7%, for the same reason.

Operating Expenses have increased approximately 1.4% in the second quarter and 0.5% on a year-to-year basis. The increase is mainly attributable to increased direct operating costs associated with increases in transmission and distribution activities, labor and health insurance costs.

Operating Income has decreased 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 in the second quarter by approximately 2.1% over the second quarter of last year; and, year-to-date versus last year by approximately 2.6%, 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 2019 are both higher than the pre-tax levels for 2018 due to the revenue and expense variations discussed above.

The income tax benefit in the current year reflects the tax treatment for the Municipal Acquisition Regulatory Asset (MARA), which is not deductible for tax purposes, and the inclusion of CIAC taxable income, due to the elimination of an exemption in the Tax Cuts and Jobs Act. Depending on year-to-date profitability levels, compared to the value of that non-deductible amount, this can impact the actual rate on earned amounts in a positive or negative manner, throughout the year. As of the end of the second quarter, the tax benefit rate is 4.2% versus the statutory rate benefit of 27.08%.

Earnings before interest, taxes, depreciation and amortization (EBITDA) are lower than EBITDA for the same periods last year due to lower revenues, coupled with slightly higher operating expense levels than 2018.

Balance Sheet

	(000's)	
	As of June 30, 2019 (Unaudited)	As of December 31, 2018 (Audited)
<u>Assets</u>		
Property, Plant & Equipment, Net	\$ <u>222,235</u>	\$ <u>221,860</u>
Current Assets:		
Cash	3,698	1,575
Restricted Cash	3,756	3,428
Restricted Cash – Bond Project Funds	46	3,337
Accounts Receivable	6,975	6,348
Inventory	600	611
Other Current Assets ^{Note 1}	<u>2,019</u>	<u>1,631</u>
Total Current Assets	<u>17,094</u>	<u>16,930</u>
Other Assets:		
Acquisition Premium	70,267	71,268
Other Assets	<u>12,910</u>	<u>13,075</u>
Total Other Assets	<u>83,177</u>	<u>84,343</u>
TOTAL ASSETS	\$ <u>322,506</u>	\$ <u>323,133</u>
<u>Shareholders' Equity and Liabilities</u>		
Shareholders' Equity	\$ <u>4,149</u>	\$ <u>8,410</u>
Bonds, Notes and Mortgages	<u>204,612</u>	<u>200,225</u>
Current Liabilities:		
Lines of Credit ^{Note 2}	6,299	6,626
Current Portion of Long-Term Debt	6,445	6,019
Other Current Liabilities ^{Notes 3 and 4}	<u>6,315</u>	<u>8,388</u>
Total Current Liabilities	<u>19,059</u>	<u>21,033</u>
Other Long-Term Liabilities:		
CIAC, net	52,938	51,961
Deferred Income Taxes	13,902	14,110
Accrued Pension Liability ^{Note 5}	10,026	10,021
Other Long-Term Liabilities	<u>17,820</u>	<u>17,373</u>
Total Other Long-Term Liabilities	<u>94,686</u>	<u>93,465</u>
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	\$ <u>322,506</u>	\$ <u>323,133</u>

Notes to Balance Sheet

Note 1 (Other Current Assets) – At December 31, 2018, approximately \$1,020,975 of this balance was comprised of prepaid property taxes, which were expensed in the first quarter of 2019, relating to taxes paid in November and December of 2018 for the second half of the property tax year ended March 31, 2019. The balance of prepaid property taxes as of June 30, 2019 is \$1,093,673.

Note 2 (Lines of Credit) – At June 30, 2019, approximately \$3,311,000 of this balance was comprised of the corporate Working Capital Line of Credit which is periodically drawn upon in support of our operations. The remaining \$2,989,000 balance relates to Pennichuck Water Works, Inc. and Pennichuck East Utility, Inc. Fixed Asset Lines of Credit (FALOC), which are used to fund Construction Work in Progress on capital projects which will be refinanced into long-term debt obligations or bond indebtedness annually.

Note 3 (Other Current Liabilities) – At June 30, 2019, approximately \$4,723,000 of this balance is comprised of accounts payable which relates to activities that were performed in the second quarter of 2019.

Note 4 (Other Current Liabilities) – At June 30, 2019, approximately \$242,000 of this balance was comprised of accrued interest. These interest costs are associated with the financed amounts for support of corporate operations and 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 2019, \$516,000 was contributed into the Pension Plan, while approximately \$340,000 in benefit payments were made to participants and approximately \$55,000 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 2019 as compared to the second quarter of 2018, and the year-to-date 2019 versus 2018, are as follows:

	(000's)			
	Quarter Ended		Year-to-Date	
	<u>June 30, 2019</u>	<u>June 30, 2018</u>	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Operating Activities:				
Net Income (Loss)	\$ <u>(1,932)</u>	\$ <u>(841)</u>	\$ <u>(4,150)</u>	\$ <u>(2,355)</u>
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:				
Depreciation and Amortization	2,097	2,018	4,194	4,020
Provision for Deferred Taxes	(84)	(136)	(170)	(994)
Other	(13)	(8)	(42)	(19)
Changes in Assets and Liabilities:				
(Increase) Decrease in Accounts Receivable	(1,066)	(1,580)	(626)	(1,097)
(Increase) Decrease in Inventory	(8)	80	11	26
(Increase) Decrease in Other Assets	(1,483)	(1,707)	(381)	(509)
Increase (Decrease) in Accounts Payable	1,799	1,700	(626)	1,291
Increase (Decrease) in Other Liabilities	<u>(622)</u>	<u>(730)</u>	<u>(1,251)</u>	<u>(1,394)</u>
Net Cash Provided by (Used in) Operating Activities	<u>(1,312)</u>	<u>(1,204)</u>	<u>(3,041)</u>	<u>(1,031)</u>
Investing Activities:				
Purchases of Property, Plant & Equipment, including the Debt Component of AFUDC	(1,813)	(1,875)	(2,594)	(2,368)
Proceeds from Sale of Property, Plant & Equipment	-	-	23	-
(Increase) Decrease in Restricted Cash	-	-	-	-
Sale of Investment Securities	-	-	-	-
Change in Deferred Land Costs	<u>(31)</u>	<u>(5)</u>	<u>(29)</u>	<u>(16)</u>
Net Cash Provided by (Used in) Investing Activities	<u>(1,844)</u>	<u>(1,880)</u>	<u>(2,600)</u>	<u>(2,384)</u>
Financing Activities:				
Borrowings (Repayments) on Lines of Credit	(4,024)	(5,025)	(327)	(4,854)
Payments on Long-term Debt	(992)	(858)	(4,134)	(3,853)
Contributions in Aid of Construction	17	80	19	81
Proceeds from Long-term Borrowings	9,056	6,685	9,090	6,697
Debt Issuance Costs	293	426	293	426
Dividends Paid	<u>(70)</u>	<u>(70)</u>	<u>(140)</u>	<u>(140)</u>
Net Cash Provided by (Used in) Financing Activities	<u>4,280</u>	<u>1,238</u>	<u>4,801</u>	<u>(1,643)</u>
Increase (Decrease) in Cash and Cash Equivalents	1,124	(1,846)	(840)	(5,058)
Cash and Cash Equivalents at Beginning of Period	<u>6,376</u>	<u>6,024</u>	<u>8,340</u>	<u>9,236</u>
Cash and Cash Equivalents at End of Period	<u>\$ 7,500</u>	<u>\$ 4,178</u>	<u>\$ 7,500</u>	<u>\$ 4,178</u>

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

Capital Expenditures

Capital Expenditures in the second quarter of 2019 were \$1.9 million as compared to \$1.7 million in the second quarter of 2018. Capital Expenditures for the year-to-date were \$2.5 million as compared to \$2.2 million in 2018.

Major expenditures in the first half of 2019 included:

Gilman Street Main Replacement, Nashua	\$406,000
Merrimack River Intake	\$400,000
Locke Lake Treatment Design	\$211,000
Chase Street Main Replacement, Nashua	\$171,000
Meter Replacements	\$130,000
West Pearl Street Main Improvements, Nashua	\$115,000
Northwest Main Improvements, Nashua	\$113,000

Financing

On February 12, 2019, Pennichuck East Utility, Inc. closed on a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water Revolving Loan Fund Program in the amount of \$4,240,000 for a 30-year term. The loan will be used to finance the cost of the Locke Lake New Groundwater Source project in Barnstead, NH. The funds for this project will be drawn-down during the 2019 and 2020 calendar years.

On February 12, 2019, Pennichuck Water Works, Inc. closed on a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water and Groundwater Trust Fund in the amount of \$3,375,000 for a 30-year term. The loan will be used to finance the cost of the Pennichuck Core Water Main Replacement project. The entire project is scheduled to be completed within 2019.

On April 4, 2019, the Company's Pennichuck Water Works, Inc. subsidiary issued approximately \$8.3 million of tax-exempt and taxable bonds through the NH Business Finance Authority as reimbursement for its 2018 capital improvements in PWW's water supply, distribution and support systems. The bond issuance was approved by the Pennichuck Board of Directors and the Sole Shareholder. This issuance had previously received NHPUC approval on Order No. 26,101, dated February 2, 2018, which authorized up to \$32.5 million in bonds via multiple issuances for the years 2018 – 2021.

On June 12, 2019, Pennichuck Water Works, Inc. closed on a financing transaction with the New Hampshire Department of Environmental Services under the State of New Hampshire's Drinking Water and Groundwater Trust Fund in the amount of \$5.5 million for a 30-year term. The loan will be used to finance the design and construction of a new deep river intake in the Merrimack River, which will provide water to PWW's water treatment plant in Nashua.

Subsequent Events

On July 22, 2019, the Company's Pennichuck East Utility, Inc. subsidiary closed on a term loan financing transaction with CoBank, ACB in the amount of \$1,153,000 for a term of 25 years. The loan proceeds were used to repay Fixed Asset Line of Credit monies borrowed during 2018 for capital projects for that year, which were placed in service by December 31, 2018.