



PENNICHUCK®

Pennichuck Corporation

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

Quarter Ended September 30, 2019

Executive Summary

- Revenues for the third quarter of 2019 were 0.7% higher than the prior year (\$13.9 million for 2019 versus \$13.8 million for 2018). Revenues on a year-to-date basis were 2.0% lower than last year (\$33.9 million for the nine months in 2019 versus \$34.6 million in 2018). Quarterly revenues were slightly higher to prior year results despite a slight decrease in consumption year-over-year, as the Company benefited from the Pennichuck East Utility, Inc. Permanent and Step rate increases which were approved by the NHPUC on Order No. 26,136 and became effective in May and October of 2018, respectively. However, the decrease to prior year results is attributed to a weather-related reduction in consumption levels in the late Spring and early Summer, versus comparative amounts. The Pennichuck Water Service Company revenues were also below 2018 comparative results, due to a reduction in their Unplanned Revenue activities, non-renewal of the Hudson contract in July of 2018 which decreased actuals versus prior year results, and the implementation of ASU 2014-09, *Revenue from Contracts with Customers* which recognizes revenue when goods and/or services are transferred to the customer, as opposed to the ratable amortization of a planned revenue contract which was in use prior to the new FASB pronouncement.
- Operating Income for the third quarter of 2019 was 2.6% higher than the prior year (\$4.0 million for 2019 versus \$3.9 million for 2018). Operating Income on a year-to-date basis was 13.6% lower than the prior year (\$5.1 million for 2019 versus \$5.9 million for 2018). Both of these variances are almost exclusively attributable to the quarter and year-to-date revenue variations as previously discussed.
- Pre-Tax Income for the third quarter of 2019 was \$1.3 million versus \$1.2 million for 2018. On a year-to-date basis, the pre-tax loss was \$3.1 million for 2019 versus pre-tax loss of \$2.2 million for 2018.
- Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA) for the third quarter of 2019 was 5.1% higher than the prior year (\$6.2 million in 2019 versus \$5.9 million for 2018). On a year-to-date basis, EBITDA was \$11.5 million for 2019 versus \$11.9 million for 2018.
- During the quarter, the Company paid approximately \$2.1 million to the City in principal, interest and dividends to fund the City Acquisition Debt. Year-to-date, the Company has paid approximately \$6.4 million to the City in principal, interest and dividends to fund the City Acquisition Debt.
- Capital expenditures for the third quarter of 2019 were \$6.9 million compared to \$4.7 million in the third quarter of 2018. On a year-to-date basis, capital expenditures for 2019 were \$9.4 million compared to \$6.9 million in 2018. The increase in activity year-over-year can be attributed mainly to the Pennichuck Water Works, Inc. Lake Street project in Nashua, which involves the upsizing of almost 3,000 linear feet of 6” diameter water main to 12” diameter, to ensure adequate fire protection flows are provided.

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 2019 as compared to the third quarter of 2018, and the nine months of 2019 as compared to the nine months of 2018, are as follows:

	(000’s)			
	Quarter Ended		Year-to-Date	
	<u>September 30, 2019</u>	<u>September 30, 2018</u>	<u>September 30, 2019</u>	<u>September 30, 2018</u>
Revenues				
Regulated Utilities	\$ 13,201	\$ 13,110	\$ 31,748	\$ 31,946
Other	<u>689</u>	<u>693</u>	<u>2,176</u>	<u>2,640</u>
Total	\$ 13,890	\$ 13,803	\$ 33,924	\$ 34,586
Operating Expenses				
Regulated Utilities	\$ 9,287	\$ 9,262	\$ 26,787	\$ 26,123
Other	<u>639</u>	<u>640</u>	<u>2,026</u>	<u>2,567</u>
Total	\$ 9,926	\$ 9,902	\$ 28,813	\$ 28,690
Operating Income	\$ 3,964	\$ 3,901	\$ 5,111	\$ 5,896
Non-Operational Income (Expense)	143	61	159	58
Net Interest Expense	<u>(2,847)</u>	<u>(2,785)</u>	<u>(8,344)</u>	<u>(8,143)</u>
Pre-Tax Income (Loss)	\$ 1,260	\$ 1,177	\$ (3,074)	\$ (2,189)
Income Tax Benefit (Expense)	<u>(437)</u>	<u>(875)</u>	<u>(253)</u>	<u>136</u>
Net Income (Loss)	\$ 823	\$ 302	\$ (3,327)	\$ (2,053)
Earnings Before Interest, Taxes, Depreciation and Amortization	\$ <u>6,153</u>	\$ <u>5,920</u>	\$ <u>11,512</u>	\$ <u>11,936</u>

Revenues from the water utility operations increased 0.8% in the quarter and decreased 0.6% 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 0.3% in the quarter and 17.6% on an annual basis, respectively. This is primarily due to the June 30, 2018 expiration and non-renewal of the Town of Hudson service contract.

Operating Expenses have increased approximately 0.2% in the third quarter and 0.3% on a year-to-year basis. The increase is mainly attributable to increased direct operating costs associated with increases in transmission and distribution related activities and labor 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 increased slightly in the third quarter by 2.2%, as compared to the third quarter of last year; year-to-date versus last year it has increased 2.5%, 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 2019 versus pre-tax levels for 2018 are due to the revenue and expense variations discussed above.

The year-to-date income tax expense in the current year reflects the treatment for the Municipal Acquisition Regulatory Asset as well as the inclusion of contributions-in-aid-of-construction ("CIAC"), which are not deductible for tax purposes. Therefore, the tax expense is -8.2% versus the statutory rate benefit of 27.08% 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 decreased revenues, increased operating expenses and increased interest expense levels than 2018.

<u>Balance Sheet</u>	(000's)	
	As of <u>September 30, 2019</u> (Unaudited)	As of <u>December 31, 2018</u> (Audited)
<u>Assets</u>		
Property, Plant & Equipment, Net	\$ <u>228,712</u>	\$ <u>221,860</u>
Current Assets:		
Cash	3,245	1,575
Restricted Cash	6,210	3,428
Restricted Cash – Bond Project Funds	46	3,337
Accounts Receivable ^{Note 1}	6,902	6,348
Inventory	592	611
Other Current Assets ^{Note 2}	<u>1,008</u>	<u>1,631</u>
Total Current Assets	<u>18,003</u>	<u>16,930</u>
Other Assets:		
Acquisition Premium	69,765	71,268
Other Assets	<u>12,825</u>	<u>13,076</u>
Total Other Assets	<u>82,590</u>	<u>84,344</u>
TOTAL ASSETS	\$ <u>329,305</u>	\$ <u>323,134</u>
<u>Shareholder's Equity and Liabilities</u>		
Shareholder's Equity	\$ <u>4,963</u>	\$ <u>8,410</u>
Bonds, Notes and Mortgages	<u>206,639</u>	<u>200,225</u>
Current Liabilities:		
Lines of Credit ^{Note 3}	5,419	6,626
Current Portion of Long-Term Debt	6,536	6,019
Other Current Liabilities ^{Note 4}	<u>9,307</u>	<u>8,388</u>
Total Current Liabilities	<u>21,262</u>	<u>21,033</u>
Other Long-Term Liabilities:		
CIAC, net	54,384	51,961
Deferred Income Taxes	14,334	14,110
Accrued Pension Liability ^{Note 5}	9,885	10,021
Other Long-Term Liabilities	<u>17,838</u>	<u>17,374</u>
Total Other Long-Term Liabilities	<u>96,441</u>	<u>93,466</u>
TOTAL SHAREHOLDER'S EQUITY AND LIABILITIES	\$ <u>329,305</u>	\$ <u>323,134</u>

Notes to Balance Sheet

Note 1 (Accounts Receivable) – During the nine months of 2019, the balance in Accounts Receivable increased approximately \$554,000 from the year-end total at December 31, 2018 of \$6,348,000. This is mainly attributed to revenue increases generated at Pennichuck East Utility, Inc., from the NHPUC approvals of Temporary, Permanent and Step increases which became effective in May and October of 2018, respectively.

Note 2 (Other Current Assets) – At September 30, 2019, the balance of \$1,008,000 represents a reduction of \$623,000 from the end of 2018, mainly due to the \$680,000 expensing of prepaid property taxes in the first quarter of 2019.

Note 3 (Lines of Credit) – At September 30, 2019, approximately \$1,281,000 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 \$4,138,000 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 tax-exempt or taxable bond indebtedness annually.

Note 4 (Other Current Liabilities) – At September 30, 2019, approximately \$7,022,000 of this balance is comprised of accounts payable which relates to activities that were performed in the third quarter of 2019.

Note 5 (Accrued Pension Liability) – During the nine months of 2019, \$917,000 was contributed into the Pension Plan, while approximately \$518,000 in benefit payments were made to participants and approximately \$81,000 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 2019 as compared to the third quarter of 2018, and the year-to-date 2019 versus 2018, are as follows:

	(000's)			
	Quarter Ended		Year-to-Date	
	September 30,	September 30,	September 30,	September 30,
	2019	2018	2019	2018
Operating Activities:				
Net Income (Loss)	\$ <u>823</u>	\$ <u>302</u>	\$ <u>(3,327)</u>	\$ <u>(2,053)</u>
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:				
Depreciation and Amortization	2,105	2,022	6,299	6,042
Provision for Deferred Taxes	444	884	274	(110)
Other	(227)	(18)	(269)	(37)
Changes in Assets and Liabilities:				
(Increase) Decrease in Accounts Receivable	72	(1,038)	(554)	(2,135)
(Increase) Decrease in Inventory	8	(13)	19	13
(Increase) Decrease in Other Assets	1,201	1,254	820	745
Increase (Decrease) in Accounts Payable	2,197	(987)	1,571	304
Increase (Decrease) in Other Liabilities	<u>653</u>	<u>1,046</u>	<u>(598)</u>	<u>(348)</u>
Net Cash Provided by (Used in) Operating Activities	<u>7,276</u>	<u>3,452</u>	<u>4,235</u>	<u>2,421</u>
Investing Activities:				
Purchases of Property, Plant & Equipment, including the Debt Component of AFUDC	(6,746)	(4,851)	(9,340)	(7,219)
Proceeds from Sale of Property, Plant & Equipment	198	-	221	-
(Increase) Decrease in Restricted Cash	-	-	-	-
Sale of Investment Securities	-	-	-	-
Change in Deferred Land Costs	<u>109</u>	<u>(3)</u>	<u>80</u>	<u>(19)</u>
Net Cash Provided by (Used in) Investing Activities	<u>(6,439)</u>	<u>(4,854)</u>	<u>(9,039)</u>	<u>(7,238)</u>
Financing Activities:				
Borrowings (Repayments) on Line of Credit	(881)	3,738	(1,208)	(1,116)
Payments on Long-term Debt	(932)	(875)	(5,066)	(4,728)
Contributions in Aid of Construction	5	319	24	400
Proceeds from Long-term Borrowings	3,008	1,390	12,098	8,087
Debt Issuance Costs	34	-	327	426
Dividends Paid	<u>(70)</u>	<u>(70)</u>	<u>(210)</u>	<u>(210)</u>
Net Cash Provided by (Used in) Financing Activities	<u>1,164</u>	<u>4,502</u>	<u>5,965</u>	<u>2,859</u>
Increase (Decrease) in Cash and Cash Equivalents	2,001	3,100	1,161	(1,958)
Cash and Cash Equivalents at Beginning of Period	<u>7,500</u>	<u>4,178</u>	<u>8,340</u>	<u>9,236</u>
Cash and Cash Equivalents at End of Period	<u>\$ 9,501</u>	<u>\$ 7,278</u>	<u>\$ 9,501</u>	<u>\$ 7,278</u>

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

Capital Expenditures

Capital Expenditures in the third quarter of 2019 were \$6.9 million as compared to \$4.7 million in the third quarter of 2018. Capital Expenditures for the year-to-date were \$9.4 million as compared to \$6.9 million in 2018.

Major expenditures in the nine months of 2019 included:

Merrimack River Intake	\$2,688,000
Lake Street Main Replacement, Nashua	\$1,412,000
Deerwood Drive, N.W. Main Improvements, Nashua	\$512,000
Carbon Filter Media Replacement	\$495,000
Gilman Street Main Replacement, Nashua	\$414,000
Manchester Street Main Improvements, Nashua	\$380,000

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/Treatment/Main Replacement 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 has and will be used to finance the cost of the Pennichuck Core Water Main Replacement project, in the northwest portion of the system's distribution system in Nashua. 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.

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.

Subsequent Events

On October 9, 2019, the NHPUC issued NISI Order No. 26,183, with an effective date of November 9, 2019, approving a 4.06% QCPAC (Qualified Capital Project Adjustment Charge) surcharge related to all capital improvements completed and placed in service by PWW in 2018. This surcharge will apply retroactively and going forward to PWW bills rendered after April 4, 2019.