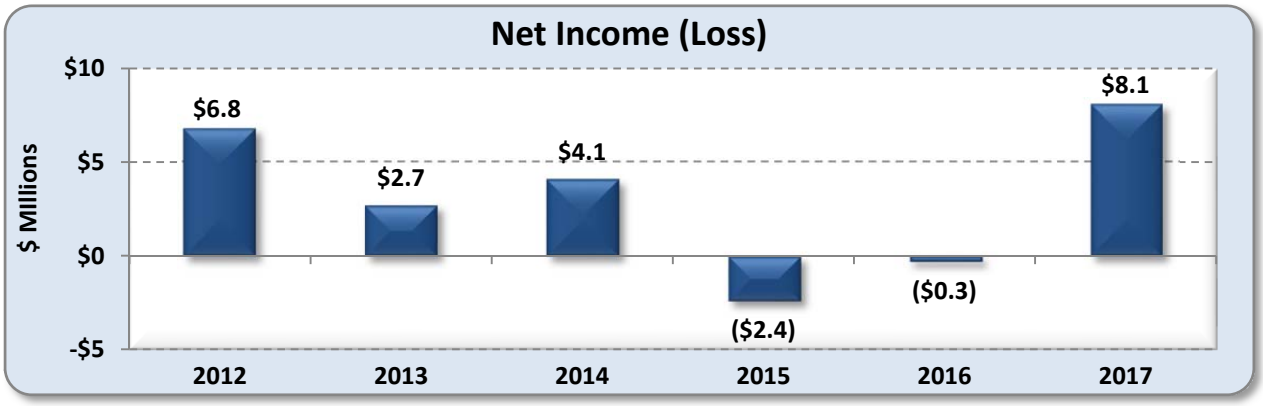
2017 Year End Summary

The District ended 2017 with an $8.1 million net gain, following two years of net losses of $0.3 million in 2016 and $2.4 million in 2015. The District's strategic business model anticipates variability in net income over time due to significant variability in retail revenue sales and power supply costs. In the long run, the District sets rates sufficient to generate positive net income in order to cover operating expenses, power expenses, capital costs in excess of depreciation, and to make interest and principal payments on bonds.

As Chart 1 illustrates, the District's net income (or loss) varies each year. This is a direct result of variability in power expense and retail revenues which are influenced by water flow through the dams, secondary market prices, and weather (a major driver of retail revenues). It is important to note that over the last six years, the District has experienced wide variations on net income. Benton PUD's combined net income for the same period was $19.0 million.

Chart 1



The District maintains adequate reserves in order to handle volatility in revenues and power expense, as seen over the past several years. These reserves help Benton PUD respond to emergencies, provide stable rates, and also help maintain Benton PUD's credit rating from rating agencies. The District has used excess reserves that were generated in years of strong positive net income to lower retail rates, defer future rate actions, and defer future debt issuances.

With 2017 resulting in a strong net gain, the District met its obligation to bondholders and internal planning requirements with a debt service coverage (DSC) ratio of 3.4 times. The DSC ratio measures the amount of net revenues that are available to make bond principal and interest payments. The DSC ratio is an important factor that is evaluated by rating agencies when assigning credit ratings (higher is better).

The District is contractually committed to its bondholders to maintain a DSC of 1.25 times. The District's financial policies require that financial plans are set to achieve a ratio of at least 2.0 times. The DSC ratio has been over 2.0 times for more than a decade.

In Fall 2016, the District issued $22.5 million in bonds to finance capital expenditures and refinance higher interest rate debt. The bond issue resulted in an average interest cost of 3.25%, $15 million available for

capital expenditures, and a net present value savings of nearly 5% on the refunding portion of the bond issue. Despite the net losses in 2015 and 2016, all three rating agencies affirmed the District's current bond ratings (A+ Fitch/S&P, Aa Moody's) due to solid financial reserves, adequate financial metrics, and moderate debt levels. The District is using the funds generated by the bond proceeds to fund a higher than normal capital plan that has new substations, expanding selected current substations, and adding new transmission and distribution lines and substations for increased growth and improved reliability.

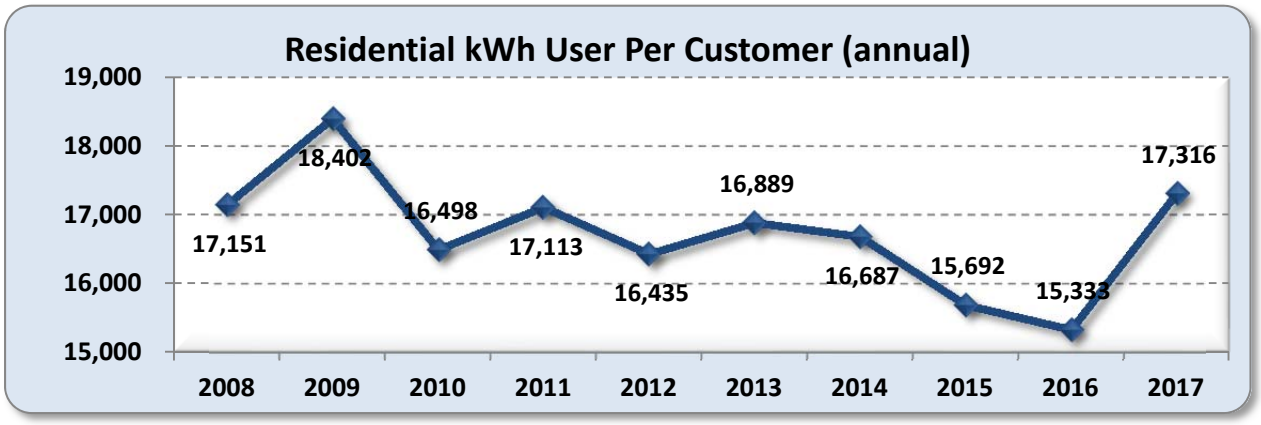
The following sections provide a background on the key factors that contribute to variations in the District's net income (or loss).

Retail Revenues:

Weather has a major influence on how much power customers use. This translates into how much revenue the District collects from its customers. The winter months of 2017 (January, February, and December) were on average 6.0° cooler than normal; also the summer months of the year (June, July, and August) were on average 2.8° warmer than normal. The variances from normal weather resulted in the District's revenues being up $2.4 million from the 2017 original budget projection.

One measure of how temperature affects power usage is a metric known as heating degree days[1]. During 2017, heating degree days were the second highest (2009 being the highest) experienced in over a decade at 111% of average. Cooling degree days in 2017 were the third highest experienced in the past decade at 115% of average. As a result, usage by the District's customers was the second highest in the last ten years, as illustrated in Chart 2.

Chart 2



[1] A "Degree day" is the difference between the actual average temperature for that day and 65° F. If it is warmer than 65°, "cooling" degree days will result. If it is cooler than 65°, "heating" degree days will result.

Each degree over or under 65° is considered a degree day. For example, if the average temperature on April 1 was 55° degrees, you subtract 55 from 65 to get 10 so that day had 10 heating degree days. By adding the degree days for all the days in a month, it provides a way to compare the months to see how much colder or warmer each month was. In the months with a larger number of heating degree days (or cooling degree days), customers will likely have a higher bill.

Power Expense:

The District uses net power expense, power supply expense less secondary market sales, as a means to measure overall financial performance related to power supply management. The District's net power supply expense increased by $2.6 million (2.7%) in 2017 to $80.9 million, primarily as a result of increased purchases to manage higher daily loads as a result of warmer weather. As compared to the original adopted budget, power supply expense increased approximately $150,000.

BPA Contracts

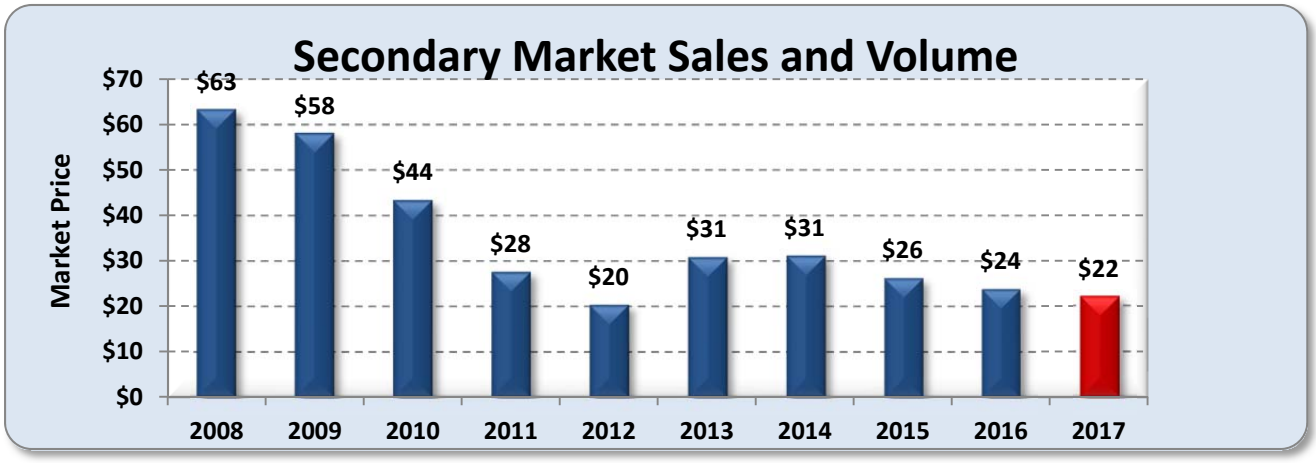
Nearly 80% of the District's power is purchased from the Bonneville Power Administration (BPA). The District is a "Slice" customer of BPA and receives a percentage (or slice) of the total Federal Power System operated by BPA, which is largely made up of hydropower. Generally, the District receives more power than is used by its retail customers and sells the excess on the secondary market. Revenues from these "excess" secondary market sales are used to "buy down" customer rates. This is referred to as being "long on power." Hydropower output can be volatile and varies based on the amount of water that flows down the rivers. The District manages the risk associated with the high degree of variability in power costs by proactively hedging future projected needs and maintaining adequate financial reserves.

Secondary Market Price

Secondary market prices have been declining since 2008/2009 as illustrated by Chart 3. The decline is largely attributable to a drop in natural gas prices, reduced demand, and an increase in power generating resources (solar and wind).

Since the District is a net seller of power into the market, lower secondary market prices have resulted in lower revenue from secondary market sales, which are used to partially offset power supply cost increases and ultimately help to buy down retail rates. In 2017, the average price the District received on the secondary market was $22/MWh compared to about $60/MWh in 2008/2009. Even with additional power to sell due to lower than planned retail sales to customers, 2017 experienced the second lowest secondary market sales revenue in the last decade.

Chart 3



Looking Ahead

As the District looks to the future, we are seeing a declining long-term trend in use per customer leading to flattening retail load. Streamflows in 2018 are expected to be above average at 120%, which may provide for more excess power to sell thus more revenue; however, the District anticipates secondary market prices will remain about the same or continue to drop even further due to excess generation. The 2018 retail revenue budget is slightly below 2017 actual and the secondary market sales budget is 10% less than last year. As noted earlier, the District receives the majority of its power from BPA which continues to see increasing cost pressures. The District anticipates BPA to continue to raise its rates in the future leading to increasing power costs. The District is not planning a rate increase in 2018.

To review the District's 2017 annual financial report, click here.

For a more comprehensive review of District financial policies and planning, please click here.