Tennessee Valley Authority

Fourth Quarter Fiscal Year 2019 Investor Media Call

November 15, 2019 at 9:15 a.m. Eastern

CORPORATE PARTICIPANTS

Jeff Lyash – *President and Chief Executive Officer*

John Thomas – *Executive Vice President and Chief Financial Officer*

Tammy Wilson – *Vice President, Treasurer, and Chief Risk Officer*

PRESENTATION

Operator

Good morning, everyone, and welcome to the Tennessee Valley Authority's Fourth Quarter Fiscal Year 2019 Conference Call. For your information, today's conference call is being recorded. If anyone on today's conference should need operator assistance, you can do so by pressing star and zero.

At this time for opening remarks, I would like to turn the conference call over to Ms. Tammy Wilson, TVA Vice President, Treasurer, and Chief Risk Officer. Ms. Wilson, please go ahead.

Tammy Wilson

Thank you, Jamie. Good morning, and welcome to the Tennessee Valley Authority's Fourth Quarter Fiscal Year 2019 Financial Review. It's somewhat unusual to be having an annual earnings call in November but TVA is a bit different in that our year end is on September 30th. Thank you for taking the time to be with us this morning. It was great to see many of you at our EEI Financial Conference earlier this week.

For our call today, I have with me TVA's Chief Executive Officer, Jeff Lyash, and TVA's Chief Financial Officer, John Thomas. Jeff will begin with the business update and then John will follow with the review of TVA's financial performance. After our prepared remarks, the call will then be opened up to give our participants the opportunity to ask questions.

Now for a few housekeeping items. Today's press release and TVA's Annual Report on Form 10-K for the fiscal year ended September 30, 2019 are available on TVA's website, and that's www.TVA.com. A replay of this call will also be available on TVA's website for a period of one year.

Today's call may include forward-looking statements that are subject to various risks and uncertainties, please refer to our Annual Report on Form 10-K for the fiscal year ended September 30, 2019 for a discussion of these factors.

With that, I will now turn the call over to TVA's President and Chief Executive Officer, Jeff Lyash.

Jeff Lyash

Thank you, Tammy. Good morning, everyone, and thank you for joining us on today's call. I'm pleased to say that TVA's financial and operational performance for fiscal year 2019 was among the strongest we've seen in recent history.

But before I discuss our performance in more depth, I want to stress that we could not have achieved many of these successes without the partnership of our local power companies and their customers. As you all know, I'm a strong supporter of the public power model and its role in helping achieve TVA's mission. That mission is delivering reliable power at the lowest feasible cost, caring for our region's natural resources, and creating and investing in sustainable economic growth. To further strengthen the connection between TVA and its local power company partners, the TVA Board approved a long-term partnership option at its August meeting. This initiative allows local power companies to enter into 20-year partnership agreements with TVA, more closely aligning our collective long-term commitments and reducing risk.

In exchange for longer contract terms, these Valley partners receive a monthly bill credit of 3.1% of wholesale demand, energy and grid access charges. The bill credit means customers that sign up for the longer contracts will pay lower effective base rates. TVA can offer this financial incentive in large part because of the significant progress we made in reducing costs in recent years.

And, our partners will be more involved in working with us on TVA's long-term business planning going forward, a step we began discussing earlier this month at a kick-off meeting for the long-term partners. I'm excited that more than 85% of our LPCs have already signed a new 20-year partnership agreement, meaning more than half of our annual base revenue is now under contract for a rolling 20-year term.

These commitments demonstrate the confidence that our customers have in a shared future with TVA and in the public power model. We believe that the success TVA had in 2019 and in recent years has inspired the long-term commitments of our customers that they are making in TVA.

And, in 2019, we had another good year for public power in the Tennessee Valley; 54% of power TVA generated in 2019 came from carbon free sources. We achieved another consecutive year, our 20th straight, of delivering power with 99.999% reliability. That's five nines. The TVA Board approved a new Integrated Resource Plan that gives directional guidance on how TVA can provide low cost, cleaner, and reliable electricity in the Tennessee Valley over the next 20 years.

TVA completed physical work for the Browns Ferry extended power uprate. This project will significantly increase the amount of carbon free generation capacity at the plant by 465 megawatts. That's enough to power approximately 280,000 homes.

We released our first environmental, social and governance report, or ESG, for the financial community in August, using the investor-driven ESG reporting standards developed by the Edison Electric Institute.

TVA reduced its financial obligations by $1.5 billion, driving our debt to the lowest level in almost 30 years. With the strong results we've had in recent years from executing our long-term plan, we were able to avoid a base rate increase for the first time in six years, and we hope to extend stable rates through the recently-approved ten-year long-range financial plan while we maintain debt in the target range of $18 billion to $20 billion and hold cost escalation below inflation.

2019 was a great year for TVA, and we look forward to building on those positive results in 2020 and beyond.

Even though we've been busy planning for the future, we can never look past the present to ensure that we deliver reliable power on a daily basis to our customers. I already mentioned that TVA achieved five nines' reliability for the 20th consecutive year. That's an impressive track record of reliability. But, it's even more impressive that our fleet performed so well in the face of adverse weather conditions. September's unprecedented heat wave produced average temperatures seven to nine degrees above normal, including the hottest September on record for Memphis, Tupelo, and Jackson. The heat wave set new September load demand records for TVA, including nine days where demand was greater than 28,000 megawatts. During this extreme weather, TVA's diversified portfolio maintained reliable power throughout the service territory.

This reliability is a result of many factors, including investment in our fleet, the dedication of our workforce and the desire for continuous improvement and performance excellence. We recognize this excellence, but we also appreciate it when others recognize it as well, which is why we're delighted to learn that S&P Global Platts has selected TVA's Browns Ferry EPU project as a finalist for the Global Energy Awards in the Construction Project of the Year classification. This nomination confirms what we already know that the success of this strategic project was the direct result of TVA employees working tirelessly to achieve excellence.

TVA's strategic planning for renewable energy is also a Global Energy Award finalist in the Award of Excellence power category. TVA's Boone Dam Project was also recently selected as the nation's Most Outstanding Geological and Engineering Project by the Association of Environmental and Engineering Geologists. The project was specifically noted for its innovative use of georeferencing data, risk-informed decision-making, and contributions to the practice of underground construction in dams.

As we continue to invest in our fleet, and make the right strategic decisions for reliability, remember that TVA has made great strides in providing energy that is also cleaner, and we will continue to do so. TVA's system carbon emissions rate is forecasted to approach a 60% reduction by 2020 and a 70% reduction by 2030 from a 2005 baseline.

Renewable energy continues to grow. As we've noted in recent announcements, our partnerships with Google, Facebook, the US military and our LPCs and other stakeholders are bringing more solar to the Valley. We also announced a request for proposal for an additional 200 megawatts of renewable energy this year. And those renewable energy additions are just beginning. The new IRP calls for a significant amount of solar additions and storage on the system over the next 20 years. TVA has committed to a cleaner energy future and to the development of solar power in the Tennessee Valley. In fact, we are proactively evaluating a path to incorporate utility-scale solar into our generation fleet.

Robust strategic planning, reliable electricity, and a commitment to a cleaner energy future, all continue to help TVA attract jobs and investment to the Valley. In FY19, companies announced capital investments of over $8.9 billion and the expected creation or retention of approximately 66,500 jobs in the Tennessee Valley. Recognizing the success of TVA and its economic development partners, *Site Selection* magazine named TVA a top utility for economic development for the 14th year in a row. We're proud of these efforts as we continue to focus on our mission of fostering sustainable economic development.

Let me now turn the call over to John Thomas. John will provide you with details on TVA's financial performance in fiscal year 2019. John?

John Thomas
Thanks, Jeff. I'll begin with the highlights. Overall year-over-year operating revenues were essentially flat. We had lower sales impacted slightly by weather offset by the base rate adjustment the Board enacted last October. Overall operating expenses were 2% lower, interest expense down 4%, driven by lower debt levels, and overall net income of $1.4 billion.

On the weather side, 2019 was a very hot summer. This chart shows cooling degree days which really is a predominant driver of overall electricity sales. You can see 2019 is significantly above normal, but 2018 was even more extreme. Relative to our budget and relative to what we planned for actually higher, but slightly less than last year that drove less volume.

Another interesting aspect of the summers are that the spring and the fall seasons are starting to change in terms of what we've seen over the last several years. This chart shows September of 2019 and the blue solid line represents what normal cooling degree days would look like. And as you would expect, over the course of the month of September, it begins to get cooler and therefore you have less cooling degree days. The blue bars represent what we saw in September. And, as you can see it was as hot at the end of September as it was at the beginning of September, and that continued into early October. While this may be good from a revenue perspective, it has impacts on us operationally as typically in the fall and the spring is when we do our maintenance outages and our nuclear refueling outages. This creates pressure on the system. It causes us to adjust operationally. I'm happy to say that our operating fleet performed quite well during the September and early October period as we continued to have extremely high reliability.

Overall in terms of power sales, they were down 1%, as I said, driven by slightly milder weather than last year but still well above normal. Overall operating revenues, base revenue up $200 million which is essentially the impact of the base rate increase, and fuel revenue down $140 million. With that volume, overall happy to say that we continue to see the fleet perform well, the diversified fleet allowed us to have an overall fuel rate that was 4% lower than it was in the previous year.

If you look at where the power supply came from in our fleet this year versus last year, overall nuclear generation about the same as it was in 2018. We had a very wet year this year and overall, hydro generation was higher. Lower coal, about the same natural gas but with slightly lower natural gas prices. This is where you see the diversity of this fleet and the ability to take advantage of the hydro generation, the ability to dispatch lower cost of gas that displaces coal and the optimization of that resulted in a lower fuel rate for our customers.

In terms of the income statement, operating revenue up $85 million, slightly higher. Overall fuel expense, $119 million higher, but the overall effective rate was lower. Operations and maintenance expenditures were heavily driven by the write-off decision at Bull Run and Paradise. Some of those write-offs impacting O&M and some of them impacting depreciation and amortization. The good news is underneath this we continue to see favorability in our controllable operating expenses, and more of the cash expenses within each of the business units.

We were roughly $80 million favorable to our plan this year. Our plan includes us offsetting about $150 million worth of inflationary pressure, we continue to see a strong focus on efficiency and maintaining the O&M reductions that we've achieved over the last several years.

Interest expense was lower by $45 million driven by the lower debt levels, and net income of $1.4 billion or about $300 million higher than the prior year. Overall operating cash flows at $3.7 billion, just slightly lower than last year. Investing essentially the same as what we saw in the prior period. Overall financing activities just allowed us to reduce our debt by $1.5 billion, now at the $22.8 billion level, which as Jeff said, is the lowest in about 30 years. Essentially flat operating revenues, lower operating expenses, continue to focus on efficiency, and our controllable O&M, successfully executing on our debt reduction plans and overall in a strong financial position moving into our next ten-year financial plan.

With that, I'll turn it over to Jamie to queue up your questions.

QUESTIONS AND ANSWERS

Operator
Ladies and gentlemen, we will begin today's question and answer session. To ask a question, you may press star and then one, using a touchtone telephone. If you are using a speakerphone, we do ask that you please pick up the handset before pressing the keys to ensure the best sound quality. To withdraw your question, you may press star and two. Once again, that it is star and then one to ask a question. We will now pause momentarily to assemble the roster.

And once again, that is star and then one to ask a question. We do have a question from David Flessner from *Chattanooga Times Free Press*. Please go ahead with your question.

Mr. Flessner, your line is open. Is it possible your phone is on mute?

David Flessner
I'm sorry. Good morning. Thanks for taking the call. I appreciate it. A quick question relative to the pension fund and the TVARS plan. With the reduction in the discount rate, it appears that your unfunded liability increased quite a bit, as much as what your earnings were. Can you comment a little bit about the pension fund and your plan to reach full funding on that and what the implications are and going forward that you're planning to put more money into the pension plan?

John Thomas
Yes. Thanks, Dave, this is John. Yes, you're right, the discount rates were extremely low this year and as you calculate the liability, you're dividing these long-term obligations by a lower number, so it increased the liability. We had a really strong year overall in terms of returns for the plan. You remember there was a market selloff back last December. We were able to earn about 5% even with that selloff, 13% in the calendar year, actually. We're able to hold the asset balance flat. We earned as much as what the payouts were. We sit today at 60% funded.

Five years ago, we put together this long-term plan to fully fund the pension, and that included us putting $300 million in a year. Several years ago, we decided to put an incremental $500 million that we would ensure, to a greater level of confidence, that we would achieve that funded status. Through this year, even with this substantial increase in the liability, we're essentially right where we thought we'd be on the plan that we put together five years ago. We're right on target.

I think it shows that that $500 million that we put in over and above what the commitment was, to ensure that we could either take a market downturn or if there was a liability increase, we'd still be in line with what we thought, so that was $500 million was well-invested in the pension plan.

David Flessner
Is the long-term debt obligations you show then, the unfunded liability—I wasn't sure if it's $4.9 billion or $5.2 billion, I saw different numbers—but is that including the long-term debt obligations? And what's the best number, $4.9 billion or $5.2 billion, as unfunded liability?

John Thomas
Probably the best way to think about the liability is to take the $13.3 billion, which is our full liability, and subtract out the roughly $8 billion in assets. The $5.2 billion when looking at that, that would be the better number to use, yes. Now, that's not included in our—

David Flessner
That's not included in your long-term debt obligations.

John Thomas
That is not. No, that's not part of our total financing obligations. Our total financial obligations is our short-term debt, our long-term debt, and our other lease obligations, yes.

David Flessner
And that's not a cause for concern? I mean you're still confident you can fully fund that. It seems—

John Thomas
Yes. We're right where we thought we'd be five years ago, when we put the plan together. We had a plan for the pension that included improving it to fully fund it and we're right in line with what we thought, and we're well ahead of where we thought we'd be in debt reduction. When you net the two together, we're still well ahead of where we thought we would be.

David Flessner
Thank you. Appreciate it.

CONCLUSION

Operator
Once again, if you would like to ask a question, please press star and one. And ladies and gentlemen, at this time, and showing no further questions, I'd like to turn the conference call back over to Mr. Lyash, for any closing remarks.

Jeff Lyash
Okay, again, thank you for your time this morning. At TVA, we're dedicated to partnering with our stakeholders because it's the best way to fulfil our mission. All the highlights I mentioned on this call were a direct result of that partnership and of the efforts of our dedicated workforce. And as we move TVA forward, we'll continue to collaborate to achieve all that we've set out to do, because in the end, this partnership approach helps create the most value for the ten million people who count on us each and every day. Thank you all for your time today.

Operator
Ladies and gentlemen, that does conclude today's conference call. We do thank you for joining today's presentation. You may now disconnect your lines.