Item #170719

Gainesville Regional Utilities

2017 Series C

Synthetic Alternatives

January 11, 2018

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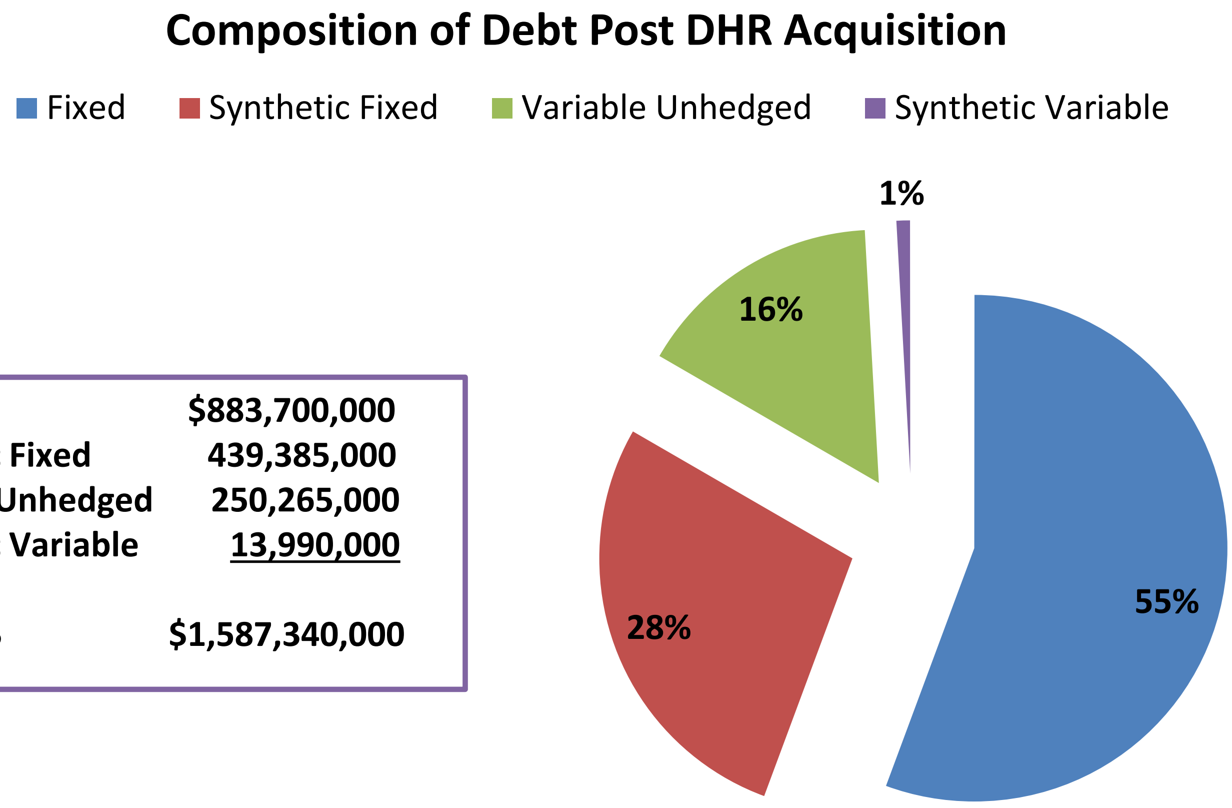
Scenario 2: 85% Fixed / 20% Synthetic/ 15% Fixed

Sources and Uses	2017 A 85% Fixed	2017 B 20% synthetic	2017 C 15% Variable	Total*
Sources				
Par Amount	$415,920	$150,000	$115,000	$680,920
Premium	73,205			73,205
Total	**$489,125**	**$150,000**	**$115,000**	**$754,125**
Uses				
GREC Purchase Proceeds	$485,844	$149,454	$114,700	$750,000
UD/COI	3,275	545	299	4,120
Total	**$489,125**	**$150,000**	**$115,000**	**$754,125**

* Excludes contingency amounts

- GRU closed the GREC transaction in early November which consisted of 3 series of bonds
  - 2017 A: Fixed rate bonds
  - 2017 B: Synthetically fixed rate bonds
  - 2017 C: Variable Rate Bonds
- For the 2017 C Bonds
  - Bonds will pay a variable rate of interest based on 70% of LIBOR plus a spread reflecting GRU's current credit ratings
  - The rate is reset each month, based on changes in 1 Month LIBOR
  - Currently, 70% of 1 Month LIBOR is ~1.05%
  - Including the credit spread, the initial rate GRU pays is ~1.46%
  - GRU budgets for the long-term variable rate to be ~2.75%
- GRU has the opportunity to address the variable interest rate risk associated with the 2017 Cs through the use of financial products such as collars, swaps, or an interest rate cap

GRU Outstanding Debt @ 12/31/2017



Fixed	**$883,700,000**
Synthetic Fixed	**439,385,000**
Variable Unhedged	**250,265,000**
Synthetic Variable	**13,990,000**
Total O/S	**$1,587,340,000**

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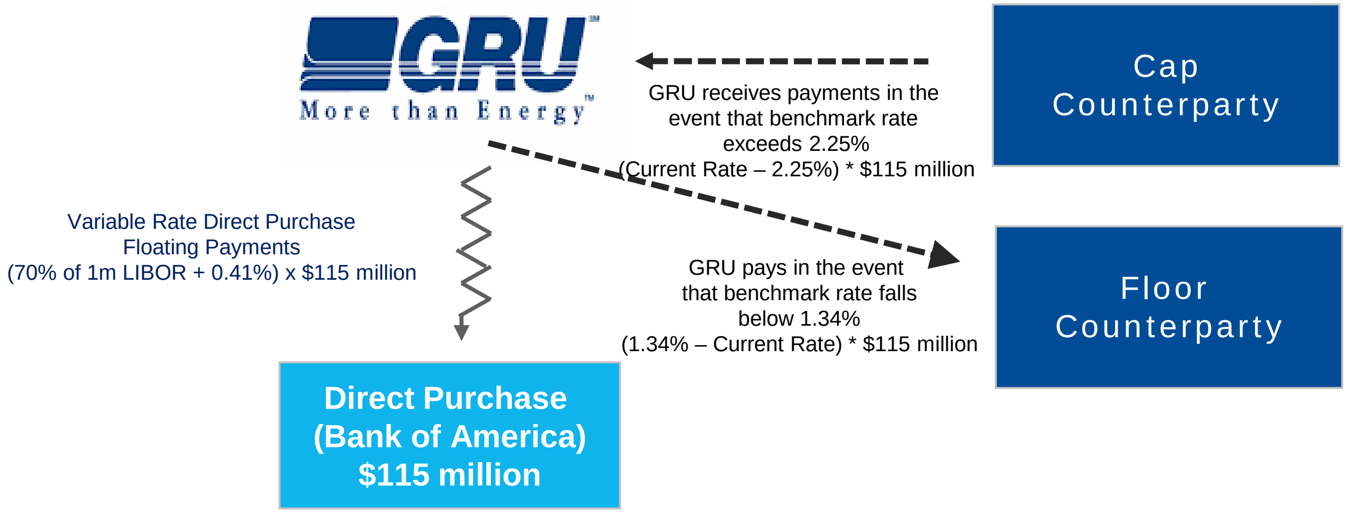
2017 C: Direct Purchase and Interest Rate Collar[1]



- To implement the "costless collar", GRU enters into 2 interest rate option transactions
  - GRU would purchase an interest rate cap – counterparty would make a payment to GRU when rates are above that amount
  - GRU would sell an interest rate floor – obligates GRU to make a payment when rates fall below that floor
  - The premium GRU received would likely offset the cost of the cap
- No payments are exchanged if the benchmark rate remains between the strike rate of the cap and the collar
  - If rates increase above the cap strike rate, GRU receives a payment from the collar counterparty
  - If rates fall below the floor strike rate, GRU makes a payment to the collar counterparty
- GRU would have protection in a rising interest rate environment but would not benefit if variable rates are low, as they were in 2016, since the floor would require a GRU payment if rates are low
- The "band" between the cap and the collar can be adjusted based on the preferred strike rates as well as direction of collar

[1] Rates effective 18 December 2017 and subject to change

Collar Example: Rates Increase Above Cap Rate

Assume Cap Rate 2.25, Floor Rate 1.34, 25 Year Term

GRU receives:
(5% LIBOR – 2.25% cap rate)
X $115 million

Cap Counterparty

Variable Rate Direct Purchase
Floating Payments
(70% of 1m LIBOR) x $115 million
5.0% X $115 million
Plus credit spread

Direct Purchase (Bank of America) $115 million

115,000,000 Par of 2017 Series C Bonds
<u>X 5%</u> 70% 1 Month LIBOR
5,750,000 Interest GRU pays to 2017 Series C Bondholders

5% 70% 1 Month LIBOR
<u>Less 2.25% Cap Rate</u>
2.75% X $115,000,000
$3,162,500 Payment from Cap Counterparty

$2,587,500 GRU **<u>Net</u>** Payment
2.25% Effective Rate for 2017 Series C Bonds = Cap Rate

- At rates above the cap rate (2.25%), GRU receives a payment that offsets the higher variable rate associated with the 2017 Series C Bonds
- Assume 70% 1 month LIBOR rises to 5.0% for the year

1. Rates effective 18 December 2017 and subject to change

Collar Example: Rates Decrease Below Floor Rate

Assume Cap Rate 2.25, Floor Rate 1.34, 25 Year Term

GRU pays:
(1.34% Floor Rate – 70% 1 Month LIBOR)
X $115 million

Floor Counterparty

Variable Rate Direct Purchase
Floating Payments
(70% of 1m LIBOR) x $115 million
1.0% X $115 million
Plus credit spread

Direct Purchase (Bank of America) $115 million

115,000,000 Par of 2017 Series C Bonds
<u>X 1%</u> 70% 1 Month LIBOR
1,150,000 Interest GRU pays to 2017 Series C Bondholders

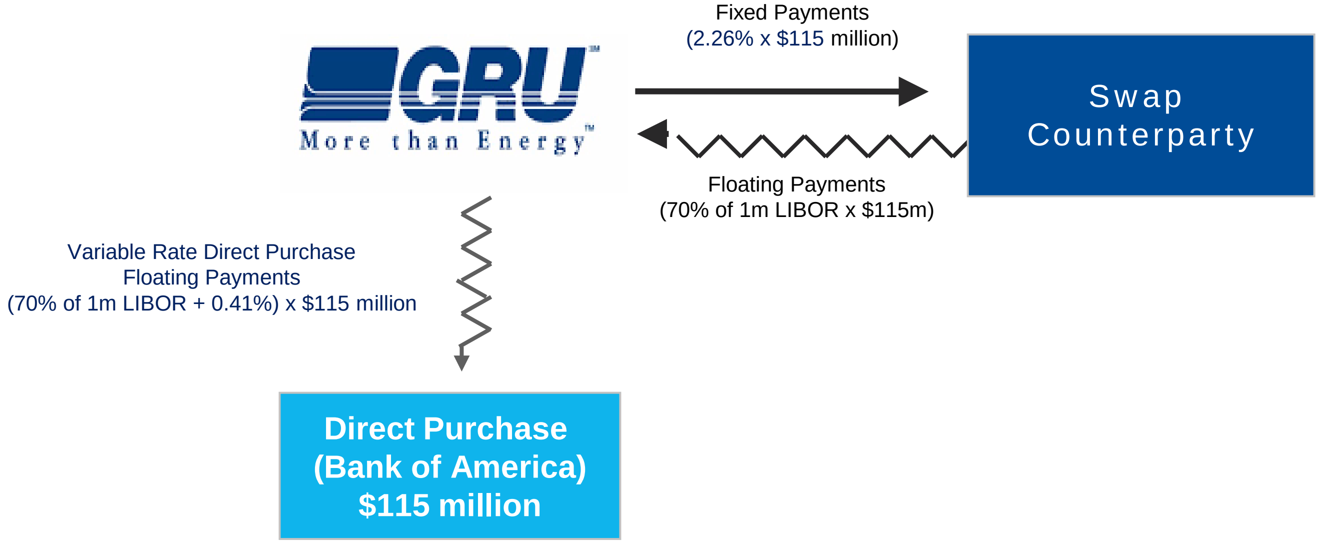
1.34% Floor rate
<u>Less 1.0% 70% 1 Month LIBOR</u>
0.34% X $115,000,000
$391,000 Payment to Floor Counterparty

$1,541,000 GRU **<u>Net</u>** Payment
1.34% Effective Rate for 2017 Series C Bonds = Floor Rate

- At rates below the floor rate (1.34%), GRU makes to the counterparty
- Assume 70% 1 month LIBOR falls to 1.0% for the year

[1] Rates effective 18 December 2017 and subject to change

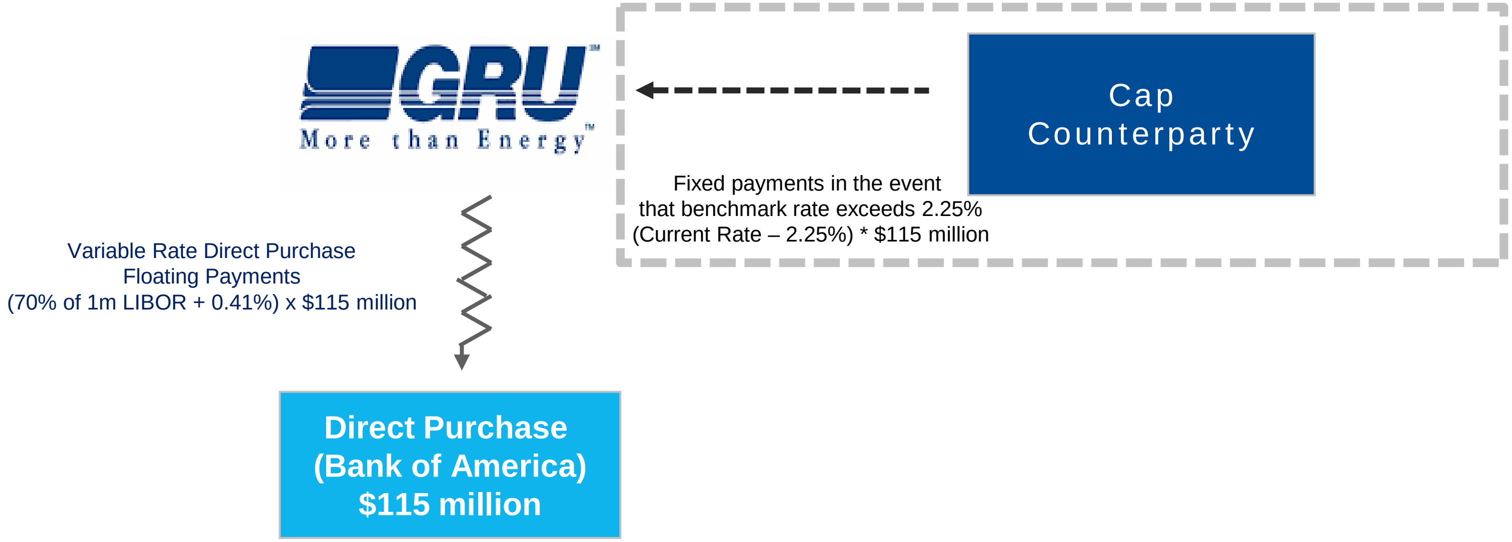
2017 C: Direct Purchase and Fixed Payer Swap[1]



- A fixed "payer" interest rate swap allows GRU to effectively convert the Bank of America Direct Purchase (floating rate debt) to fixed rate debt
- With the swap, GRU becomes a "fixed rate payer", paying a *predetermined* fixed rate and receiving a floating rate payment from the swap counterparty
- The variable rate received by GRU from the swap counterparty "flows" to Wells Fargo for the Direct Purchase.
- GRU's debt cost for this part of the transaction equals the fixed swap rate + credit spread plus any ancillary fees
- GRU can have the ability to cancel the swap at pre-determined times
  - Cancel in 10 years — Swap rate of 2.26% (as illustrated in diagram above)
  - No cancellation Option — Swap rate of 1.79%

1. Rates effective 20 December 2017 and subject to change

2017 C: Direct Purchase and Interest Rate Cap [1]



- GRU can also purchase an interest rate cap
- With an interest rate cap, the counterparty will pay GRU in the event that a determined benchmark rate exceeds a certain, contractual level
- Allows GRU to benefit when variable rates are low while also providing some protection in the event that variable rates exceed that contractual level
- GRU can have the ability to set the parameters of the cap (contractual cap rate and duration of the cap) and this will influence the premium paid
  - 2.25% Cap, effective through maturity of 2017Cs — GRU pays a premium of $7.54 million
  - 2.25% cap, effective for 10 years — GRU pays a premium of $2.11 million

1. Rates effective 18 December 2017 and subject to change

Advantages and Disadvantages of Interest Rate Collar

ADVANTAGES:

- Floor and Cap strikes can be set so that no upfront cash outlay required (Zero Cost Collar)
- Mitigates interest rate risk above the Cap strike rate

DISADVANTAGES:

- No ability to benefit if future decline in interest rates below Floor strike rate
- May immediately increase floating rate debt cost depending on level of Floor strike rate
- Collar mark-to-market value will become negative if rates decline
- Possible collateral posting requirement depending on terms of the ISDA Agreement
- Credit exposure (default risk) to bank counterparty
- Large bid/offer spread (transactions costs) for long-dated interest rate options

Advantages and Disadvantages of Interest Rate Cap

ADVANTAGES:

- Mitigates interest rate risk above the Cap strike rate
- Ability to benefit if interest rates decline or remain unchanged
- Can set Cap strike rate out of the money (above current rates) if only need “disaster insurance”
- Cap always remains an asset to purchaser (can never have a negative mark-to-market value)

DISADVANTAGES:

- Upfront cash outlay (premium) required
- Credit exposure (default risk) to bank counterparty
- Large bid/offer spread (transactions costs) for long-dated interest rate options

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Bank of America Costless Collar Proposal Matrix

Current 70% 1m LIBOR Reset: 1.05%

Effective Date 12/18/17

70% 1 Month LIBOR Costless Collar Floor Strike			
		Floor Strike Rate	
Cap Strike Rate	5 Year	10 Year	25 Year
2.25%	1.16%	1.23%	1.34%
2.50%	1.05%	1.09%	1.20%
2.75%	0.94%	0.95%	1.19%

Bank of America Upfront Premium Interest Rate Cap Proposal
Effective Date 12/18/17

70% 1 Month LIBOR Cap - Upfront Premium			
Strike Rate	**5 Year**	**10 Year**	**25 Year**
2.25%	**$535,000**	**$2,114,000**	**$7,535,000**
2.50%	**$376,000**	**$1,625,000**	**$6,243,000**
2.75%	**$262,000**	**$1,252,000**	**$6,473,000**

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Synthetic Alternative Product Comparison

Assuming 2.25% Cap Strike Rate, 25 Year Term				
Excluding 41 BP Credit Spread (consistent for all products)				
Non-cancellable swap	1.79%	Collar	never pay less than 1.34%, never pay more than 2.25%	
Swap cancellable in 10 years	2.26%			
Interest rate cap , up front payment	$ 7,535,000			

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Synthetic Alternative Product Comparison

Assuming 2.25% Cap Strike Rate, 25 Year Term			
Excluding 41 BP Credit Spread (consistent for all products)			
Non-cancellable swap	**1.79%**	**Collar**	**never pay less than 1.34%, never pay more than 2.25%**
Non-cancellable swap preferable to collar if rate >1.79		Collar preferable to non-cancellable swap if rate below 1.79	
1 - 46 BPS if rate between 1.79 & 2.25		1 - 45 BPS if rate between 1.34 & 1.79	
46 BPS if rate above 2.25		45 BPS if rate below 1.34	
Both of these products carry some similar risk factors: mark-to-market risk, potential collateral posting, counterparty risk			
<u>**Swap cancellable in 10 years**</u>	**2.26%**		
From a rate perspective, non-cancellable swap and collar are preferable			
However, option to cancel at 10 years mitigates some of the mark-to-market, collateral posting and counterparty risk associated with other products			
<u>**Interest rate cap , up front payment**</u>	**$ 7,535,000**		
Requires up front out of pocket cash outlay			

QUESTIONS?

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