

Associated Electric Cooperative Inc.

A Touchstone Energy[®] Cooperative 

Financial Statements

For the Quarterly Periods Ended

March 31, 2020 and 2019

MANAGEMENT'S DISCUSSION AND ANALYSIS

Associated Electric Cooperative, Inc. (Associated) is pleased to present the enclosed interim financial statements, which include balance sheets, statements of revenues and expenses, and statements of cash flows as of, or for the periods ended March 31, 2020 and 2019. The discussion below is not meant to be comprehensive but rather to identify significant aspects in the current quarter and year-to-date performance of Associated.

Overview

Net margin for the three-month period ended March 31, 2020, was \$46.3 million as compared to \$39.1 million in the same period of 2019. Total assets were \$3.0 billion at March 31, 2020 as compared to \$3.1 billion at March 31, 2019. Significant factors contributing to Associated's financial performance for these periods are discussed in detail in the paragraphs below.

Operating Revenues

Revenue from members for the quarter ended March 31, 2020, decreased \$21.4 million, or 8.1%, as compared to the same period of 2019. Member revenue consists of an energy and a demand component. Energy revenue decreased \$16.3 million due to an 8.3% decrease in energy sales volume primarily related to weather, as compared to the same period of 2019, and a board-approved \$0.50/MWh energy discount for 2020. Demand revenue decreased by \$5.1 million due to a decrease in billing demand determinants, as compared to the same period of 2019. Associated's board approved a demand rate discount of \$1.12/kWh for both 2019 and 2020.

Revenue from nonmembers decreased \$0.9 million, or 1.2%, for the first quarter of 2020 as compared to the same period of 2019. The decrease was primarily due to a \$1.1 million decrease in nonmember energy sales. Interchange sales volume increased 26.5% mostly due to increased sales into the MISO market from the Dell generating unit. The increase in sales volume was more than offset by a decrease in the weighted average sales price as a result of decreased natural gas prices for the three-month period ended March 31, 2020, as compared to the same period of 2019.

Generation Operation

Generation operations expense decreased \$28.4 million, or 17.6%, for the first quarter of 2020 as compared to the same period of 2019. The decrease was primarily due to both lower coal and gas fuel expense. Coal generation decreased 574,042 MWh, or 14.3%, and the weighted average cost of coal burned was 8.4% lower for the first quarter of 2020 as compared to the same period of 2019. Gas generation increased 496,857 MWh, or 17.9%, as compared to the first quarter of 2019, primarily at the Chouteau power plant due to low natural gas prices in the Oklahoma market and the Dell power plant due to additional sales into the MISO market over 2019. The increased gas generation was more than offset by

lower natural gas prices, which resulted in a 33.5% decrease in the average fuel cost/MWh for the gas fleet.

Generation Maintenance

Generation maintenance expense decreased \$3.9 million, or 17.7%, for the first quarter of 2020 as compared to the same period of 2019. The decrease was primarily due to the elimination of the deferred maintenance program at the end of 2019. The first quarter of 2019 included amortization of deferred maintenance projects, but Associated's board approved the recovery of previously deferred maintenance costs at the end of 2019. Partially offsetting this decrease was an increase in variable fees for the gas plants due to increased generation for the first quarter of 2020 as compared to the first quarter of 2019.

Financial Position:

Significant changes in the balance sheet at March 31, 2020, as compared to the prior year include the following:

- Utility plant, including construction work in progress, increased \$105.3 million, or 2.5%, primarily due to boiler component, generator and environmental projects at the New Madrid power plant and various ongoing projects at the Thomas Hill and Dell power plants. Accumulated depreciation increased \$96.5 million, resulting in an increase in utility plant, net of accumulated depreciation, of \$8.8 million, or 0.4%.
- Other restricted and designated assets and restricted short-term investments decreased \$209.7 million, or 42.8%, primarily due to the prepayment of Federal Financing Bank (FFB) debt out of the cushion of credit in the amount of \$228.0 million including accrued interest.
- Cash and cash equivalents increased \$120.8 million, or 143.8%, primarily due to funds provided by operating activities, partially offset by expenditures for plant additions.
- Accounts receivable decreased \$12.1 million, or 10.2%, primarily due to lower member sales resulting from lower sales volume, a \$0.50/MWh energy discount and lower nonmember energy sales.
- Fuel inventories increased \$9.3 million, or 21.5%, primarily due to a 68.9% increase in tons of coal on the ground as compared to March 31, 2019.
- Patronage capital increased \$33.4 million, or 5.0%, due to margins and the retirement of \$23.5 million in patronage capital in May of 2019.
- Long-term debt, including current maturities, decreased \$232.3 million, or 12.5%. This decrease was due to a prepayment of \$226.9 million of FFB debt through use of the Cushion of Credit investment. The Agriculture Improvement Act of 2018 allowed balances in the cushion of credit to be used to pay FFB debt without penalty. Debt was

further reduced by a reduction in the line of credit balance of \$100.0 million and principal payments of \$93.0 million. These decreases were partially offset by advances from FFB of \$77.4 million for a plant equipment loan; \$48.8 million for a plant-purchase reimbursement; \$44.4 million for a New Madrid Unit 1 project; and \$17.0 million for a transmission construction loan.

- Asset retirement obligation, including the current portion, increased \$10.0 million, or 18.6%, primarily due to changes in the estimates of the amounts and timing of retirement costs related to coal combustion residual storage facilities at Thomas Hill.
- Payable to member cooperatives increased \$50.4 million, or 137.1%, due to additional funds being invested by member G&Ts and distribution cooperatives.
- Deferred regulatory credits, including the current portion, increased by \$29.0 million, or 11.6%, primarily due to the deferral in December of 2019 of \$34.0 million of member revenue subject to future refund in the form of lower rate requirements. Partially offsetting the increase was a \$3.6 million decrease in deferred gains on diesel and natural gas swaps and a \$1.4 million recognition of previously deferred revenue related to the New Madrid Unit 1 purchase.
- Other deferred liabilities increased \$23.2 million, or 65.7%, primarily due to increases in the derivative liabilities related to an interest rate swap and diesel and natural gas hedging activity.

Associated Electric Cooperative, Inc.
Statement of Operations
For the Three Months Ending 3/31/2020
(In thousands of dollars)

	Three Months Ended March 31		Three Months Ended March 31	
	2020	2019	2020	2019
Operating revenues:				
Members	\$243,743	\$265,151	\$243,743	\$265,151
Nonmembers	73,296	74,174	73,296	74,174
	<u>317,039</u>	<u>339,325</u>	<u>317,039</u>	<u>339,325</u>
Operating expenses:				
Generation operation	132,553	160,909	132,553	160,909
Contracted generation	11,563	11,204	11,563	11,204
Power purchased	32,434	30,891	32,434	30,891
Depreciation and amortization	22,527	22,304	22,527	22,304
Transmission Expense	23,173	22,997	23,173	22,997
Generation maintenance	17,988	21,856	17,988	21,856
Administrative and general	18,846	16,851	18,846	16,851
Taxes	1,629	1,698	1,629	1,698
Accretion of asset retirement obligations	393	412	393	412
	<u>261,106</u>	<u>289,122</u>	<u>261,106</u>	<u>289,122</u>
Operating margin before interest expense	<u>55,933</u>	<u>50,203</u>	<u>55,933</u>	<u>50,203</u>
Interest Expense:				
Interest on long-term debt	16,404	20,093	16,404	20,093
Less: interest capitalized	(641)	(492)	(641)	(492)
	<u>15,763</u>	<u>19,601</u>	<u>15,763</u>	<u>19,601</u>
Operating margin	<u>40,170</u>	<u>30,602</u>	<u>40,170</u>	<u>30,602</u>
Nonoperating:				
Interest and dividend income	5,900	8,397	5,900	8,397
Other nonoperating income	545	365	545	365
Interest expense	(308)	(309)	(308)	(309)
Total nonoperating	<u>6,137</u>	<u>8,453</u>	<u>6,137</u>	<u>8,453</u>
Net margin (loss)	<u><u>46,307</u></u>	<u><u>39,055</u></u>	<u><u>46,307</u></u>	<u><u>39,055</u></u>

These interim financial statements are unaudited. In the opinion of management all adjustments, which are normal recurring accruals, necessary for a fair presentation of results for interim periods have been included. The interim financial statements should be read in conjunction with the Notes to the Financial Statements included in the 2019 Annual Report.

Associated Electric Cooperative, Inc.
Balance Sheet
For the Three Months Ending 3/31/2020
(In thousands of dollars)

Assets	<u>Current Month</u>	<u>Prior Year</u>
Utility Plant:		
Electric plant in service	\$4,255,299	\$4,193,202
Construction work in progress	132,687	89,504
	<u>4,387,986</u>	<u>4,282,706</u>
Less accumulated depreciation	(2,308,467)	(2,212,012)
	<u>2,079,519</u>	<u>2,070,694</u>
Other property and investments:		
Nonutility property	31,663	31,663
Net investment in direct financing leases	3,201	3,512
Advanced construction funds	18,991	20,175
	<u>53,855</u>	<u>55,350</u>
Restricted assets:		
Investments in associated organizations	28,976	28,108
Other restricted assets and designated assets	205,229	370,418
	<u>234,205</u>	<u>398,525</u>
Current assets:		
Cash and cash equivalents	204,732	83,969
Restricted short-term investments	74,969	119,488
Accounts receivable, net	105,995	118,061
Fuel inventories	52,648	43,319
Materials and supplies inventories	88,517	84,610
Other current assets	17,295	17,306
Current portion of deferred regulatory debits	17,785	1,787
	<u>561,941</u>	<u>468,540</u>
Deferred regulatory debits	62,700	84,914
Other deferred assets	27,860	37,328
	<u>90,560</u>	<u>122,242</u>
 Total Assets	 <u><u>3,020,080</u></u>	 <u><u>3,115,351</u></u>

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Associated Electric Cooperative, Inc.
Balance Sheet
For the Three Months Ending 3/31/2020
(In thousands of dollars)

	Current Month	Prior Year
Capitalization and Liabilities		
Patronage capital and other equities:		
Memberships	12	12
Patronage capital	706,904	673,485
Other equities	55,561	55,561
Accumulated other comprehensive inc. (exp)	(19,535)	(14,551)
	742,942	714,507
Long-term debt, excluding current maturities:		
Federal Financing Bank	1,041,620	1,111,656
CoBank	170,781	291,118
Other long-term debt	337,215	352,640
	1,549,616	1,755,415
Asset retirement obligation	47,663	39,182
Accumulated provision for postretirement benefits	40,080	35,066
Current Liabilities:		
Payable to member cooperatives	87,124	36,751
Accounts payable	75,276	89,646
Other current and accrued liabilities	49,803	44,441
Current maturities of long-term debt	73,371	99,898
Current portion of asset retirement obligation	16,483	14,926
Current portion of deferred regulatory credits	1,513	2,870
	303,570	288,532
Deferred regulatory credits	277,794	247,393
Other deferred liabilities	58,415	35,255
	336,209	282,648
Total Capitalization and Liabilities	3,020,080	3,115,351

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Associated Electric Cooperative, Inc.
Statement of Cash Flows
(in thousands)

	Three Months Ended March 31, 2020	Three Months Ended March 31, 2019
Cash flows from operating activities:		
Net margin(loss)	\$46,307	\$39,055
Adjustments to reconcile net margin to net		
Cash provided by operating activities:		
Provision for depreciation and amortization	24,138	23,562
Amortization of loan expenses and other costs	94	144
Decrease (increase) in deferred debits	(9,102)	3,360
Increase (decrease) in deferred credits	812	4,852
Increase (decrease) in asset retirement obligation	(499)	563
Change in assets and liabilities:		
Accounts receivable	20,570	12,419
Fuel inventories	(8,260)	4,303
Materials and supplies inventories	(81)	(443)
Accounts payable	(47,477)	(36,429)
Other current and accrued liabilities	13,760	14,439
Other operating activities, net	(1,211)	(1,209)
Net cash provided by operating activities	39,051	64,616
Cash flows from investing activities:		
Construction expenditures for utility plant	(29,750)	(19,229)
Sale (purchase) of investments	(2,691)	(5,465)
Investments in associated organizations	(505)	(560)
Direct financing lease proceeds	80	74
Other investments	587	450
Reimbursement of capital expenditures	(10)	(3)
Net cash (used) in investing activities	(32,289)	(24,733)
Cash flows from financing activities:		
Increase (decrease) in net borrowings from member cooperatives	40,425	1,639
Issuance (retirement) of long-term debt, including change in current maturity	24,535	(59,667)
Net cash (used) in financing activities	64,960	(58,028)
Net increase (decrease) in cash and cash equivalents	71,722	(18,145)
Cash and cash equivalents, beginning of period	133,011	102,115
Cash and cash equivalents, end of period	204,732	83,969
Supplemental disclosure of noncash activities:		
Change in plant expenditures included in accounts payable	(16,289)	(8,194)
Supplemental disclosure of cash flow information:		
Cash paid for interest (net of amount capitalized)	17,405	7,342

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