**National Rural Utilities Cooperative Finance Corporation**
**FY2019 Third Quarter Investor Call**
**April 25, 2019**
**11:00 AM EST**

Operator: Good day, everyone, and welcome to the National Rural Utilities Cooperative Finance Corporation fiscal year 2019 third quarter investor call. Today's call is being recorded and at this time I would like to turn the conference over to Ling Wang. Please go ahead.

Ling Wang: Hi. Good morning. This is Ling Wang, Vice President of Capital Markets at National Rural Utilities Cooperative Finance Corporation. Thank you for joining us today to review our 9-month fiscal year 2019 financial results. Andrew Don, our Senior Vice President and Chief Financial Officer will discuss our financial results for the period from May 31, 2018 to February 28, 2019.

During today's call we will make forward-looking statements within the Security Act of 1933 as amended and Exchange Act of 1934 as amended. The forward-looking statements are based on certain assumptions and describe our future plans, strategies and expectations are generally identified by our use of words such as intend, "plan," "may," "should," "will," "project," "estimate," "anticipate," "believe," "expect," "continue," "potential," "opportunity" and similar expressions, whether in the negative or affirmative. All statements about future expectations or projections are forward-looking statements. Although we believe that the expectation reflected in our forward-looking statements are based on our reasonable assumptions, actual results and performance may differ materially from our forward-looking statements.

Factors that could cause future results to vary from forward-looking statements about our current expectations are included in our annual and quarterly periodic reports previously filed with the U.S. Securities and Exchange Commission. Except as required by law, we undertake no obligations to update or publically release any revisions to forward-looking statements to reflect events, circumstances, or changes in expectations after the date on which the statement is made.

We will have a Q&A session at the end of this presentation. You can ask questions via phone or submit your questions online if you are participating in this event via webcast. We encourage you to take this opportunity to ask any questions you may have. In addition, all of the materials for this event, including the presentation slides and financial reports, are available on our website at nrucfc.coop. A replay and call transcript will be made available on our website after the event.

With that, I'll turn the call over to Andrew.

Andrew Don: Thank you, Ling. Again, good morning and thank you for joining us today for National Rural Utilities Cooperative Finance Corporation's call to review our financial performance for our third quarter of fiscal 2019, the period ended February 28, 2019. We provide our results based on Generally Accepted Accounting Principles or GAAP in our Form 10-Q, which we filed on April 11, 2019. In addition to our GAAP results, during parts of this discussion, I'll refer to certain financial measures that are calculated based on amounts that include adjustments to amounts determined under GAAP and are therefore referred to as “adjusted”. The primary adjusted metrics include adjusted net income, adjusted net interest income and adjusted net interest yield, adjusted times interest earned ratio or TIER, and adjusted debt-to-equity ratio.

We provide a reconciliation of our adjusted measures to the most comparable GAAP measures in our recently filed Form 10-Q. It's important to note that we use our adjusted measures to manage our business and evaluate our financial performance. Additionally, the financial covenants in our revolving credit agreements and debt indentures are based on our adjusted measures rather than the comparable GAAP measures. We therefore believe these adjusted measures are also useful to investors in evaluating our performance.

As reflected in the top left graph, over the 9-month period that ended February 28, 2019, our total assets increased by $720 million from our prior fiscal year end of May 31, 2018. This increase was primarily due to the growth in our loan portfolio of $839 million as indicated in the top right graph. The 9 months ended February 28, 2019, we had an increase in CFC distribution loans of $724 million and an increase in power supply loans of $123 million, which were partially offset by a $15 million decrease in NCSC loans and a $10 million decrease in RTFC loans. It's worth noting that of the $839 million in loan growth, $488 million was due to an increase in line-of-credit borrowings by our members. The net growth in long-term loans during this period was very modest at $351 million.

CFC's gross long-term loan advances to our members totaled $1.4 billion during the 9-month period. Approximately $1.2 billion or 85% of these new advances were for capital expenditures and 13% were made to refinance other lenders' loans. In comparison, long-term loan advances during the same prior-year period was $1.9 billion. The decrease in long-term loan advances from the same prior-year period was driven by more limited opportunities to refinance loans made by other lenders.

Our members' equity, which excludes derivative forward value gains and losses and accumulated other comprehensive income, increased by $84 million to $1.6 billion at February 28, 2019 from May 31, 2018. The increase was primarily due to adjusted net income of $123 million for the 9-month period, partially offset by patronage capital retirement of $48 million. Our adjusted debt-to-equity ratio increased to 6.29 to 1 at February 28, 2019, from 6.18 to 1 as of May 31, 2018, primarily attributed to an increase in debt outstanding of $684 million to fund the loan growth. Based on our current forecast of loan advances and debt activity over the next 12 months, we anticipate that our adjusted debt-to-equity ratio will decrease to be closer to or below our target level of 6 to 1 over the next 12 months.

In the 9 months ended February 28, 2019, CFC generated an adjusted TIER of 1.19 times, compared to an adjusted TIER of 1.16 times for the same prior-year period. As reflected in the top right graph, adjusted net income totaled $123 million for the 9 months compared with $103 million for the same prior-year period. The $20 million increase in adjusted net income was primarily driven by an increase in adjusted net interest income of $31 million, which was partially offset by the loss on the early extinguishment of debt of $7 million that occurred during the first quarter of the fiscal year, and an increase in operating expenses of $4 million.

As indicated in the bottom left chart, for the 9 months ended February 28, 2019, our adjusted net interest income totaled $189 million, an increase of $31 million or 19% over adjusted net interest income of $158 million for the same prior-year period. The increase in adjusted net interest income was driven by a 12 basis point, or 14% increase in the adjusted net interest yield to 96 basis points, and a 4% increase in average interest earning assets. The 12 basis point increase in adjusted net interest yield reflected primarily a 7 basis points decrease in our overall average funding cost although interest rates increased during the time period. The reduction in our funding cost was largely attributable to the interest savings from the 10.375% collateral trust bonds, which were paid off in full on November 1, 2018. We replaced this high-cost debt with lower-cost funding, which more than offset the increase in the average cost of our variable rate funding, due to higher short-term interest rates. We expect that the benefit from the payoff of the 10 and three-eighths % high coupon debt will continue to have a favorable impact on our adjusted net interest yield, adjusted net interest income, and adjusted TIER over the next 12 months.

The overall composition of our loan portfolio at quarter end February 28, 2019 remained largely unchanged from fiscal year end May 31, 2018, with $26 billion, or 99%, of our portfolio consisting of loans to rural electric systems and $353 million, or 1%, to the telecommunications sector. The percentage of CFC's long-term fixed-rates loans was at 88% as for February 28, 2019, compared with 90% at May 31, 2018. We typically lend to our members on a senior secured basis, with 91% of our loans being senior secured at February 28, 2019, compared with 93% at May 31, 2018.

The credit quality of our loan portfolio remains strong with our members continuing to demonstrate solid financial and operational performance. We had no loan defaults or charge-offs during the current fiscal year, nor the prior fiscal year. In addition, we have had no delinquent or nonperforming loans in our portfolio for greater than 2 years that is since June 1, 2016.

For the 9 months ended February 28, 2019, our total debt outstanding increased by $684 million from our prior fiscal year end of May 31, 2018 to fund loan growth during this time period. CFC continues to maintain diverse funding sources to minimize the risk of being dependent on any single source or market. Our overall funding mix has been very stable over the past several years. As of February 28, 2019, $4.2 billion, or 17% of CFC's funding came from our members in the form of short-term and long-term investments. At February 28, 2019, our total outstanding balance under the Guaranteed Underwriter Program increased by $578 million from the prior fiscal year end and our outstanding balance under the notes payable with Farmer Mac increased by $281 million. Both increases were attributable to our need to fund the loan growth.

Our capital markets related funding sources, which represented nearly 50% of our funding, remained around the same level at February 28, 2019 as our prior fiscal year end date of May 31, 2018. During this fiscal year, we issued $1.6 billion of collateral trust bonds and $300 million of dealer medium-term notes, primarily to refinance the $1.8 billion in collateral trust bond maturities.

This slide presents CFC's long-term debt maturities and amortization over the next 12 months. We had a $350 million dealer medium-term note, which matured earlier this month on April 5th. Excluding this dealer medium-term note, our total long-term debt maturities over this period are expected to be very modest and manageable at $1.9 billion with $705 million in collateral trust bond maturities and $300 million in dealer medium-term note maturities. With respect to the $457 million member medium-term notes due over this period, historically, our members have chosen to roll over their investments at maturity. We believe we have ample sources of liquidity to meet each of the maturities, as will be highlighted in the next slide.

This slide depicts the various non-capital market dependent sources of liquidity that CFC had in place at February 28, 2019, compared with our prior fiscal year end of May 31, 2018. The amount of sources of liquidity CFC had at February 28, 2019 decreased slightly by $177 million from May 31, 2018, primarily due to a $281 million decrease in availability under the Farmer Mac revolving note purchase agreement and $110 million decrease in commitments available under our bank revolving line of credit facilities, offset by an increase of $125 million in the commitments available under the Guaranteed Underwriter Program and an increase of $156 million in scheduled long-term loan amortization and repayments that we expect over the next 12 months.

As indicated in the graph, we had an aggregate of $5.6 billion of member and non-member debt maturities over the next 12 months as of February 28, 2019, compared with $6.6 billion as of May 31, 2018. At February 28, 2019, we had access to $3.4 billion, or 1.6 times, of liquidity greater than the combined member and non-member debt maturity needs. The $5.6 billion of debt maturities over the next 12 months includes $2.7 billion of short-term investments that our members have with CFC. We consider our member investments to be a very stable and reliable source of funding for CFC. If we exclude the $2.7 billion debt maturities related to our member investments, we would have access to $6.1 billion, or 3.1 times, of liquidity in excess of dealer commercial paper and the current portion of non-member long-term debt maturities during the 12 months subsequent to February 28, 2019.

This slide presents CFC's projected sources and uses of cash over the next 18 months from February 28, 2019. As indicated, our total projected cash needs over this time period are approximately $5.2 billion, with 47% of this amount expected to satisfy projected new loan advances and 53% to meet maturities of long-term debt. As mentioned earlier, of the total $839 million increase in loans to members during the 9-month period ended February 28, 2019, $488 million was due to an increase in line-of-credit borrowings. As indicated under the other loan repayments column, we expect that a good portion of these line-of-credit advances will be paid off during the last quarter of this fiscal year and refinanced into long-term loans with us.

That said, our current expectation is that our loan growth over the next 18 months will be modest. For future potential funding needs, we will continue to look to balance capital market and non-capital market, secured and unsecured financings while always looking to access the most attractive cost of funds for our member borrowers. This table highlights major financing activities we completed during the 9 months in fiscal year 2019. Specifically, during our third fiscal quarter that is from December 1, 2018 to February 28, 2019, we completed several financing transactions through various funding sources totaling approximately $1.8 billion primarily to fund the $839 million in loan growth as well as $650 million in debt maturities.

In January 2019, we accessed the capital market and issued $450 million of 10-year and $500 million of 30-year collateral trust bonds. In January and February 2019, we advanced a total of $525 million under the Guaranteed Underwriter Program. In February 2019, we borrowed $425 million under the note purchase agreements with Farmer Mac. We subsequently paid off in March 2019 $100 million of the $425 million borrowings from Farmer Mac.

To conclude our call, I'd like to leave you with a few key takeaways when you consider CFC as an investment opportunity. These items are areas that CFC is consistently focused on and represent key credit strengths when viewing CFC as an investment. As indicated, CFC's ratings remain strong and stable. S&P Global recently reaffirmed our ratings and outlook and published an updated credit opinion on April 12, 2019. Our ratings and outlook from all three rating agencies were reaffirmed within the last 6 months. CFC has a long-term incentive compensation plan which is tied to our credit ratings. Our goal is to maintain strong long-term credit fundamentals.

The overall quality of our loan portfolios was strong with 99% of our loans to rural electric systems and 91% of our loans being on a senior secured basis. We have not had any delinquent or nonperforming loans in our portfolio for over 2 years, that is since June 1, 2016, we have not had any loan charge-offs during the past 10 quarters. At February 28, 2019, the coverage ratio of our allowance for loan losses, which is an estimate of probable losses inherent in our loan portfolio was 0.07%, or 7 basis points of our total loan portfolio, the same allowance coverage ratio as of May 31, 2018.

CFC continues to receive strong support from our members both in terms of new lending business and as a valuable funding source. Our member investments stood at $4.2 billion at February 28, 2019, representing 17% of our total funding. As a member-owned cooperative organization, CFC cannot issue common or preferred equity. However, we are committed to grow our equity through retained earnings. Our members' equity has grown by 60% to $1.6 billion from $998 million since 2013. We continue to maintain diversified funding sources and demonstrate a strong liquidity profile. Our funding sources are very well established and have remained stable.

From a liquidity perspective, at February 28, 2019, we had $3 billion committed revolving credit facilities from our relationship banks, $1.4 billion committed availability in the Guaranteed Underwriter Program, and $2.3 billion revolving credit capacity via the Farmer Mac secured note purchase agreements. In addition, as a supplemental source of liquidity, at February 28, 2019, we had $561 million of held-to-maturity investment securities consisting primarily of high-quality liquid short-to intermediate-term corporate bonds. These sources, together with cash and scheduled loan amortization and other repayments from our members, resulted in CFC having $9 billion of liquidity available at February 28, 2019 to meet the $5.6 billion of debt maturities over the next 12 months, a 1.6 times liquidity coverage ratio. Excluding debt maturities related to our member investments which historically have had a high reinvestment rate, our liquidity coverage ratio would be 3.1 times.

Thank you once again for joining us today to review our results for our fiscal quarter ended February 28, 2019. We appreciate your interest in CFC and look forward to discussing our financial performance and funding plans in the future. I'd like to ask the operator to open the lines for any questions and also suggest that you submit other question via the web service, so that we may be able to respond to those as well. Thank you.

Operator: Thank you. If you would like to ask a question on the phone lines today, you can press "*, 1" on your telephone keypad. If you are on a speakerphone, please make sure your mute option is turned off to allow your signal to reach our equipment. Once again, everyone, that is "*, 1" to ask a question over the phone lines.

And there are no phone questions at this time, but I would like to remind everyone it is "*, 1" on the telephone.

Andrew Don: Okay, operator. I think since there are no questions, we'll sign off now. So again, thank you to everyone for participating and joining us today, and we look forward to talking to you in the future. Have a good day.

Operator: Thank you. And that does conclude today's presentation. Thank you for your participation and you may now disconnect.