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Conference Title: **FY2024 Year-End Investor Conference Call**

Moderator: **Harris Spryn**

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Operator: Good afternoon and welcome to the National Rural Utilities Cooperative Finance Corporation Fiscal Year 2024 Year-End Investor Conference Call. Today's conference is being recorded. At this time, I'd like to turn the call over to Miss Heesun Choi. Please, go ahead.

Heesun Choi: Thank you, operator. Welcome to our Investor Conference Call for our Fiscal Year 2024. Today I'm joined by our CEO, Andrew Don, and our CFO, Ling Wang. Andrew and Ling will discuss our year-end results and answer your questions. Before we get started, I would like to remind you that today's presentation slides and financial reports filed with the SEC can be found on our website at nrucfc.coop under Investor Relations. This call is being recorded and a replay and call transcript will be made available on our website as well.

Our presentation today will include forward-looking statements and certain non-GAAP financial measures. Please review the disclosures on slides two and three of the presentation regarding these statements are majors. I would like to remind you that any forward-looking statements that we may make during today's call as of August 5, 2024, are subject to risks and uncertainties. Factors that may cause actual results to differ materially from expectations are described on slide two of today's presentation, as well as in our annual and quarterly reports filed with the SEC.

Information about any non-GAAP financial measures referenced during the presentation, including reconciliations to GAAP measures, can also be found in our Form 10-K filed with the SEC on August 1, 2024, as well as in the appendix of the presentation slides. At the end of the presentation, we will open the call and Andrew and Ling will take all your questions. You can ask questions over the phone or submit your questions online. With that, I will turn this call over to Andrew.

Andrew Don: Thank you, Heesun. Good afternoon. Thank you for joining our call today to review the results of our fiscal year 2024, which concluded on May 31, 2024. I'm pleased to report that we experienced another successful year, as evidenced by strong financial performance and robust demand for capital in support of our members financing needs. As many of you know, CFC was created by America's electric cooperative network with a clear and focused mission of being in a position to meet the financing needs of rural electric cooperatives.

Unlike many financial institutions that prioritize growth through its own interest, our primary objective remains meeting the financial needs of our members. Our success is aligned with our members' success. We have stayed true to this mission by continuing to provide loans and financial products to our members, helping them achieve their goals and maintain their operations. Our commitment to service, integrity and excellence has once again demonstrated its value as evidenced by our solid financial performance. Today, I look forward to discussing our successful results with you in greater detail.

I will start on slide five. I'd like to summarize our fiscal year 2024 by highlighting four key components of our business model, namely the continued strong loan demand from our membership, a significant member equity position, a superior quality loan portfolio and high investment grade credit ratings. Our financial results reflect the credit strength of our members and our focus on strategically managing our balance sheet to fund our members' capital needs.

During fiscal year 2024, our loans to members increased by $2 billion, or 6%, from $32.5 billion at May 31, 2023, to $34.5 billion at May 31, 2024. This $2 billion loan growth is the second largest year-over-year growth CFC has experienced since 2002. Based on our analysis of the calendar year-end date of December 31, 2023, our total loans outstanding represented 25% of the total loans outstanding in the electric cooperative sector. We continue to be the largest private lender in the space.

Consistent with our historical experience of very limited charge-offs, loan defaults, loan delinquencies and non-performing loans in our electric portfolio, the overall quality of our loan portfolio remained pristine during fiscal year 2024, with 98% of our loans to rural electric systems that provide essential electric utility services. We had no charge-offs during fiscal year 2024. Instead, we recorded $1 million in net loan recoveries. Non-performing loans represented only 0.14% of our total loans outstanding at May 31, 2024, compared to 0.27% at May 31, 2023.

Our financial position remains strong as we continue to generate strong financial metrics. During fiscal year 2024, our adjusted TIER was 1.24 times, which was well above our targeted goal of 1.1 times. Our capital position continued to improve during fiscal year 2024, with our members' equity surpassing $2.3 billion at fiscal year-end 2024. Our members' equity consists primarily of our retained earnings. By comparison, our members' equity at fiscal year 2014 was approximately $1 billion.

Through prudent financial practices, we have more than doubled our members' equity over the past 10 years by steadily accumulating retained earnings. Furthermore, during fiscal year 2024, CFC's Board of Directors approved a change in the patronage capital allocation of net earnings that will allow us to retain additional earnings and further enhance our capital position. As a result of the change in the patronage capital practice, we are retaining 79% of adjusted net income for fiscal year 2024 in members' capital reserve, compared to 56% for fiscal year 2023.

Our liquidity position remains healthy and resilient as we maintain diversive, well-established funding sources to minimize the risk of being dependent on any single source or market. We are committed to having strong investment credit ratings from Fitch, Moody's and S&P. We currently have long-term senior secured ratings of A+, A1, A- and long-term unsecured ratings of A, A2, A-, all with a stable outlook. As we have stated on prior calls, we have an incentive payout structure where incentive payments for named executive officers are directly tied to CFC's credit ratings.

Lastly, I'm pleased to inform you that we recently published our 2024 Corporate Citizenship Report, which is available on our website. This report includes information about how we support our members who are dedicated to delivering essential electric and/or broadband services that improve the quality of life in rural America's unserved or underserved communities. Now I'm turning to slide six.

As you can see in the middle of the slide, our loans to members increased nearly $9 billion, or 33%, over the last five years, from the end of fiscal year 2019 to the end of fiscal year 2024. Our members have experienced increased financing needs, primarily driven by several factors that I will review with you now.

First, our members are experiencing increased electricity demand in their service areas. Based on our analysis, both total kilowatt hour sales and total operating revenue increased by 1.2% in 2023 compared to 2022. Additionally, according to research published by S&P Global, electricity demand is forecast to grow substantially in all U.S. regions through 2040. Over the next decade, demand growth is expected to be driven primarily by new data centers and new manufacturing facilities, as well as strong electric vehicle growth and beneficial electrification trends.

Rural electric cooperatives have become increasingly supportive of beneficial electrification, which refers to the replacement of fossil fuel powered systems with electric systems such as electric vehicles and heat pumps in a way that reduces overall emissions, while providing benefits to the environment and to households.

Secondly, our members continue to enhance resilience and reliability for their electric systems. We observed an increase in capital expenditures by electric cooperatives to proactively strengthen existing electric systems, as well as replace systems in the aftermath of damages from weather related incidents, including hurricanes, winter storms and wildfires. We believe that the adverse impact on electric systems from weather related incidents has resulted in a heightened awareness by electric cooperatives of the need to focus attention on making infrastructure upgrades to improve both the resiliency and reliability of electric systems.

Third, our members have an increased focus on clean energy supply investments. Due in part to the New Empowering Rural America, referred to as New ERA, funding available to electric cooperatives, many electric power supply and electric distribution cooperatives are increasingly focused on efforts to identify potential opportunities to increase investments in renewable power supply, transmission and storage. The New ERA Program is a $9.7 billion initiative established under the Inflation Reduction Act, specifically designed to help rural electric cooperatives transition to clean, affordable and reliable energy. This program is the largest investment in rural electrification since the Rural Electrification Act of 1936.

Lastly, electric cooperatives have increasingly invested in broadband to address the digital divide in rural America. Many rural cooperatives have made or are making infrastructure investments that include building fiber optic lines to improve electric grid system reliability, efficiency and cost savings, as fiber operations offer enhanced communications to monitor electric systems, identify outages and speed electric restoration. Many electric cooperatives are also leveraging community relations to offer broadband services in their service territory.

Based on the aforementioned drivers, our members are expected to make substantial investments in new power supply, transmission and other related infrastructure in order to meet future demand and other strategic goals. We believe these investment priorities will necessitate funding and may lead to an increased demand for capital from us.

Turning to slide seven. We serve a geographically diverse group of electric and telecommunications borrowers throughout the U.S. The consolidated number of borrowers with loans outstanding totaled 885 in 49 states and the District of Columbia. The top three states that have the largest loan growth for fiscal year 2024 were Texas, Arkansas and Georgia. You can see the increases in loans in those three states in the map represented in the slide. The growth of the top three states was primarily driven by our members funding needs for electric capex and/or broadband projects.

Separately, we continue to experience a decrease in loans outstanding in Louisiana, as some of the outstanding balances on emergency line of credit loans were repaid using reimbursement funds from FEMA, the Federal Emergency Management Agency. We continue to see an increase in members' needs for bridge financing for broadband projects. At May 31, 2024, our outstanding loans to our CFC distribution members for their broadband projects increased to approximately $3.1 billion, which is a $748 million, or 32%, increase compared to the May 31, 2023, level of $2.4 billion. The $748 million increase in broadband loans represented 37% of the overall loan growth during fiscal 2024. The three states with the largest CFC loans outstanding for broadband projects were Arkansas with $396 million, Missouri with $337 million and Indiana with $334 million.

Moving on to slide eight, we recently published our annual preliminary Key Ratio Trend Analysis (KRTA) results for 812 electric distribution cooperatives for the year-ended December 31, 2023. Our KRTA is an annual assessment of financial trends among electric distribution cooperatives nationwide. Based on the preliminary KRTA results for 2023, despite a high interest rate environment, electric cooperatives continued their consumer and utility plant growth and have maintained strong financial metrics, including improved margins. This underscores electric cooperatives' sustained financial health and operational efficiency.

Consumer growth slightly tapered to 0.89% at December 31, 2023, compared to 0.99% at May 31, 2022, with approximately 88% of the cooperatives reporting showing increases in consumers served. Notable states that had greater than 2% growth were Florida, Idaho and Utah. Investment in utility plant continued at a rapid pace, which exceeded 5% for the first time since 2008. 2023 KRTA ratios also showed that inflationary pressures have been abating, especially with power costs. Although costs increased over 2022 levels, cooperatives were able to manage them, as demonstrated by a decrease in power costs as a percentage of revenue. This is significant because, unlike in 2022, cooperatives were able to generate higher margins in 2023, which produced healthy coverage ratios.

In another positive sign, both accounts receivable over 60 days and write-offs continued at their pre-pandemic lows. Accounts receivable remained at 0.08% of operating revenue, and write-offs remained at 0.06% of revenue. We believe that the 2023 KRTA results demonstrated that our member cooperatives' financial condition continues to be resilient, sound and stable. With that, I will now turn the call over to Ling.

Ling Wang: Thank you, Andrew, and good afternoon, everybody. I'm going to turn to slide 10 to delve into our fiscal year 2024 financial results. Unless specified otherwise, I will be primarily focusing on year-over-year comparisons while discussing our fiscal year 2024 outcomes. Slide 10 shows our balance sheet information. Our total assets at the fiscal year-ended May 31, 2024, were approximately $36.2 billion, an increase of $2.2 billion, or 6%, from the prior fiscal year, and an increase of $8 billion, or 28%, from fiscal year 2020.

Our balance sheet growth was primarily driven by increase in loans to electric borrowers. Our total liabilities increased by $1.7 billion, or 6%, to $33.2 billion at May 31, 2024, as we issued debt to fund loan growth. Since fiscal year 2020, our total liabilities increased by $5.7 billion, or 21%. Our members equity, which excludes cumulative derivative forward value gains and accumulated other comprehensive income, increased by $176 million, or 8%, to $2.4 billion from the prior fiscal year. The $176 million increase was a result of an adjusted net income of $289 million during fiscal year 2024, which was partially offset by $113 million retirements of the patronage capital during fiscal year 2024. Since fiscal year 2020, we have been able to build up our members' equity through retained earnings by $679 million, from $1.7 billion to $2.4 billion, a 40% increase.

As a cooperative, CFC allocates a portion of its net earnings to our members on an annual basis. Our current policy, approved by our Board of Directors, is to allocate a portion of the fiscal year 2024 net earnings to CFCs members in the form of patronage capital. The specific retire amount and schedule are subject to yearly approval by the CFC Board of Directors. As Andrew mentioned earlier, the CFC Board of Directors has approved a change in the patronage capital allocation practice to balance our leverage with the strong loan growth that we are currently experiencing.

In July 2024, the CFC Board of Directors authorized $61 million, or 21%, of fiscal year 2024 adjusted net income as patronage capital to our members and $228 million, or 79%, of adjusted net income to members' capital reserve. In comparison, last year the CFC Board of directors authorized $110 million, or 44%, of adjusted net income for fiscal year 2023 as patronage capital to our members, and $140 million, or 56%, of adjusted net income to members' capital reserve.

The members' capital reserve represents net earnings that we retain and have not been specifically allocated to members. The members' capital reserve may be allocated to individual members in the future as patronage capital, if authorized by the CFC Board of Directors. Also in July 2024, CFC's Board of Directors further authorized the retirement of patronage capital totaling $47 million, consisting of $30 million, which represents 50% of the $61 million patronage capital I mentioned earlier, and $17 million, which represents the allocation from fiscal year 1999 net earnings that has been held for 25 years pursuant to CFC's Board of Directors policy.

We expect to return this amount to our members in cash in the second quarter of fiscal year 2025. The remaining $31 million of fiscal year 2024 patronage capital allocation will be retained by CFC for 25 years. The CFC Board of Directors adopted this guideline in June of 2009. Our adjusted debt-to-equity was 6.24-to-1 at May 31, 2024, an increase from 6.04-to-1 at May 31, 2023, and an increase from 5.85-to-1 from four years ago.

The higher adjusted debt-to-equity ratio was primarily due to increase in total debt outstanding to fund our loan growth. While our goal is to maintain adjusted debt-to-equity ratio of approximately 6-to-1, we anticipate that our adjusted debt-to-equity ratio may remain above this level. The elevated ratio reflects our strong loan growth in recent years. We will continue to proactively seek and implement strategies to effectively manage our adjusted debt-to-equity ratio.

Looking at slide 11 for our loan portfolio. The composition of our loan portfolio remained largely unchanged from the prior fiscal year-end and has shown no significant changes in the past five years. Our loan portfolio consists primarily mainly of long-term fixed-rate secured loans to rural electric cooperatives. Our long-term fixed-rate loans were 88% of total loans outstanding at May 31, 2024, similar to the level of 87% at May 31, 2023.

Our long-term loans are typically secured by substantially all assets of the borrowers. We typically lend to our members on a senior secured basis, with 92% of our loans being senior secured at May 31, 2024, unchanged from May 31, 2023, level. In terms of loan growth, during fiscal year 2024, the $2 billion increase in loans to members reflected net increases in loans to distribution, power supply, statewide and associated and NCSC telecom members, partially offset by a decrease in NCSC electric loans.

More than 93%, or $1.87 billion, of the net loan increase was driven by increases in loans to our distribution and power supply borrowers. Loans to distribution members increased by $1.7 billion to $27.1 billion, and loans to power supply members increased by $205 million to $5.6 billion during fiscal year 2024. We also experienced increases in CFC statewide and associated loans and NCSC telecom loans of $37 million and $111 million, respectively, while NCSC's electric loans decreased slightly by $11 million.

At the end of fiscal year 2024, $34 billion, or 98%, of our loans consist of loans to rural electric members and $599 million, or 2%, to the telecommunication members, compared to 99% to electric borrowers and 1% to telecommunication borrowers at the prior fiscal year-end. During fiscal year 2024, long-term loan advances totaling $3.4 billion, of which $3.2 billion, or nearly 94%, were fixed-rate loans. Additionally, approximately $3.1 billion, or 93%, of advances were for capital expenditure purposes, compared to 95% during prior fiscal year. The remaining balance was used to refinance other lenders debt or for other purposes.

We typically offer long-term fixed-rate loans with terms up to 35 years, allowing our members to choose a fixed-rate for any period from one year up to the loan's final maturity. When the selected fixed-rate term expires, our members may select another rate term. We have observed that our members continue to choose shorter terms for long-term fixed-rate loans due to the current elevated interest rate environment. The weighted average fixed-rate term was 11 years for the new $3.2 billion fixed-rate term loan advances during fiscal year 2024, whereas it was 18 years during fiscal year 2023.

That said, at May 31, 2024, the average remaining maturity of our long-term loans, which accounted for 90% of total loans outstanding, was 19 years. In terms of loan type, during fiscal year 2024, our long-term loans increased by $1.7 billion, reaching a total of $31.1 billion, while our line of credit loans rose by $299 million, bringing the total to $3.4 billion. Although the growth in our line of credit loans slowed during fiscal year 2024, the average line of credit loan portfolio has shown a steady increase in recent years, growing from $1.6 billion in fiscal year 2021 to $3.3 billion in fiscal year 2024.

Our credit metrics are presented on slide 12. We continue to maintain high-quality loan portfolio, reflecting our prudent lending practices and the strong financial health of our members. At May 31, 2024, we had only one non-performing loan outstanding, totaling $49 million, or 0.14% of total loans outstanding. This loan was made to an electric power supply borrower and was put on non-performing loans during fiscal year 2020. In comparison, we had loans to two CFC electric power supply borrowers totaling $89 million, or 0.27% of total loans outstanding, classified as non-performing as of May 31, 2023.

During fiscal year 2024, one of the non-performing loans was fully paid off and we received a $36 million payment on the other non-performing loan we have on our book, reducing the outstanding balance to $49 million. Our allowance for credit losses decreased by $4 million to $49 million at May 31, 2024, compared to $53 million at May 31, 2023. The allowance coverage ratio decreased to 14 basis points at May 31, 2024, from 16 basis points at May 31, 2023. The $4 million decrease in the allowance for credit losses reflected a $8 million reduction in the asset-specific allowance, partially offset by a $4 million increase in the collective allowance due to loan growth and a slight decline in the overall quality of our loan portfolio, as well as a slightly higher expected default rate derived from a third-party utility sector default data that's used in estimating the allowance of credit losses.

During fiscal year 2024, we had no loan charge-offs and no delinquent loans. We recorded $1 million in net loan recoveries during fiscal year 2024. We believe that the overall quality of our loan portfolio remains strong at May 31, 2024, evidenced by the limited defaults and losses in our electric utility portfolio since the inception of CFC. In our 55-year history, we have experienced only 18 defaults in our electric utility portfolio. Out of the 18 defaults, one is in the process of being resolved, nine had no losses and eight led to a cumulative net charge-offs of only $100 million.

Moving on to slide 13. During fiscal year 2024, our adjusted net income increased by $40 million, or 16%, to $289 million from the prior fiscal year, primarily due to a $32 million increase in adjusted net interest income, $16 million favorable shift from losses to gains recorded on our investment securities, a $6 million favorable shift from provision to benefit for credit losses and a $5 million increase in fee and other income, partially offset by a $19 million increase, mainly in operating expenses. The $32 million increase in adjusted net interest income during fiscal year 2024 was driven by a 7% increase in our interest earning assets and an increase in adjusted net interest yield of 3 basis points. Specifically, our adjusted net interest yield was 1.11% for fiscal year 2024, compared to 1.08% for fiscal year 2023.

Being a member-owned finance cooperative association, our primary financial goal focuses on earning an annual minimum adjusted time interest earned ratio, or TIER, of 1.1 times. For fiscal year 2024, our adjusted TIER was 1.24 times, compared to the fiscal year 2023 level of 1.25 times. Our adjusted TIER for fiscal year 2024, and for the last four years, comfortably exceeded our target of 1.1 times.

Slide 14, shows our total outstanding information. So our total debt outstanding was $32.7 billion at May 31, 2024, an increase of $1.7 billion, or 6%, from the May 31, 2023 level, primarily to fund the growth in our loan portfolio. During fiscal year 2024, we accessed the capital markets in multiple occasions and raised a total of $3.9 billion, consisting of $3.8 billion dealer medium-term notes and $100 million subordinated deferral debt. We also borrowed $800 million under our Farmer Mac note purchase agreement and $275 million under the guaranteed underwriter program.

We have strategically developed and continue to maintain diverse funding sources, including funding from our members, Farmer Mac, USDA's guarantee underwriter program, as well as access to capital markets. At May 31, 2024, $4.9 billion of CFC's funding came from our members in the form of short-term and long-term investments, a slight increase of $43 million from the May 31, 2023 level.

Our members' investments represented 15% of our total debt outstanding at May 31, 2024, compared to 16% at May 31, 2023. At May 31, 2024, our funding under the guarantee underwriter program and notes payable with Farmer Mac totaled $10.4 billion, representing 32% of our total debt outstanding, a $483 million, or 5% increase from the prior fiscal year-end level, primarily due to a net increase of $713 million in borrowings from Farmer Mac, partially offset by a net decrease of $229 million in borrowings under the guarantee underwriter program.

Our capital markets related funding sources totaled $17.5 billion at May 31, 2024, a $1.2 billion, or 7%, increase from the prior fiscal year-end level. The increase was primarily due to a net increase of $2.8 billion in dealer medium-term notes, offset by net decreases of $838 million in collateral trust bonds and $789 million in dealer commercial paper outstanding. Our dealer commercial paper outstanding decreased to $504 million at May 31, 2024, compared to $1.3 billion at May 31, 2023. At May 31, 2024, 52% of our total debt issued was on a secured basis and 48% was issued on an unsecured basis, compared to 56% secured and 44% unsecured at the prior fiscal year-end.

Our short-term borrowings decreased by $213 million to $4.3 billion, accounting for 13% of our total debt outstanding, at May 31, 2024, compared to $4.5 billion, or 15%, of total debt outstanding at May 31, 2023. The decrease in short-term borrowings was driven primarily by a decrease in outstanding dealer commercial paper, partially offset by increases in member short-term investments and short-term borrowing from Farmer Mac. In May 31, 2024, a total of $3.3 billion, or 77%, of our short-term borrowings came from our member investments, compared to $3.3 billion, or 72%, at May 31, 2023.

Our member short-term investments have averaged $3.5 billion over the last 12 fiscal quarter-end reporting periods. The weighted average cost of our outstanding short-term borrowings increased to 5.34% at May 31, 2024, 38 basis points increase from 4.96% at May 31, 2023. The weighted average maturity of our short-term borrowings increased to 49 days at May 31, 2024, from 44 days at May 31, 2023.

Slide 15 shows the various sources of liquidity CFC had in place at May 31, 2024. Our available liquidity from various sources, included cash investments, committed bank loans, guaranteed underwriter program and Farmer Mac revolving note purchase agreement totaling $6.7 billion at May 31, 2024. As indicated in the table on the right side, at May 31, 2024, we had a total of $7 billion in debt maturities over the next 12 months, with 47%, or $3.3 billion, of these debt maturities representing short-term investment from our members.

As we have consistently stated, the investments from our members are a very reliable funding source with little reinvestment risk, as our members continue to invest a large portion of their excess funds with us. The remaining $3.7 billion in debt maturities includes $505 million dealer commercial paper, a $500 million short-term notes payable to Farmer Mac and $2.7 billion long-term and subordinated debt obligations. These non-member related obligations are well covered by the $6.7 billion liquidity discussed previously.

It is also worth noting that the $6.7 billion liquidity does not include the $1.6 billion scheduled repayment and amortization on long-term loans that we expect to receive from our members over the next 12 months. In addition, as a strong investment grade company, we believe we will continue to have access to capital markets to meet our capital needs.

Slide 16 summarizes CFC's projected long-term debt issuance needs over the next 18 months, subsequent to May 31, 2024. Our cash needs are derived from two primary areas, refinancing existing debt maturities and funding loan advances to our members, partially offset by the amortization and repayment of loans from our members. Our funding needs are also driven by our member investment levels. Over the next 18 months, from June 2024 through November 2025, we have a total of nearly $5 billion of long-term debt maturities and amortization, consisting of approximately $3.6 billion in capital markets debt and $1.4 billion in non-capital markets debt.

We expect our loan growth over the same period to be approximately $2.3 billion. As indicated in the chart, we expect to raise approximately $6 billion in long-term debt, utilizing both capital markets and non-capital markets funding sources, over this time period to refinancing existing debt maturities and to fund the anticipated loan growth.

Thank you once again for joining us today to review our fiscal year 2024 results. We appreciate your interest in CFC and look forward to discussing our financial performance and funding plans in the future. Now, I would like to ask the operator to open the line for questions, and also suggest that you may submit your questions via the web services so we can respond to those as well. Thank you.

Operator: Thank you. If you would like to ask a question, please signal by pressing star one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal for questions. Again, that is star one to ask a question. We do not have any questions in the queue.

Ling Wang: Okay. Thank you for joining us for the call today. If you have any questions in the future, please feel free to contact myself or Heesun Choi. Now, we can just conclude our call today. Thank you.

Operator: Thank you. This concludes today's call. Thank you for your participation. You may now disconnect.