Metro

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June 21, 2018

TO: BOARD OF DIRECTORS

THROUGH: PHILLIP A. WASHINGTON
CHIEF EXECUTIVE OFFICER

PAW

FROM: NALINI AHUJA
CHIEF FINANCIAL OFFICER

Nalini Ahuja

SUBJECT: NATURAL GAS HEDGING PROGRAM

ISSUE

The Natural Gas Hedging Program (the "Hedging Program") requires that we report compliance with the Hedging Program Guidelines and program performance to the Board on a quarterly basis. This report is provided for the quarter ended March 31, 2018.

DISCUSSION

The purpose of this report is to present the status of compliance and performance for the hedged portion of our compressed natural gas ("CNG") budget. As Metro has not entered into any hedges for fiscal year 2018, this report presents the actual cost of our CNG in comparison to what was budgeted for the quarter. Operations related variances are presented in order to provide an overall perspective for CNG costs.

COMPLIANCE

As of the date of this report the Hedging Program is in compliance with all the specified limitations and requirements. The individual compliance items are listed on Attachment A.

PERFORMANCE

Infrastructure costs associated with pipelines and storage facilities contributed to significant increases in transportation related fees for CNG starting in fiscal year 2016. The hedging agreements related to the wholesale base cost of natural gas do not cover these infrastructure costs thereby reducing the efficiency and benefit of the hedge. Although we have observed a decrease in the fees, at current levels the surcharges would reduce the gas cost savings expected to offset payments for the hedge. Hence, staff decided against hedging the CNG costs in fiscal year 2018.

For the quarter ending March 31, 2018, CNG costs were approximately $1,316,000 under budget as actual usage was approximately 1,243,000 therms below budget primarily due to operating fewer miles than budgeted and more favorable weather conditions. The actual average gas price was under budget at $0.446 per therm vs. the budgeted amount of $0.510 (see Attachment B).

Since the end of the second quarter, inventories continued to decline going from 5.8% less than the five year average to 20.4% less than the five year average inventory. The number of drilling rigs exploring for natural gas increased from 182 to 194 and prices decreased during the quarter. The current market environment (as of June 11th) presents the potential to hedge FY 2019 at an index gas cost of around $0.2333 per therm (plus the current additional cost of $0.1889 per therm in SoCal Gas Company charges), for a total expected cost of about $0.4222 per therm for the fiscal year 2019, compared to the FY19 budgeted cost of $0.4500 per therm.

Beginning August 1, 2017 Metro began a one year pilot program with Clean Energy as a Biomethane Gas Provider. Under the terms of the contract, Clean Energy provides CNG for a single bus division as a pilot program at a $0.005 per therm discount to the SoCal Border Index. For the quarter ended March 31, 2018, Metro procured CNG through Clean Energy at a cost roughly $52,000 lower than if it had purchased from its other supplier SoCal Gas Company. Given the success of the pilot to date, Metro is looking to extend this strategy to the remaining bus divisions. The possibility of extending the strategy to the remaining divisions will have no material effect on the economic results of natural gas hedging in the future. However, with this new strategy the gas commodity will be invoiced by the Biomethane Gas Provider(s), separate from SoCal Gas Company's transmission charges enabling a clearer view of the effects of hedging on cost.

NEXT STEPS

- Enter into hedges for FY 2019 as warranted
- Continue to monitor the surcharge/tariffs with SoCal Gas and the CPUC
- Continue to monitor the effects of the Contract with Clean Energy

ATTACHMENTS

A. Program Compliance
B. Quarterly Summary of CNG Costs and Variances

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ATTACHMENT A

Program Compliance

Maximum Trade Maturity – The guidelines specify that the maximum trade maturity for hedges is 30 months forward to coincide with the last business day of the fiscal year being hedged. – As of March 31, 2018 there are no hedges in place.

Hedge Ratio - Limited to 100% of planned volume –There are no hedges in place for FY18 therefore we are in compliance with the Hedging Program Guidelines.

Counterparty Credit Criteria – Requirements to post collateral are based on credit ratings of the counterparties and volume of hedges; there are no hedges in place therefore we are in compliance.

- Aa3/AA- or better — No collateral required
- A3/A- or better — $25 million limit without collateral
- Baa1/BBB+ — $15 million limit without collateral
- Baa2/BBB — $10 million limit without collateral
- Baa3/BBB- — $ 2.5 million limit without collateral

Re-Confirm Assumptions –Before entering into new hedges we will reconfirm assumptions with our hedging advisor.

Re-Confirmation of Therms - The amount of therms will be reconfirmed with Operations prior to entering into new hedges.

All information is as of March 31, 2018, unless otherwise specified.

ATTACHMENT B

Quarterly Summary of CNG Costs and Variances
FY 2018 QTR3

Performance vs. Budget	Price per Therm	Volume in Therms	Total Cost
Budget	$ 0.5100	11,889,094	$ 6,063,438
Actual therms consumed	$ 0.4460	10,646,313	$ 4,747,917
Variance to Budget excluding hedge: Fav (Unfav)	**$ 0.0640**	**1,242,781**	**$ 1,315,521**
Variance Analysis:			
Actual volume vs budget variance fav (unfav)	$ 0.5100	1,242,781	$ 633,818
Actual price vs budget variance fav (unfav)	$ 0.0640	10,646,313	$ 681,702
Variance to Budget excluding hedge: Fav (Unfav)			**$ 1,315,521**
Therms Hedged and net receipts (payments) for hedge (a)		-	$ -
% of budgeted therms hedged		0.00%	
Total variance to budget (No hedges entered)			**$ 1,315,521**
Total cost of gas including hedge (No hedges entered)	**$ 0.4460**		**$ 4,747,917**
Actual cost as a percentage of budget			78.3%

(a) No hedges were in place for 3rd quarter FY18.