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Conference Title: FY2024 Third-Quarter 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, Third-Quarter Investor Call. Today's conference is being recorded. At this time, I'd like to turn the conference over to Heesun Choi, vice president capital market relations.

Heesun Choi: Thank you, operator. Welcome to our investor conference call for our third-quarter of fiscal year 2024. Joining with me today are Andrew Don, our Chief Executive Officer, and Ling Wang, our Chief Financial Officer. Andrew and Ling will discuss our financial and operating resources during the three months and nine months ended February 29, 2024.

Today's presentation slides and financial reports filed with the SEC are available on our website, www.nrucfc.coop, under Investor Relations. This call is being recorded and a replay and transcript will be made available under Investor Relations.

Our presentation today will include forward-looking statements and certain non-GAAP financial measures. Please review the disclosures on slide two and slide three of the presentation regarding these statements and measures. I would like to remind you that any forward-looking statements that we may make during today's call as of April 17, 2024, are subject to risk 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-Q filed by the SEC on April

12, 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 your questions. You can ask any 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 morning and thank you for joining our call today to review our business and operating results during the nine months ended February 29, 2024, which is our third fiscal quarter of 2024.

I'm moving to slide five to discuss highlights during the quarter. We experienced another strong quarter marked by robust loan growth. We strategically managed the growth by effectively utilizing our various funding sources resulting in superior financial metrics and maintaining a high-quality loan portfolio. Our loans to members continued to grow and reached $34.4 billion, reflecting an increase of approximately $1.9 billion, or 6%, during the nine months ended February 29, 2024. We had no charge-offs during the fiscal year and our loan portfolio remained pristine with only 25 basis points of loans classified as non-performing at the quarter end. We also successfully maintained a strong financial position.

Our adjusted TIER was 1.25 times during the nine months ended February 29, 2024, well above our goal of 1.1 times. We remain committed to growing our members' equity to support the loan growth. Our members' equity stood at $2.3 billion at February 29, 2024.

Our liquidity position remains sound as we maintain diverse, well-established funding sources to minimize the risk of being dependent on any single source or market. Our diverse liquidity sources consist of cash, investments, committed bank lines, committed loan facilities under the guaranteed underwriter program, revolving note purchase agreement with Farmer Mac and access to repo facilities.

We remain committed to maintaining strong investment grade ratings from Fitch, Moody's and S&P. Our short-term and long-term credit ratings and outlook are unchanged. During the quarter, S&P and Moody's affirmed all of CFC's credit ratings with a stable outlook.

Now I'm turning to slide six to discuss our loan portfolio. As I mentioned, our loans to members increased by $1.9 billion, $34.4 billion at February 29, 2024, compared to $32.5 billion at May 31, 2023. Specifically, during the third quarter, we recorded an addition of $858 million in our loans to members, which accounts for nearly 46% of the fiscal year-to-date loan growth. 92%, or $1.7 billion, of the net loan increase was driven by increase in loans to our distribution of power supply borrowers.

At February 29, 2024, our loans to distribution members totaled $26.9 billion and our loans to power supply members totaled $5.7 billion, accounting for 94% of total loans to members. As we mentioned on a prior quarterly call, the sale of RTFC's business to NCSC was finalized and effective on December 1, 2023. Consequently, beginning this quarter, we will refer to the RTFC loans as NCSC telecom loans and the electric loans previously under the NCSC portfolio as NCSC electric loans.

During the nine months ended February 29, 2024, we experienced increases in loans outstanding across all member classes. Our distribution loan portfolio increased by $1.4 billion and our power supply loan portfolio increased by $294 million.

We also experienced increases in NCSC telecom loans of $61 million, CFC statewide and associate loans of $58 million and NCSC electric loans of $28 million during the nine months ended February 29, 2024. In terms of the loan type, long-term loans increased by $1.5 billion to $30.9 billion, and line of credit loans increased by $407 million to $3.5 billion at February 29, 2024, compared to the levels of May 31, 2023. During the nine-month period, we made long-term loan advances for a total of $2.7 billion. Approximately $2.5 billion, or 95%, of those advances were for

capital expenditure purposes, the remaining balance being for other purposes, primarily business acquisitions.

Additionally, of the $2.7 billion total long-term loans advanced, $2.5 billion were fixed-rate loan advances with a weighted average fixed-rate term of 12 years. In comparison, the fixed-rate term was 18 years for long-term loans advanced during the same period from our prior fiscal year. Our members continue to show a preference for slightly shorter fixed-rate term loans, given the prevailing higher interest rate environment.

Our loan growth is partially driven by increased loans outstanding for broadband projects. We estimate that there are over 200 electric cooperatives engaged in rural broadband projects at various stages of development. Generally speaking, these projects are financed through a mix of grants and debt funding. At February 29, 2024, CFC's total outstanding loans associated with these broadband projects was approximately $2.9 billion, an increase of $512 million compared to the May 31, 2023, level of $2.4 billion. We typically fund our members' broadband projects through their electric balance sheet rather than extending loans to a separate broadband subsidiary. With that, I will now turn the call over to, Ling, who will review our financial results in greater detail. Thank you.

Ling Wang: Thank you, Andrew, and good morning, everyone. I am going to move on to slide eight to discuss our financial results for the nine-months ended February 29, 2024, which I am going to refer to it as the current fiscal quarter end. Our total assets at the current fiscal quarter end were approximately $35.9 billion, an increase of $1.9 billion, or 6%, from the prior fiscal year-end level. The primary driver of this growth was a $1.9 billion increase in loans to members.

Our total liabilities increased by $1.6 billion, or 5%, to $33 billion at the current fiscal quarter end, as we issued debt primarily to fund the loan growth. Our members' equity, which excludes cumulative derivative forward value gains and accumulated other comprehensive income,

increased by $111 million to $2.3 billion from the prior fiscal year-end, primarily due to the adjusted net income of $224 million during the first nine months of this fiscal year, partially offset by the CFC Board of Directors authorized patronage capital retirement of $113 million. The $113 million patronage capital retirement comprised of a $72 million paid to members in September 2023 and $41 million paid from CFC to RTFC in December 2023 in connection with the RTFC sale transaction.

Our adjusted debt-to-equity ratio was 6.29-to-1 at the current fiscal quarter end, a decrease from 6.38-to-1 at November 30, 2023, but an increase from 6.04-to-1 at May 31, 2023. The decrease from the November 30, 2023, level was driven by an increase of an additional $100 million subordinated deferral debt and the redemption of the $400 million in short-term time deposit to pay down a portion of our maturing long-term debt. We expect our adjusted debt-to-equity ratio will remain above our target of 6-to-1, as we project an increase in total debt outstanding to fund anticipated loan growth.

Looking at slide nine for our loan portfolio. The composition of our loan portfolio remained largely unchanged from the prior fiscal year-end. Our loan portfolio consists mainly of long-term fixed-rate secure loans to rural electric cooperatives.

At the current fiscal quarter end, $34 billion, or 98%, of our loans consist of loans to rural electric systems, and $549 million, or 2%, to the telecommunication sector. Our long-term fixed-rate loans were 88% of total loans outstanding at the current fiscal quarter end, 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 approximately 91% of our loans being senior secured at the current fiscal quarter end, similar to the level of 92% at May 31, 2023.

We generally offer long-term amortized loans to our members for up to 35 years. The average remaining maturity of our long-term loans, which accounted for 90% of total loans outstanding at the current fiscal quarter end, was 19 years.

Slide 10 represents historical performance of our loan portfolio for the past five years. The quality of our loan portfolio continued to demonstrate strength and we observed positive trends in our credit metrics. We had only one non-performing loan outstanding at the current fiscal quarter end, totaling $85 million, or 0.25%, of total loans outstanding. This loan was made to an electric power supply borrower.

In comparison, we had loans to two CFC electric power supply borrowers, totaling $89 million, classified as non-performing as of May 31, 2023. During the first quarter of this fiscal year, we received $4 million in loan principal payments from one of the non-performing borrowers, which paid off the outstanding balance of its non-performing loan.

Subsequent to February 29, 2024, we received a $36 million payment on the one 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 the current fiscal quarter end, compared to $53 million at May 31, 2023.

The allowance coverage ratio decreased to 14 basis points at the current fiscal quarter end from 16 basis points at May 31, 2023. The $4 million decrease in the allowance for credit losses reflected an $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 credit quality and risk profile of our loan portfolio.

During the nine months ended February 29, 2024, we had no loan charge-offs. We recorded a $1 million in net loan recoveries to a previously charged-off loan amount during fiscal year 2024. We

believe that the overall quality of our loan portfolio remains strong at the current fiscal quarter end, evidenced by the limited default and losses in our electric utility portfolio since the inception of CFC. We celebrated our 55th year in business last week, and 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 cumulative net charge-off of only $100 million.

Moving on to slide 11. During the third quarter, our adjusted net income increased by $8 million, or 11%, primarily due to a $13 million increase in adjusted net interest income and a $6 million favorable shift from losses to gains recorded on our investment securities, partially offset by a reduction in the benefit for credit losses of $5 million and a $5 million increase in operating and non-interest expenses. For the nine-month period, our adjusted net income increased by $39 million, or 21%, primarily due to a $29 million increase in adjusted net interest income, $14 million favorable shift from losses to gains recorded on our investment securities, a $9 million favorable shift from provision for credit losses and a $3 million increase in fee and other income, partially offset by a $16 million increase in operating and other non-interest expenses.

The $13 million increase in adjusted net interest income during the third quarter and the $29 million increase in adjusted net interest income for the nine-month period were driven by a 7% increase in our average interest earning assets and increases in adjusted net interest yield of 7 basis points and 4 basis points for the third quarter and for the nine-month period, respectively.

Specifically, our adjusted net interest yield was 1.18% for the third quarter, compared to 1.11% for the same prior year quarter, and our adjusting net interest yield was 1.13% for the nine-month period, compared to the 1.09% for the same prior year period.

Being a member-owned finance cooperative association, our primary finance goal focuses on earning an annual minimum adjusted time interest earned ratio, or a TIER, of 1.1 times. For the third quarter and nine-month period, our adjusted TIER decreased by 0.01 to 1.29 and 1.25 times,

respectively, compared to the same prior-year periods. Both comfortably exceeding our target of 1.1 times.

Our total debt outstanding was $32.5 billion at the current fiscal quarter end, an increase of $1.5 billion, or 5%, from May 31, 2023, level, primarily to fund the loan growth in our portfolio. We continue to maintain diverse funding sources, including funding from our members, as well as capital markets and non-capital markets funding. At the current fiscal quarter end, $4.7 billion of CFC's funding came from our members in the form of short-term and long-term investments, a slight decrease of $100 million, or 2%, from the May 31, 2023, level. Our member investments represented 15% of our total debt outstanding at the current fiscal quarter end, a slight decrease from 16% at May 31, 2023.

At the current fiscal quarter end, our funding under the guaranteed underwriter program and notes payable with Farmer Mac totaled $11 billion, or 33%, of our total debt outstanding, an $854 million, or 9%, increase from the May 31, 2023, level, and this is primarily driven by net increases of $733 million in borrowings under the Farmer Mac note purchase program and $122 million under the guaranteed underwriter program.

Our capital markets related funding sources totaled $17 billion at the current fiscal quarter end, a $787 million, or 5%, increase from the May 31, 2023 level. The increase was primarily due to a net increase of $2 billion in dealer medium-term notes, offset by net decreases of $842 million in collateral trust bonds and $394 million in dealer commercial paper outstanding.

Dealer commercial paper outstanding decreased to $899 million at the current fiscal quarter end, compared to $1.3 billion at May 31, 2023. At the current fiscal quarter end, capital markets related funding sources accounted for 52% of our total funding, unchanged from the May 31, 2023 level. Also, at the current fiscal quarter end, 54% of our total debt was secured and 46% was unsecured, slightly shifted from 56% for secured and 44% for unsecured at May 31, 2023.

Our short-term borrowings increased by $59 million to $4.6 billion, accounting for 14% of our total debt outstanding at the current fiscal quarter end, compared to $4.5 billion, or 15%, of total outstanding at May 31, 2023. The decrease in short-term borrowings was driven by a $500 million short-term borrowing from Farmer Mac, partially offset by $394 million decrease in dealer commercial paper and a $47 million decrease in short-term member investment. At the current fiscal quarter end, a total of $3.2 billion, or 70%, of our short-term borrowing come from short-term investments made by our members, compared to $3.3 billion, or 72%, at May 31, 2023.

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. Our member short-term investments have averaged around $3.5 billion over the last 12 fiscal quarter-end reporting periods.

Slide 13 shows various sources of liquidity CFC had in place at the current fiscal quarter end. Our available liquidity includes cash, investments, committed bank lines, committed loan facility under the guaranteed underwriter program and Farmer Mac revolving note purchase agreements totaling $6.6 billion at February 29, 2024. As I mentioned in the prior call, in December 2023 we closed an additional $450 million committed loan facility under the guaranteed underwriter program, resulting in the increase of the total availability under this program from $750 million to $1.2 billion.

As indicated in the table on the right side, at the current fiscal quarter end, we had a total of $7 billion in debt maturities over the next 12 months, with 46%, or $3.2 billion, of these debt maturities representing short-term investment from our members. Because our members have traditionally rolled over a large portion of their short-term investments with us at maturity, we consider our member investments to be a very stable and reliable source of funding for CFC.

The remaining $3.8 billion in debt maturities include $899 million dealer commercial paper, a $500 million short-term notes payable to Farmer Mac and $2.4 billion long-term and subordinated debt obligations. These obligations are well covered by the $6.6 billion liquidity discussed previously. It is also worth noting that the $6.6 billion liquidity does not include the $1.5 billion scheduled repayment and amortization on our long-term loans that we expect to receive from our members over the next 12 months.

Slide 14 summarizes CFC's projected debt issuance needs over the next 18 months, subsequent to the current fiscal quarter end. 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.

During the third quarter, we issued a total of $1.85 billion in fixed and floating rate medium-term notes, ranging from three to seven years, and $100 million in subordinated deferral debt to fund our loan growth and to refinance maturing long-term debt.

Over the next 18 months, from March 2024 through August 2025, we have a total of $4.5 billion of long-term debt maturities and amortization, consisting of $2.6 billion in capital market debt and $1.9 billion in non-capital market debt. We expect our loan growth over the same period to be approximately $2.6 billion.

As indicated in the chart, we project to issue approximately $5.1 billion in long-term debt over this period to refinance existing debt maturities and to fund our expected loan growth. Thank you again for joining us today to review our results for our third fiscal quarter end of February 29, 2024. We appreciate your interest in CFC and look forward to discussing our financial performance and funding plan in the future. I would like to ask the operator to open the lines for questions and also

suggest that you may submit your questions via web services, so we may respond to those as well. Thank you.

Operator: Thank you. If you're dialed in via the telephone and 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 an audio question. If you are in the event via the web interface and would like to ask a question, simply type your question in the ask a question box and click send.

Again, that is star one. If you would like to ask phone questions, star one. We'll pause for a moment. And we do have a question from Chris Haberlin, with Agincourt Capital Management.

Chris Haberlin: Thanks very much for taking the question. First question on the non-performing loans. If you had a balance of $85 million at the end of the quarter and received a payment after the end of the quarter, leaving you with around $50 million outstanding on the non-performing loan, what's the outlook there for that remaining balance on that loan? Are you expecting to recover that over time or was the payment that you received in the third quarter just a one-off?

Andrew Don: It's a complicated loan structure and as I said, we did put it on a non-performing, I think in 2020, and it's under the restructuring agreement we have with this borrower. They're required to make certain minimum payments really based on their cash flow. It's not a very typical loan arrangement. That's the structure. So it's hard to, because it is based on, to be frank, how the borrower performs from a cash flow perspective. Having said that, yes, they have consistently outperformed in terms of cash flow from operations, which has resulted in these kinds of payments that have exceeded what was anticipated.

To answer your question, I think that we would expect to potentially recover a reasonable portion of the amount that's still outstanding. But it is highly dependent on their cash flow from operations,

which is dependent on market conditions, primarily utility market conditions, not capital market conditions or interest rate environment conditions. It's really related to the cash flow of that particular borrower.

Chris Haberlin: Great. Thanks so much for the color on that. And then just second question, wanted to ask about ratings and specifically the rating at S&P. I know they had downgraded I think in March of 2021 following Winter Storm Uri. Obviously with the Brazos and Brazos Sandy Creek issues kind of largely in the rearview mirror, and I think you took relatively minimal charge-offs as a result of those storms. Can you just talk about the dialogue you've had with them and getting the rating returned back to, I believe it was at A plus there prior to the downgrade? Any outlook or update on discussions with S&P?

Andrew Don: Sure. Well, I think we were at A, not A plus because S&P some time ago equalized our senior secured an unsecured rating. But they did go from A to A minus. Obviously, we were disappointed in that action because I think what we told the agency at that time is we believe that the issues related to Winter Storm Uri were not widespread to Texas. It was something specific to that borrower, and we thought that very likely it would be resolved appropriately as it has been.

So to answer your question, yes, we have had a very frank, robust discussion with the analyst at Standard & Poor's, pointing out the history, pointing out the way this has worked out. To be frank, it's disappointing that they are not reflecting the outcome to date. So if you'd like to share your view with them, we would certainly welcome that. But yes, we have told them as well that we don't believe it's reflective of, again, what's happened and how people view the result in terms of the way this has worked out. But yes, we continue to have a discussion with them, continue to be very frank. I said it's disappointing that they won't change their view.

Chris Haberlin: I understand your disappointment. I share your disappointment and certainly agree with where you're coming from. So thanks very much for the update, and I'll get back in queue.

Andrew Don: Yep. Thanks for your interest.

Operator: Thank you. And then once again, if you would like to signal with phone questions, please press star one on your touchtone telephone. Again, that's star one. If you'd like to ask a question via the web interface, simply type your question in the ask a question box and click send. We'll pause for just a moment.

Ling Wang: So we do have a couple of questions that's submitted through the web. One of them is to ask us to comment on the leverage and the trend in leverage. So, at the end of February 29, 2024, our adjusted debt-to-equity ratio is about 6.29-to-1. That is a decrease from 6.38-to-1 from the last fiscal quarter, but it is an increase from 6.04-to-1 from May 31, 2023. I think we have publicly stated that our target is 6-to-1, and we believe that we will be above our target, because we do project an increase in our total debt outstanding in order to support our loan growth. That's the comment on the leverage.

I think another question from the web, I think the question is, what triggers a member to not roll over their short-term investment?

Andrew Don: Or loans? Is it loans?

Ling Wang: I don't believe it's short-term loans. Right.

Andrew Don: Well, I guess maybe do what?

Ling Wang: Yeah, whoever asked the question, if you could ask?

Andrew Don: Are you interested in short-term loans or short-term investments?

Ling Wang: Short-term loans will be the line of credit loans and short-term investment will be the three-point, yeah.

Andrew Don: The deposits with us. Yeah.

Ling Wang: The deposit with us, and maybe I'll just comment on short-term investments.

Andrew Don: We can respond to both, I guess, just to make it clear.

Ling Wang: Sure. So for short-term investments, I think our members, they have pretty consistently invested their excess cash with us. What will make them not to reinvest will be if they have cash needs so they don't have excess cash, and that will impact our member investment level. It is investments. Yeah. The other reason would be maybe if they want to compare rates, maybe if their local bank offers a higher rate, which I think is unlikely. We tend to offer pretty attractive rates to our members in terms of member investment. So I think from our perspective, historically, members, if they don't roll over, it's typically because they have use for that cash.

Andrew Don: Sometimes they will get, especially if they're an RUS borrower, as an example, they might get a large funding, and it might be for an upcoming project that they haven't fully funded yet. So they'll put it on deposit with us. There's some timing issues that might drive a large investment amount.

Operator: And at this time, there are no further phone questions.

Andrew Don: Okay. Well, great. Thank you for joining us this morning. I look forward to talking to you in the future. Have a nice day.

Operator: Well, thank you. And that does conclude today's conference. We do thank you for your participation. Have an excellent day.