Review of Swap Policy and Outstanding Swaps

Finance & Insurance Committee
Item 7.a.
September 9, 2013

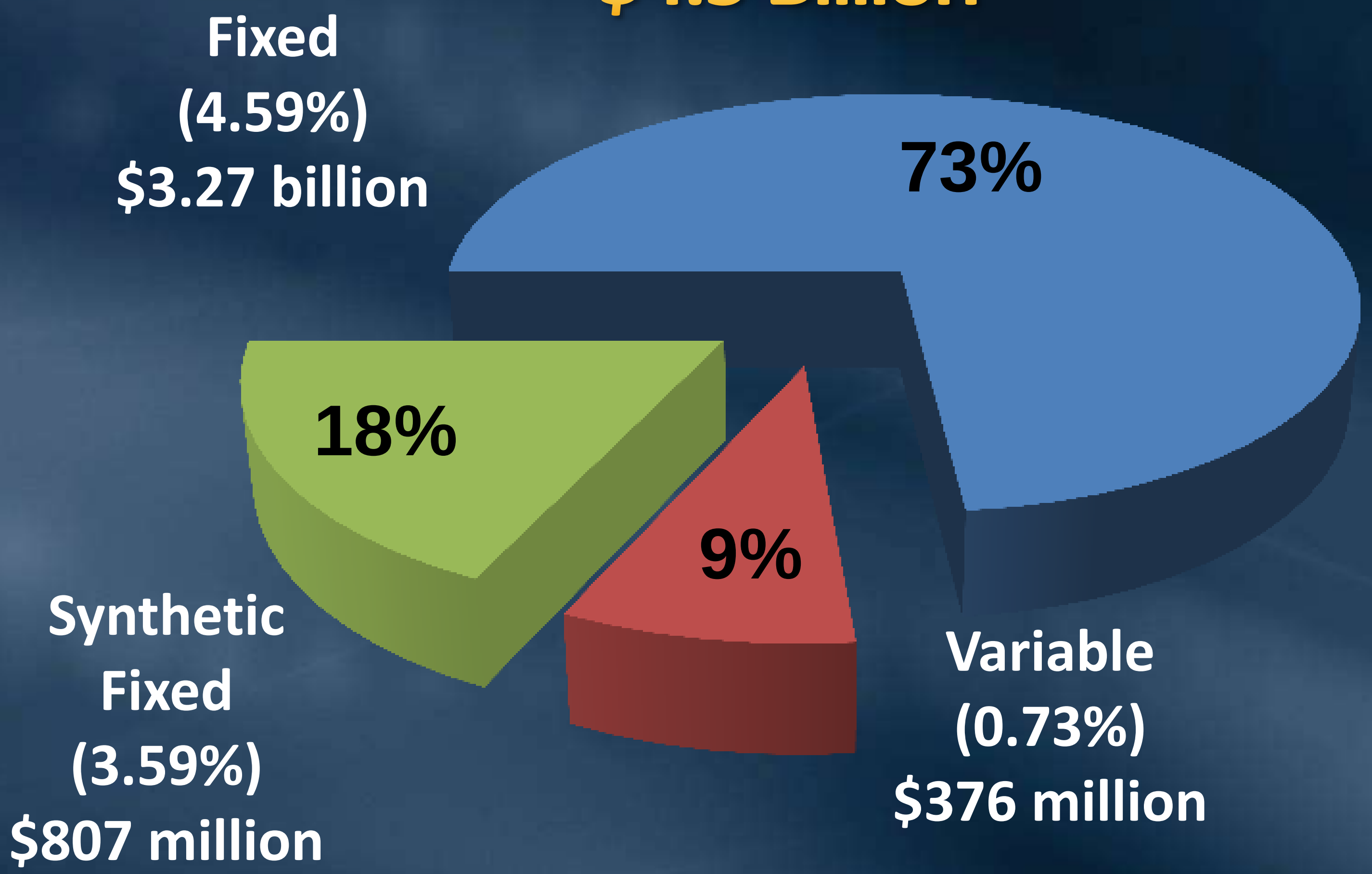
Outline

- Outstanding Debt and Swaps
- Example of an Interest Rate Swap
- Metropolitan’s Interest Rate Swap Policy
- Benefits of Interest Rate Swaps
- Risks Associated with Interest Rate Swaps
- Mark to Market Values
- Rating Agency Report
- Summary

Revenue Bond Debt Outstanding

June 30, 2013

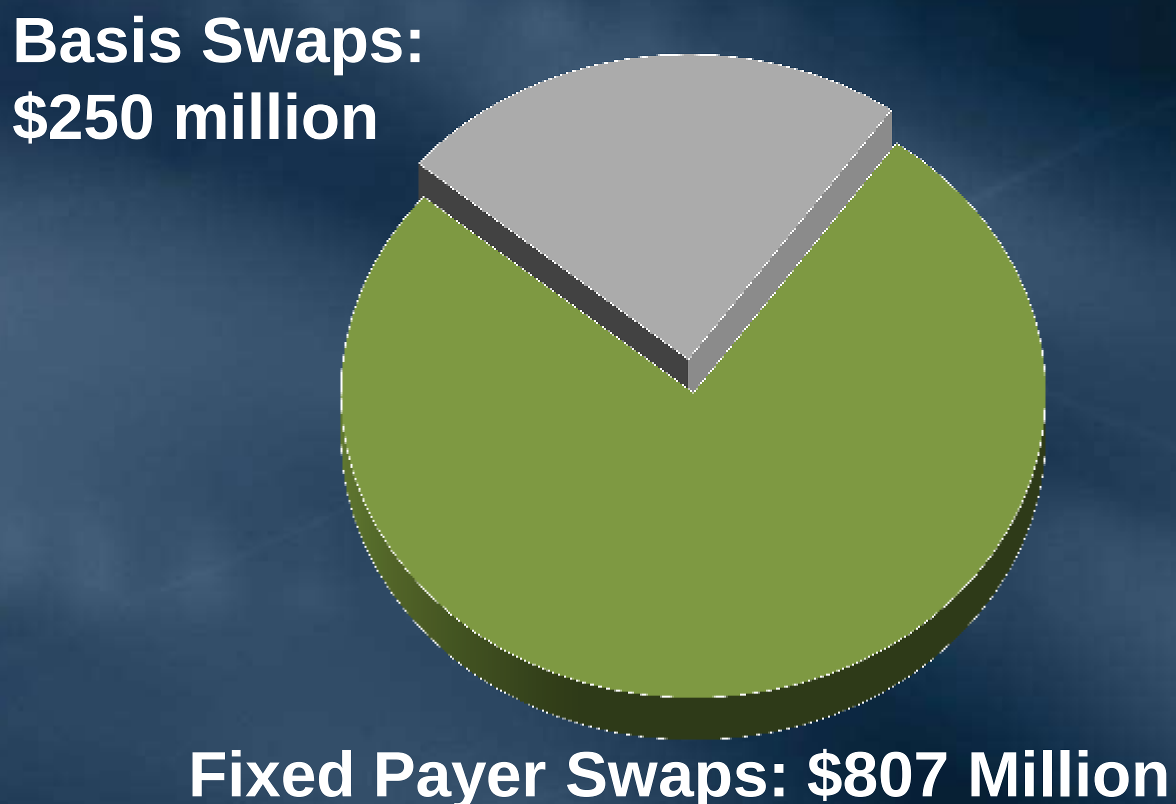
$4.5 Billion



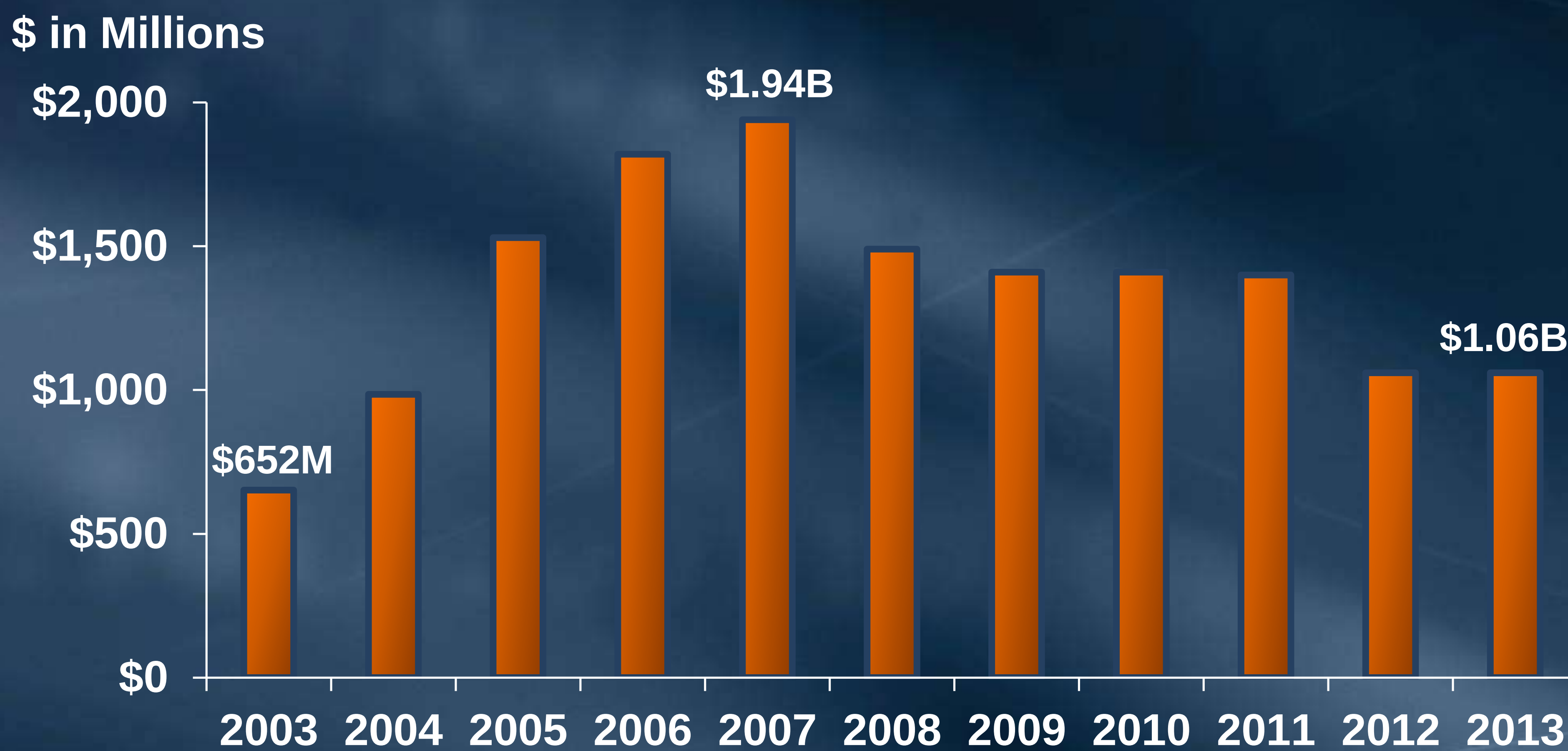
Interest Rate Swaps

June 30, 2013

$1.1 Billion

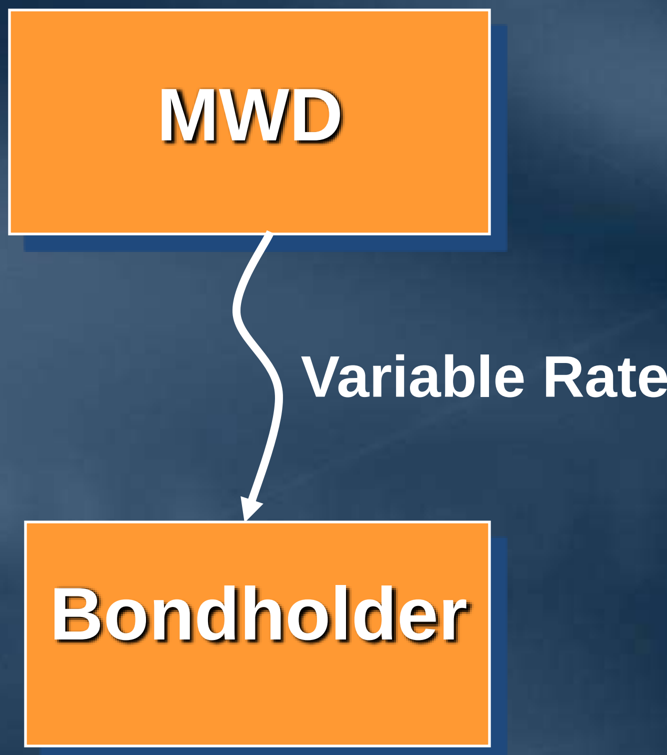


Metropolitan's Swap Program
Notional Amount Outstanding



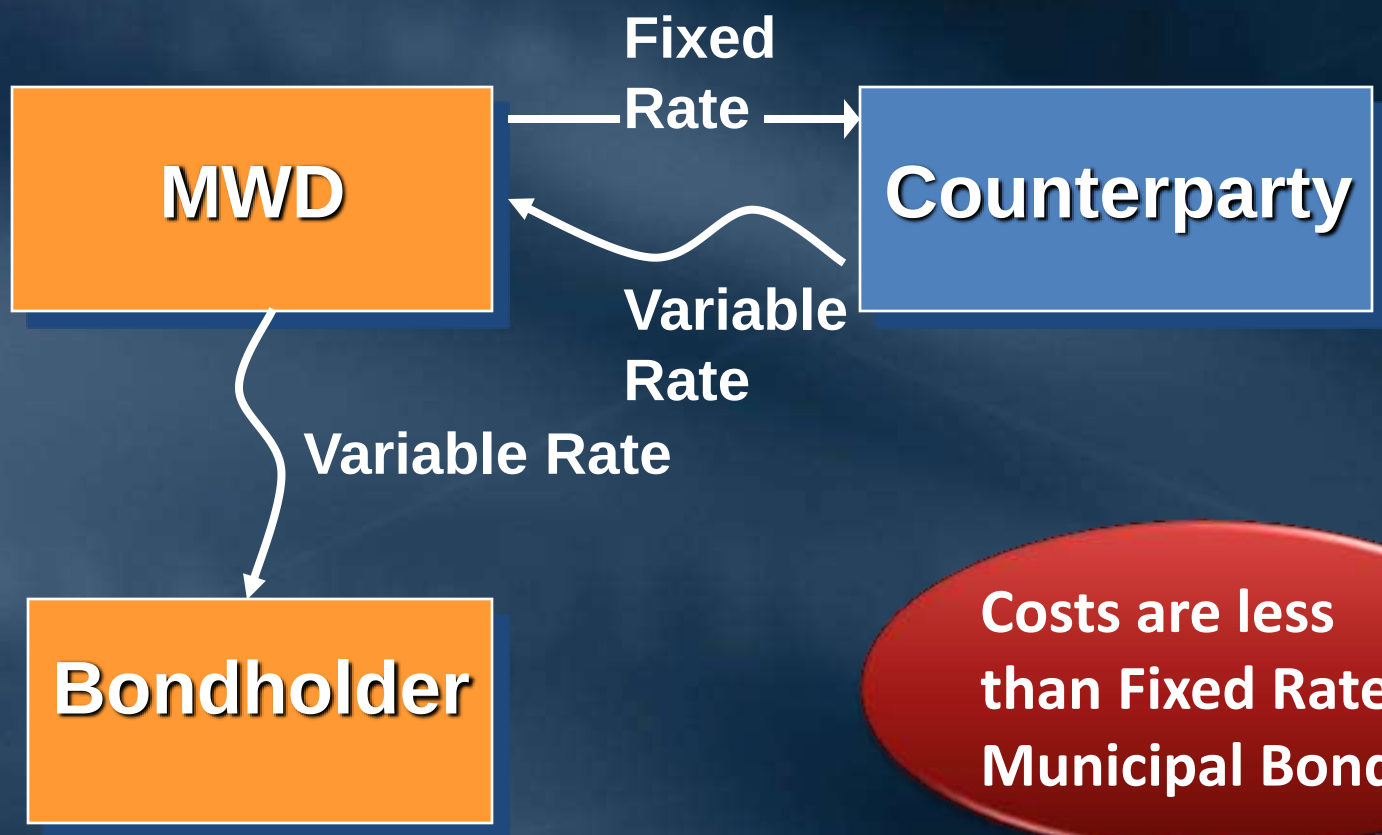
Example of an Interest Rate Swap

Variable Rate Debt Issuance



Example of an Interest Rate Swap

Floating to Fixed Rate Swap
(Fixed Payer Swap)



Costs are less than Fixed Rate Municipal Bonds

Metropolitan's Swap Program is Based on Board Policy

- Master Swap Resolution (2001)
  - Section 5922 California Government Code - finding required
  - Defines authority to execute swaps
  - Approval for authorized swaps and agreements
  - Security and payment provisions
- Master Swap Policy (2001, amended 2009)
  - Purpose
  - Parameters and guidelines
  - Counterparty qualifications and limitations

Metropolitan's Swap Program
June 30, 2013

- Notional Balance: $1.1 billion
- Thirteen swaps
  - $21 million to $164 million
- Four counterparties
  - Credit Ratings range from "Baa2" to "Aa3"
  - Qualified swap counterparty credit rating: "Aa3" or "AA-"
- Mark-to-Market Value: ($116.1 million)
- Collateral Posting: $7.2 million
- Savings to date: $91.6 million

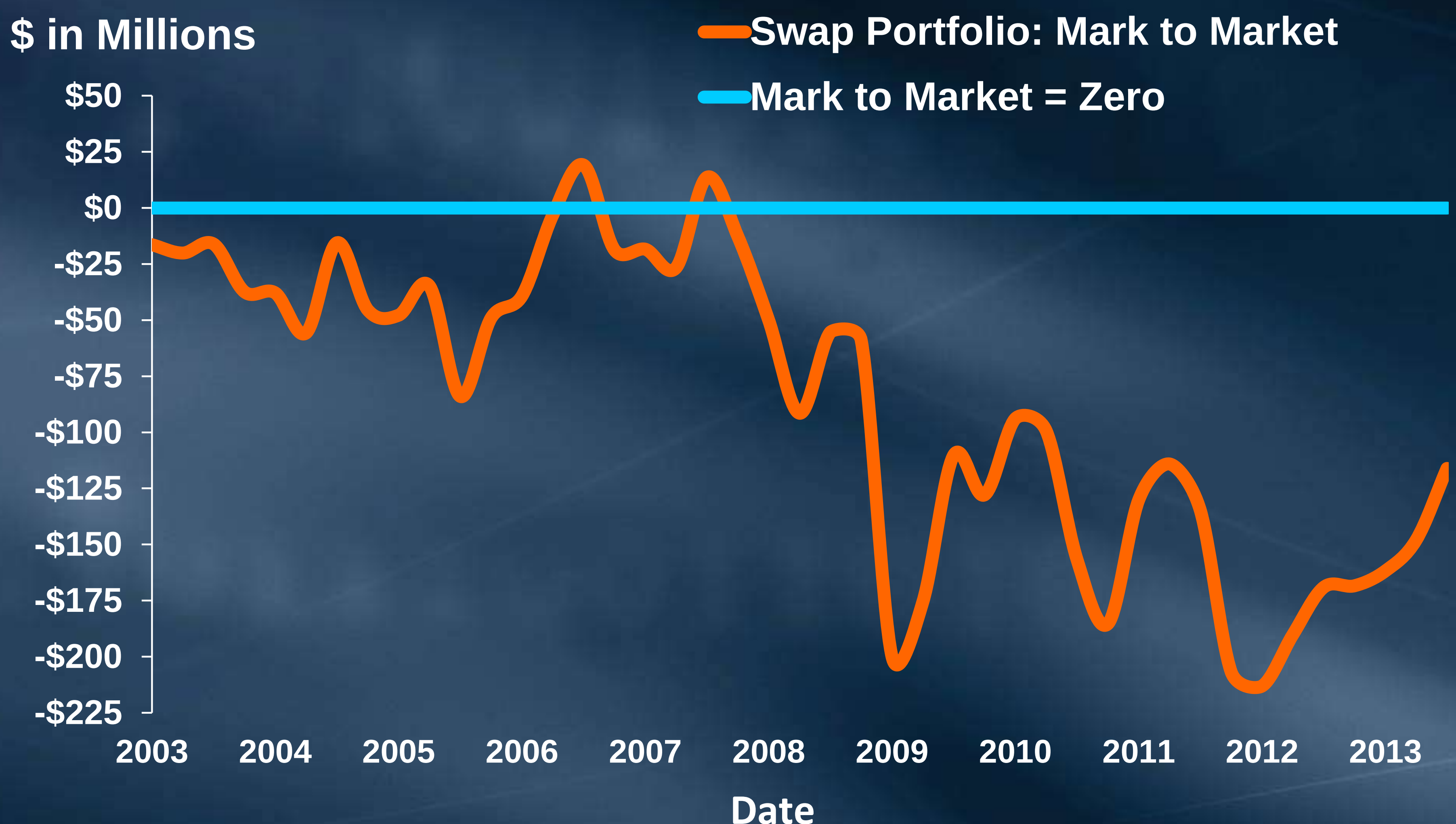
Interest Rate Swaps : Benefits

- Lower costs than bond financing
  - Refunding debt for savings
- Increase variable rate exposure without debt issuance or liquidity costs
- Flexibility to take advantage of favorable market conditions
- Realize economic savings while preserving call option on bonds
- Hedge against rising interest rates

Interest Rate Swaps : Risks

- Basis risk – the difference between actual interest rates and the index
  - Market dislocations for extended periods
  - Refunding savings assumed “built-in basis loss”
- Tax risk - change in marginal tax rates will affect value and cash flow
- Counterparty risk
  - Rating requirements for qualified counterparties
  - Demonstrated success in changing counterparties when needed (UBS and Bear Stearns)
- Termination payments

Mark to Market Values
2003 to 2013



Metropolitan's Swap Program

Rating Agency Report

- "MWD's interest rate swap portfolio represents a very low credit risk because of highly rated swap counterparties, a low degree of involuntary termination risk because of moderate ratings trigger spread, and strong management oversight, including a formally adopted swap management plan, quarterly review of the swap portfolio, and counterparty diversification requirements".

Summary

- Interest rate swaps are “marked-to-market” every month
  - Mark-to-market varies with interest rates, ($116.1 million) as of June 30, 2013
- Disclosure of swap position
- Savings of $91.6 million since 2001
- Risks have been mitigated with June 2012 refunding and swap terminations
- Successful management of program

End of Presentation