

BRIEFING NOTE

DECISION

2023-2024 ENERGY & INFRASTRUCTURE DIVISION COMMODITY BASED BUSINESS OPERATING & CAPITAL BUDGET

NOVEMBER 2, 2022

ISSUE:

Approval of the 2023-2024 Operating and Tangible Capital Asset Budget for the commodity-based business unit.

RECOMMENDATION:

It is recommended through the Administrative Committee that City Council approve the 2023-2024 Operating Budget update as well as the 2023-2024 Tangible Capital Asset Budget update for the commodity-based energy business unit (Comco).

COUNCIL STRATEGIC PRIORITY

Resilience & Sustainability

The 2023-2024 budget will prioritize sustaining capital investment based on detailed long-range business plans, optimize energy portfolio, and identify growth capital to support energy transition and green infrastructure opportunities.

KEY RISKS:

Health, Safety and Environmental Impact:

The Energy & Infrastructure Division's objective to conduct business in a safe and ethical manner within regulatory standards and remain compliant. Environmental protection is a constant consideration.

Financial Impact:

Funding Request:	Yes	If yes, amount: As noted below.
Budgeted Item:	Yes	Funding Source: Reserves, Debenture, Working Capital and/or Third-Party Funding
Funding Explanation:	As noted below.	
Budget Amendment Form?	No	

The City of Medicine Hat operates within the commodity business; as such, Council accepts there is a higher risk associated with operating an oil, gas and power enterprise versus the standard *Municipal Government Act's* risk parameters.

Operating Budget

Operating Budget in thousands (,000)	2022 APPROVED BUDGET	2023 / 2022 BUDGET CHANGES	2023 BUDGET	2023 / 2022 BUDGET % CHANGES	2024 / 2023 BUDGET CHANGES	2024 BUDGET	2024 / 2023 BUDGET % CHANGES
Revenues	\$260,973	\$49,754	\$310,727	19%	(\$54,564)	\$256,163	-18%
Expenses	\$205,131	\$25,636	\$230,767	12%	(\$37,847)	\$192,919	-16%
Transfers	\$9,306	(\$2,647)	\$6,658	-28%	\$2,280	\$8,938	34%
EBITDA	\$46,584	\$26,711	\$73,294	57%	(\$18,990)	\$54,304	-26%

*2022 forecasts are based on YTD actuals as of September 30, 2022, plus remaining months re-forecasted using the most up-to-date data models and analysis.

Legal / Policy Impact:

The City of Medicine Hat, being an operator, is required to operate according to the *Oil and Gas Conservation Act and Electric Utilities Act* that is enforced and administered by the respective provincial regulator. Additionally, the Government of Canada has made commitments to reduce emissions which will impact the future regulatory landscape. The City as a responsible operator, is committed to adhering to these Acts and regulations and operating in an environmentally responsible manner.

Public Implications:

The 2023-2024 budgets were developed based on City Council's Strategic Priorities, most notably, Resilience & Sustainability; Partnerships & Governance; and Service Orientation. The public needs safe reliable energy provided at market competitive rates.

BACKGROUND:

The Operating Budget and Tangible Capital Asset Budget were prepared based on the commodity-based Business Plans which aligns with City Council's Strategic Priorities. A high-level review occurred with the following key changes implemented:

- Update to volumes to reflect changes to large commercial/industrial load forecast, continuation of the Abandonment & Reclamation (A&R) Program, asset dispositions and modifications to original plans.
- Update to commodity price forecasts which affect all revenues, Payment in Lieu of Tax, natural gas purchases, and carbon compliance costs.
- Update to Operations & Maintenance expenses corresponding with changes to volumes stemming from asset dispositions, continuation of the Abandonment Reclamation (A&R) Program and modifications to operating plans.
- Update to General & Administration expenses to correspond with a reduction in staffing requirements and increase in the expected carbon compliance cost (volume related).
- Update to Capital plans to reflect asset dispositions, small-scale development program to enhance existing asset portfolio, and prioritizing sustaining capital investments to ensure infrastructure integrity.

OPTIONS CONSIDERED & POTENTIAL IMPLICATIONS:

It is recommended that Council approve the Comco 2023 - 2024 Operating Budget, Tangible Capital Asset Budget.

IMPLEMENTATION PLAN:

- Subject to Council approval, execute the 2023-2024 Operating and Tangible Capital Asset Budgets.
- Follow the 2023-2024 Business Plans.
- Measure results, communicate and celebrate successes.

PREPARED BY & DATE:	Joel Higgins, Business Analyst, Josh Barclay Energy Marketing Specialist	October 28, 2022
REVIEWED BY & DATE:	Boyd Mostoway, Director, Medicine Hat Power & Water Grayson Mauch, Director, City Operations Travis Tuchscherer, Manager Energy Marketing and Business Analysis	
APPROVED BY & DATE:	Brad Maynes, Managing Director, Energy & Infrastructure	
ATTACHMENTS:	#1: 2023-2024 Comco Operating Budget #2: 2023-2024 Comco Capital Budget	

OPERATING BUDGET

Operating Budget <small>in thousands (,000)</small>	2022 APPROVED BUDGET	2023 / 2022 BUDGET CHANGES	2023 BUDGET	2023 / 2022 BUDGET % CHANGES	2024 / 2023 BUDGET CHANGES	2024 BUDGET	2024 / 2023 BUDGET % CHANGES
Revenue							
Electric Generation	173,042	31,382	204,424	18%	(32,514)	171,909	-16%
Production	87,931	18,372	106,303	21%	(22,050)	84,254	-21%
Total Revenues	260,973	49,754	310,727	19%	(54,564)	256,163	-18%
Expenses							
Electric Generation	109,656	19,344	129,000	18%	(19,920)	109,080	-15%
Production	95,475	6,292	101,767	7%	(17,928)	83,839	-18%
Total Expenses	205,131	25,636	230,767	12%	(37,847)	192,919	-16%
Transfers (to)/from Gas Retail	24	(20)	4	-85%	(3)	1	-85%
Transfers (to)/from Electric Retail	(9,282)	2,620	(6,662)	-28%	(2,277)	(8,939)	34%
Earnings Before Interest, Taxes and Amortization							
	46,584	26,718	73,302	57%	(18,996)	54,305	-26%
Interest Revenue	5,100	2,172	7,272	43%	55	7,327	1%
Interest Expenses	(3,213)	(600)	(3,813)	19%	207	(3,606)	-5%
Amortization	(22,365)	2,023	(20,342)	-9%	2,042	(18,300)	-10%
Depreciation/Depletion/Accretion	(21,339)	11,997	(9,342)	-56%	317	(9,025)	-3%
Net Earnings/ (Loss)	4,767	42,310	47,077	888%	(16,375)	30,702	-35%

CAPITAL BUDGET

Tangible Capital Asset Budget in thousands (,000)	2022 APPROVED BUDGET	2023 / 2022 BUDGET CHANGES	2023 BUDGET	2023 / 2022 BUDGET % CHANGES	2024 / 2023 BUDGET CHANGES	2024 BUDGET	2024 / 2023 BUDGET % CHANGES
Growth Capital	\$6,632	(\$6,632)	\$0	-100%	\$0	\$0	0%
Sustaining Capital	\$20,788	(\$10,653)	\$10,135	-51%	\$1,015	\$11,150	10%
Abandonment & Reclamation	\$5,800	\$350	\$6,150	6%	(\$6,150)	\$0	-100%
Tangible Capital Assets	\$33,220	(\$16,935)	\$16,285	-51%	(\$5,135)	\$11,150	-90%

- The Carbon Capture, Utilization, and Storage capital is not included in the 2022 approved budget above.



Commodity Based Business

2023-2024 Operating and Tangible
Capital Asset Budget

City Council
November 7, 2022



Commodity Based Business (COMCO)

2023-2024 Operating and Tangible Capital Asset Budget

Agenda

- Macro view of Commodity Markets
- COMCO Strategy
- Current Activities and Opportunities
- Budget Key Inputs
- 2022 in Review
- 2023-2024 Outlook
- Operations Budget Update
- Capital Budget Update
- Recommendation

Macro View of Commodity Markets

Ongoing impacts due to:

- Significant volatility
- Supply response
- Substitution response

This market environment is going through a period of significant changes and requires a strategic view on how the City will transition to a decarbonized market in the future.

COMCO Strategy

- Continue to optimize the GENCO natural gas generation assets
- Develop and implement an Energy Transition Strategy for the City
- Continue with long term strategic projects for Carbon Capture Utilization and Storage (CCUS) and hydrogen development
- Continue to execute the previously approved abandonment and reclamation program

Current Activities and Opportunities

Base Operations

- forecasted to be in a positive EBITDA position for 2023-2024

Financial Plan

- Continue with shallow gas abandonment and reclamation program
- Streamline processes
- Optimize operations and facilities while discontinuing uneconomic business activities
- Optimize power assets while maximizing exports when possible
- Expect steady electric and natural gas retail demand alongside continued decline of natural gas production volumes

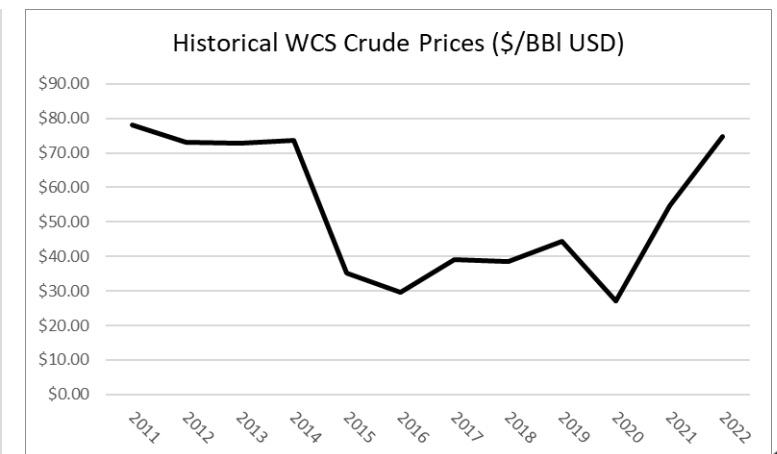
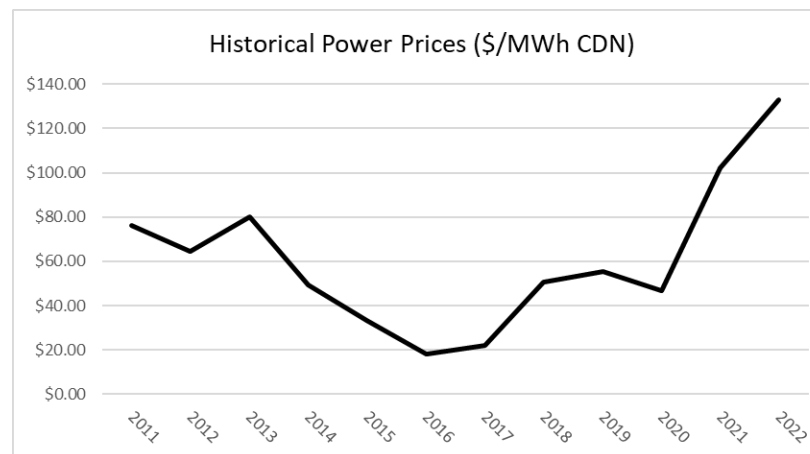
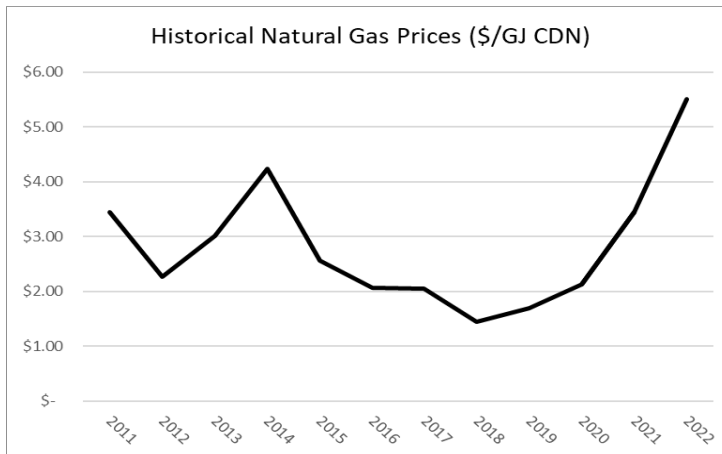
Budget – Key Inputs

The 2023-2024 budget was conducted with the following key inputs implemented:

- Forward pricing and volume forecast
- Revenues (function of volume and price)
- Gas purchases and gas sales
- Operations and maintenance expenses
- Interest earnings/interest expense
- Depreciation expense
- Tangible Capital Asset Budget

2022 in Review

- Highest power prices since the market deregulated
- High market volatility
- Gas prices trading at highest level in years
- Strong oil prices



2023-2024 Outlook

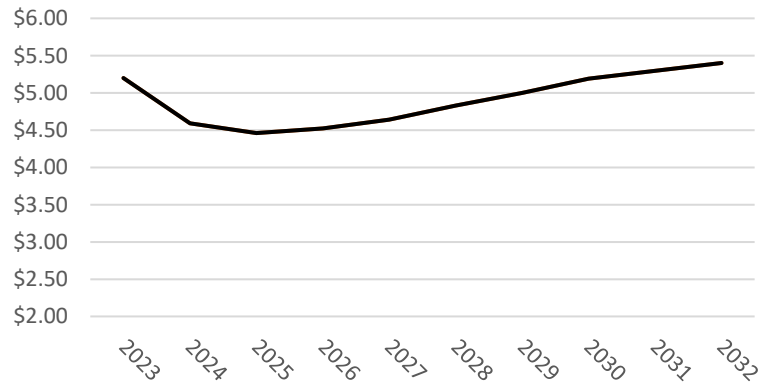
- Power market is expected to stay strong in 2023-2024 as the market continues to transition as part of net zero plan, this has created period where of tight supply and peaking generation setting market AESO System Marginal Price. This trend should continue until additions of base load combined cycle units
- Natural gas pricing has been very strong throughout 2022 and is expected to remain relatively strong throughout 2023-2024 due to increased power burn and LNG exports with global supply demand issues in Europe.

Commodity Price

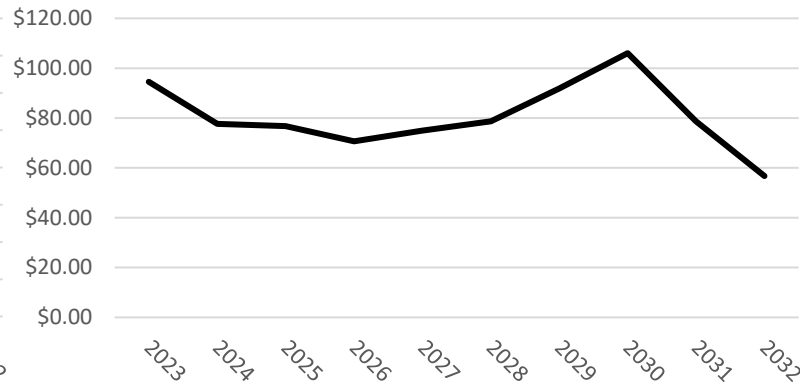
- 2023-2024 budget price vs. 2022 amended budgeted price

	2022 APPROVED BUDGET FORECAST PRICES	2023 / 2022 BUDGET CHANGES	2023 FORECAST	2023 / 2022 % CHANGES	2024 / 2023 BUDGET CHANGES	2024 FORECAST	2024 / 2023 % CHANGES
Gas	\$3.32	\$1.88	\$5.20	57%	(\$0.61)	\$4.59	-12%
Power	\$73.42	\$21.11	\$94.53	29%	(\$16.87)	\$77.66	-18%
Oil	\$72.35	\$10.16	\$82.50	14%	(\$9.03)	\$73.47	-11%

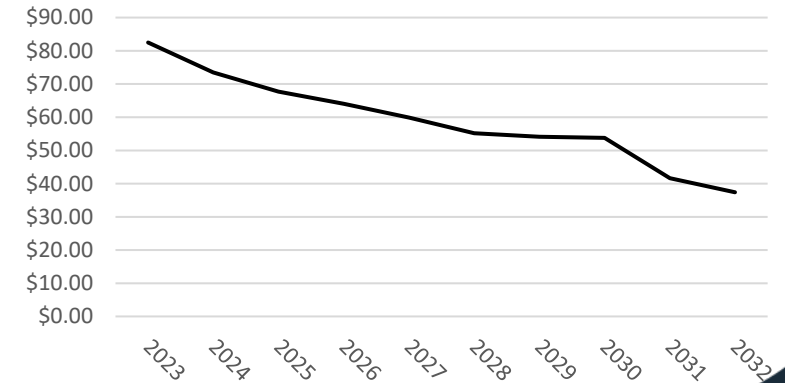
Forecast Natural Gas Prices (\$/GJ CDN)



Forecast Power Prices (\$/MWh CDN)



Forecast WCS Crude Prices (\$/BBI CDN)



Operation Budget 2023-2024

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*Price forecast based on September (NGX - ICE and Western Canadian Select)

- Revenues higher due to higher forecasted commodity prices
- Expenses increase mainly due to increase in forecasted natural gas price in 2023-2024
- Transfers decrease due to a lower variance between retail contracts compared and market prices

*EBITDA funds to be used largely for future capital expenditures, abandonment and reclamation expenditures, and debt payments. The estimated 2023-2024 performance of COMCO is expected to be strong but this is not expected to persist over the long term.

Capital Budget Request 2023-2024

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Developmental drilling in operated assets:

- 2023-24 budget does not include any new growth capital.

Lower sustaining capital due to asset dispositions

- Sustaining Capital will be used to optimize existing facilities and production assets.

Abandonment and Reclamation Capital

- Mainly used for well repairs on Surface Vent Leaks and Manyberries abandonments.

Recommendation

That City Council approve the 2023-2024 Commodity Based Business Tangible Capital Asset & Operating Budgets.

Questions?