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PUBLIC RESOURCES ADVISORY GROUP

July 20, 2016

Mr. Jeffery Peltola
Chief Financial Officer
Department of Water and Power of the City of Los Angeles
111 North Hope Street
Los Angeles, CA 90012

Dear Mr. Peltola:

The Department of Water and Power of the City of Los Angeles ("LADWP") has requested that Public Resources Advisory Group ("PRAG"), as financial advisor to LADWP, discuss the merits of negotiated bond transactions for the issuance of refunding debt related to the Water System. We understand that LADWP is currently seeking authorization to issue up to \$1 billion of refunding bonds for the Water System.

The benefits of negotiated versus competitive sales have been analyzed by municipal market participants for many years. The debate will continue into the future due to the rare frequency (or possible absence) of simultaneous negotiated and competitive bond pricings for the same issuer, same credit, and same maturities. In general, PRAG believes, that all things being equal, a competitive sale will provide an issuer with the lowest cost of funds for the majority of issuances, but not necessarily in all cases. There are other important factors and market circumstances that have an impact on the decision for issuers to negotiate bond sales. The following are some of the factors that LADWP faces with its upcoming refunding of Water System Revenue Bonds that support the reasoning for issuing on a negotiated basis:

- A negotiated sale will allow LADWP to provide meaningful roles for local and regional firms;
- Retail investors can be an important factor in the market, as the retail buyer is typically less sensitive to price compared to the institutional investor and retail orders in significant volume can only be achieved through a negotiated sale;
- LADWP relies on commercial banks to provide a significant amount of credit support for its \$2.26 billion of variable rate debt;
 - By offering negotiated underwriting business, LADWP receives more aggressive credit support fee bids and, very importantly, will often secure bids from banks that have received negotiated underwriting business during periods of time when other banks refuse to offer credit;
- Negotiated sales allow LADWP to structure specific portions of an issuance to meet investor demand (such as, bifurcated coupons, callable premium bonds, non-traditional call features, specified par amounts, non-traditional couponing and similar features);
- Refunding bonds issued on a negotiated basis provide LADWP with maximum flexibility to refund the maximum amount of bonds that meet LADWP's savings objectives while competitive sales have limitations on upsizing or downsizing a refunding based on market conditions;

- Refunding outstanding debt requires funding defeasance escrows which adds a level of complexity to the issuance process;
- An underwriter is the party that can best assist LADWP with comprehensive investor outreach (e.g. investor road shows, meetings, conference calls, etc.) as they have direct relationships with investors; and
- Negotiated bond sales provide increased flexibility in timing and structuring which will allow LADWP to navigate through difficult market conditions;
 - Recent market conditions, include significant and rapid shifts in interest rates, changing supply and demand relationships for municipal bonds, volatility in the public capital markets with the Federal Reserve policymakers continuing to contemplate future Federal Funds rate increases, geopolitical events impacting the fixed income markets, and the narrowing and widening credit spreads;
 - Negotiated issuers, including LADWP, have been able to respond to then current market conditions by modifying the timing and structure of their bonds to better meet investor demands.

In our opinion, the factors above should be considered by LADWP when making the decision to issue refunding bonds on a negotiated sale basis. I hope the foregoing meets your needs. Please call me at 310-477-1453 or Michelle Issa at 310-477-2786 if you have any questions on this matter.

Sincerely,



Edmund Soong
Executive Vice President