



2018 BUDGET LETTER

Originally constituted in 1911, the Port of Houston Authority (the “Authority” or “Port Houston”) is a political subdivision of the State of Texas and operates as a navigation district under Article XVI, Section 59 of the Texas Constitution. Port Houston serves as the local sponsor of the Houston Ship Channel (the “Channel”), a federal waterway stretching 52 miles from the City of Houston to the Gulf of Mexico. The Authority’s boundaries are coterminous with Harris County.

The greater Port of Houston, which includes the Authority’s terminals and over 150 privately-held facilities along the Channel, is ranked first in the nation in foreign waterborne tonnage, first in U.S. import tonnage, first in U.S. export tonnage and second in the U.S. in total tonnage. The Port of Houston is the primary factor for the Houston metropolitan area serving as the nation’s second largest export market in terms of dollar value (as reported by the U.S. Bureau of Economic Analysis for commercial activity through 2016), and also contributes to Texas being the nation's top exporting state for 15 consecutive years.

Port Houston’s mission is “to move the world and drive regional prosperity.” This includes the promotion of sustainable trade and commerce to create jobs and economic development for the local region, Texas, and the nation. Management considers transparency, fiscally sound business practices, and prudent evaluation of risks and opportunities to be necessary elements for achieving such goals. In addition, a greater focus on financial planning and liquidity management is considered essential, in light of significant infrastructure investments required in the next few years. Expense management and creating operating efficiencies also continue as major objectives for the Authority.

In accordance with statutory requirements specified in Chapter 5007, Texas Special District Local Laws Code, the Port Commission, as the governing body of the Authority, approves an annual budget and a one-year capital plan. Port Houston also develops a five-year forecast and a long-range plan addressing goals, strategies and priorities.

The Authority’s budget presentations and other materials are posted on its website (<http://porthouston.com>) in compliance with statutory requirements. Port Houston’s commitment to financial transparency is evident in its participation and awards received under the Texas Comptroller Transparency Stars program.

Operating Budget

A proposed 2018 operating and capital budget was developed to guide staff in the operation and management of Port Houston facilities and activities for Fiscal Year 2018. It was presented to the Port Commission for discussion at an open meeting on November 14, 2017, and approved on that date.

From a sustainability perspective, the Authority's operating revenues, derived primarily from tariffs related to its vessel and cargo activities, dredge material agreements and lease revenues, have generally been sufficient to cover its operating and maintenance costs. Based on the latest projections, Port Houston expects to generate annual cash flows ranging from \$157 million to \$212 million per annum over the next several years. Such excess cash is reinvested in the Authority's capital infrastructure.

In order to make the budget numbers understandable to the general public, the budget presentations posted on the Authority's website include additional narrative on cargo volume assumptions, detail of major changes in revenues and expenses (e.g., increases in terminal maintenance costs and depreciation resulting from investments in equipment and capital assets, etc.), as well as information on Port Houston's budgeted expenditures for promotion and development in compliance with State statutes.

Shown below are highlights of the 2018 operating budget, compared to 2017 (in millions):

	<u>2018 Budget</u>	<u>2017 Budget</u>
Operating Revenues*	\$ 368.2	\$ 311.9
Non-operating Revenues**	<u>5.9</u>	<u>11.3</u>
Total Revenues	\$ 374.1	\$ 323.2
Total Expenses	<u>284.3</u>	<u>266.1</u>
Net Income	<u>\$ 89.8</u>	<u>\$ 57.1</u>
Cash Flow	\$ 157.9	\$ 132.2

* Includes general and administrative revenues.

** Consists primarily of federal grants, insurance claims, and interest income.

For 2018, the Authority budgeted total operating revenues of \$368.2 million. This represents an 18% increase over the 2017 budget of \$311.9 million, reflecting growth in container volumes (especially export loads), and an increase in channel development revenues (primarily dredge management placement fees and leases of submerged lands). Non-operating revenues in 2018 reflect an expected decrease in federal grant reimbursements, and reduced interest income as cash balances continue to be expended for capital infrastructure projects.

Total expenses are budgeted at \$284.3 million, an increase of 7% versus the prior year, due primarily to higher terminal operating and union labor resulting from increased volumes, as well as depreciation and amortization, asset maintenance, and general and administrative expenses.

Excluding revenues and expenses related to property taxes (see the next section on “Tax Revenues and Debt Service”), Port Houston projects net income of \$89.8 million for 2018, an increase of 57% compared to the 2017 budget.

Tax Revenues and Debt Service

It should be noted that the operating budget does not include tax revenues. As the Authority’s unlimited ad valorem tax bonds were approved by Harris County voters at duly-called bond elections, the Authority works closely with the county on an annual basis to ensure that sufficient taxes are levied to cover the principal and interest debt service payments due on the Authority’s outstanding tax bonds.

Net tax receipts, after payment of collection fees to the Harris County Tax Assessor-Collector, are deposited in a segregated account and the funds are used exclusively to meet such debt service requirements, which are approximately \$53.0 million for calendar year 2018. Information on Port Houston’s outstanding debt is posted on its website, including the official statements of bond issuances and details of annual debt service payments.

Capital Plan

In recent years, the local region and the State of Texas have experienced significant population growth and economic expansion, due to the business-friendly environment and the expansion of the petrochemical industry. Investments made by local taxpayers in the Authority’s facilities and areas along the Houston Ship Channel over the years also have contributed to economic growth, job creation and expansion of the county, region and state tax base.

In order to accommodate larger vessels and increased cargo demands in the next 10 to 20 years, Port Houston must continue to develop, expand and renew its facilities. Replacing aging infrastructure, such as the Barbours Cut Terminal which opened in 1977, with more modern equipment supports our legislative mandate to facilitate commerce, navigation and safe waterways.

As shown in the Five Year Plan posted on the Authority’s website, we estimate capital investments of almost \$1 billion will be required during the period 2018 through 2022. Over \$620 million of those capital expenditures are planned for infrastructure and rail expansion at the two container terminals, with another \$98 million for improvements at the general cargo and bulk terminals, and \$134 million for channel development. The balance is designated for projects relating to security, information technology, real estate and maintenance operations.

In July 2014, Port Houston commenced a dredging project in the Barbours Cut and Bayport channels to increase the operating depth by 5 feet (to match the 45-foot authorized depth of the Houston Ship Channel) and widening those channels to accommodate larger vessels. As the uncertain federal appropriation process was estimated to take over 10 years, the Authority funded the \$80 million dredging project in its entirety to ensure there is no lost opportunity for cargo through our Port and for the benefit of our region. This dredging project at Barbours Cut and Bayport was completed in 2017.

During 2017, the Authority's investments in capital infrastructure and improvements were funded from its general fund and from grant monies received from federal and other governmental programs. The proceeds from tax bonds issued in prior years have been fully expended.

Port Houston's 2018 capital budget was approved by the Port Commission on November 14, 2017 for up to \$275 million for various infrastructure improvements (see the chart on Page 5). Approximately \$169 million will be allocated to the container terminals for continuing development of Bayport and modernization at Barbours Cut, while \$14 million is designated for channel development projects and another \$24 million relates to improvements at the general cargo and bulk terminals in the Turning Basin area. The remaining 2018 capital budget funds will be used for railroad improvements, port security, building renovations and information technology.

Although the capital plan may be approved as to maximum annual amount of capital expenditures, individual items exceeding \$50,000 (both operating expenditures and capital projects) will continue to be presented separately to the Port Commission for approval in accordance with statutory requirements.

Five Year Plan and Liquidity

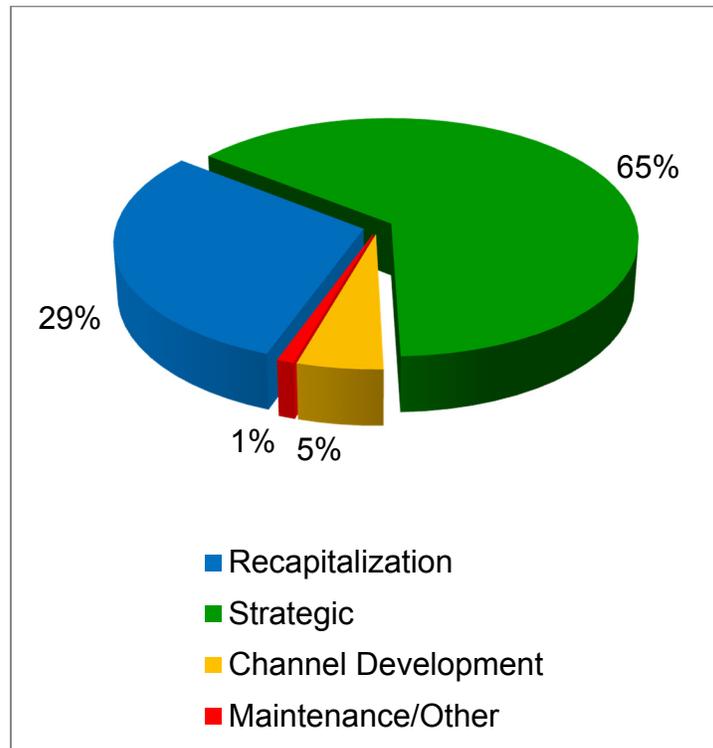
The Authority has estimated that capital improvements of about \$1 billion are required every five to seven years, in order to accommodate industry growth and continue to meet its mission for job creation and economic development.

As outlined in the Five Year Plan, despite strong operational and financial performance, Port Houston is not able to fund such capital projects entirely from internally-generated cash flows. Additional financing is likely required in 2019-2020.

In the past, the Authority has relied on ad valorem tax bonds to help fund its capital infrastructure investments, but it may also consider interim financing alternatives to provide added liquidity in the next few years. As the capital improvement plan is implemented, the Authority will balance the infrastructure needs against available cash and funding resources to provide the greatest return on investment to the taxpayers in the form of jobs and economic growth.

2018 CAPITAL IMPROVEMENT PROGRAM

\$275 MILLION



- Recapitalization projects = \$79 million
 - *Investments required to sustain high service levels and/or enhance productivity*
- Strategic projects = \$179 million
 - *These investments support new growth opportunities*
- Channel projects = \$14 million
 - *Development at container terminals and DAMP areas*
- Remaining projects = \$3 million
 - *Includes maintenance equipment and other replacements*

Summary

Port Houston has produced strong financial results in recent years. The budgeting and planning processes are designed to help the Port Commission and Authority staff, as stewards of the public trust, make informed decisions that enhance sustainability.

The economic impact of activities along the Houston Ship Channel is significant – \$265 billion annually and over 1.1 million jobs in Texas alone, according to a study published in 2015 by Martin Associates. These activities represent 16% of the State’s Gross Domestic Product. It is incumbent upon all stakeholders to ensure that this economic engine continues to produce jobs and economic development for the region, Texas and the nation.

Questions relating to the Authority’s budget and financial results may be submitted as a public information request by following the instructions on the Authority’s website (<http://porthouston.com/portweb/governance/public-information-requests/>).