FitchRatings

Fitch Rates Massachusetts Port Authority Revs 'AA'; Affirms Outstanding Revs

Fitch Ratings-New York-15 June 2017: Fitch Ratings has assigned a 'AA' rating to the Massachusetts Port Authority's (Massport, the authority) approximately $170.6 million in series 2017-A revenue and refunding bonds. Fitch has also affirmed approximately $1.3 billion of Massport's outstanding revenue bonds at 'AA'. The Rating Outlook is Stable.

KEY RATING DRIVERS

Summary: The 'AA' revenue bond rating reflects the solid Boston service area, which has supported Logan Airport's (the airport) large, resilient traffic base of over 17 million enplanements and the Port of Boston's (the port) stable container and cruise activity. The rating also reflects Logan's role as a strategically important regional airport with minimal carrier concentration, low competition, and robust service offerings. The rating also incorporates Massport's strong cost recovery framework and Logan's competitive cost per enplanement (CPE) levels. Massport's financial profile is expected to remain robust despite additional expected capital-related borrowings of $500 million over the next five years, evidenced by healthy debt service coverage ratios (DSCRs) above 2x and low leverage (net debt/cash flow available for debt service) levels below 5x.

Revenue Risk: Volume - Stronger
Strong Airport and Port Activity: Massport benefits from a robust service area which underpins its strong aeronautical and maritime operations. The port's main business lines consist of container and cruise, whose volumes have been relatively stable over time. The airport's traffic base contains mostly origin and destination (O&D) passengers, which Fitch expects to result in minimal future traffic volatility. Additionally, the airport has a well-diversified carrier mix between both domestic and foreign flag carriers. Logan is the dominant airport in the region despite the presence of some nearby

competing airports (TF Green and Manchester) due to its wider breadth of service offerings.

Revenue Risk: Price - Stronger
Well-Structured Cost Recovery Framework: Massport's charge-setting framework with airlines and maritime users allows for strong cost recovery and flexible control of facilities. Airport properties have historically comprised the majority of Massport's revenue profile at over 80%, with port properties at roughly 14%. Together, aeronautical and port revenues cover the majority of Massport's operating and debt service costs, with the remainder supported by the airport's healthy commercial revenue streams. Logan's CPE has remained between $13 and $14, which is comparable to that of other large-hub airports, and expected to remain competitive.

Infrastructure Development and Renewal - Stronger
Manageable Infrastructure Needs, Some Borrowings: Massport's facilities are very well-maintained and supported by a strong infrastructure development program. The five-year, $2 billion program is manageable and is expected to be 44% debt-financed with the remainder financed via passenger facility charges (PFCs), grants, customer facility charges (CFCs) and other internally generated funds. While short-term and long-term needs are well-defined, the demand-driven nature of the plan affords some flexibility to adjust the timing and scope of projects as necessary.

Debt Structure - Stronger
Conservative Debt Structure: Massport's debt structure is conservative, with all fully-amortizing senior debt and a declining debt service profile. The debt has strong structural features, evidenced by cash-funded debt service reserve funds and a solid rate covenant and additional bonds test. Massport's debt is expected to be all fixed-rate once the series 2017-A bonds have been issued. The authority may issue additional variable-rate bonds, but floating-rate exposure is expected to remain minimal.

Low Leverage, Strong Coverage: Massport had low leverage of roughly 2.4x in fiscal 2016 (ended June 30), and is expected to remain below 5x under rating case conditions despite additional planned borrowings. Coverage levels continued to strengthen in fiscal 2016, approaching 3x, and are expected to remain robust under Fitch's rating case. Specifically, rating case DSCRs remain above 2x through fiscal 2020 before declining to 1.95x in fiscal 2021 due to increasing debt service obligations.

PEER GROUP

Comparable airport peers include Los Angeles International Airport (LAX; 'AA'/'AA-'/Outlook Stable) and San Francisco International Airport (SFO; 'A+'/Outlook Stable). LAX, SFO and Logan all serve as large-hub facilities with strong revenue risk profiles, competitive airline costs, and healthy financial metrics. LAX and Logan's higher ratings are explained by their lower leverage levels.

RATING SENSITIVITIES

Future Developments That May, Individually or Collectively, Lead to Negative Rating Action:

Volatility in aviation and maritime operations or significantly more debt than currently expected, which dilutes revenue bond coverage below 2x and/or increases general revenue bond leverage above 8x

Future Developments That May, Individually or Collectively, Lead to Positive Rating Action:

Massport's general revenue bond ratings are capped at 'AA' given the airport sector's operational and financial reliance on its airline counterparties, which generally exhibit weaker credit quality.

TRANSACTION SUMMARY

Massport expects to issue approximately $170.6 million of par in series 2017-A revenue bonds. Of the issuance, $90.1 million will consist of new money which will primarily be used to fund a portion of the authority's Terminal B optimization project. The remainder of the issuance is expected to refund outstanding series 2007-C and 2010-D. The proposed bond issuance will be on parity with existing senior revenue bonds and will convert all pre-existing variable-rate debt to fixed-rate.

The new money's bond proceeds and expected premium will fund a $91 million deposit to the project fund, capitalized interest, a debt service reserve fund, costs of issuance, and the underwriter's discount. The refunded bonds' proceeds, expected premium, and releases from the debt service and debt service reserve funds will fund a $95 million deposit to a refunding escrow account, and will also cover costs of issuance and the underwriter's discount. Refunding of the 2007-C bonds is expected to provide about $3.2 million in net present value savings (or 14% of refunded par). True net present value savings for the 2010-D bonds remains unknown at this time as savings depend on market conditions at the time of future issuance. The refunding bonds will reach final maturity in 2029, without extending the maturities of the refunded bonds. The new money portion of the issuance will reach final maturity in 2047, extending the tenor of Massport's overall debt profile by one year.

CREDIT UPDATE

Performance Update

Enplanement performance continued to exceed Fitch's base case expectations in fiscal 2016 and year-to-date (YTD) for the nine months of fiscal 2017, growing 7.9% and 7.8%, respectively, in comparison to expectations of 6.3% and 1.5%. Outperformance reflects notable passenger growth from low-cost carriers Southwest and JetBlue, as well as continued expansion of international service. Specifically, international enplanements have grown at an impressive five-year compounded annual growth rate (CAGR) of 8.7%, allowing YTD 2017 foreign flag carrier market share to increase to 14.4% of passenger traffic from 9.4% in fiscal 2012. Growth of foreign travel has primarily been bolstered by new travel to and from Asia and the Middle East, as well as Canada and Europe. Simultaneously, American Airlines and US Airway's combined market share declined below 20% for the first time in 2017 as JetBlue and foreign flag carriers accumulated market share.

Container throughput saw strong growth of 12% in fiscal 2016, which could be the result of cargo diversion from other larger and more congested Atlantic ports of call. However, YTD 2017 container growth has been much more modest at roughly 1.2%. Cruise passengers declined by 12.5% in fiscal 2016 as a result of a reduced number of calls by the Norwegian Cruise Lines'

Norwegian Dawn, which remained in drydock for part of the cruise season. Fitch does not consider the recent volatility in Massport's cruise operations to be a material credit concern as the authority's cruise business line is only a small portion of overall port revenues at 6%. Instead, the majority of the Massport's port business is driven by container and real estate revenues, which historically have enjoyed greater stability.

Outperformance, in terms of both enplanements and container throughput, drove total revenue outperformance in fiscal 2016. Specifically, non-airline revenues grew 5% compared to expectations of 2.0% and port revenues grew 9.1% compared to expectations of 7.1%. Nearly all of Massport's revenues have continued to outperform YTD 2017, bolstered by continued strong enplanement growth, opening of new concessions, and increased port real estate activity. Consequently, fiscal 2016 DSCR surpassed estimates by roughly 30 bps, leverage was 50 bps lower than expected, and CPE improved by $0.65. Fiscal 2017's financial metrics are also expected to outperform original expectations by a similar magnitude.

Overall, Massport's capital plan has remained largely the same as the previous year's plan, though slightly larger at approximately $2.0 billion compared to $1.7 billion. The plan remains expansion-focused and demand-driven, involving the accommodation of additional expected growth by the addition of 5,000 new parking spaces, new international gates (four over the next five years, seven over the next 10 years), and optimization of terminal space.

The increase in plan size reflects the addition of several new projects, whose added costs are expected to be mostly funded by additional internally generated funds. Fitch does not consider the assumption of increased expected cash-funding ambitious, as Massport's sizable revenue base and favorable growth trends allow the authority to accrue and retain cash rapidly. The quantum of expected near-term capital-related issuances has also decreased as a result of certain capital projects which were previously included in the five-year plan being moved outside of the five-year window. Fitch expects that additional debt to support these projects will be included in the authority's future capital plans as Massport's planned capital-related debt issuances increase to $1 billion over a 10-year period from $500 million over a five-year period. However, the additional debt is not currently expected to be credit adverse.

Fitch Cases

Fitch's base and rating case include $500 million of additional pro forma debt through fiscal 2021, with all new issuances supported by cash-funded debt service reserve funds.

In the base case, enplanements grow at a five-year CAGR of 3%. Concession and parking revenues roughly track enplanement growth at a five-year CAGR of 4% and 5%, respectively, with parking growth slightly higher than concession growth as a result of planned rate increases. Airline revenue growth is slightly higher than airport expense growth at 6.7% and 5.9% CAGRs, respectively, reflecting some capital expense pass-through to airlines. Port revenues and expenses grow at 5.6% and 4.3% CAGRs, respectively, considered conservative in comparison to recent historical trends.

Fitch's rating case includes a 5% decline in enplanements during fiscal 2018 followed by a partial recovery, reflecting Fitch's view that Massport's mature air service area should result in modest future volatility. In fiscal 2018, concession and parking revenues decline severely by 16% and 8%, respectively, rebounding with enplanement growth thereafter. Port revenues decline by 15% in fiscal 2018 with a partial recovery thereafter. At the time of the decline, airport and port expenses are modest at 1%-2%, reflecting expected cost management; expenses rebound to 4%-6% annual growth thereafter. Airline revenues grow at a lower rate than the base case at 5.2%, reflecting lower overall cost growth.

Fitch's base case yields an average DSCR of 3.0x and fiscal 2021 leverage of 3.3x. Fitch's rating case yields a lower but still strong average DSCR of 2.4x and higher fiscal 2021 leverage of 4.6x. CPE increases to a maximum of $16.64 in the base case, and $16.81 in the rating case. Fitch does not view Massport's rising CPE negatively, as CPE levels typically increase as airports expand international service and Logan's airline costs remain competitive in comparison to other large-hub airports. Massport's credit is well-aligned with its 'AA' rating, evidenced by leverage levels which remain well below the 'AA' category indicative threshold of 8.0x for airports with stronger revenue risk attributes.

SECURITY

Massport's revenue bonds are secured by the net revenues generated from port authority properties, including Logan International Airport and various maritime facilities within the Port of Boston.

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Applicable Criteria
Rating Criteria for Airports (pub. 14 Dec 2016)

(https://www.fitchratings.com/site/re/891804)
Rating Criteria for Infrastructure and Project Finance (pub. 08 Jul 2016)
(https://www.fitchratings.com/site/re/882594)

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