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Ratings

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Port of Portland, Oregon
Portland International Airport; Airport

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Port of Portland, Oregon
Portland International Airport; Airport

Credit Profile		
US$238.495 mil arpt rev bnds (AMT) (Portland Intl Arpt) ser 24B due 07/01/2036		
Long Term Rating	AA-/Stable	New
US$23.84 mil arpt rev bnds (Non - Amt) (Portland Intl Arpt) ser 24A due 07/01/2036		
Long Term Rating	AA-/Stable	New
Port of Portland, Oregon		
Portland Intl Arpt, Oregon		
Port of Portland (Portland International Airport)		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA-' long-term rating to the Port of Portland, Ore.'s pro forma $23.8 million series 24A and $238.5 million series 24B general airport revenue bonds (GARBs), issued for the Portland International Airport (the airport, or PDX). In addition, S&P Global Ratings affirmed its 'AA-' long-term ratings on the port's GARBs outstanding, and affirmed its 'A' rating on the airport's stand-alone passenger facility charge (PFC) bonds outstanding. The outlook on all ratings is stable.

The series 24 bonds will finance about $226.9 million in PDX capital improvements, including loading bridge replacements, taxiway rehabilitation, and portions of larger terminal balancing and terminal core redevelopment projects. The bonds are expected to fund about 12% of the airport's five-year capital improvement plan (CIP) that requires substantial additional debt over the next five years.

The ratings reflect our view of the following credit strengths:

- The predominantly origin-destination (O&D) nature of passenger traffic and the airport's dominant market position in the region;
- The airport's strong to very strong liquidity position and historically strong debt service coverage (DSC) that we expect to remain strong, despite the port's additional borrowing plans; and
- The demonstrated strong management of operations, finances, capital projects, and administration of the PFC program.

In our view, these credit strengths are partly offset by a very large $1.9 billion five-year CIP that requires substantial additional debt.

The GARBs are secured by a senior lien on the net revenues of the airport only, and there is no pledge of additional port revenues. The PFC bonds are secured and payable solely by PFC revenues pledged up to $4.50 per enplaned passenger. Prior to issuing the series 24 bonds, the airport has about $135 million in stand-alone PFC bonds outstanding, including a direct purchase agreement with Wells Fargo. In addition, the airport has approximately $440 million in GARBs outstanding. The airport has entered into six swaps with a current mark-to-market value of $31 million, not in favor of the port.

The port is a municipal corporation and a legal subdivision of the state that operates maritime, aviation, and industrial properties. The airport is located on 3,200 acres on the southern edge of the Columbia River, 12 miles northeast of downtown Portland. The airport is considered a large hub by the Federal Aviation Administration (FAA) as of calendar year 2015 enplaned passengers and was the 30th largest airport in the U.S., according to Airports Council International, based on 2015 total passengers. Seattle-Tacoma International Airport is the closest major airport facility (160 miles to the north) and does not, in our opinion, provide a viable alternative for air access to the Portland region. As such, we believe competitive pressure on PDX is limited.

Outlook

The stable outlook reflects our expectation that demand for the airport will remain generally stable or positive, management will adjust rates and charges to maintain strong financial margins despite rising debt levels from future debt issues planned to fund the CIP, and the port's liquidity position will be maintained near current levels.

Upside scenario

We do not expect to raise the ratings in the next two years, given the port's future borrowing plans.

Downside scenario

We could lower the ratings in the next two years if the port's DSC or liquidity position materially erodes as a result of funding the CIP.

Airport Demand Expected To Remain Generally Stable Or Positive

The airport is located on 3,200 acres on the southern edge of the Columbia River, 12 miles northeast of downtown Portland. In our view, the airport is largely insulated from competitive pressures. The closest major airport facility is Seattle-Tacoma International Airport (160 miles to the north), which we do not believe provides a viable alternative for air access to the Portland region. The only other commercial service airports in the state are smaller airports that are at least 100 highway miles from Portland. The airport has two parallel east/west runways and one northeast/southwest crosswind runway. The passenger terminal includes five attached concourses.

PDX has a strong market position, in our opinion. The primary air service area includes seven counties--five in Oregon and two in Washington. Population growth within the air service area has been strong over the past decade, outpacing both the state and national annual growth rates. Historically, Portland experienced steady growth in passenger traffic. However, the airport has also shown a susceptibility to large downturns associated with extreme events, as were demonstrated in the aftermath of the Great Recession as well as the events of Sept. 11, 2001.

PDX experienced strong enplanement growth from 1990-2000, at an average annual rate of 8.3%, boosted by the arrival of Southwest Airlines in fiscal 1994. Due to disruption, an economic downturn, and the cessation of international service by Delta, the number of enplaned passengers decreased by 1.7% in fiscal 2001 and 10.8% in fiscal

2002 to 6.0 million. Enplanements began trending positively again in fiscal 2002, reaching a historical high of 7.4 million by fiscal 2008. After a substantial decrease to 6.5 million from fiscal 2009 through fiscal 2010, enplanements began to recover again. Fiscal years 2014 through 2016 have seen three successive record-high enplanement years.

In our view, the airport's enplanement trends over the last two to three decades have demonstrated generally strong demand characteristics with the exception of notable declines during significant economic downturns. Although we note that air travel demand is susceptible to substantial economic downturns, such declines in traffic were followed by a relatively quick recoveries in demand. We attribute the port's relatively resilient air travel demand to the strength of PDX's service area economy, limited competition, and air travel demand that is primarily driven by O&D passengers. We expect these factors will support generally strong air travel demand for the foreseeable future. Over the last seven years, enplanements grew at a compound average annual rate of 5.2%. For planning purposes, management forecasts 1.9% annual enplanement growth through 2022. We view this as a conservative assumption that is likely to be achieved or exceeded.

We consider PDX's consistently high percentage of O&D passengers a credit strength, providing generally stable activity levels. Approximately 84% of total enplanements at PDX are O&D passengers. Most of PDX's enplanements are domestic enplanements, with only about 3% international enplanements. PDX's strong O&D nature and moderate airline carrier concentration mitigate some risks regarding air carrier hubbing decisions, in our view. The top three carriers account for about three-fourths of total market share. Alaska Air Group, which includes Alaska and Horizon Airlines, had a 42% market share in fiscal 2016, followed by Southwest, with an 18% market share, and Delta, with a 14% market share.

General Airport Finances Are Expected To Remain Strong

Airport management implemented a formalized strategic planning process over the past four years. This Project Portfolio Office (PPO) process provides a framework for prioritizing capital projects and for aligning capital and financial planning. The PPO process includes a goal of maintaining cost per enplanement (CPE) at manageable levels, and of maintaining DSC of at least 1.7x, well in excess of the 1.3x required under the bond covenants.

Over the past seven years, financial performance has been strong. DSC has ranged from 1.7x to 2.1x from fiscals 2010 through 2016, with the past two years showing the highest levels for this key metric. DSC has improved for four consecutive years, which coincides with implementation of the PPO process. Despite the recent improvement in DSC, we expect DSC could likely fall, but still remain strong, as the port issues additional debt to fund its airport CIP. More specifically, management forecasts DSC will remain strong, ranging from about 1.8x to 2.1x for fiscals 2017 through 2022 before being pressured in 2023 as a result of rising debt service requirements. These projected DSC levels are based on forecasts that include several conservative assumptions, including a modest 1.9% annual growth rate for enplanements through fiscal 2022, which is an average growth rate much lower than demonstrated in recent years; all debt will be GARB debt with limited or no outside funding, though we expect management may leverage customer facility charges (CFCs) and PFCs, if necessary, to contain increases to PDX's airline cost structure. Cost per enplanement is projected to gradually increase to over $12.00 by fiscal 2022 from a moderate $10.27 in fiscal 2016.

The airport's liquidity position remains a key credit strength. Cash and equivalents within the airport fund alone amounted to approximately $98.1 million at fiscal 2016, equivalent to over eight months' cash on hand. In addition to the airport fund, port general fund cash may also be applied to support the airport's expenses. Portwide liquidity for fiscal 2016 was much stronger, at $293.2 million. In our view, this provides the airport with an ample financial cushion, offsetting some risks associated with the prospect of short-term enplanement stress. We expect management will maintain a relatively strong liquidity position as the port funds its significant CIP.

Stand-Alone PFC Maximum Annual Debt Service (MADS) Coverage Expected To Remain Strong

PFC revenues collected by the airport have provided, in our view, consistently strong MADS coverage. PFC MADS coverage has improved to 2.4x from 2.0x over the past four years, according to our coverage calculations. We expect PFC MADS coverage will remain strong moving forward, assuming enplanements remain generally stable and the port does not issue a significant amount of stand-alone PFC bonds to fund a portion of its CIP, which port officials have no plans to do at this time.

Rising Debt Levels From Large CIP Could Pose Some Risk

Continued strong demand growth at PDX, in addition to management's striving to maintain a top quality airport experience for passengers, is leading the airport into an especially capital-intensive period. The airport's five-year CIP totals $1.9 billion, which we consider very large. Projects include a terminal balancing project, which will result in increased efficiency in distributing operations throughout the north and south sides of the terminal, as well as increased capacity; loading bridge replacements; taxiway and apron rehabilitations; the addition of a new public parking facility and a consolidated rental car facility, which will increase parking and rental car capacity while enhancing revenue generation in future years; and a terminal core redevelopment project that will ultimately expand terminal capacity and enhance the passenger experience at PDX.

As a result of this GARB issue and additional debt issuances projected to total about $932 million and to occur over the next two to five years, total debt outstanding is slated to rise to about $1.5 billion. We believe this level of debt is high, but we believe it will be manageable because of PDX's generally resilient demand characteristics. Although preliminary, the port's current bonding plans for the next five years call for $140 million in CFC bonds, with the remainder to be issued as GARBs. The effects of this additional debt are reflected in the financial forecast. We expect that management will effectively manage the CIP and rising debt service requirements, adjusting rates and charges as needed to maintain its strong DSC and liquidity position.

Airport Airline Lease And Operating Agreement

Beginning with the July 1, 2015, airline lease and operating agreement, the CPE methodology includes airline common use rentals and excludes the airfield cargo carrier requirement. We consider this change to be credit neutral.

The airline agreement was effective July 1, 2010, expired June 30, 2015; however, management and the airlines extended the term of the agreement through 2025. The agreement has a hybrid rate-making model, with residual rate-making for the airline cost center covering operations and maintenance (O&M) expense plus 1.3x annual funded DSC. The agreement has a majority-in-interest disapproval process for airline cost center projects, exceeding $1 million in project cost, and includes a provision for revenue-sharing of nonairline revenues of up to $6 million per year (plus additional revenue sharing if the airport DSC exceeds 1.75x). We consider the airline agreement to be credit neutral.

GARB Legal Provisions

The GARBs are secured by the net revenues of PDX and by the moneys held in certain funds and accounts established by the bond ordinances. The pledged revenues for the GARBs do not include other nonairport activities, such as maritime operations, under the port's control. Overall, the legal structure of the airport enterprise is favorable, in our opinion.

While the GARB bond provisions regarding the flow of funds and debt service reserve levels are typical, we believe the airport has a strong additional bonds test of 1.30x, which may be calculated on either historical or projected net revenues. Under the bond ordinance, the airport has covenanted to impose rates and charges so that the annual net revenues are equal to 1.30x debt service; it also requires annual payment of DSC from the airlines, rather than the industry's standard rolling coverage. While PFCs are legally defined as revenues, federal law restricts their use to specific, approved projects. The airport does not use these revenues in the calculation of rates and charges. PFC revenues are excluded from the calculation of net available revenues under the bond covenants, and are not considered available for the payment of GARB debt service at this time.

Technically, the airport's GARBs were issued on a subordinate-lien basis; however, there is no other debt with a prior claim on airport revenues. The port has covenanted to not incur any obligations superior to the lien on the outstanding GARBs, with the exception of O&M expenses.

Stand-Alone PFC Bond Provisions And Bond Ordinance

The PFC bonds are secured solely by PFC revenues and PFC revenue interest earnings. The airport may pledge additional revenues to the bonds, though currently no additional revenues are pledged.

The PFC is a $4.50 charge levied by the port on each "PFC-eligible" enplaned passenger, which is collected and remitted monthly by airlines serving the facility--subject to an administrative fee of 11 cents on each PFC retained by the airline. By federal statute, there are certain classes of passengers that cannot be charged a PFC, including travelers using frequent-flier tickets. On a one-way flight, a passenger may be charged a PFC only at the first two airports where PFCs are collected. On a round-trip flight, a passenger may be charged a PFC only at the first two enplaning PFC-collecting airports on the outbound leg and the last two enplaning PFC-collecting airports on the inbound leg. In recent years, between 90% and 92% of enplaned passengers at PDX paid a PFC. Management has established a strong track record of obtaining FAA approval of PFC applications, with 13 applications approved amounting to a total of approximately $1.2 billion in PFC funds authorized for collection and use.

The airport deposits PFC revenues as collected to the PFC fund, and applies the fund in the following order: to pay debt service on the PFC bonds, to make any required deposits to the reserve account, to make any subordinate-lien PFC obligation payments, to make any required deposits to a subordinate-lien PFC reserve account, and to deposit to the PFC Capital Account to be used for approved projects or any other use authorized under federal PFC regulations.

Under the PFC bond ordinance, the port must, at all times, comply with a first-lien sufficiency covenant. Under this covenant, the following calculation must exceed 1.05x at all times:

PFC Authority:

- Less: costs paid to date on PFC pay-as-you-go improvements
- Less: pay-as-you-go contractual commitments
- Less: debt service paid to date on PFC bonds
- Less: projected aggregate subordinate-lien debt service
- Plus: any funds on deposit in the subordinate-lien obligations account or reserve and any additional pledged revenues.
- Divided by: projected aggregate first-lien debt service, less funds on deposit in the first-lien debt service account and first-lien reserve fund.

The airport may issue additional first-lien PFC bonds if an aviation consultant certifies that the first-lien sufficiency covenant will be met after the issuance, and projected pledged revenues for the five years after issuance provide at least 1.50x MADS.

Contingent Liquidity Risk That We Consider Low

The airport has six swaps with three counterparties outstanding. The combined current mark to market for the airport is approximately negative $31 million. We consider the risk exposure low, given the rating differential between airport's rating level and the rating triggers for swap termination.

The airport currently has about $5.2 million in collateral posted under one of the swaps, which is required because the swap carries a negative fair value. Additional collateral postings would be required if the mark-to-market on the PFC swaps exceeds negative $15 million, or if the airport's ratings fall below certain thresholds. At present, we do not consider the possibility of required collateral postings a credit risk, due to the strong liquidity available to the airport, in addition to the fact that the airport's bond ratings would have to fall by at least two notches, which we view as unlikely.

The airport also has a direct purchase agreement with Wells Fargo Municipal Capital Strategies LLC. There is currently about $53.3 million outstanding under the direct purchase, which was originally issued in the amount of $57.7 million in 2012. The direct purchase agreement is for the series 2012A PFC bonds. We consider the contingent liquidity risks to be low given the airport's strong liquidity, with over $293 million, including the port's general fund unrestricted cash balances, available to the airport at fiscal 2016.

Ratings Detail (As Of December 23, 2016)

Ratings Detail (As Of December 23, 2016) (cont.)		
Port of Portland, Oregon		
Portland Intl Arpt, Oregon		
Port of Portland (Portland Intl Arpt) passenger fac chg rev bnds		
Long Term Rating	A/Stable	Affirmed