S&P Global
Ratings

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Port of Portland, Oregon
Portland International Airport; Airport

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Port of Portland (Portland Intl Arpt) PFC		
Long Term Rating	A+/Stable	Upgraded

Rationale

S&P Global Ratings raised long-term and underlying ratings on Port of Portland, Ore.'s passenger facility charge (PFC) revenue bonds to 'A+' from 'A'. The outlook is stable.

The upgrade reflects the application of our "U.S. And Canadian Not-For-Profit Transportation Infrastructure Enterprises" (TIE) criteria (published March 12, 2018).

Securing the bonds is a $4.50 fee levied on enplaned passengers at Portland International Airport (PDX), which the port owns and operates.

The ratings reflect our opinion of PDX's very strong enterprise risk profile and the strong financial risk profile associated with the stand-alone PFC pledge. In general, our enterprise risk profile assessment incorporates the favorable characteristics of an expanding metropolitan area and limited competition from other airports, and the resulting fundamental passenger demand for PDX. Our financial risk profile assessment considers the port's strong historical and projected maximum annual debt service (MADS) coverage of the PFC obligations, offset by a narrow fixed-rate revenue pledge. The financial risk profile assessment also reflects our expectation of declining PFC debt levels due to no planned additional parity debt and drawing down the PFC fund balance to fund projects included in the port's capital improvement program (CIP) for PDX.

We base the enterprise risk profile on our view of the airport's:

- Very strong market position, reflecting favorable total enplanement trends (compound annual growth rate of 5.8% from fiscal years 2014-2018) that we expect to continue. PDX serves a relatively large and growing origin-destination (O&D) passenger base (85% of fiscal 2018 total enplanements of 9.7 million), supported by the expanding Portland metropolitan area and limited competition from other airports. There is moderate airline concentration, with Alaska Air Group Inc. accounting for about 43% of total enplaned passengers. A rising airline cost structure from debt financing a large CIP tempers our assessment;
- Extremely strong service area economic fundamentals, which include favorable economic activity as measured by GDP per capita, a population of approximately 2.4 million in the Portland-Vancouver-Hillsboro metropolitan statistical area (MSA), above-average expected population growth, and unemployment rates lower than the national average;

- Low industry risk relative to that of other industries and sectors; and
- Extremely strong management and governance, reflecting a very experienced and effective management team that we believe employs prudent financial policies and procedures to mitigate the port's financial and operational risks.

We base our financial risk profile on our view of PDX's:

- Adequate financial performance reflective of PFC MADS coverage of 2.6x (based on fiscal 2018 audited results), a level we consider strong, tempered by a narrow fixed-rate revenue pledge that is sensitive to changes in enplanement levels;
- Extremely strong debt and liabilities capacity due to annual PFC revenues near or above current levels and the amortization of the airport's stand-alone PFC debt, with no additional new money stand-alone PFC debt planned; and
- Very strong liquidity and financial flexibility, considering our expectation of that the PFC fund balance will be drawn on to fund a portion of PDX's CIP.

Securing the bonds is a first claim on PFC revenue the port collects, with no claim on its other revenues. The Federal Aviation Administration (FAA) has authorized the port to impose a $4.50 PFC (the maximum allowable under current law), which airlines serving PDX collect and remit monthly, subject to an 11-cent-per-passenger administrative fee retained by the airlines. Under federal law and subject to FAA regulation, PFCs can only finance or pay eligible, approved airport-related project costs, which the port has done. The FAA authorizes the port to impose and use approximately $1.2 billion of PFC revenues for various projects, of which approximately $657 million has been collected and approximately $531 million has been spent on approved PFC projects as of September 2018. The port expects that during fiscal years 2019-2024 it will use, on a pay-as-you-go basis, approximately $235 million of PFC revenue to pay costs of CIP projects.

We consider the port's stand-alone PFC bond provisions credit neutral. Because PFC revenue are a fixed revenue stream with no possibility for adjustments to compensate for traffic declines, the port has covenanted to protections that limit additional debt. A senior-lien PFC sufficiency covenant requires management to calculate annually and before any additional debt, whether the remaining PFC authorization is at least 105% of debt service outstanding. PDX may issue additional first-lien PFC bonds if an aviation consultant certifies that the first-lien PFC sufficiency covenant will be met after the issuance, and projected pledged revenues for the five years after issuance provide at least 1.50x MADS. The airport deposits PFC revenues as collected to the PFC fund. Money in the PFC fund are applied in the following order: to pay debt service on the PFC bonds, make any required deposits to the reserve account, make any subordinate-lien PFC obligation payments, make any required deposits to a subordinate-lien PFC reserve account, and deposit to the PFC capital account. The account is for approved projects or any other use authorized under federal PFC regulations.

The port has two swaps and direct purchase debt related to its stand-alone PFC debt. It has about $2.2 million in collateral posted related to its PFC swaps, which is required because the swap carries a negative fair value. Collateral postings are required when the posted collateral's fair market value is less than the negative mark-to-market on the swap, or if the ratings on the airport fall below certain thresholds. We do not consider the possibility of required collateral postings a credit risk because PDX bond ratings would have to fall by at least two notches, which we view as unlikely. The port has series 2012A PFC bonds outstanding, which are direct purchase bonds held by Wells Fargo Municipal Capital Strategies LLC. There is about $54 million outstanding under the direct purchase agreement. We consider the contingent liquidity risk from this debt remote.

The federal government highly regulates the port's ability to levy and collect PFCs. The FAA may terminate or reduce the port's authority to impose PFCs if it determines that the airport operator has violated provisions of federal law or that management is not using PFC revenue for approved PFC projects, among other provisions. In addition, the FAA could deny PFC applications if it determines that the operator violated any of its federal grant assurances or violated certain federal statutes and regulations applicable to airports. Amounts received or receivable under the PFC program are also subject to the FAA's audit and adjustment. S&P Global Ratings considers the port's long history of applying for and receiving multiple PFC authorizations and administering the program as mitigating the risk from long-term sufficiency of PFC revenue relative to debt obligations.

The port operates PDX, which is on 3,200 acres on the southern edge of the Columbia River, 12 miles northeast of downtown Portland. The FAA considers PDX a large-hub airport, ranking 30th busiest airport in the U.S., based on 2017 enplaned passenger data from the FAA. 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. The only other commercial service airports in the state are smaller and at least 100 miles from Portland. PDX has three runways. The passenger terminal includes five attached concourses. Port-owned parking facilities provide approximately 17,000 public and employee parking spaces across several garages and lots.

Outlook

The stable outlook reflects our expectation that pro forma PFC MADS coverage will remain strong during the two-year outlook period from generally steady enplanement levels and no additional parity debt plans.

Upside scenario

We could raise the rating in the next two years if pro forma PFC MADS coverage based on actual results exceeds 3x and we believe it will stay above this level.

Downside scenario

Although unlikely, we could lower the rating if pro forma PFC MADS coverage erodes significantly due to a severe decline in enplanements or the port issuing significant parity debt.

Enterprise Risk Profile

Our assessment of the PDX's enterprise risk profile considers the airport's service area economic fundamentals, industry risk, market position, and management and governance.

Economic fundamentals

The service area economic fundamentals reflects our assessment of the Portland-Vancouver-Hillsboro metropolitan area. The Portland metro area has very favorable economic activity as measured by GDP per capita of $64,892 (which is higher than the national average), unemployment rates below or comparable with the national average, a population of about 2.4 million, and above-average expected population growth over the next three years. Portland is the largest city in Oregon and second-largest in the Pacific Northwest after Seattle. The area has a broad and diverse economy with leading sectors that include technology, transportation, manufacturing, tourism, higher education, and health care.

Market position

Our market position assessment considers PDX's general favorable enplanement trends from serving the expanding Portland metropolitan area and limited competition. The airport has a relatively large O&D enplanement base, totaling 8.4 million in fiscal 2018 or 85% of 9.7 million total enplanements. Enplanements rose strongly from fiscal years 2014-2018, at a compound annual growth rate (CAGR) of 5.8%. Fiscal 2018 total enplanements increased 3.3% to 9.7 million. Enplanements for fiscal 2019 is projected to increase 2.4% to nearly 10 million. PDX has a moderately concentrated air carrier mix with Alaska Air, the leading carrier by passenger volume, accounting for 43.1% of total enplanements in fiscal 2018. The airport's cost per enplanement (CPE) is projected to increase to $18.53 by fiscal 2024 following the port issuing $867 million of additional GARBs to fund its $2.1 billion CIP. In fiscal 2018, CPE was a moderate $9.82.

Management and governance

The managerial and governance assessment reflects the port's strategic positioning; risk management and financial management; and organizational effectiveness. We also consider the port's governance structure credit neutral.

The port's strategic plan, most recently updated in 2018, includes several key initiatives, of which customer-service improvements at PDX is among them. We expect the port to modify the plan as necessary until the next scheduled update in 2023.

The port has formal financial targets, which include maintaining minimum general airport revenue bond (GARB) debt service coverage (DSC) of 1.7x, stand-alone PFC DSC of 2.0x, and airport revenue fund balance of 300 days' cash on hand, which it has met or exceeded consistently. The port has also covenanted to comply with PFC laws and regulations, noise regulations, and to manage the PFC program so that remaining PFC authority less contractual commitments exceeds 105% of defined unpaid debt service. Management annually updates the port's long-term operating forecast alongside the capital plan, using forecast to develop financial and operating targets for airline cost per enplanement, landing fees, terminal rents, income projections, and capital funding plans. The port uses key management targets and metrics from its annual budget and long-range planning forecasts to measure actual performance. Senior leaders and the executive management team review and discuss monthly results and evaluate quarterly year-end projections. If actual results are trending unfavorably relative to budget, senior management will discuss what it can defer or what opportunities are available to generate additional revenue.

The port has adopted policies for debt, swaps, and seismic resiliency. Internal control policies relate to execution of contracts and expenditure approval, investments, employee ethics, and providing an employee hotline to report any wrongdoing anonymously. The port's risk-management program includes insurance to protect the port against a variety or risks such as cybersecurity breaches, property damage, floods, earthquakes, terrorism events, casualty and liability, personnel, and financial losses.

Signatory airline agreements are in place, as are many agreements with airport concessionaires. The PDX airline agreement extends through 2025 and has a hybrid ratemaking 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's GARB DSC exceeds 1.75x).

The management team takes a comprehensive approach when evaluating capital needs. This includes long-term planning to ensure the facilities can handle future activity levels, mitigate some risks (like seismic events), and target service levels. It uses an asset management program. To help with the decision-making process, the port's asset management program provides an analysis of alternatives to replace an asset and the consequences if management postpones a project. The port reviews the first five years of the CIP frequently for changes in business priorities, asset conditions, regulatory requirements, funding opportunities, and other conditions. Management monitors and reviews annually the CIP's out-years in the context of meeting operational capabilities, supporting port financial targets, and deciding on a programmatic approach to assets.

We consider the port's management team very experienced and effective and in running all aspects of a large-hub airport. There are no plans for changes to senior management, except for a new CFO, who officially joins the port's senior management team on June 10, 2019. We view management's ability to administer and maintain PFC program eligibility favorably. The port has never been found in violation of or been notified by the FAA as not complying with federal grant assurances or applicable federal statutes and regulations related to the collection or use of PFCs.

Financial Risk Profile

Our financial risk profile assessment considers PDX's historical and pro forma figures in assessing its financial performance, debt and liabilities capacity, and liquidity and financial flexibility. We also consider the metrics under various lower enplanement scenarios because the narrow fixed-rate revenue pledge is sensitive to changes in enplanement levels. More specifically, we consider PDX's historical enplanements trends for which the level of annual PFC revenues is derived, current stand-alone PFC debt level, no additional parity debt plans, and plans to draw on the PFC fund balance to pay for certain CIP project costs. Our financial profile assessment also considers the port's financial policies (transparency and disclosure, investments, debt profile, contingent liabilities, and legal structure), which we view as credit neutral.

The financial projections that were prepared in connection with port's last GARB issue (series 25) assume total enplanements will increase 2.3%, on average from fiscal years 2019-2024, which is lower than the 2.7% CAGR the airport had from 2008-2018, during which enplanements grew to 9.7 million in fiscal 2018 from 7.4 million in fiscal

2008. This includes a 10.7% drop and 2.7% drop in fiscal years 2009 and 2010. The forecast also projects PDX's airline cost per enplanement increasing to nearly $19 in fiscal 2024 from a moderate $9.82 in fiscal 2018. Although we consider these assumptions reasonable, we evaluated the financial metrics of the port's stand-alone PFC debt based on historical enplanement levels.

Financial performance

We view PDX's financial performance as strong, reflecting demand characteristics at the airport that support PFC revenue generation that will produce at least strong MADS coverage. Our assessment, however, also considers the narrow fixed-rate revenue pledge that is sensitive to changes in enplanements. While there is no rate-setting flexibility, MADS coverage, based on fiscal 2018 annual PFC revenues of $38.1 million is a strong 2.6x; and ranges from a strong 2.9x to a very strong 3.25x from fiscal years 2019-2024, if enplanements grow 2.3% per year. The port does not have plans for additional debt backed solely by PFCs.

Debt and liabilities

The debt and liabilities capacity assessment, reflects our expectation that PDX's enplanement levels will be generally steady, the amortization of PDX's stand-alone PFC debt, and that certain project costs included in port's $2.1 billion CIP will be funded with PFC revenue on a pay-as-you-go basis, but not with proceeds from additional stand-alone PFC debt. Consequently, we expect PDX's stand-alone PFC debt to annual PFC revenue to be extremely strong (below 5x). The metric is 3.4x based on actual stand-alone PFC debt and annual PFC revenues reported for fiscal 2018; and ranges from 1.4x-2.6x based on projections for 2019-2024.

Liquidity and financial flexibility

The liquidity and financial flexibility assessment reflects our expectation that the port's PFC fund balance to stand-alone PFC debt ratio could fluctuate between levels we consider very strong (50% to 85%) and extremely strong (over 85%) because of the port using PFC fund money to pay capital projects included in its CIP, if enplanements trend lower than forecast.