S&P Global
Ratings

RatingsDirect®

A.B. Won Pat International Airport Authority, Guam; Airport

Primary Credit Analyst:
Paul J Dyson, San Francisco (1) 415-371-5079; paul.dyson@spglobal.com

Secondary Contact:
Todd R Spence, Dallas (1) 214-871-1424; todd.spence@spglobal.com

Table Of Contents

A.B. Won Pat International Airport Authority, Guam; Airport

Credit Profile		
A.B. Won Pat Intl Arpt Auth (AGM)		
Unenhanced Rating	BBB+(SPUR)/Stable	Upgraded
A.B. Won Pat Intl Arpt Auth gen rev bnds		
Long Term Rating	BBB+/Stable	Upgraded
A.B. Won Pat Intl Arpt Auth gen rev bnds (non-AMT)		
Long Term Rating	BBB+/Stable	Upgraded

Many issues are enhanced by bond insurance.

Rationale

S&P Global Ratings raised its long-term rating and underlying rating (SPUR) to 'BBB+' from 'BBB' on A.B. Won Pat International Airport Authority, Guam's outstanding senior-lien general revenue bonds using our "U.S. And Canadian Not-For-Profit Transportation Infrastructure Enterprises" criteria, published March 12, 2018. The outlook is stable.

The rating reflects our opinion of the airport's adequate enterprise risk profile and strong financial risk profile. The adequate enterprise risk profile reflects our assessment of the airport, which provides an essential service to the island, tempered by our expectation of fluctuating activity levels as a result of the island's unique exposures. The strong financial risk profile reflects our expectation of coverage that we expect will decline modestly but be maintained at levels we view as at least adequate, and debt and liabilities capacity that we expect will remain very strong given no borrowing plans over the next five years.

The adequate enterprise risk profile reflects our view of the airport's:

- Vulnerable market position despite the essential service the airport provides to the island, given its limited growth potential and exposure to items beyond its control such as its remote location, tourism trends, global economic shocks, security concerns, and weather events;
- Very strong service area economic fundamentals, which include a GDP per capita of around $36,000 but with unemployment that is above the national average;
- Low industry risk relative to that of other industries and sectors; and
- Adequate management and governance, with detailed financial planning, as well as adequate risk management practices and organizational effectiveness.

The strong financial risk profile reflects our view of the airport's:

- Adequate financial performance, with historical coverage that we view as strong, although, based on the authority's financial forecast, coverage may be only adequate in future years as expense growth outpaces revenue growth;
- Very strong debt and liabilities capacity as the authority is continuing to pay down its debt with no plans for

additional debt for the next five years; and

- Strong liquidity and financial flexibility, although, according to forecast, liquidity will experience modest declines over the next three years as the airport funds critical capital projects.

The bonds are secured by net revenue, which are defined in the bond indenture as all of the revenue received during a particular period less all operations and maintenance expenses of the airport incurred in that period. According to the bond indenture, the authority is permitted to include excess revenue from the previous period in its calculation for debt service coverage. The authority has covenanted to maintain coverage of 1.25x annual debt service payments. The additional bonds test states that net revenue must be at least 1.25x annual debt service payments in the previous fiscal year or projected at 1.25x annual debt service for the current year. The airport had $216 million of general revenue bonds outstanding and a subordinate loan payable to the First Hawaiian Bank of $8.3 million outstanding as of Sept. 30, 2017.

Outlook

The stable outlook reflects our anticipation that the airport's financial performance will remain steady, supported by our view that the airport will retain sufficient demand.

Upside scenario

Although we are unlikely to do so, we could raise the ratings during the two-year outlook period in case of a material increase in demand that we believe is sustainable.

Downside scenario

We could lower the ratings if debt service coverage, per our calculations, declines to a level we view as vulnerable.

Enterprise Risk Profile

Our assessment of the airport's enterprise risk profile as adequate reflects its very strong economic fundaments, low industry risk, vulnerable market position, and adequate management and governance.

The airport's service area has very strong economic fundamentals given the territory's GDP per capita of about $36,000, although Guam's unemployment is slightly above the national average. Guam's estimated population was 162,896 as of 2017, and the island encompasses 212 square miles. Guam is located 3,800 miles southwest of Honolulu and 1,500 miles southeast of Tokyo, and, in our view, its remote location is a credit limitation. Guam's economic activity is largely based on tourism and military spending. Because of this, many of the government's economic development initiatives focus on these pillars, especially tourism. Hotel property owners have invested substantially in hotel renovations and expansions in recent years, with more than 600 new rooms available now compared with five years ago, including the 419-room Dusit Thani Guam hotel. Construction of another 340-room luxury hotel, the Tsubaki Tower, is also underway with completion estimated by the end of 2020.

The airport is the only commercial airport on the island for passengers and cargo serving the U.S. mainland, Asia, Australia, and various islands in the Pacific region (although the Port Authority of Guam handles most cargo). The authority is a component unit of the Government of Guam (BB-/Stable GO rating), but there is no general fund transfer or direct exposure. Median household effective buying income for Guam is about 73% that of the U.S., but Guam is experiencing moderate economic growth, with increased tourism, diversification thereof, and related expansions. Fiscal 2017 yielded a record number of visitor arrivals at 1.56 million and continued good growth is anticipated, especially from the thriving Korean market. Korean visitors represented 42% of arrivals in fiscal 2017 with visitors from Japan at 43%, a significant change from 10% and 76%, respectively, in 2007. The unemployment rate was just 4.9% as of 2017, a significant decline from 13.3% in March 2011. Although the territory's economy is stable, it is also very narrow and susceptible to outside events, such as the economic condition of other countries and regions, changes in strategic policies of the U.S. with regard to its military installations on the island, and even severe weather given its exposure to typhoons. It also experiences military threats from North Korea from time to time, including in fiscal 2018, and this is having a modest negative effect on visitors and enplanements.

The U.S. military buildup on Guam is gaining considerable momentum. Approximately 4,700 active duty personnel, along with family members, support and civilian staff, vendors, and suppliers, are relocating to Guam from Okinawa, Japan (although down from the originally proposed 9,000). What was once estimated at a $15.0 billion economic impact is now estimated at $8.7 billion. Nevertheless, nine projects have been completed, valued at $510 million, with eight projects awarded and under construction totaling $495 million. The National Defense Authorization Act for Fiscal 2019 was signed into law in August 2018, authorizing $449 million for Guam, and the denial of H-2B visas to foreign construction workers has been resolved, paving the way for heightened activity. A 13-year period (revised from seven years) of moderate construction followed by a gradual phase-out is planned. All facets of Guam's government, from the general government to utilities, the port, and airport, have reached a general understanding with the U.S. Department of Defense that any impact from the relocation would be cost neutral to Guam, even if many of the details are undetermined. In our view, the military buildup is positive for the island's future economic growth and airport operations, but we expect the related growth in pledged revenue to be gradual.

We consider the airport's overall market position vulnerable, despite the essential service the airport provides to the island, given its exposure to items beyond its control such as its remote location, tourism trends, global economic shocks, security concerns, health scares and weather events. Additional considerations include the limited growth potential of the service area and the concentrated economic base it serves, despite our views stated above about its economic fundamentals. The Federal Aviation Administration classifies the airport as a small hub. The airport served approximately 1.86 million enplaning passengers in fiscal 2017 (ended Sept. 30) and primarily serves tourist-oriented origin-and-destination (O&D) passengers, most of whom are from Japan or Korea, as well as local and regional interisland traffic. The authority's key credit strengths, in our opinion, are its essential role in providing air service to the island and its history of relatively stable financial performance despite volatility in passenger volumes produced by economic swings, weather events, security threats, and other factors. In fact, fluctuations in passenger traffic volumes are common. Enplanements grew a strong 4.7% in fiscal 2017, but are projected to decline 1.0% in 2018 before growing 0.7% in 2019 and 3.4% annually from 2020 to 2023 given the island's growth and tourism prospects. Although essentially flat in fiscal 2015 relative to fiscal years 2014 and 2013, enplanements increased by 7.8% in fiscal 2013 and 9.4% in fiscal 2012, primarily as a result of an increase in visitors. Enplanements declined 2.1% to 1.4 million in fiscal 2011 from 1.5 million in fiscal 2010. This decline primarily was due to the March 2011 earthquake and subsequent events in Japan that adversely affected Guam's primarily O&D market. Enplanements were up by 12.6% in fiscal 2010, but were down 9.6% in fiscal 2009 and 3.2% in fiscal 2008, primarily as a result of the global economic recession. Enplanements are still below historical levels. The peak of enplanements was in 1997 at approximately 1.9 million.

Although management has been aggressively pursuing new service, including low-cost carriers, overall, we still view the air carrier mix as somewhat concentrated, with United Air Lines carrying 45% of passenger enplanements in fiscal 2017, followed by KAL at 12% and Jeju Air at 11%. But, we also recognize that air carrier mix has diversified significantly over the past decade, and additional diversification in fiscal 2018 is anticipated such that United's share may decline to 37%. O&D enplanements are a strong 94% of total enplanements, and visitor arrivals grew 3.3% in 1.56 million in fiscal 2017 from 1.51 million in fiscal 2016, partly as a result of strong attendance at several locally hosted conventions and festivals, but also as a result of continued growth in the Korean visitor market (which has mitigated a shrinking Japan market). Visitor arrivals by country continue to diversify and South Korea now has nearly the same market share as Japan at 42% of the visitor market compared with Japan's 43%. This represents a major shift, as Japan had 50% of the visitor market share in fiscal 2016, and 78% in fiscal 2004 compared with Korea's 8%. Visitor arrivals from Korea grew 25% in fiscal 2017 to 649,400 after 35% growth in fiscal 2016 and 31% growth in fiscal 2015. Based on results from the Guam Visitors Bureau as of July 2018, visitor arrivals for the fiscal year to date were down 3.1% in light of the North Korea threat in October 2017, but are expected to be down only 1.0% for the full fiscal year.

The airport's management and governance, in our view, are adequate, reflecting our view that management has engaged in detailed financial planning and adequate capital planning as well as good risk management, with all fixed-rate debt, although it lacks specific liquidity targets or formal succession planning. While management lacks a minimum unrestricted cash target, it monitors liquidity on a monthly basis. Management prepares its annual budget based on enplanement projections from the airlines, the amount of revenue required to meet the rate covenant, and any available funds from the previous fiscal year, in addition to projections for each revenue and expense category for the upcoming fiscal year. Management also closely tracks monthly actual results versus budget. Management has considerable experience operating a small hub airport, but we do not view it as particularly strong in comparison with peers. We also note that the ongoing litigation with regard to the concessionaire contract with Lotte Duty Free Guam LLC (in terms of whether it was properly awarded) is a source of uncertainty.

Financial Risk Profile

Our assessment of the airport's financial risk profile as strong reflects our view of the airport's adequate financial performance, very strong debt and liabilities capacity, and strong liquidity and financial flexibility. Our financial profile risk assessment considered historical and pro forma figures from fiscal 2020, which reflect our expectation that the authority will be drawing on its cash to fund capital improvement programs through 2020 and will continue to pay down its debt outstanding. Our financial profile assessment also considered the airport's financial policies, which we consider credit neutral.

The adequate financial performance assessment reflects our calculation of coverage on an all-in basis and considers financial projections. Senior-lien bond debt service coverage in audited fiscal 2017 was 1.60x, including available revenue from a coverage account, and 1.35x per our calculations, excluding the coverage account. These are down from 1.82x and 1.57x, respectively, in fiscal 2016. When including debt service related to a subordinate-lien bank loan, we calculate all-in debt service coverage of 1.27x for fiscal 2017, down from 1.47x in fiscal 2016 but up from 1.23x in fiscal 2015. Passenger facility charge revenue is considered revenue in both the indenture and our calculation. (It is not used as an offset to debt service.) All-in coverage per our calculations is projected at about 1.1x to 1.2x for fiscal years 2018 to 2023 as a result of expenditure growth slightly outpacing revenue growth. Airline cost per enplanement has been fairly steady over the past five years at a moderately high $17 (reflecting Guam's status as an international destination), although projections indicate it will stay below $18 through 2023.

We assessed the airport's debt and liabilities capacity as very strong based on our expectation that the authority has no additional debt issuance plans over the next five years and will continue to reduce its debt outstanding. We consider the debt burden, at about $122 per enplaned passenger in fiscal 2017, moderate compared with the median for 'BBB' rated airports, which is $96 (the level that the airport projects having by 2020). The capital plan through fiscal 2019 totals a very large $186 million, as the authority has several critical projects to complete. However, no additional debt is anticipated until potentially 2023, when an additional financing is possible to address aging airport infrastructure. Capital projects for 2018 and 2019 will be funded 56% ($105 million) from the previously issued series 2013 bonds, 31% ($57 million) from federal grants, and 13% ($25 million) from cash on hand.

We assessed the airport's liquidity and financial flexibility as strong, reflecting our expectation that although the liquidity for the system has been increasing over the past three years, it may decline somewhat in 2019 and 2020 as it is used for capital improvement projects. Liquidity has increased steadily from $36 million in 2015 to $72 million in 2017, resulting in unrestricted cash on hand at a level considered very strong for the past two years at about 570 days. Management plans on using its liquidity, however, to fund future capital improvement projects, and liquidity is projected to decline to around $55 million, or 384 days' cash on hand by fiscal 2020. Adjusting these liquidity metrics for the contingent liquidity risks related to the authority's direct purchase debt outstanding, described below, results in cash that is approximately 60 days lower than the amount cited above for fiscal 2017 and about 30 days less for fiscal 2020 (as the direct purchase debt balance declines).

Direct Purchase Evaluation

The authority executed a loan with First Hawaiian Bank in 2012 in the amount of $11.9 million to finance certain energy efficiency upgrades to the terminal building. As of Sept. 30, 2017, the balance was $8.3 million, with the loan fully due by January, 2024. Although contingent liability risk is not material to liquidity metrics or the rating outcome in this case, we nonetheless are factoring it in given various provisions in the loan agreement. According to the agreement, the bank is permitted to accelerate debt if, at its discretion, it concludes that there has been any adverse change in the general financial condition of the authority that has or could have a material adverse effect on the authority's ability to perform its obligations under the loan documents. We view the scope of the material adverse effect provision as very broad, and we believe that this provision is inherently vague, which makes it difficult to gauge the authority's proximity to the contingent claims on liquidity that the provision presents. There are other events of default that are quite broad and give the bank the right to immediately accelerate the debt. Nevertheless, at the current rating and based on the authority's financial performance, we view the likelihood of the bank availing itself of these provisions as remote.