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New Issue

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Contacts

Maria Matesanz 212-553-7241
Senior Vice President
maria.matesanz@moodys.com

Michael Mulvaney 212-553-3665
MD-Project Finance
michael.mulvaney@moodys.com

Hawaii (State of) Airport Enterprise

New Issue: Moody's assigns A2 to Hawaii's Airport System 2017A CFC Revenue Bonds; outlook stable

Summary Rating Rational

Moody's Investors Service assigns initial A2 to the State of Hawaii's $250 million Series 2017A Airport System Customer Facility Charge (CFC) Revenue Bonds (Taxable). The rating outlook is stable.

The rating is rooted in steady growth in rental car transaction days and pledged customer facility charge (CFC) revenues that are expected to produce DSCRs above 2.0x. Other considerations include the additional planned $226 million of debt for projects in construction, strong legal protections and rental car agreements that require the car rental companies (RACs) to make contingent deficiency payments if needed and maintenance of strong liquidity balances equal to annual debt service through the 2023 forecast. The rating is also supported by a moderate daily CFC rate of $4.50 and an unlimited ability to raise the rate as needed. The rating is tempered by a dependence on sustained growth in tourism, on-going construction risk for two new facilities and possible additional debt to finance additional facilities at other system airports.

Credit Strengths

» Stable and improving economic conditions and sustained growth of tourism have led to a history of growing rental car demand at the statewide airports system fueled by growth in Hawaii's appeal as a domestic and international tourist destination

» The majority of rental car companies serving the Daniel K. Inouye International Airport (HNL) and Kapalui (OGG) airports have signed the rental car concession agreement that requires them to pay CFCs and contingent fees if CFCs are insufficient to meet a minimum 1.15x DSCR without rolling coverage

» Ratio of rental car transaction days to O&D enplanements among one of the highest for US airports

» Strong legal protections include 1.4x rate covenant and the Department of Transportation's (DOT's) ability to raise CFC rates at any time with no cap

» Projected DSCRs are forecasted to be strong at 2.0x without rolling coverage; FY 2016 CFC collections provide 2.0x coverage of forecasted maximum annual debt service (MADs)

Credit Challenges

- » Debt is supported only by a single revenue stream of CFC collections as well as contingent rent from the RACs
- » State assesses $3.00 daily rental motor vehicle surcharge tax on all car rental transactions that is not pledged to ConRAC bonds. A significant rate increase on this surcharge could negatively impact car rental demand
- » Potential for cost overruns for two CONRAC facilities in construction could result in additional debt, though none currently expected
- » Potential for additional debt for construction of new facilities at other system airports
- » Potential for some erosion of car rental demand at Honolulu due to the planned development of mass transit to the airport and the possible introduction of ride-sharing services

Rating Outlook

The rating outlook is stable. We expect that the airport will achieve reasonable forecasted annual enplanement growth of 1.9% and comparable rental transaction and revenue growth from FY 2017 to FY 2023 to achieve above 2.0x DSCR for the ConRAC bonds.

Factors that Could Lead to an Upgrade

- » CFC collections that produce DSCRs, without the benefit of rolling coverage fund balances account balances, consistently over 2.0x
- » Significantly higher than currently forecasted transaction days and CFC revenue collections that produce higher than 2.0x DSCRs

Factors that Could Lead to a Downgrade

- » Additional debt above the planned $226 million 2019 bonds to complete facility construction
- » Significant increases in planned future debt above current expectations for a maximum of $100 million for ConRAC facilities at other system airports
- » Significant transaction day declines that reduce DSCRs, without the benefit of account balances, below 1.75 times.

Key Indicators

Exhibit 1

	2013	2014	2015	2016	2020 Forecast
Change in Transaction Days (%)	N/A	-3.0	19.9	5.2	1.8
Enplanement Annual Growth (%)	6.1	-1.1	2.0	3.2	1.5
CFC Debt/Outstanding ('000s)	N/A	76,000	76,000	76,000	479,970
CFC Collections ('000)	55,390	54,083	64,992	68,250	74,287
DSCR by CFC Collections*	1.65	1.62	1.94	2.04	2.22

*Based on forecast 2020 debt service of $33,471,000
Source: Moody's Investors Service

Detailed Rating Considerations

The airport system has a virtual monopoly on all non-military passenger traffic in Hawaii with 97% of all visitors to the state arriving by air, and 88.3% of visitors traveling for tourism.

The largest airport is HNL on Oahu with 58% of total enplanements, but which accounts for only 29.7% of rental car transaction days compared to OGG on Maui which accounts for one-fifth of total enplanements but over one-third of transaction days. This is due to the high tour group visitor mix at HNL and more mass transit options for transportation to dominant tourist destinations such as Waikiki compared to the fewer options in Maui and the more dispersed nature of tourism there.

The five major RACs serving the airports have all signed onto the lease agreement that expires the later of 30 years from the date of facility occupancy, or final bond maturity in 2048. RAC agreements cover access to statewide rental car facilities, including the HNL, OGG and any future ConRACs that the department will construct. Off airport RACs began paying the CFC on July 1, 2014 (including Alamo, Dollar, Thrifty at HNL and Advantage at OGG). All signatory RACs will be on airport after the HNL and OGG ConRACs are completed. Upon project completion dates, estimated to be April 2019 for the OGG ConRAC and December 2020 for the HNL ConRAC, the signatory RACs are required to pay a minimum annual required deficiency payment should the CFC be insufficient to cover 115% of debt service on the bonds plus required reserve deposits.

The two ConRAC projects are being constructed under design-build contracts, with cost increases largely borne by the contractors, with the exception of change orders requested by the airports division, which could add additional costs and require more debt financing. Given that CFCs have been collected since 2008 and that 50% of the construction costs are being paid by available cash collections, we believe that there is room to absorb some cost increases.

The HNL ConRAC's construction includes interim and permanent phases and is projected to cost $438.2 million. The interim ConRAC was opened in November 2015 and consists of a consolidated customer service area on the ground level and ready-to-rent vehicle parking spaces on four levels of the eastern portion of the existing Overseas Terminal Parking Garage. The ConRAC is currently 10% complete and scheduled to be completed in 2020. The facility will consist of a five-level reinforced concrete structure on approximately eight acres of land. The construction of the permanent contract facility was awarded to Watts Constructors, Inc. The project is expected to cost $438.2 million. When the permanent ConRAC becomes operational, the Interim ConRAC will revert to use as a public parking facility.

The Kahului ConRAC will be a three-level facility and an electric tram located close to the terminal that will eliminate the need for rental car shuttle buses on airport roadways. Construction of the facility began in April 2016 and is expected to reach completion in May 2019. It is currently 35% complete. The facility will consist of a consolidated customer service building, ready/return vehicle areas, a QTA facility, overflow vehicle storage area, service yard, airport employee parking, and the tram. Construction of the ConRAC was awarded to Hawaiian Dredging Construction Company. The project is expected to cost $436.4 million.

Revenue Generating Base

The revenue generating base includes all airport car rentals in the Hawaii airport system although only the five primary airports and Molokai currently collect CFCs. Economic conditions in the State of Hawaii (GO, Aa1) remain stable and support continued passenger growth. The state's low unemployment at 2.7% and robust tourism industry undergird its rating. The state's economy benefits from substantial revenues attributed to tourism and as noted by Moody's Economy.com has seen continued expansion in the tourism sector since the prior calendar year. The defense industry is also noted as a critical anchor in Hawaii's economy, with military personal growing 6% since 2010 and the increased strategic importance of the military bases in the current federal administration. Continued airline seat growth in FY 2017 (202,096) attests to an expanding tourism industry that will continue to serve as a basis of support the economy and revenue generation for the state.

Operational and Financial Performance

CFC collections have grown to nearly $68.25 million in FY 2016 from $54.99 million in FY 2015, a 5.2% increase following a 20.2% increase in FY 2015. The 20.2% increase in FY 2015 reflected the collection of the CFC from off airport RACs following the executed RAC agreement. In FY 2014 CFCs dipped 2.4% due to two RACs moving off airport. The legislature suspended the $4.50 CFC in FY 2012, but reinstated the fee in FY 2013. The contractual pledge created in the bond indenture would preclude this from occurring until all the bonds are repaid.

Based on FY 2016 CFC collections we estimate that projected DSCR will be above 2.0x in FY 2020, including all debt expected to be issued to complete the projects. Under the base case proforma that includes annual growth in CFC collections, the DSCR is forecast at

2.47x excluding rolling coverage account balances. Under a stress scenario that layers on $150 million in additional debt the DSCR dips to a low of 1.70x in FY 2021 excluding rollling coverage balances

LIQUIDITY

The strong performance of transactions days has resulted in a significant accumulation of CFCs. Total CFC balances, excluding debt service reserves, reached $216 million in FY 2016. While much of this balance will be expended for the project construction, we expect the discretionary balance to remain above annual debt service, including the planned $226 million bond issuance in 2019.

Debt and Other Liabilities

DEBT STRUCTURE

The $250.18 million Series 2017 bonds are fixed rate and have level debt service through bond maturity in 2048. The system has $76 million parity EB-5 bonds that were issued in 2014 to finance initial construction of the ConRAC facility. The planned $226 million Series 2019 will be applied to repay the 2014 EB-5 bonds and fund ConRAC project completion costs.

The debt service schedule remains flat even with the anticipated issuance of $226 million in 2019. Including the 2019 issue, debt service is forecasted to be flat at about $34 million from 2020 through final maturity. Given annual collections of $68.25 million in FY 2016, combined with modest conservative forecast growth in enplanements and car rentals, absent significant additional debt we expect CFCs to comfortably produce over 2.0x DSCRs.

DEBT-RELATED DERIVATIVES

None.

PENSIONS AND OPEB

The airport system participates in a defined benefit pension plan and reimburses the State's Employees' Retirement System. For FY 2016, Hawaii Airport's reported net pension liability was $115 million. Moody's adjusted net pension liability (ANPL) calculation for the airport for FY 2016 was $213.14 million. Its total pension liability was $305.27 million. Its FY 2016 issuer contribution was $14.74 million, higher than its contractually required contribution of $11 million.

Management and Governance

The State of Hawaii's airport system is operated by the Hawaii Department of Transportation-Airports Division. The Department of Transportation is one of 18 principal executive departments of the State of Hawaii and it is empowered to establish, maintain and operate the transportation facilities of the state, including highways, airports, harbors and other transportation facilities. The airports division operates all state airports and the ConRAC as a single integrated system for management and financial purposes.

The department is headed by the director, who is appointed by the governor and confirmed by the state senate. The governor also appoints, without state senate confirmation, four deputy directors of transportation. The director and deputy directors of transportation serve four-year terms conterminous with the governor's term.

Legal Security

The bonds are secured by pledged system wide CFC revenues now charged to rental car users at the 5 primary commercial system airports and Molokai. The bonds are special limited obligations of the state payable solely from and secured solely by gross pledge of receipts from the CFCs collected by RACs at the five primary airports and Molokai as well as minimum annual requirement deficiency fees paid by the RACs if CFCs are insufficient to cover 115% debt service, excluding rolling coverage account. The state has covenanted to impose CFCs and other user fees sufficient to pay debt service on the bonds, fulfill reserve requirements and meet all covenants in the bond documents and is authorized to increase the CFC rate at any time.

The bonds additionally benefit from a strong rate covenant of 1.40x, an additional bonds test of 1.25x MADS as well as a cash funded debt service reserve fund (DSRF) equal to maximum annual debt service (MADS) and a debt service rolling coverage fund (cash funded to 25% of MADS).

Use of Proceeds

The current issue along with CFC fund balances and future collections will finance project construction costs of facilities. Additional bonds of approximately $226 million are expected to be issued in 2019 to complete the project and will also refund $76 million of outstanding EB-5 parity bonds.

Obligor Profile

The department operates and maintains 15 airports at various locations within the state. Virtually all non-military passenger traffic throughout Hawaii passes through the system, which includes five primary airports and 10 secondary airports. The primary airports are Daniel K. Inouye International Airport (on the Island of Oahu), Kahului (on the Island of Maui), Hilo International and Kona International (both on the Island of Hawaii), and Lihue (on the Island of Kauai).

Methodology

The principal methodology used in this rating was Publicly Managed Airports and Related Issuers published in November 2015. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 2

Hawaii (State of) Airport Enterprise

Issue	Rating
Airport System Customer Facility Charge Revenue Bonds Series 2017A (Taxable)	A2
Rating Type	Underlying LT
Sale Amount	$250,175,000
Expected Sale Date	07/12/2017
Rating Description	Revenue: Government Enterprise

Source: Moody's Investors Service

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Contacts

Maria Matesanz 212-553-7241
Senior Vice President
maria.matesanz@moodys.com

Michael Mulvaney 212-553-3665
MD-Project Finance
michael.mulvaney@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

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