MOODY'S
INVESTORS SERVICE

New Issue: **MOODY'S ASSIGNS A2 RATING TO HAWAII AIRPORT SYSTEM'S SERIES 2011 BONDS; OUTLOOK IS STABLE**

Global Credit Research - 06 Sep 2011

AIRPORT CURRENTLY HAS $1.17 BILLION RATED DEBT OUTSTANDING

Airport
HI

Moody's Rating

ISSUE		RATING
Airport System Revenue Bonds, Series 2011		A2
Sale Amount	$296,000,000	
Expected Sale Date	09/12/11	
Rating Description	Revenue	

Opinion

NEW YORK, Sep 6, 2011 -- Moody's Investors Service has assigned an A2 rating to the $296.0 million State of Hawaii Airport System Revenue Bonds Refunding Series 2011. Moody's is also affirming the A2 rating on the airport's outstanding parity debt in the amount of $1.17 billion. The outlook is stable.

SUMMARY RATING RATIONALE

Both the rating and the outlook reflect the strength of the airport system's near monopoly over air travel to and from the islands, the essentiality of air service for tourism and intrastate travel, and the solid historical financial performance. The airport system's financial liquidity is a key measure of its financial strength and that cash is expected to continue to decline as the system continues to move forward with its extensive capital improvement plan (CIP). The airport system has not provided any rate relief to the airlines in FY 2011 and none is planned for FY 2012. This move toward full cost recovery is a key positive for the system's credit, especially as it moves forward with its large capital plan.

USE OF PROCEEDS: The proceeds of the bonds will provide for a current refunding of some of the systems' outstanding revenue bonds for savings. Net present value savings are currently expected to be greater than 6%.

LEGAL SECURITY: Gross revenues of the airport system and Aviation Fuel Tax revenues

INTEREST RATE DERIVATIVES: None.

STRENGTHS:

* Demand for air service is stabilized by Hawaii's remote location, need for inter-island travel, and a substantial military and government presence that requires frequent mainland service

* Position as a premier international tourist destination brings high demand for overseas flights, but the economy's reliance on that industry poses significant risks

* Strong current financial position with low debt and high liquidity provides the airport financial flexibility, though these strengths are expected to wane as additional debt is issued

CHALLENGES

* Debt service coverage and unrestricted cash are both expected to decline substantially beginning in 2012, but remain within levels commensurate with the current rating category

* Economic conditions and the failure of Aloha airlines in FY 2008 caused a sharp reduction in enplanement levels that have not yet recovered

* State has a history of subsidizing airline rates and charges resulting in lower revenues and modest liquidity declines and cost per enplanement is expected to rise to $14.50 in 2016; this practice did not occur in FY 2011 and is not expected to occur in FY 2012

* Airport system has extensive capital needs that will require a sizeable increase in debt

DETAILED CREDIT DISCUSSION

Economic conditions in the State of Hawaii (GO rated Aa2) have stabilized, though the outlook for future growth is not particularly promising. Tourism has performed solidly with visitors increasing 8.7% and 3.0% in 2010 and the first seven months of 2011, respectively, after decreasing -4.5% in 2009. The state also benefits from low unemployment of 6.4% in July, which has remained approximately 3% below the national average. Moody's Economy.com expects economic growth for both Honolulu and the entire state to underperform national levels due to the remote location, reliance on tourism, and high oil prices.

Enplanements have also stabilized, increasing 0.9% in FY 2011 and 1.6% in FY 2010 after falling 15.2% in FY 2009. Although total enplanements remain well below peak levels from 2007, increasing service from a number of carriers is helping to offset the losses of Aloha Airlines and ATA airlines, which ceased operations in 2008. The addition of China Eastern Airlines, and growth from Hawaiian Airlines, Alaska Airlines, and go!/Mokulele airlines have helped to stabilize enplanements.

Unaudited operating results for FY 2011 are quite strong as a result of stable activity and increases in airline charges. Operating revenue increased 9% due primarily to a 21% increase in aeronautical rent revenues driven by rate increases set forth in the airline lease agreement, but also benefitted from increased landing fee and concession revenue. The terminal rental increase is expected to be a one-time adjustment with rates increasing in line with inflation in future years. In addition to increased rates, the airport system has not provided any rate relief to the airlines in FY 2011 and none is planned for FY 2012. This move toward full cost recovery is a key positive for the system's credit, especially as it moves forward with its large capital plan.

The increased airline rates have raised the average airline cost per enplanement (CPE) to approximately $8.78 in FY 2011 from $7.66 in FY 2010. Airline costs are expected to continue to rise as debt service requirements build in the coming years. Debt service coverage remained solid at an unaudited 1.99 times, much higher than the 2009 forecast of 1.27 times because of higher than expected revenues, lower than forecast expenses, and greater than expected coverage account balance. Coverage is expected to decrease to 1.33 times in FY 2012 and remain between 1.33 times and 1.42 times through 2016 due to escalating debt service requirements and operating expenses as a result of the new facilities. Moody's believes these coverages are in line with expectations in the current rating category and we think the system is likely to outperform its forecasts.

The airport system's cash balances remain a driver for the rating. The system's historic use of cash to subsidize airline rates and charges would be viewed as an important credit negative if it brought cash balances below median levels. According to unaudited financial results, cash increased approximately 8.0% on top of the system's already strong FY 2010 liquidity position of 831 days cash on hand based on Moody's calculations. The improved cash position is due to solid financial performance and delays in CIP expenditures. Management expects cash balances to slowly fall to near Moody's U.S. airport median days cash on hand of 416 days as it continues its large CIP. If financial liquidity falls below 400 days cash on hand according to Moody's calculations, the current rating on the airport system will be under pressure.

The airport remains in the midst of its capital program that totals $1.3 billion in projects system-wide. Expenditures have been slower than expected as the environmental review process of the largest project, construction of the Mauka Concourse, has been delayed for review by the new gubernatorial administration. Moody's believes the system's large capital program is exposed to significant cost increases, particularly if it does not remain near its original schedule. However, we also see a slowing of capital expenditures as a credit positive as it should keep financial metrics above projections and may give added flexibility if the operating environment changes. The schedule has already delayed the next debt issuance, which is expected to provide $426 million in funds, until FY 2013 and further changes to the schedule or project scope are possible.

Outlook

The stable outlook is based on Moody's expectation that system-wide enplanement levels will remain near current levels and airline costs will increase in order to generate revenues sufficient to maintain debt service coverage ratios based on net revenues above 1.0 times. Moody's expects that the system will and maintain days cash on hand above the Moody's U.S. airport sector median currently at 416 days.

What could change the rating--UP

Continued strong enplanement levels and full cost recovery through airline rates and charges that brings net revenue debt service coverage based above 1.25 times, while maintaining high internal liquidity to manage operational risks and financial risks could place upward pressure on the rating.

What could change the rating--DOWN

An inability or unwillingness by the airport system to fully recover costs from the airlines that reduces unrestricted liquidity balances below the Moody's U.S. airport median could negatively pressure the rating.

KEY INDICATORS

Type of Airport: O&D

FY2010 Enplanements: 15,208,000

5-Year Enplanement CAGR 2006-2011: -1.5%

FY 2011 vs. FY 2010 Enplanement growth: 0.9%

% O&D vs. Connecting, System, FY 2011 (5 YR AVG): 98% (98%)

% Inter-island vs. Overseas, FY201134.8%

Largest Carrier by Enplanements, System (share): Hawaiian (47.9%)

Airline Cost per Enplaned Passenger, FY 2010 (5 YR AVG): $7.65 ($5.83)

FY 2011 projected: $8.78

Debt per Enplaned Passenger, FY 2010 (5 YR AVG): $52 ($33)

Bond Ordinance Debt Service Coverage, FY 2011 unaudited: 1.99x

Utilization Factor, FY 2010: 11.35

Outstanding Bonds:

Series 2001 Airport System Revenue Refunding Bonds, $345.2 million, A2

Series 2010A, Airport System Revenue Refunding Bonds, $479 million, A2

Series 2010B Airport System Revenue Refunding Bonds, $166 million, A2

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The principal methodology used in this rating was Airports with Unregulated Rate Setting published in July 2011. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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