S&P Global
Ratings

RatingsDirect®

Summary:
Hawaii
Hawaii Airport System; Airport

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Summary:

Hawaii
Hawaii Airport System; Airport

Credit Profile		
US$261.905 mil airport sys rev bnds (AMT) ser 2020A due 12/01/2050		
Long Term Rating	A+/Negative	New
US$181.855 mil rfdg airport sys rev bnds (non-AMT) ser 2020C due 12/01/2030		
Long Term Rating	A+/Negative	New
US$98.17 mil rfdg airport sys rev bnds ser 2020D		
Long Term Rating	A+/Negative	New
US$23.02 mil airport sys rev bnds (non-AMT) ser 2020B due 12/01/2039		
Long Term Rating	A+/Negative	New
Hawaii		
Hawaii Arpt Sys, Hawaii		
Hawaii (Hawaii Airport System)		
Long Term Rating	A+/Negative	Downgraded, Removed from CreditWatch

Rating Action

S&P Global Ratings lowered its long-term rating and underlying rating (SPUR) to 'A+' from 'AA-' on the Hawaii Airport System's (HAS or the system) outstanding senior-lien general airport revenue bonds (GARBs) and its long-term rating to 'A' from 'A+' on the system's series 2013 lease revenue subordinate-lien certificates of participation (COPs). At the same time, we removed the ratings from CreditWatch, where they had been placed with negative implications on Aug. 7, 2020. Concurrently, S&P Global Ratings assigned its 'A+' long-term rating to HAS' pro forma $285 million senior-lien revenue bonds, series 2020A-B, and its $280 million senior-lien revenue refunding bonds, series 2020C-D. The outlook on the long-term ratings is negative.

The ratings on HAS' bonds, along with many other U.S. airport ratings, were previously placed on CreditWatch to reflect the material negative impact of the COVID-19 pandemic on traffic levels, expected financial performance metrics, and overall credit quality. For more information, see "U.S. Airport Ratings Placed On CreditWatch Negative On Severe Passenger Declines And Weakening Credit Metrics," published Aug. 7, 2020, on RatingsDirect.

The state of Hawaii owns and operates the system through its Department of Transportation, Airports Division. The system includes all commercial facilities in the state, and the state accounts for them as a single integrated enterprise fund. The airports division has the authority to levy rates and charges that, along with aviation fuel taxes, are sufficient to comply with the bond indenture's requirement. The extensive 15-airport system consists of one large-hub airport, one medium-hub airport, three small-hub airports, and 10 nonhub or small secondary airports. It is the sole provider of commercial aviation facilities in the state, and multiple airports in the system can accommodate overseas flights (direct

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flights from the U.S. mainland to the neighboring islands has been a growing trend), helping to diversify system risk. Daniel K. Inouye International Airport, or Honolulu International Airport (HNL), serving the state's largest population center, has by far the largest share of systemwide traffic (nearly 60% of enplanements) with long (12,000-foot) parallel runways and ample gate capacity, including 33 overseas gate positions and 13 interisland gate positions.

The series 2020 bonds are secured senior-lien system revenue and aviation fuel tax revenue after operations-and-maintenance costs. The airports system's series 2013 COPs are special limited obligations of the airports division and were issued to fund $150 million in costs related to the implementation of an energy performance contract between the department and Johnson Controls Inc. The COPs represent assignment of a proportionate interest in the lease and in the right to receive rent payments under the lease. Lease payments are secured solely by revenue and aviation fuel tax revenue, but are junior in priority to the pledge of the revenue securing the airports system revenue bonds outstanding, which are rated one notch higher at A+/Negative.

The COPs rating is also based on the application of our "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" criteria, published Nov. 20, 2019. The airports system includes the lease payments in its annual budget, which is subject to appropriation by the state legislature, but this annual appropriation by the state legislature is the same process as the airports system's overall budget, which includes revenue bond debt service. Appropriation and payment of debt service is not contingent on verification of energy savings or receipt of any energy savings shortfall payments, and the project has strong, unanimous support and approval through a concurrence letter from the signatory airlines, which have agreed to include lease payments in their rates and charges. Debt service reserves (DSRs) provide additional liquidity for bondholders. The DSR for the senior-lien GARBs totals approximately $102.5 million, all of which is cash-funded. With the severe decline in passenger traffic attributable to the COVID-19 pandemic, management anticipates no draws from the DSRs to make required debt service payments at this time.

Proceeds of the sale of the series 2020A-D bonds will be used to refund portions of outstanding senior-lien bonds for interest savings, fund portions of the airport's ongoing capital improvement program (CIP), and make a deposit to the DSR. The purpose of the refunding transaction is for interest savings but also to reduce debt service in 2021 and 2022 and slightly push out the maturity schedule. We view the proposed restructuring to mitigate the near-tem financial impact of the COVID-19 pandemic on the system as credit neutral and the magnitude of the debt restructuring as moderate. We also considered HAS' historically high, somewhat variable traffic levels, its importance to the state and its economy, and willingness to maintain financial margins and financial projections. However, more generally, debt restructurings that materially increase debt service, debt levels, or final maturity could be a credit risk, particularly if they require the issuer to generate significant revenue growth to meet higher requirements.

As of Sept. 1, 2020, the airport system has approximately $1.3 billion in debt outstanding, consisting of $1.25 billion of senior-lien GARBs, $133.9 million of COPs outstanding, and $424.3 million of customer facility charge (CFC) revenue bonds. The CFC bonds are a separate credit.

Credit overview

The downgrade and negative outlook reflect our expectation that activity levels at the airport system will be materially depressed or unpredictable, or demonstrate anemic growth due to the COVID-19 pandemic and associated effects that are out of management's control. In our view, the severe drop in demand has diminished HAS' overall credit quality

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and will likely pressure financial metrics relative to historical levels in the next several years. We view this precipitous decline not as a temporary disruption with a relative rapid recovery, but as a backdrop for what we believe will be a period of sluggish air travel demand that could extend beyond our rating outlook horizon.

HAS entered the pandemic operationally and financially strong, with combined total enplanements near an all-time peak of 18.7 million, strong debt service coverage (DSC) levels, and very strong overall liquidity levels. However, combined enplanement levels were down 23% in fiscal 2020 (June 30 year-end) compared with fiscal 2019 and down approximately 85% for the month of July year over year. Consequently, we believe a lot of uncertainty exists regarding the trajectory of a recovery in aviation activity, complicating financial planning and increasing operational challenges. For additional information, see "This Time Is Different: An Anemic And Uncertain Passenger Recovery Will Challenge U.S. Airports' Credit Quality, " published Aug. 7, 2020, and "Activity Estimates For U.S. Transportation Infrastructure Show Public Transit And Airports Most Vulnerable To Near-Term Rating Pressure," published June 4, 2020.

The long-term rating reflects the airport's very strong enterprise risk profile and strong financial risk profile. Our forward-looking view resulted from a weakening of HAS' market position assessment, which in turn lowered our enterprise risk profile assessment to very strong from extremely strong. Under our criteria, market position is a primary credit factor that incorporates activity level trends, passenger volatility, rate-setting flexibility, and additional considerations outside the operator's control, including health scares. Within our overall enterprise risk profile, the market position assessment is the highest weighted factor (60%), followed by industry risk (20%), economic fundamentals (10%), and management and governance (10%). Within our overall financial risk profile, we consider such factors as financial performance (55%), debt and liabilities capacity (35%), and liquidity and financial flexibility (10%). For additional information regarding our criteria, see "U.S. And Canadian Not-For-Profit Transportation Infrastructure Enterprises: Methodologies And Assumptions," published March 12, 2018.

Our revised market position assessment for HAS results in a lower, but still very strong, enterprise risk profile. This reflects our view of the system's historically high volume of activity, importance to the state, and status as a virtual monopoly. Despite the system's important role, it and the state it serves remain exposed to cyclicality associated with the discretionary travel related to the tourism industry. The system has historically experienced larger passenger volume swings because of U.S. and international economic fluctuations; security, weather, and geological events such as the March 2011 earthquake and tsunami in Japan; previous health concerns (e.g., H1N1 and SARS); and airline service-level decisions.

Our overall financial risk profile is unchanged at strong, as we continue to evaluate management's strategy as well as the shape of the traffic recovery along with the expected impact of the passenger decrease on financial metrics. Our financial risk profile incorporates the system's historically strong financial performance, with DSC in 2019 (S&P Global Ratings-calculated) at or above 1.25x for fiscal years 2017-2019, debt-to-net revenues at 11x tempered by a large CIP that requires additional debt, and strong liquidity and financial flexibility (with days' cash on hand no lower than 550 and an available liquidity-to-debt ratio at no lower than approximately 32% for fiscal years 2017-2019).

We anticipate financial performance (DSC) in fiscal years 2020 and 2021, however, will be lower than in recent years. Existing liquidity in concert with various mitigation measures taken thus far to reduce outlays, and the $133 million in Coronavirus Aid, Recovery, and Economic Security (CARES) Act funding will allow the airport to weather the

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near-term activity decline. Management used $50 million of CARES Act money in fiscal 2020 to offset GARB debt service and expects to use the remaining portion of approximately $83 million in CARES Act money in fiscal 2021 to maintain DSC on the GARBs, reduce airline rates and charges, and preserve existing liquidity. HAS estimates enplanements for the fiscal year ended June 30, 2020, were approximately 24% below those reported in fiscal 2019. The budget for fiscal 2021 assumes 9.9 million enplanements, which is a 53% drop from fiscal 2019 levels. Management elected to defer landing fees and terminal rentals from April 2020 through Oct. 31, 2020 to be repaid in six equal monthly payments commencing with the first payment in January 2021. Although the estimated revenue effect appears to be manageable, projected effects on key financial metrics, in our view, are still subject to considerable uncertainty. We could weaken the financial risk profile if enplanements remain depressed for an extended period, further pressuring financial metrics including DSC (S&P Global Ratings-calculated) and debt-to-net revenue, especially if the airport issues significant debt and materially draws down its cash reserves to fund CIP projects, while enplanement trends remain materially depressed or unpredictable.

HAS management team's baseline forecast included in the recently completed airport consultant's report assumes a recovery to 2019 enplanement levels in 2026, which lags S&P Global Ratings' April activity estimates of 2024. We consider this management baseline forecast reasonable, including the assumption that the system's demand may take longer to recover given the uncertainties associated with long-distance leisure travel from the U.S. mainland and Japan, which historically accounted for a combined approximately 80% of visitor arrivals in 2019. The forecast assumes an effective COVID-19 vaccine becomes widely available and in use over the forecast period, with enplanements reaching 17.0 million by 2023 and 19.6 million by 2026.

Key credit strengths, in our opinion, include HAS':

- Favorable service area economic fundamentals, which will support robust air travel demand due to good economic activity as measured by GDP per capita, a large population base, above-average expected population growth, and ample employment opportunities despite the spike in unemployment because of COVID-19;
- Very strong management and governance, as evidenced by management's ability to adjust revenue, expenses, and capital spending to protect sound financial operations and planning for required capital spending to maintain assets and plan for growth; and
- Very strong liquidity position in recent years, averaging nearly $500 million, or above 650 days of operating costs.

Partially offsetting these strengths, in our view, are HAS':

- Exposure to potentially prolonged weak or unpredictable enplanement levels as a result of the ongoing COVID-19 pandemic, and lingering ancillary effects (such as the pandemic-induced recession, shifting travel restrictions, stay-at-home and social distancing restrictions, or behavioral changes with respect to air travel, particularly business travel), which complicates budgeting and planning;
- Hampered cash-flow-generation ability, particularly derived from activity-based concession revenue sources and a weakened rate-setting environment; and
- Moderately high airline concentration, with financially stressed Hawaiian Airlines (CCC+/Negative/--), the largest carrier within the system, accounting for approximately 50% of fiscal 2019 total enplaned passengers.

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Environmental, social, and governance (ESG) factors

Our rating action reflects health and safety risks posed by the COVID-19 pandemic and its impact on passenger activity due to mobility restrictions and behavioral changes related to travel, which we view as a social factor in our ESG factors, resulting in significant operating and financial pressures for HAS. We analyzed the airport's risks related to environmental and governance factors, and consider them to be in line with our view of the standard for the airport sector. While we acknowledge that Hawaii's location also exposes it to considerable environment-related risks, which could dampen its tourism-based economy in the short term, the state has generally displayed resilience over the longer term as demand for tourism has remained strong despite periodic challenges. We will continue to evaluate these risks as the situation evolves.

Negative Outlook

Downside scenario

We could lower the ratings if we come to believe that HAS' enplanements will remain materially depressed for longer than we currently expect, negatively affecting financial metrics for an extended period.

Return to stable scenario

We could revise the outlook to stable in the next two years with improved clarity on the trajectory of HAS' enplanement recovery and stabilization of activity levels. When making this assessment, we will evaluate whether the airport's ability to maintain financial metrics is achievable, sustainable, and consistent with the ratings.

Credit Opinion

S&P Global Economics acknowledges a high degree of uncertainty about the evolution of the pandemic and its effect on the economy and air travel. The consensus among health experts is that the pandemic may now be at, or near, its peak in some regions but will remain a threat until a vaccine or effective treatment is widely available, which may not occur until the second half of 2021. We are using this assumption in assessing the economic and credit implications associated with the pandemic. Our current economic forecasts anticipate a slower recovery beginning in third-quarter 2020, ending at a negative 5.0% real GDP growth rate in 2020 and rebounding to 5.2% growth in 2021--a full percentage point weaker than our previous 2021 estimate of 6.2%. With this summer's national virus transmission rates rising to new peaks, uncertainty is elevated again. Several states had shut down parts of their economies and instituted new quarantine restrictions, which could possibly erode the bounceback in third-quarter 2020 real GDP growth of 22.2% (annualized). The recovery remains fragile--in particular, because of uncertainty about the timing of an effective vaccine being readily available, fears of another wave of COVID-19, and the reluctance of surviving businesses to quickly rehire workers. Our economic forecasts and macro credit implications associated with the pandemic assume a vaccine or effective treatment is widely available in the second half of 2021. (See "U.S. Economic Update: A Recovery At Risk As COVID-19 Surges," published July 22, 2020, and "Economic Research: U.S. Real-Time Economic Data Continues To Paint A Mixed Picture," published Aug. 14, 2020.)

HAS' total passengers for the first eight months of fiscal year 2020 (June 30 year-end) were 7.6% ahead of 2019. However, as the COVID-19 pandemic became more widespread with accelerating new cases, business shutdowns, and

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travel restrictions, total passengers plummeted in March 2020 to 60% below March 2019 levels, and further in April 2020 to 96% below April 2019 levels. Total passengers for May, June, and July were approximately 95%, 90%, and 85% below those in the same months in 2019, respectively, with total enplanements for fiscal year-end (June 30, 2020) down an estimated 23%, which is close to S&P Global Ratings' baseline activity estimates. The fiscal 2021 budget for HAS is based on a passenger-recovery scenario of 53% of fiscal 2019 levels, which falls between our baseline and downside activity estimates.

HAS' management team has taken a variety of actions to mitigate the collapse of passenger activity across the system that has negatively affected volume-based revenues, including those derived from concession as well as aeronautical revenues such as landing and international arrival fees. These actions include a pause in the timing, scope, and funding of its $1.1 billion 2022-2026 CIP, which includes projects that are currently in the design stages and are not expected to start construction until January 2022 and beyond, as well as a 5% reduction in operating expenses implemented at the end of fiscal 2020 and carried forward into fiscal 2021. Nonairline revenues and particularly duty-free concessions constituted approximately 40% and 9%, respectively, of total operating revenue in 2019. Management waived minimum annual guarantees for all concessionaires through Oct. 31, 2020, with fees and charges during April-October 2020 to be paid in six equal monthly payments commencing with the first payment in January 2021. Given the high degree of revenue exposure derived from concessions, a weaker recovery in concessions spending leading to reduced nonairline revenues could be a source of credit pressure in the near term. Management has also been using CARES Act money strategically to encourage a return of flights and operations by applying this federal aid to reduce airline costs at the airport and offset debt service. If the pandemic extends longer than expected, we anticipate management will consider additional actions. In addition, while Hawaii implemented a 14-day quarantine period for overseas travelers and all persons traveling from within the state, the state will be implementing a pre-travel testing program on Oct. 15, which will allow overseas visitors to avoid quarantine if they can provide documentation of a negative COVID-19 test conducted within three days of departure to Hawaii. While the effect of such policy changes is unclear, it is demonstrative of the state and airport management's willingness to be proactive in seeking solutions to mitigate the pandemic.

Currently, HAS expects to maintain its ongoing CIP spending totaling $1.6 billion, of which $659 million has been spent as of June 30, 2020. Anticipated funding sources include:

- Proceeds from previous GARB issues that are funding projects near completion that will be included in the airline rate base in fiscal year 2021,
- HAS' restricted cash funds and PFC pay-go fund balances that have been allocated or earmarked for airport projects and soft costs that are not part of the airline rate base, and
- A portion of the series 2020 bonds.

Several major capital projects are planned or underway that are aimed at modernizing the facilities, increasing system capacity, enhancing revenue, and improving passengers' overall experience. Key projects within the airport system's ongoing CIP include:

- Mauka Concourse Program at HNL ($547 million total project cost; of which $354 has been spent as of June 30, 2020),

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- Terminal improvements at HNL ($581 million total project cost; of which $155 has been spent), and
- Kona terminal modernization program ($90 million total project cost; of which $84 has been spent).

Related Research

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of September 25, 2020)		
Hawaii Arpt Sys airport system rev bnds ser 2015A due 07/01/2045		
Long Term Rating	A+/Negative	Downgraded, Removed from CreditWatch
Hawaii Arpt Sys AIRPORTS		
Long Term Rating	A/Negative	Downgraded, Removed from CreditWatch
Hawaii		
Hawaii Arpt Sys, Hawaii		
Hawaii (Hawaii Airport System) (AGM) (SEC MKT)		
Unenhanced Rating	A+(SPUR)/Negative	Downgraded, Removed from CreditWatch
Many issues are enhanced by bond insurance.		

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