MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns A1 to Hawaii Airports System Revenue Bonds Series 2022A and B

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New York, January 07, 2022 -- Moody's Investors Service has assigned A1 to Hawaii (State of) Airport Enterprise's approximately $217.9 million Airports System Revenue Bonds, Series 2022A (AMT) and $54.3 million Airports System Revenue Bonds, Refunding Series 2022B (AMT). Hawaii Airport Enterprise also has outstanding $1.53 billion of parity Airports System Revenue Bonds rated A1 and $123 million of Lease Revenue Certificates of Participation rated A2. The outlook is stable.

RATINGS RATIONALE

The A1 rating reflects the system's strong financial flexibility to manage COVID-related pressures as passenger levels trend toward full recovery over the next 2-4 years.

This financial flexibility is based on a combination of 1) strong liquidity, with over 600 days cash on hand and $140 million of unused federal COVID relief grants (equivalent to 160 days of O&M expenses) in FY 2021; 2) a supportive cost recovery framework, provided by a hybrid airline agreement with extraordinary coverage protection; 3) a uniquely strong competitive position, as the monopoly provider of air travel for a multi-island economy that is a major tourist destination; and 4) relatively modest airline costs, with both CPE and leverage below large hub peers pre-COVID and CPE expected to stabilize near $16 by the end of the forecast period (FY 2027) notwithstanding additional debt issuance for capital projects.

These factors mitigate the risk of a more gradual traffic recovery relative to the sector. The system's overall activity level partially reflects the significant impact to international travel, which accounted for 17% of enplanements in FY 2019, but also reflects the constraints on domestic travel as a result of stringent health measures/travel restrictions employed by Hawaii, which were especially pronounced in the first 6-9 months of the pandemic. As a result of this more extended recovery pattern, enplanements are not expected to reach 95% of 2019 levels until mid-2024, compared to our expectation that the sector in aggregate will reach this in mid-2023. However, we believe demand for leisure travel to the island remains robust and will reflect in a strengthened recovery as quarantine restrictions are relaxed. This is evidenced by the near full recovery of domestic overseas passenger levels in the 12 months following the state's October 15, 2020 relaxation of the initial quarantine. Despite the continued headwind from depressed international travel, overall traffic is trending favorably toward pre-COVID levels and total enplanements have recovered to range between 65%-80% of 2019 levels for the first half of FY 2022.

The rating continues to reflect the expectation of additional leverage to fund portions of the remaining $1.5 billion capital improvement plan, the scope of which has been refined based on a reprioritization of projects by the airport. The majority of spending is for airfield or terminal projects, and these costs can be recovered from airline revenue even if the airport were to set rates by ordinance. Though these projects will increase airline costs, the cost structure will be manageable given the airport's monopoly position for air travel and the demonstrable demand for O&D travel to Hawaii in normal operating conditions.

RATING OUTLOOK

The stable outlook reflects Moody's expectation that leisure travel demand will continue a strong recovery to the island as quarantine requirements are relaxed and virus containment progresses. The outlook reflects our view that the airport's strong cost recovery framework, liquidity and manageable cost structure will mitigate a slower than expected recovery.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Return to near normal operating conditions and passenger levels at the airport

- Further progress on the capital plan financing that provides for expected net revenue debt service coverage ratios above 1.3x on revenue bonds and total coverage of 1.15x while maintaining strong liquidity

- Demonstrated willingness to exercise rate setting to sustain key financial metrics amid enplanement volatility or economic pressure

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Significant reduction in enplanement levels and slower than anticipated recovery following the coronavirus outbreak

- Failure to roll the current favorable use and lease agreement, or a new agreement that increases rate recovery risks

- Additional debt-funded capital improvements that raise debt per O&D enplanement above $200

- Reduced liquidity below 300 days cash on hand

LEGAL SECURITY

Senior lien bonds are secured by a pledge on net revenues of the airport system and aviation fuel tax revenues. The rate covenant is 125% senior debt service and 100% total debt service with unlimited rolling coverage. The senior lien bonds have an additional bonds test (ABT) that requires revenues plus rolling coverage equal 125% of maximum annual debt service (MADS) or that the rate covenant has been met and will be met, including additional bonds, to the later of 5 years after issuance or 3 years beyond the use of capitalized interest. The bonds also have a debt service reserve that is sized at the lesser of the three-prong test and is fully cash funded.

The COPs are secured by a proportionate interest in the rights of the lease agreement, including the lease agreement payments made by the airport system as a junior obligation to the lessor, Johnson Controls, Inc. JCI has assigned its rights as lessor, including the right to receive rent payments, to the trustee for payment of debt service of the COPS. The airport system's obligation to make payments under the lease agreement from year to year is subject to annual appropriation by the State of Hawaii under a separate line item for capital leases in the department's budget. The payments are treated as "other lawful purposes" of the airport's system.

If the state fails to appropriate the lease payment, the contract can be terminated at the end of the fiscal year for which money has been appropriated and the holders of the certificates would gain recourse to the equipment. Moody's believes this equipment would have little to no value outside of its use with the airport system, but its removal would be significantly detrimental to the operations of the airport system.

USE OF PROCEEDS

The 2022A bonds will provide an estimated $228.5 million for capital projects and the 2022B bonds will provide $57 million to refund existing bonds. Proceeds will also provide approximately two years of capitalized interest (for the 2022A bonds) and required deposits to the common debt service reserve fund.

PROFILE

The Hawaii Department of Transportation (DOT) operates and maintains 15 airports at various locations within the state and served 18.7 million enplaned passengers in FY 2019, or pre-COVID. The system served 6.1 million enplaned passengers in FY 2021. The DOT is one of 18 principal executive departments of the state and is empowered to establish, maintain and operate the transportation facilities of the state, including highways, airports, harbors and other transportation facilities. The DOT is headed by the director, who is appointed by the governor and confirmed by the state senate. The governor also appoints a deputy director of transportation of Administration. The director and deputy directors of transportation of Administration serve four-year terms conterminous with the governor's term. The director also appoints three other deputy directors of transportation of Airports, Highways and Harbors. Through the Airports Division all state airports are operated as a single integrated system for management and financial purposes. Virtually all non-military passenger traffic throughout Hawaii passes through the airport system, which includes five primary airports and ten secondary airports. The primary airports are Honolulu (on the Island of Oahu, HNL), Kahului (on the Island of Maui, OGG), Hilo International and Kona International (both on the Island of Hawaii), and Lihue (on the Island of Kauai).

METHODOLOGY

The principal methodology used in these ratings was Publicly Managed Airports and Related Issuers published in March 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1140469. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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