FitchRatings

RATING ACTION COMMENTARY

Fitch Upgrades Philadelphia International Airport's $1.37B Airport Rev and GARBs to 'A+'

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Fitch Ratings - New York - 15 Aug 2024: Fitch Ratings has upgraded the rating on Philadelphia International Airport's (PHL) approximately $1.37 billion of senior lien general airport revenue and revenue refunding bonds (GARBs) to 'A+' from 'A'. The Rating Outlook is Stable.

RATING RATIONALE

The upgrade reflects PHL's continued positive progression to full traffic recovery and improved financial performance, benefitting from the recent airline use and lease agreement (AUA). This agreement will enhance airport liquidity and preserve a leverage profile consistent with the 'A+' rating level. Fitch assessed the potential impact of all the prospective future debt to support the $1.8 billion capital program, which has strong signatory airline support and may include over $1 billion in future borrowings. Under the Fitch rating case, leverage only rises nominally to about 7x from under 5x, which well within the 9x rating sensitivity for a positive rating action.

The rating reflects PHL's role as the main air service provider to a large and stable service area that generates a solid base of origination and destination (O&D) traffic. This is offset by a high degree of concentration in American Airlines (B+/Stable) and some connecting traffic exposure. The rating further reflects PHL's recently adopted strong residual airline agreement, which provides for full recovery of operating expenses and debt service costs. However, it also results in narrow coverage and adequate liquidity levels.

KEY RATING DRIVERS

Revenue Risk - Volume - Stronger

Large Market with Connecting Exposure: PHL's service area is the large and stable Philadelphia MSA, which has typically provided approximately 13 million-14 million O&D enplanements annually. Though the airport has connecting traffic exposure of around 26% of total enplanements. PHL is also a leading connecting hub for American Airlines, which lends to sizable carrier concentration of around 63%. Service reduction risk is partially mitigated by American's long-standing presence at the airport. Airline costs are competitive for a large-hub airport at below $13 per enplanement although these costs would rise as the capex plan moves forward.

Revenue Risk - Price - Stronger

Strong Cost Recovery Rate Setting: The airport's AUA was put into effect last year and runs through 2026. The agreement features two one-year renewal options. The new agreement provides pre-approval for new capital funding in support of operations at PHL, allows for the establishment of more robust cash reserves, and provides for the set aside of additional reserve funding. Fitch views this positively, given the airport's sizable capital program.

PHL's cost per enplaned passenger (CPE) level has typically been maintained in the $12-$16 range and is expected to rise over $20 in Fitch's conservative rating case. The rising costs over the next few years are mitigated by the airport's franchise strength and airline support for the capital program.

Infrastructure Dev. & Renewal - Midrange

Expanded Capex Plan with Borrowings: The airport's most recent multi-year capital development program (CDP) is approximately $1.8 billion and focuses primarily on state of good repair projects on the airfield, terminal, taxiways, security and technology. PHL plans to fund the majority of the CDP with proceeds from existing bonds and expected issuance of additional long-term debt in fiscal 2025 through 2032. The remainder will be funded from PFC's and grants as well as a small amount of operating cash. The CDP projects and funding sources are subject to change based on the operational needs of the airport, and any deferred projects may commence after the projection period.

Debt Structure - 1 - Stronger

Conservative Debt Structural Terms. PHL benefits from all senior, fully amortizing, fixed-rate and synthetically fixed-rate debt in addition to a $350 million commercial paper (CP) program. Fitch views the structural features as adequate and protective to bondholders, with fully cash-funded debt reserves at maximum annual debt service (MADS) balanced with permissive rate covenants. Fitch expects debt service obligations to be elevated over historical levels over the intermediate term and increase with additional borrowings for the CPE.

Financial Profile

The airport has historically managed to narrow cashflow only debt service coverage levels (excluding fund balances), an to still improve its liquidity position to the current 400-500 days cash range in recent years. The new airline agreement positions PHL for improved DSCR metrics while maintaining residual rate setting. However, PHL has some limits to its ability to fund its current capital plan without resulting in increases to the airline rate base. Fitch's conservative rating case expects leverage to increase from the current levels of approximately 4.8x to around 7.3x before 2030 when considering all potential debt borrowings for the capex plan.

PEER GROUP

Peer airports for PHL include Miami (A+/Stable) and Charlotte (AA-/Stable), both of which serve as hubs for American Airlines and exhibit carrier concentration and connecting traffic exposure. Miami applies a full residual cost recovery agreement with its signatory airlines while Charlotte applies a hybrid methodology. Charlotte's higher rating reflects significantly lower CPE, reaching around $9 and leverage peaking at 6.7x. Charlotte also has stronger liquidity and debt service coverage despite higher exposure to American Airlines' hubbing operations. Miami has a stronger traffic base as a leading international gateway hub despite slightly higher leverage, reaching 9x and CPE, peaking around $25.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

--A material reduction in, or elimination of, American's hubbing activity, which reduces financial flexibility;
--Borrowings for the new capital plan that result in leverage metrics rising to and remaining at or above 9x on a sustained basis.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

--Unlikely in the near term given the expected borrowings to support the capital program costs;

--Longer term, continued favorable trends in operational and financial performance resulting in leverage below 6x, inclusive of additional borrowings for the capital plan.

SECURITY

The bonds are secured by the net revenues generated through the operations of the airport. In addition, the airport may pledge certain passenger facility charge (PFC) revenues for eligible projects.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Philadelphia International Airport (PA)				
Philadelphia (PA) /Airport Revenues - First Lien/1 LT	LT	A+ Rating Outlook Stable	Upgrade	A Rating Outlook Positive

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Seth Lehman
Senior Director
Primary Rating Analyst
+1 212 908 0755
seth.lehman@fitchratings.com
Fitch Ratings, Inc.
Hearst Tower 300 W. 57th Street New York, NY 10019

Jim Code
Associate Director
Secondary Rating Analyst
+1 312 368 3194
jim.code@fitchratings.com

Anne Tricerri
Senior Director
Committee Chairperson
+1 646 582 4676
anne.tricerri@fitchratings.com

MEDIA CONTACTS

Sandro Scenga
New York
+1 212 908 0278
sandro.scenga@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

Infrastructure & Project Finance Rating Criteria (pub. 17 May 2023) (including rating assumption sensitivity)

Transportation Infrastructure Rating Criteria (pub. 18 Dec 2023) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

GIG AST Model, v1.4.2 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Philadelphia (PA)	EU Endorsed, UK Endorsed

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4 notches and worst-case downgrades of 8 notches at the 99th percentile. For more details on sector-specific best- and worst-case scenario credit ratings, please see Best- and Worst-Case Measures under the Rating Performance page on Fitch's website.

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