FITCH AFFIRMS MAINE TURNPIKE AUTHORITY REV BONDS AT 'AA-'; OUTLOOK STABLE

Fitch Ratings-New York-28 April 2017: Fitch Ratings has affirmed the 'AA-' rating on approximately $353.3 million in the Maine Turnpike Authority's (the authority) outstanding revenue bonds and the 'A-' rating on the authority's approximately $32.2 million in outstanding special obligation bonds.

KEY RATING DRIVERS

The 'AA-' and 'A-' ratings reflect the authority's mature and stable traffic base, which has a relatively high exposure to discretionary and commercial traffic. The ratings are further supported by the authority's strong rate making ability, evidenced by a history of above-inflationary toll rate increases. An additional $510 million in future debt expected to be raised over the next 20 years is not expected to be detrimental to the authority's financial profile given robust financial margins coupled with planned future toll increases to help fund future capital plan requirements.

The three-notch differential between the senior and special obligation liens reflects the special obligation lien's weaker security package and deeply subordinated status, with payment after deposits into the reserve maintenance account. The differential also considers the wide differential in coverage between the two liens, evidenced by average 10-year rating case coverages of 2.8x senior and 1.6x total.

Revenue Risk - Volume: Midrange
Mature Traffic Base, Leisure Exposure: The Maine Turnpike is a mature asset and serves as the primary travel corridor through the southern portion of Maine. It provides access to the coastal areas resulting in relatively high exposure to discretionary traffic, while serving as an essential artery for commercial vehicles. Traffic has historically remained stable even through the most recent economic downturn, demonstrating low elasticity to toll increases with the most recent toll increase implemented in November 2012. In Fitch's view, the current toll rate of six cents per mile for passenger vehicles is low, supporting the authority's strong economic rate-making flexibility.

Revenue Risk - Price: Stronger
Demonstrated Rate-Making Ability: The authority benefits from unlimited legal authority to change toll rates as needed. Historically, management has demonstrated a willingness to increase revenues through periodic, above-inflationary toll rate increases to ensure the funding of capital needs and maintenance of financial flexibility. Toll rates are expected to be raised in the future as necessary, though the turnpike's current robust financial profile will likely not require such an increase until 2031.

Infrastructure Development/Renewal: Stronger
Manageable Capital Program: The authority's approximately $1.8 billion 25-year capital program is manageable, mostly addressing maintenance needs and marginal improvements as the turnpike is not currently facing material capacity constraints. Management plans to potentially issue debt in small increments every three to five years to assist with the funding of its capital plan; Fitch does not expect these possible issuances to be onerous given the strength of the authority's financial profile and the vast majority of capital needs being cash-funded.

Debt Structure: Senior - Stronger, Special Obligation - Midrange

Sound Debt Structure: The authority's debt is all fixed-rate and fully amortizing with a declining debt service profile. The senior bonds are further supported by a cash debt service reserve fund, which is currently funded at half of maximum annual debt service given that senior DSCR has remained above 2.0x. There is no dedicated debt service reserve supporting the special obligation bonds. On the special obligation lien, deep structural subordination and a weak sum sufficient covenant and additional bonds test (ABT) provide for weaker bondholder protection.

Financial Metrics:
Solid Coverage, Low Leverage: The authority's financial position is healthy, featuring high debt service coverage ratios (DSCR) and modest debt levels, which are expected to provide the authority with financial flexibility through periods of economic downturn or unforeseen cost increases. Fiscal 2016 (year ended Dec 31.) coverage was 3.06x senior and 1.77x total. Current leverage levels on a net debt to cash flow available for debt service (CFADS) basis are appropriate for each lien's respective rating category, at 3.22x senior and 6.49x total. Coverage levels are expected to remain at approximately 2.8x senior and 1.6x total, while leverage is expected to decline to 3.4x senior and 6.0x total in Fitch's rating case when incorporating potential future debt issuances.

Peers: Maine Turnpike's closest peer is New Hampshire Turnpike System ('A+'/Outlook Stable), with each operating strong turnpike systems comprising both urban and rural segments. Maine Turnpike features higher DSCRs than New Hampshire, reflective of its higher rating level.

RATING SENSITIVITIES
Negative - Underperformance of traffic and revenue or poor management of operating and capital expenses, which results in sustained senior and total coverage materially below 2.0x and 1.4x, respectively, without plans to remedy with a near-term toll increase.

Positive - While the near-term financial profile is robust, given peers at 'AA' with stronger volume risk profiles, positive rating movement is unlikely in the near term.

CREDIT UPDATE

Performance Update
Fiscal year 2016 was an all-time traffic and revenue record for the authority, driving net toll revenue growth of 4.4% to well surpass Fitch's base case estimates of 3%. Traffic growth was a healthy 5.2%, slightly higher than that of revenue growth, primarily reflecting the authority's volume-based discounts.

2016 traffic and revenue growth was attributed to favorable economic conditions and a milder winter, which significantly boosted traffic growth during January and February. Additionally, the turnpike experienced some positive traffic growth due to traffic diversion onto the Maine Turnpike from I-295, as the turnpike serves as a less congested alternative for northbound passengers travelling through the Portland area.

Traffic and revenue growth for the two months of 2017 has been slightly more modest than that of the recent past, at 0.7% and 1.2%, respectively, with slightly higher revenue growth reflecting a greater percentage of higher toll-paying commercial vehicles. Lower growth during the first two months of the year primarily reflects significantly harsher winter weather during the month of February. While Fitch expects harsher weather could adversely affect traffic and revenue performance during the winter and early spring months of 2017, modest growth through the remainder of the year is anticipated. As such, Fitch has assumed management's net revenue growth projection of 0%-0.5% over the next two years for conservatism, which is considered appropriate given that net toll revenue growth has recently trended about 1% below traffic growth. Lower expected traffic growth over the next two years is not a material credit concern given the resiliency of the turnpike's financial profile.

Expenses were slightly higher than expected in 2016, at 4.6% in comparison to Fitch's expectation of 3%, primarily as a result of signing bonuses being given to union employees upon signature of new three-year collective bargaining agreements' (CBA) in December 2016. Fitch does not expect high operating expense growth to continue, but larger than usual operating expense increases are possible every three years as CBA's are renewed. Overall, outperformance in revenue growth more than offset increases in operating expenses, leading to stronger DSCRs and lower leverage than previously expected. Specifically, senior and total DSCR were approximately 3.1x and 1.8x in comparison to expectations of 3.0x and 1.7x, respectively. Senior and total leverage were 3.2x and 5.5x in comparison to expectations of 3.3x and 5.7x, respectively.

The authority's updated $1.8 billion 25-year capital plan has remained essentially unchanged. Fitch regards the capital program as manageable, focusing mostly on maintenance and marginal improvements such as rehabilitation and repaving of roads and bridges. The authority plans to periodically issue debt to assist with the funding of its capital plan and has increased its planned 2035 issuance amount to $125 million from expectations of $25 million during Fitch's last review. Fitch does not consider the potential additional debt a concern, as rating case senior DSCRs are expected to remain above 2x and leverage is expected to remain below 4x during periods following the issuance, consistent with the current rating. Fitch also views the mostly cash-funded nature of the capital plan as a credit positive, with about 87% of capital needs expected to be funded via operating cash flow or other internal liquidity.

Fitch Cases

For this review, Fitch has adopted management's forecast as its base case, as the revenue and expense assumptions within are considered slightly conservative yet appropriate given recent performance which has influenced future expectations. Both Fitch's base and rating case include the aforementioned debt issuances occurring every three to five years and a toll increase of approximately 25% in 2031 once the turnpike begins to reach its pinch point. The toll increase results in minimal demand elasticity, which Fitch considers suitable given the authority's low toll rates and low historical elasticity to past toll increases.

Fitch's base case assumes modest toll revenue growth of 0%-1% growth from 2017-2019, which increases to 1.25% through the end of the projection period in 2041. Fitch's rating case includes 0.5% growth in toll revenues with a 3% shock in 2020, slightly lower than the turnpike's experienced shock in traffic during the Great Recession. Operating expense growth is assumed at 3.76% in the base case and 4.27% in the rating case.

Fitch's base yields 10-year average DSCRs of 3.0x senior and 1.8x total, while the rating case's 10-year average DSCRs are slightly lower at 2.8x senior and 1.6x total. By year five, leverage is 3.2x senior and 5.4x in the base case, which increases to 3.4x senior and 6.0x total in the rating case. Additionally, Fitch's breakeven analysis indicates the authority would only need 0.9% growth to service senior obligations and 1.2% growth to service all obligations, reflecting the authority's modest dependence on toll revenue growth to meet obligations.

In Fitch's view, senior lien metrics are considered consistent with the 'AA-' rating, including extra financial cushion to offset the turnpike's additional volume risk which other peers with the 'AA' ratings do not possess. Additionally, metrics on a total basis appropriately warrant an 'A-'rating for the special obligation bonds, reflecting the substantial differential in rating case coverage levels as well as additional debt structure risk.

Security:

The senior lien bonds are secured by a pledge of all turnpike revenues, including all monies, funds and other income received by the authority from the operation of the turnpike.

The special obligation bonds are secured by a pledge of all special obligation revenues, specifically all monies, funds and other income transferred to the trustee after all obligations for the more senior liens and the deposit into the reserve maintenance fund has been satisfied.

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Applicable Criteria
Rating Criteria for Infrastructure and Project Finance (pub. 08 Jul 2016)
https://www.fitchratings.com/site/re/882594
Rating Criteria for Toll Roads, Bridges and Tunnels (pub. 11 Aug 2016)
https://www.fitchratings.com/site/re/886038