FITCH RATES METROPOLITAN WASHINGTON AIRPORTS AUTHORITY REVS 'AA-'; OUTLOOK STABLE

Fitch Ratings-New York-18 May 2018: Fitch Ratings has assigned an 'AA-' rating to the Metropolitan Washington Airports Authority's (MWAA) approximately $612 million series 2018A airport system revenue and refunding bonds. Fitch has also affirmed the authority's approximately $4.5 billion outstanding airport revenues bonds at 'AA-'. The Rating Outlook is Stable.

KEY RATING DRIVERS

SUMMARY: The rating reflects MWAA's very strong credit attributes, including the resilience of its complementary dual-large hub airport system serving the strong and growing District of Columbia air trade service area; well-balanced system-wide carrier mix; recently completed capital program at Dulles International Airport (IAD), with a new, smaller program focused at Reagan National Airport (DCA) to be able to serve projected demands; and stable financial profile. The large debt burden and rising airline cost profile, particularly at IAD, remain concerns. However, MWAA's current airline use and lease agreement (AUL) partially mitigates this with enhanced revenue sharing between airports. Rating case leverage is projected to increase in the near term, but fall below 7x net debt/cash flow available for debt service (CFADS) by 2023.

STRONG MARKET POSITION - Revenue Risk (Volume): Stronger
MWAA's large traffic base, anchored by a strong underlying economic region and diverse, complementary domestic and international service offerings at IAD and DCA, reached a new peak of 23.3 million enplanements in 2017. Following the most recent recession, enplanement declines at IAD were offset by steady, solid growth at DCA. Positively, IAD has returned to growth mode and is forecast to grow faster than DCA through 2023. United Continental Holdings, Inc. (BB/Stable) is the lead carrier at IAD with a 63% carrier market share, while American Airlines Group, Inc. (BB-/Stable) handles approximately 50% of DCA. On a system wide basis, market share is more diverse, with United having the largest share at 35%. Nearly 80% of system traffic is O&D leading to greater stability and the airports system maintains a 64% regional market share.

FAVORABLE RATE SETTING APPROACH - Revenue Risk (Price): Stronger
MWAA's AUL runs through 2024 with a hybrid compensatory model, providing an overall favorable airport system cost recovery approach by bridging significant cost imbalances. Revised terms allow for tiered surplus revenue sharing from DCA to subsidize IAD's costs tied to substantial debt-financed capital investments. An increased level of hard coverage recovery, coupled with provisions such as extraordinary coverage protection and net revenue sharing with the carriers, is provided within the rate setting framework. Proactive management has allowed the authority to contain airline costs and continuously beat both budget and original airport consultant forecasts for CPE while maintaining stable to improving coverage levels.

MAJOR CAPITAL NEEDS ADDRESSED - Infrastructure Development/Renewal: Stronger
Both airports are modern facilities in good condition. The prior 15-year $5 billion capital construction program (CCP) focused on IAD whereas the new $1.9 billion 2015-2024 CCP is predominantly for DCA. It will be approximately 91% bond funded, however DCA should have the debt capacity. IAD is already benefitting by way of increased revenue generation from the former CCP and the new CCP should similarly enhance DCA's revenue generating ability.

LARGELY CONSERVATIVE CAPITAL STRUCTURE - Debt Structure: Stronger
MWAA's debt is fully amortizing with more than 82% fixed-rate obligations, 12% synthetically fixed-variable-rate obligations and only 5% unhedged variable-rate debt. Further, this exposure

is partially mitigated by the authority's large unrestricted cash position. Sound covenants and reserve requirements are similar to other rated airports. Management is proactive with refunding opportunities and another $1.6 billion of outstanding debt will be callable through 2024.

FINANCIAL PROFILE

Leverage in 2017 of 7.2x net debt/CFADS is consistent with the current rating; however, it is forecast to peak around 9.0x before returning to 7.0x or less by 2023. The largely stable historical debt service coverage ratio (DSCR) of 1.4x-1.5x has been improving of late, with a slightly higher expectation over the medium term given the current AUL and recent enplanement trends. Liquidity remains strong at 984 days cash.

PEER GROUP

Comparable large-hub, international gateway peers include Los Angeles International Airport (LAX; senior/sub AA/AA-/Stable) and San Francisco International Airport (SFO; A+/Stable). Both airports similarly have stronger volume and price assessments as well as high debt levels incurred for infrastructure spending. LAX benefits from a greater, more resilient enplanement base with less carrier concentration, lower leverage, and higher coverage accounting for its higher rating. SFO has stronger enplanement trends, but slightly higher leverage and a higher CPE. Further, its operational and financial profiles are tied to a single airport whereas MWAA benefits from a dual-airport system.

RATING SENSITIVITIES

Future Developments That May, Individually or Collectively, Lead to Negative Rating Action:

--Additional leverage sustained in excess of 8.0x net debt/CFADS for the new capital program that materially affects financial flexibility;
--Significant or unanticipated changes in the airport's current traffic base or shifts in commitments from leading carriers;
--The authority's inability to manage the airports system cost profile putting pressure on debt coverage metrics and charges to carriers.

Future Developments That May, Individually or Collectively, Lead to Positive Rating Action:

--Upward rating migration is unlikely in the near-to-medium term given the authority's leverage and cost profile; however, in the longer term, sustained leverage below 6.0x may support a rating upgrade.

TRANSACTION SUMMARY

MWAA is expected to issue approximately $612 million of series 2018A (AMT) airport system revenue and refunding bonds with approximately $389 million par to refund series 2008A and 2009C bonds for debt service (DS) savings and the remaining $223 new money to fund project costs, reserves and cost of issuance. The refunding bonds will be 21-year fixed rate, will not extend the final maturity of the refunded bonds, and are estimated to generate NPV DS savings of $35 million. The new money bonds will also be fixed rate, but with a 30-yr term. The bonds are expected to price the week of May 28, 2018.

Performance Update

The authority's two airport system experienced system-wide enplanement growth of 2.8% in 2017, building upon the 1.9% experienced in 2016, and resulting in a five-year CAGR of 2.1%. Enplanements now total 23.3 million, continuing to set a new peak level. Overall, enplanements have been fairly resilient supported by the economic strength of the airports' catchment area and the complementary nature of the dual-airport system structure.

Notably, stronger growth of 4.2% occurred at Dulles while National grew 1.5%, reflecting a slowdown from the previous growth that resulted from American's slot divestitures and increased service by LCCs at DCA. IAD's international service continues to expand (up 3.7% in 2017), however, United increased its domestic service (up 4.9%) leading to Dulles' domestic enplanements growing a strong 4.5% in contrast to many years of flat-to-negative domestic growth. Positive trends continue through the first two months of 2018, though are dampened by lower volumes in January 2018 due to weather-related flight cancellations and lower load factors as well as an uptick in 2017 from the inauguration and Women's March. February began the reversal with DCA enplanements holding flat and IAD growing a robust 7.1% due to new domestic service and increased capacity, with Frontier (252.4% increase) and SWA (23.7% increase) leading the way, and IAD's international enplanements (up 6%) due to increased service and capacity as well as higher load factors. Going forward, stronger growth is anticipated to continue at IAD than DCA.

The authority's current AUL took effect in 2015 and, coupled with its recent enplanement growth, generated a 2017 indenture-based DSCR of 1.77x, notably higher than the 1.45x in 2014 and above the budgeted 1.59x. Fitch's calculation of DSCR, which treats passenger facility charges (PFC) as revenue rather than debt service offsets, was 1.67x. Relative to the old agreement, the 2017 financial results benefit from increased hard coverage charged to the carriers as well as more favorable provisions for sharing of net remaining revenues (NRR).

In addition to improving coverage, the hybrid commercial compensatory agreement now allows MWAA to use DCA's NRR to subsidize IAD's sizeable cost base (resulting from its recent capital program) according to a tiered structure. The AUL taken together with a Commonwealth of Virginia grant resulted in a 2017 reported CPE of $17.00 at IAD, down significantly from $26.55 in 2014 and once again below forecast. The grant should again provide some reprieve to carriers in 2018 before CPE stabilizes around $22-$23 in Fitch's rating case, reasonable for an international gateway in a major market with a newly constructed facility.

CPE remained flat at DCA at $13.44 in 2017, a level in-line with forecast and largely consistent with the historical average (excluding 2014) and projected $13-$15 range through 2023. Still, should enplanements fall short of forecast or management be unable to contain expenses, CPE could rise to levels inconsistent with the current rating, especially at Dulles International.

In return for DCA's sharing of NRR, a new $1.2 billion capital program will be undertaken at the airport through 2024, matching the term of DCA's agreement. The first universal amendment to the AUL extends the term of IAD's agreement to be co-terminus with that of DCA in exchange for another $446 million of projects added to the CCP for Dulles such that it totals $652 million through 2024.

The authority's prior $5 billion 2001-2016 CCP focused primarily on IAD. Therefore, the current 2015-2024 $1.9 billion 10-year capital program is predominantly focused on development at DCA. Key projects include a new north concourse and securing National Hall behind the TSA screening point. A new parking garage is also still in the planning stages for the end of the CCP. Similar to the developments at IAD, several of the projects at DCA should be revenue generating in nature.

Fitch Cases

Fitch believes management's case assumptions are reasonable given past performance and Fitch's expectation for future performance taking into account a view of the local and national economies as well as future air service and adopted this case as its base case. MWAA's forecast reflects assumptions of a 1.5% traffic compound annual growth rate (CAGR) between 2017 and 2023 and management of expense growth at a 4.5% CAGR over the same period. DSCR averages 1.7x through 2023. If PFCs are treated as revenues instead of being used to offset annual debt service, coverage hovers around 1.6x through 2023. CPE ranges from $11-$14 for DCA and remains below $20 at IAD. Leverage peaks around 8.7x in 2019 as a result of new borrowings for the CCP; however, it evolves to a more moderate 6.9x by 2023.

Fitch developed a rating case scenario under which system-wide enplanements decline by 3.9% in 2019 followed by recovery of 1.5%-2.0% annual growth through 2023. Non-airline revenues were adjusted to reflect weaker performance in terms of enplanements such that the concession revenue CAGR for 2017-2023 was 1.6% (compared to 2.4% in the base case). Transfers from the general purpose fund were also assumed to be slightly lower (2.1% CAGR versus 2.8% in the base case). Operating expenses were conservatively still grown at 4.5% CAGR despite the lower enplanement volume. The results are an approximate 2 basis point drop in coverage on average, indicating slightly less financial flexibility, and CPE increases over the management case by approximately $0.88 at DCA and $3.45 at IAD by 2023. The modest decrease in DSCRs reflects the strength of the revenue framework in which airlines make higher payments to support MWAA's financial profile. Similar to the base case, leverage increases in the near-term to 9.0x before falling to below 7.0x by 2023. Additional leverage beyond that already anticipated or operational or financial conditions that prevent this downward trend in leverage could be a cause for rating concern to the extent it remains above 8.0x for a sustained period.

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Applicable Criteria
Airports Rating Criteria (pub. 23 Feb 2018)
https://www.fitchratings.com/site/re/10021613
Rating Criteria for Infrastructure and Project Finance (pub. 24 Aug 2017)
https://www.fitchratings.com/site/re/902689