FitchRatings

Fitch Affirms Illinois State Toll Highway Authority's Revs at 'AA-'; Outlook Stable

Fitch Ratings-Chicago-09 August 2018: Fitch Ratings has affirmed the 'AA-' rating on the Illinois State Toll Highway Authority's (ISTHA) $6.1 billion of outstanding toll highway senior revenue bonds. The Rating Outlook remains Stable.

KEY RATING DRIVERS

Summary: The rating reflects the essentiality of the tollway system, evidenced by its long-term growing traffic base and moderate price elasticity. The rating further reflects ISTHA's prudent debt management with strong historical and projected debt service coverage ratios (DSCR) with a major capital program underway. The potential risks posed by ISTHA's large capital program are largely mitigated by a history of delivering capital programs on time and under budget, a very robust balance sheet position, and an already implemented 60% aggregate commercial toll increase phased in since 2015, which complements the 88% passenger vehicle toll increase in 2012.

ESSENTIAL ROAD NETWORK WITH STABLE DEMAND (Revenue Risk: Volume - Stronger)
The tollway system provides critical transportation links that serve the Chicago and northern Illinois metropolitan area providing key connections to interstate highways. Toll transactions have grown nearly every year since 1974; the 2012-2017 compounded annual growth rate (CAGR) of 4.4% is slightly muted by some elasticity to the 2012 passenger toll increase. However, price elasticity has proven relatively inelastic for passenger traffic and even more so for commercial vehicles. The network benefits from a passenger vehicle base, comprised mostly of commuters, that accounts for nearly 89% of total transactions.

DEMONSTRATED RATE-MAKING FLEXIBILITY (Revenue Risk: Price - Stronger)
While ISTHA has full legal authority to adjust toll rates and has demonstrated in the recent past a willingness to implement significant increases when necessary, future toll increases beyond those currently approved are uncertain. A passenger vehicle toll increase of 88% was implemented in 2012 and an aggregate 60% commercial toll increase was phased in between 2015-2017, with CPI-based increases to commercial

tolls thereafter.

LARGE CAPITAL PLAN PARTIALLY DEBT FUNDED (Infrastructure Development/Renewal - Midrange)
ISTHA is in the seventh year of its 15-year, $14.3 billion MOVE Illinois capital program. Funding is expected to come from $6.0 billion of new money debt issuances ($2.8 billion of which has already been issued) with the remainder from cash flow, supported by recent and future toll increases as well as the implementation of a new video toll fee effective as of February 2018. The authority has substantially completed its existing $5.7 billion congestion relief program (CRP) on time and under budget, and MOVE Illinois is similarly proceeding according to plan.

REDUCED VARIABLE-RATE EXPOSURE (Debt Structure - Stronger)
All debt is senior lien and fully amortizing. Further, the ISTHA has taken steps to stabilize its capital structure evidenced by reducing its variable rate exposure to approximately 19% of aggregate debt and fully hedging its interest costs through swaps with multiple financial counterparties, all rated at least 'A' category by Fitch, with the exception of Deutsche Bank(BBB+/Stable). Maximum annual debt service (MADS) is currently $486 million in 2030 but is estimated by the authority to increase to approximately $644 million after all MOVE Illinois borrowing is taken into account.

Financial Metrics: The current tollway system's $6.1 billion debt burden is expected to increase measurably to $8.0 billion in conjunction with the completion of the capital program. However, the authority's net debt-to-cash flow available for debt service (CFADS) is moderate at approximately 4.0x for FY17 and is not expected to increase higher than 6.5x as a result of the MOVE Illinois program. DSCR has historically been above 2.0x, including over 2.5x since fiscal 2015. Fitch's rating case projections indicate DSCR should average 2.2x through the next 10 years. Strong liquidity of over 1,400 days cash on hand as of fiscal 2017 provides the authority with additional financial flexibility, although this will contract to partly fund the MOVE Illinois program.

PEER GROUP
The closest Fitch-rated large expressway network peers include Harris County Toll Road Authority (HCTRA, AA/Stable) and Central Florida Expressway Authority (CFEA, A/Stable), despite a significantly larger annual volume and toll revenue base for ISTHA. The authority has higher coverage and lower leverage than CFEA but lower coverage and higher leverage and capital needs when compared to HCTRA, which largely explains its rating relative to these peers.

RATING SENSITIVITIES

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

--Stabilized leverage above 8.0x;
--DSCR falling below 1.8x for a sustained period;
--A rising interest rate environment given the authority's vast and prolonged borrowing needs.

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

--Given the authority's sizeable, multi-year capital program, upward migration is not likely at this time.

CREDIT UPDATE

Performance Update

A 6.7% increase in commercial tolls was implemented in January 2017, and as of the end of FY17 toll revenues were up 7.6% year over year. FY17 was the last of three approved commercial toll increases that began in 2015 and totalled a cumulative 60% increase in commercial tolls. From 2018 forward, the tollway plans annual inflationary increases to their commercial toll rates, while holding the passenger toll constant.

For the first five months of FY18, transactions are up 3.5% and revenues are also up 4.7% with solid growth coming from both passenger cars and commercial vehicles. Year-to-date both revenues and expenses are closely tracking to budget, which would equate to annual DSCR of around 2.5x, consistent with historical levels should similar performance trends continue.

Despite increased debt service obligations from MOVE Illinois borrowings, DSCR grew to a very robust 2.7x in 2017 as a result of strong traffic growth coupled with prudent operating expense management (grew just 3.3%) and the commercial toll increase. Coverage exceeded Fitch's base case projection of 2.5x but is expected to temper somewhat as the additional operational and debt service costs of the MOVE Illinois program advance.

Through 2018, around $5 billion will have been invested by the Illinois Tollway since the Move Illinois Program began in 2012. The 15-year nature of the program allows flexibility in timing and funding should it become necessary, but the project remains on schedule and on budget.

Fitch Cases

Under Fitch's base case scenario, which assumes more tempered traffic growth than the authority's projections (Fitch assumed a 2.0% CAGR between 2017 and 2027) but similar operating expense assumptions (CAGR of 4.6%), 10-year DSCR averages 2.3x and never drops below 2.0x assuming no further passenger car toll rate increases. This scenario includes another anticipated $2.9 billion in new money bonds for the MOVE Illinois program with a majority borrowed at a 5.5% rate, which Fitch believes is a reasonable rate assumption. Despite debt outstanding growing to $8.0 billion by the end of the program, leverage remains fairly constant, peaking at 6.0x.

Fitch's rating case assumes greater price elasticity to the toll increases for commercial traffic as well as a less positive impact on transactions from MOVE Illinois capital improvements such that total traffic grows at a 1.5% CAGR between 2017 and 2027. Expenses are also assumed to grow at least 50-100 bps higher than the base case in each year. All additional MOVE Illinois debt service was modelled identically to the base case. Under this scenario, the 10-year average DSCR assuming no further passenger toll increases is 2.2x and remains above 1.8x. Leverage peaks slightly higher at 6.1x but still remains within the bounds for a large, mature network in the 'AA' rating category.

Fitch also conducted breakeven analyses to determine what growth in revenue would be needed in both the base and rating case to produce DSCR of at least 1.0x using estimated 2018 revenue. Both scenarios indicated very little-to-negative dependence on future growth with revenue breakevens of -0.19% average annual revenue growth in the base case and just a modest 0.16% in the rating case. This dependence on revenue growth in the Fitch rating case is only necessary because of the authority's increasing operating expense profile modelled at 4.5% per annum, which causes CFADS to fall over time.

In addition, Fitch analysed MADS coverage using projected 2018 CFADS from its rating case and coverage is a strong 2.2x, again indicating little reliance on growth as the 2018 CFADS could more than cover the projected escalation in annual debt service resulting from the additional MOVE Illinois borrowing. The tollway's strong franchise strength taken together with its robust financial metrics and very limited dependence on growth remain commensurate with its 'AA' category rating.

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A January 2018 district court ruling that dismissed claims regarding payment of Puerto Rico Highways and Transportation Authority debt has raised questions about the scope of protections provided by Chapter 9 of the U.S. bankruptcy code to bonds secured by pledged special revenues. Fitch's rating criteria treat special revenue obligations as independent from the related municipality's general credit quality. The outcome of the litigation could result in modifications to Fitch's approach. For more information, see "What Investors Want to Know: The Impact of the Puerto Rico Ruling on Special Revenue Debt" available at www.fitchratings.com.

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Additional information is available on www.fitchratings.com

Applicable Criteria

Rating Criteria for Infrastructure and Project Finance (pub. 27 Jul 2018) (https://www.fitchratings.com/site/re/10038532)
Toll Roads, Bridges and Tunnels Rating Criteria (pub. 30 Jul 2018) (https://www.fitchratings.com/site/re/10038900)

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