S&P Global
Ratings

RatingsDirect®

San Francisco City and County Airport Commission
San Francisco International Airport; Airport; Joint Criteria

Primary Credit Analyst:
Paul J Dyson, San Francisco (1) 415-371-5079; paul.dyson@spglobal.com

Secondary Contact:
Kevin R Archer, San Francisco + 1 (312) 233 7089; Kevin.Archer@spglobal.com

Table Of Contents

San Francisco City and County Airport Commission
San Francisco International Airport; Airport; Joint Criteria

Credit Profile		
US$807.175 mil 2nd series rev bnds (San Francisco Intl Arpt) ser 2019E due 05/01/2050		
Long Term Rating	A+/Stable	New
US$272.875 mil 2nd series rev rfdg bnds ser 2019H due 05/01/2030		
Long Term Rating	A+/Stable	New
US$112.385 mil 2nd series rev bnds (San Francisco Intl Arpt) ser 2019F due 05/01/2050		
Long Term Rating	A+/Stable	New
US$39.445 mil 2nd series rev bnds (San Francisco Intl Arpt) ser 2019G due 05/01/2030		
Long Term Rating	A+/Stable	New

Rationale

S&P Global Ratings assigned its 'A+' long-term rating to the following proposed bonds being issued by the San Francisco City and County Airport Commission:

- $807.2 million second series revenue bonds, series 2019E (AMT);
- $112.4 million second series revenue bonds, series 2019F (Non-AMT/governmental purpose);
- $39.4 million second series revenue bonds, series 2019G (federally taxable); and
- $272.9 million second series revenue refunding bonds, series 2019H (AMT).

At the same time, we affirmed our 'A+' long-term rating and underlying rating (SPUR) on the commission's other parity debt outstanding. The above ratings were assigned and affirmed using S&P Global Ratings' "U.S. And Canadian Not-For-Profit Transportation Infrastructure Enterprises" criteria, published March 12, 2018 on RatingsDirect.

Finally, we affirmed our 'AA+/A-1' dual rating on various other bonds outstanding, reflecting the application of joint criteria, assuming low correlation.

All bonds are being or were issued for the San Francisco International Airport (SFO). The outlook is stable.

The ratings reflect our opinion of the airport's extremely strong enterprise risk profile and adequate financial risk profile. We applied a one-notch positive adjustment using holistic analysis in arriving at the final 'A+' long-term rating and SPUR, which reflect our view of the airport's history of typically meeting or exceeding most forecast operating and financial metrics as a result of relatively high activity and favorable enplanement trends. We believe this adjustment better reflects our view of the airport's overall creditworthiness.

The extremely strong enterprise risk profile reflects our view of SFO's role as a large connecting hub of very high international, national, regional, and strategic importance that has favorable demand characteristics as a result of relatively limited competition within the Bay Area, and SFO's robust service area economy. The adequate financial risk profile reflects our expectation that coverage (S&P Global Ratings-calculated) will remain adequate and liquidity will remain strong. The adequate financial risk profile further reflects our view of SFO's very large capital plan and a debt burden that is forecast to increase 39% to about $10.1 billion by 2023 from $7.3 billion as of unaudited fiscal 2019. In our view, SFO's rising debt burden and cost structure could constrain the airport's rate-setting flexibility.

The extremely strong enterprise risk profile further reflects our view of the airport's:

- Extremely strong market position. SFO has an economically deep and diverse service area, relatively high activity (averaging 25.7 million enplanements over the past five audited fiscal years), strong regional market share, and very favorable enplanement trends. We expect this to continue given its strong 81% origin-and-destination (O&D) enplanement levels, and despite SFO's moderately high carrier concentration in United Airlines, which handles roughly 46% of the airport's total enplanements. The assessment also reflects our view of only moderate competition for O&D passengers given SFO's status as the primary commercial airport within the Bay Area and as a large international hub.
- Extremely strong service area economic fundamentals, which include favorable income levels and economic activity as measured by GDP per capita, a very robust population base, and below-average unemployment levels
- Low industry risk relative to that of other industries and sectors
- Extremely strong management and governance, with management generally achieving or exceeding financial and operational goals, detailed financial projections, an experienced and deep management team, generally well-defined project plans and targets that mitigate key risks, and a history of successful operations

The adequate financial risk profile reflects our view of the airport's:

- Coverage (S&P Global Ratings-calculated) that we expect will remain adequate at 1.1x to 1.2x, not including transfers from the contingency account, although the residual nature of airline use agreements somewhat offsets this;
- Debt and liabilities capacity that we expect will be maintained at a level we consider strong, taking into consideration the airport's debt burden increasing to about $10.1 billion by 2023 from $7.3 billion (as of June 30, 2019) after issuance of additional debt in fiscal years 2020 through 2023; and
- Strong liquidity at $458 million, or approximately 286 days' cash on hand, in fiscal 2018, well above minimum policy mandates, a level that management anticipates it will maintain over the next few years.

The commission will use series 2019E, 2019F, 2019G, and 2019H bond proceeds to finance a portion ($955 million) of costs to complete various airport capital improvement projects, to refund certain commercial paper (CP) notes outstanding, to refund various debt outstanding and terminate associated swaps, and to fund an $8 million deposit to the contingency fund.

The bonds are secured by net revenue of the airport. Of SFO's total debt to be outstanding subsequent to the series 2019E, 2019F, 2019G, and 2019H bonds' being issued, an estimated 5% will be variable-rate (synthetic fixed- and floating-rate) with 95% traditional fixed-rate. As of July 1, 2019, the airport had $560 million of letter-of-credit-supported variable-rate debt. The airport also has three interest rate swaps, with an unfavorable mark-to-market of $46 million as of July 1, 2019. The swaps, in our view, pose low contingent liquidity risk to the airport, given the rating differential between the SPUR on the airport's revenue bonds and the rating triggers that would prompt the airport to make a swap termination payment if the swap valuation at the time of the termination is not in the airport's favor. SFO has a $500 million CP program (subordinate lien) that is backed by four irrevocable direct pay letters of credit. Repayment of CP notes is a subordinate obligation to the bonds. As of July 1, 2019, CP outstanding totaled $23 million, almost all of which will be repaid with the proceeds of the series 2019E, 2019F, and 2019G bonds.

The airport, located 14 miles south of downtown San Francisco in an unincorporated area of San Mateo County, occupies approximately 2,383 acres on a 5,171-acre site. (The remaining acreage is undeveloped tidelands.) The existing domestic passenger terminal complex totals 2.8 million square feet, and the international terminal 2.5 million. The airport has 94 operational gates, four runways, and over 15,000 public (nonemployee) parking spaces. The City and County of San Francisco owns and operates the airport as an enterprise department. A five-member airport commission, the members of which the mayor appoints to four-year terms, governs the airport.

In addition to meeting growth needs, the airport's capital plan aims to address safety and security, improve information technology infrastructure and the customer experience, and maintain the airport's strong competitive position. The capital improvement plan (CIP) consists of 66 projects totaling $7.6 billion in spending through fiscal 2029, including $4 billion that has been funded to date. The CIP is broken down further into two components: the Ascent Program--Phase I, and the fiscal 2020 Infrastructure Projects Plan. The Ascent Program--Phase I consists of $6.9 billion in projects from the fiscal 2017 capital plan plus a $379 million program reserve to cover unanticipated project needs. The Infrastructure Project Plan includes $350 million in projects that address newly identified needs. Capital needs have grown considerable recently; in fiscal 2016 the airport's 10-year CIP (fiscal years 2017 through 2026) totaled $6.1 billion. Subsequent phases of the Ascent Program are likely to derive from the commission's Airport Development Plan, depending on demand. The plan is under environmental review, and in the future may be designated as the Ascent Program--Phase II.

Our assessments incorporated SFO's updated financial forecast, reflecting the impact of the airport's CIP and related debt issuances, with additional debt of about $4 billion through 2023, including the abovementioned bonds. We do not expect additional significant increases to the CIP.

Outlook

The stable outlook reflects our expectation that SFO's enplanement trends will remain generally favorable and that management will maintain coverage (S&P Global Ratings-calculated) we consider adequate within or near a range of 1.1x to 1.2x. We also expect the airport's debt and liabilities capacity to remain strong, despite the airport's plans to issue significant debt to fund CIP projects.

Upside scenario

Given our view of SFO's adequate coverage (S&P Global Ratings-calculated), significant additional debt needs, and debt profile, we do not expect to raise the ratings during the next two years. However, to the extent that coverage, per our calculations, materially improves, and if we come to believe the improvement is sustainable, all other factors equal, we could raise the rating.

Downside scenario

We could lower the rating if enplanements decline materially, reducing the airport's capacity to manage rising debt, or if the airports' coverage, per our calculations, significantly declines to an insufficient level on a sustained basis.

Enterprise Risk Profile

Our assessment of SFO's enterprise risk profile as extremely strong reflects our view of its low industry risk as well as its extremely strong economic fundamentals, market position, and management and governance.

Economic fundamentals

The service area has extremely strong economic fundamentals as a result of favorable income levels and economic activity as measured by very high GDP per capita of more than $109,000, below-average unemployment levels at about 3%, and slightly above-average expected population growth.

We believe that the large, wealthy service area (14 counties consisting of 9.7 million people) with strong employment trends and a deep and diverse economy has historically provided a robust traffic base, and the area serves as a popular tourist and convention destination. About 25.8 million people visited San Francisco in 2018, and the hotel occupancy rate was 89% in 2017 (most recent data available). San Francisco ranked fifth in the U.S. for overseas visitors (excluding Canada and Mexico) in 2017, preceded by New York, Miami, Los Angeles, and Orlando. The San Francisco Bay Area is the fifth-most-populous combined statistical area in the U.S., and No. 2 in California. Leading industries in the regional economy include high-tech, social media, health care, biotechnology, finance, foreign trade, and higher education. Prominent colleges and universities in the area include the University of California, Berkeley; Stanford; St. Mary's; the University of San Francisco; and Santa Clara University. In 2017, approximately 58% of San Francisco County residents 25 years of age or older attained a bachelor's degree or higher, compared with 45% of the San Francisco combined statistical area and 34% of California residents, according to the U.S. Census Bureau.

Market position

We consider SFO's overall market position extremely strong given its status as a large connecting hub airport that handled about 28.8 million enplanements in fiscal 2018. SFO has the highest share (81%) of O&D traffic of any connecting large hub airport. In terms of competition, SFO is the second-largest international gateway on the West Coast and has a very strong competitive position in the San Francisco Bay Area versus Oakland International Airport (OAK) and San Jose International (SJC), not only for domestic traffic (enplanements and deplanements) but even more so for international and long-haul flights. In terms of overall Bay Area market share versus that of OAK and SJC, SFO's has grown to an estimated 57% as of fiscal 2019 from 42% in fiscal 2005, although it is down from 61% in 2014.

In fiscal 2018, 54 passenger and five cargo-only airlines served the airport. United and United Express accounted for what we consider a concentrated 44.6% of total enplanements in fiscal 2018, with Virgin America and Alaska (now a merged entity as Alaska Airlines) accounting for a combined 13.2%. Overall, the leading 10 airlines accounted for 86% of enplanements in fiscal 2018, and about 85% for the first 11 months of fiscal 2019. In terms of international enplanements, United represented 30.7% in fiscal 2018, with Air Canada second at 8.0%. United Airlines' commitment to SFO remains very strong with continued long-term investments and SFO's gaining the largest share of United's international capacity growth since 2010. SFO is United's fifth-busiest hub and has five active leases with the airport through fiscal years 2021 and 2023. Alaska Airlines is also making sizable local investments at SFO.

For fiscal 2018 (ended June 30), SFO's total enplanements increased 7.2%, on the heels of likewise healthy growth of 4.9% in fiscal 2017, 6.7% in fiscal 2016, and 4.5% in 2015. Based on the latest estimates for fiscal 2019, management reports that total enplanements dipped slightly by approximately 0.7%, but that international growth remained strong, up an estimated 7%. According to management, the enplanement decline for fiscal 2019 was mainly due to Alaska Airlines' various adjustments to its routes after the merger with Virgin America, Southwest Airlines' restructuring of routes to increase service at San Jose Airport, and domestic gate constraints because of high gate utilization. In our view, the slight dip in enplanements estimated for fiscal 2019 is not a credit weakness given that enplanements have significantly exceeded forecasts in recent years, and given our view that management's forecast of continued growth is reasonable. Domestic traffic has grown impressively, in our opinion, particularly in the five years through fiscal 2018. Management attributes this growth primarily to the introduction of service in fiscal 2007 by three low-cost carriers--Southwest Airlines, JetBlue, and Virgin America--that have grown to 17.5% of the market from 6.0%.

The previous airport consultant's report, from December 2018, projected enplanement growth of 0.5% for fiscal 2019 and 2.0% for 2020, followed by growth of 1.5% to 1.9% for fiscal years 2021 through 2025. The current airport consultant's report projects enplanement growth of 2.0% for fiscal 2020, 1.9% for fiscal years 2021 and 2022, and 1.5% to 1.7% for fiscal years 2023 through 2026. We anticipate the airport at least meeting, if not exceeding, the revised forecast. The airport ranks fourth among U.S. airports in terms of domestic and international O&D enplanements, and its international enplanements alone grew slightly more than 10.0% in fiscal 2017 to 6.4 million, 7.9% in fiscal 2018 to 6.9 million, and an estimated additional 6.7% in fiscal 2019 to more than 7.3 million.

Because of the airport's demand characteristics and historical enplanement trends, we expect SFO's enplanement trends will remain generally favorable with some modest fluctuations as a result of the airport's moderate air carrier concentration, potential for weak economic cycles, fuel price changes, airline service decisions, constrained terminal facilities, and potential disruptions from redevelopment of the terminal facilities.

Management and governance

The airport's management and governance, in our view, are extremely strong, reflecting our view of the airport's strategic positioning; risk management and financial management; and organizational effectiveness.

SFO has a record of achieving most of its financial and operational goals. SFO has historically operated in a fiscally prudent manner, budgeting conservatively, maintaining strong cash reserves, and refinancing higher-cost debt ahead of modernizing and enhancing terminal facilities. The CIP, supported by the airlines, is demand-driven and modular, and the commission has several measures in place to mitigate construction risk. In addition, management has detailed standards for operational and financial goals, and a formalized succession plan. The airport also has a low-risk debt profile, with 95% pro forma fixed-rate amortizing debt. The rate-setting methodology under the agreement is residual, whereby rates and charges are set on an annual basis to produce projected airline payments equal to projected net costs. We consider the airport's organizational effectiveness very strong, reflecting a management team that is very experienced, deep, and capable with a good track record of operating the facility.

The commission maintains prudent insurance policies as well, including business interruption insurance, and requires signatory airlines to post collateral with the airport commission to guarantee performance and payment. Management is also addressing environmental risks such as flood risk and sea level rise. The airport may need to improve or add structures to be above the floodplain, and the commission is in discussion with the U.S. Army Corps of Engineers to develop a feasibility study to recommend improvements to address long-term sea level rise at the airport. The commission has proposed a shoreline protection program (the updated program is not yet in its CIP) that, if approved by the San Francisco Board of Supervisors, is estimated to begin in fiscal 2025. The U.S. Army Corps of Engineers might partly fund costs related to sea-level rise mitigation.

Financial Risk Profile

Our assessment of SFO's financial risk profile as adequate reflects our view of the airport's adequate financial performance, declining debt and liabilities capacity that we expect will remain at least strong, and strong liquidity and financial flexibility. Our financial profile risk assessment in some cases incorporates pro forma figures, which reflect the impact of $4 billion of additional debt needed to fund the CIP. Our financial profile risk assessment also incorporates SFO's financial policies, which we consider credit neutral.

Our assessment incorporates the airport's updated financial forecast, which assumes issuance of the additional aforementioned debt, 1.4% compound annual growth rate in enplanements for fiscal years 2018 to 2026, increasing signatory airline cost per enplanement on a nominal basis to $27 in 2024 from $18 in fiscal 2019, and increasing debt per enplanement to around $335 by 2022 from $256 in fiscal 2018. SFO has $7.3 billion of debt outstanding. We consider the forecast reasonable given its conservative estimates and because of the airport's good recent track record of generally exceeding prior years' forecast metrics.

Financial performance

The adequate financial performance assessment reflects our evaluation of SFO's updated financial forecast, the fully residual nature of the airport's airline use and lease agreements, and a rising airline cost structure. We expect coverage (S&P Global Ratings-calculated), which was 1.23x in fiscal 2018, to hold in a range of 1.1x to 1.2x through 2026, even with rapidly rising debt service requirements. According to the forecast, coverage per our calculations will decline to near 1.10x by fiscal 2025, exclusive of the $204 million transfer of the contingency reserve, which the master resolution permits (1.35x including the transfer). Our coverage calculation includes passenger facility charges pledged or committed to general airport revenue bond debt service as part of revenue rather than as a debt service offset and excludes SFO's rolling coverage (contingency fund) account.

While coverage is forecast to decline and cost per enplanement is anticipated to rise considerably, we also believe the forecast is conservative: SFO has a history of generally outperforming the airport consultant's projections, especially over the past 10 years. Thus, we anticipate these metrics will be more favorable than the forecast indicates. We consider SFO's airline cost structure moderately high, at slightly more than $18, but we note that this is skewed as a result of the heavy volume of international enplanements the airport generates; domestic-only cost per enplaned passenger is considerably lower and more competitive.

Debt and liabilities

We assess SFO's debt and liabilities capacity as strong but declining based on increasing debt to net revenue, assuming the airport continues to issue significant debt for its CIP. We are basing our debt-to-liabilities assessment on pro forma figures that, in our opinion, accurately reflect our forward view of leverage, but we note that pro forma figures for debt to net revenue do not materially differ from recent or current-year figures. Consequently, our assessment incorporates the assumption that SFO's pro forma debt to net revenue will be about 12x by 2023, including all projected debt issuances and considering that a portion of passenger facility charges will be committed to paying debt service. Our assessment also incorporates the airport's pro forma debt per enplanement that we project will peak at about $335, reflecting the impact of all anticipated bond issuances. To the extent that enplanement growth exceeds the airport consultant's forecast, these metrics will be more moderate.

Key projects within the Ascent Program--Phase I include Terminal 1 projects ($2.4 billion), Terminal 3 West Redevelopment projects ($1.2 billion), an on-airport hotel slated to open in September 2019 ($240 million), and various other terminal and groundside projects. SFO also recently opened its long-term parking garage 2 in February 2019. SFO is now spending over $120 million per month on its CIP, making recent months the busiest in history in terms of SFO's capital program. SFO carefully manages construction risk and cost escalation through value engineering, maintenance of several contingencies, and identification of deferrable projects or project components. Management reports that increases in tariffs on steel and other tariffs have not significantly affected cost estimates.

Liquidity and financial flexibility

Unlike our financial performance and debt and liabilities assessments, our liquidity and financial flexibility assessment did not incorporate pro forma figures in terms of cash or available liquidity to debt, because long-term liquidity balances were not available. Management plans to maintain cash near current levels, but we anticipate that the nominal amount will grow with the airport's budget. We assess SFO's liquidity and financial flexibility as strong, reflecting about 286 days' cash on hand in audited fiscal 2018, with available liquidity to debt at 7.3%.

Ratings Detail (As Of July 25, 2019)		
San Francisco Intl Arpt second ser var rt rev bnds		
Long Term Rating	AA+/A-1	Affirmed
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco Intl Arpt second ser var rt rev bnds		
Long Term Rating	AA+/A-1	Affirmed
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Airport Commission of the City and County of San Francisco, California		
San Francisco Intl Arpt, California		
San Francisco City & Cnty Arpt Comm (San Francisco Intl Arpt) arpt rev rfdg bnds rmktd		
Long Term Rating	A+/Stable	Affirmed
San Francisco City & Cnty Arpt Comm (San Francisco Intl Arpt) AIRPORTS		
Long Term Rating	A+/Stable	Affirmed

Ratings Detail (As Of July 25, 2019) (cont.)		
San Francisco City & County Airport Commission (San Francisco International Airport)		
Long Term Rating	A+/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport) VRDB		
Long Term Rating	AA+/A-1	Affirmed
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport) VRDB		
Long Term Rating	AA+/A-1	Affirmed
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport) VRDB (ASSURED GTY)		
Long Term Rating	AA/NR/Stable	Current
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport) VRDB (ASSURED GTY)		
Long Term Rating	AA/NR/Stable	Current
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport) (ASSURED GTY)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
San Francisco City & County Airport Commission (San Francisco International Airport)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.