FitchRatings

Philadelphia International Airport (PA)

Ratings

$1.37 Billion Philadelphia International Airport (PA) – Senior Lien Airport Revenue Bonds	A+

Rating Outlook

Stable

Applicable Criteria

Infrastructure & Project Finance Rating Criteria (May 2023)

Transportation Infrastructure Rating Criteria (December 2023)

Related Research

Peer Review of U.S. Airports (January 2024)

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Summary

The upgrade of Philadelphia International Airport's (PHL) ratings reflects continued positive progression to full traffic recovery and demonstration of financial performance that is benefiting from the recently introduced airline use and lease agreement which will enhance airport liquidity while preserving 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. Leverage only rises nominally to about 7x, from under 5x, well within the 9x rating sensitivity for a positive rating action, under the Fitch rating case.

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, offset by a high degree of concentration in American Airlines (B+/Stable) and connecting traffic. The rating also reflects PHL's strong residual airline agreement which provides for full recovery of operating expenses and debt service costs but also results in narrow coverage and adequate liquidity.

Key Rating Drivers

Revenue Risk - Volume - Stronger

Large Market with Connecting Exposure: PHL's service area is the large and stable Philadelphia metropolitan statistical area (MSA), which has typically provided about 13-14 million O&D enplanements annually. Though the airport has connecting traffic exposure of about 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 capital plan moves forward.

Revenue Risk - Price - Stronger

Strong Cost Recovery Rate Setting: The airport's airline use agreement (AUA) put into effect last year runs through 2026 and 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, which Fitch views 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 Development and Renewal - Midrange

Expanded Capex Plan with Borrowings: The airport's most recent multi-year capital development program (CDP) is about $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 passenger facility charges (PFCs) 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. The structural features are adequate and protective to bondholders, with fully cash-funded debt reserves at maximum annual debt service (MADS) balanced with permissive rate covenants, according to Fitch. We expect debt service obligations to be elevated over historical levels in the intermediate term and increase with additional borrowings for the capital plan.

Financial Profile

The airport has managed to narrow cashflow-only debt service coverage levels (excluding fund balances) but still improved liquidity to the 400-500 days cash range of recent years. The AUA positions PHL for improved DSCR metrics while maintaining residual rate setting. Still, the airport has limits to its ability to fund its 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 about 4.8x to about 7.3x before 2030 when considering all potential debt borrowings for the capex plan.

Peer Analysis

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 at about $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.

Overview

The airport system, which is owned by the city of Philadelphia and operated by Philadelphia’s Department of Aviation, consists of PHL (the airport), the main revenue generating asset of the system and principal passenger airport serving the Philadelphia metropolitan area, and Northeast Philadelphia Airport, a general aviation reliever facility. The airport is classified by the Federal Aviation Authority (FAA) as a large hub and it is used as a major hub by American Airlines.

The airport occupies a 2,390-acre site in Philadelphia and Delaware counties, about seven miles southwest of central Philadelphia. The airport benefits from direct highway access and Southeastern Transportation Authority rail access to downtown Philadelphia. Northeast Philadelphia Airport, which handles the majority of the region’s general and business activities located 10 miles northeast of the city.

The airport’s key facilities include four runways, a passenger terminal complex consisting of seven concourses providing 126 aircraft parking gates for domestic and international operations, and six active cargo facilities, and an

American Airlines aircraft maintenance hangar, and a former United States Postal Service building located at the western end of the airport.

Credit Update

Enplanements are approaching full recovery from the Covid-19 pandemic, and recent uplift in enplanements over the first 11 months of fiscal 2024 support Fitch's expectations that enplanements could reach 2019 levels by 2025. In fiscal 2023, enplanements increased to 14.0 million, which was 4% above Fitch's prior year base case expectations. Enplaned passengers recovered to 91% of 2019 volume levels in fiscal 2024, 11 months year-to-date. The airport shows commitments towards its relationship with American Airlines through the addition of new international and domestic routes and the continued growth of American's Landline service.

Total airline revenues for fiscal 2023 increased by about 8.3% and total non-airline revenues grew by 41.1%, resulting in overall operating revenues rising by 21.6% to $396 million. Non-airline revenues increased due to payments from the Airport's new Chase Sapphire Lounge, which management expects going forward to increase by 3% per year.

Operating expenses rose by 5.5% in fiscal 2023 due to backfilling of positions vacated during the pandemic and increased contractual services as passenger levels increased. Management's estimate for fiscal 2024 costs is lower than the projected budget, due to lower contractual services, utility and insurance costs and fringe benefits. Debt service coverage calculated by Fitch (including interdepartmental charges but excluding fund balances) remained relatively narrow at about 1.2x in fiscal 2023 while leverage was relatively moderate for a large-hub facility at 4.8x.

The airport's AUA was most recently updated in July 2023 and runs through June 2026, with the option for two additional one-year extension periods. The AUA also confirms the pre-approval of $935 million in new capital funding to support airport infrastructure needs. The funding will be used for repair work, upgrades to terminals, cargo program projects and initial funding to support aviation related development within PHL's Economy lot. PHL also benefits from a new TNC agreement, which increases the pickoff/drop-off fee from $4.00 to $4.35 through June 30, 2026, with additional incremental rate increases expected thereafter.

The updated multi-year capital program covered in the airport's AUA totals $1.8 billion, including $935 million in new projects, $385 million of which has been completed. The airport anticipates new debt issuances of $266 million in 2025 and $300 million in 2027, which Fitch incorporated into its cases.

Key Features

Project Summary Data		**Financial Summary Data**	
Project Type	Airport	Rated Debt Terms	Outstanding: $1.37 billion senior lien airport revenue bonds Non-Fitch rated: $115.5 mil senior lien taxable notes
Project Location	Philadelphia, PA	Amortization Profile	Fully amortizing
Project Status	In operation	Hedging Counterparty	Floating-to-fixed swap for 2005C VRDB JPMorgan Chase ('AA-'/Stable)
Applicable Regulation	State Law & FAA	Advisors	Ricondo & Associates, Inc.; AVK Consulting, Inc.
Operator	City of Philadelphia	Liquidity Provider	Letters of credit for commercial paper (2005C variable rate/synthetically fixed bonds), must be 'A' category or above
		Reserves	Debt service reserve fund: $136.3M
		Transaction Triggers	Rate covenant: 1.5x for Test 1; 1.0x for Test 2 (includes interdepartmental charges as an operating expense). Both tests include PFCs and fund balances available for debt service in cash flow available for debt service. Additional bonds test: rate covenant is met for previous fiscal year or 12 consecutive months out of 18

Source: Fitch Ratings

Financial Analysis – Financial Profile and Rating Case

Current Cases

Fitch conducted updated base and rating cases that incorporate the expected new debt issuances in 2025 and 2027, and planned uses of federal relief funds in fiscal 2023 and fiscal 2024.

Fitch’s base case assumes enplanements reach 91% of 2019 levels in fiscal 2024 and fully recover to 2019 levels in fiscal 2025. CPE remains elevated averaging $18.82 from 2024 through 2028. Non-airline revenues move broadly in relation to passenger traffic trends. Airline revenues adjust to comply with the rate covenant. Fitch-calculated coverage averages 1.5x from 2024 to 2028.

Operating expenses increase at a compound annual growth rate of 6.6% from fiscal 2023 to 2028, with a particularly large increase in fiscal 2024 due to higher personnel and contractual services costs. Fitch-calculated debt service coverage (excluding fund balances) averages 1.5x through 2028 and projected leverage is 6.2x in fiscal 2028.

Fitch's rating case contemplates slower traffic recovery with enplanements reaching 2019 levels in fiscal 2027. As in the base case, airline revenues average to 1.3x coverage from 2024 to 2028 and non-airline revenues move in line with enplanements. Operating expenses grow at 50bp more per year than the base case. Leverage is similar to the base case levels around 6x to 7x. CPE averages $18.95 from 2024-2028.

While the airport's enplanement recovery lags behind the national average, Fitch expects that a continuation of the recovery trajectory, together with the PHL's residual airline lease and prudent expense management throughout the pandemic, will result in sound financial performance.

SOLICITATION & PARTICIPATION STATUS

For information on the solicitation status of the ratings included within this report, please refer to the solicitation status shown in the relevant entity's summary page of the Fitch Ratings website.

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