FITCH AFFIRMS ALAMEDA CORRIDOR TRANSPORTATION AUTH, CA'S SR, SUB & SECOND SUB REVS; OUTLOOK STABLE

Fitch Ratings-New York-23 March 2018: Fitch Ratings has affirmed the Alameda Corridor Transportation Authority's (ACTA) $983.6 million in senior bonds at 'A', $441.7 million in subordinate revenue bonds at 'BBB+', and $556.9 million in second subordinate revenue bonds at 'BBB'.

The Rating Outlook on all bonds is Stable.

ACTA also has $83.7 million in unrated series 2012 bonds, which are on parity with the rated senior revenue bonds.

KEY RATING DRIVERS

The ratings reflect a vital rail corridor that handles nearly a third of the throughput for the San Pedro Bay ports (SPB ports; Port of Los Angeles and Port of Long Beach, both rated 'AA' senior/ Outlook Stable). Backstop commitments from the ports provide some revenue stability and mitigate against the authority's exposure to throughput volatility and rate adjustment limitations. Credit concerns include ACTA's heavily back-loaded debt structure, which Fitch expects to trigger several years of shortfall advances after 2026 if the debt is not restructured and/or volume and inflation growth remains modest.

Specifically, the 'A' rating on the senior lien reflects superior coverage levels, stronger structural protections, and an expected lack of dependence on shortfall advances, while acknowledging the open nature of the lien for future restructuring transactions. The first subordinate and second subordinate bond ratings of 'BBB+' and 'BBB', respectively, reflect the liens' subordinated positions within the ACTA debt structure, lower coverage levels, weaker structural protections, and expected reliance upon shortfall advances post 2026.

Essential Corridor, Elevated Volatility - Revenue Risk (Volume): Midrange

The corridor provides an essential intermodal transportation link between the SPB ports and two of the nation's largest railroads, Union Pacific and BNSF. However, ACTA's loaded throughput has exhibited slightly more volatility than that of the SPB ports as a result of its exposure to trans-loading and shipment of intermodal cargo to some lower growth regions beyond the Southern California basin. ACTA's import cargo is also somewhat susceptible to diversion, though limited diversion is expected given timing efficiencies provided by the SPB ports and the railroads. ACTA's share of SPB port cargo has declined modestly in recent years to capturing roughly 30% of total TEUs. Positively, elasticity to rate increases has been low and is expected to remain low going forward given ACTA's current rate framework.

Moderate Rate-Making Ability - Revenue Risk (Price): Midrange

ACTA has a moderate ability to modify rates, evidenced by its rate framework which tracks rate increases to changes in the consumer price index (CPI). Annual rate increases are subject to a minimum threshold of 1.5% and a maximum threshold of 4.5%, which protects against very low or negative inflation but limits the authority's ability to offset sharp declines in volume with commensurate rate increases. Rate increases for fiscal 2017 and 2018 were 2.2% and 3.1%, respectively. Periods of lower inflation growth are somewhat mitigated by the allowance of shortfall advances by the SPB ports, which have an obligation to cover up to 40% of any debt service shortfall. ACTA is also able to pass through maintenance and operational (M&O)

costs to the BNSF and Union Pacific railroads, though ACTA remains responsible for its own administrative costs (roughly $5 million annually).

Minimal Capital Needs - Infrastructure Renewal/Development: Stronger
ACTA's capital improvement planning mechanisms are considered strong and reflect the anticipated needs of both the ports and the railroads. The corridor is in good condition and is currently operating well above medium-term throughput forecasts, resulting in modest future expected capital needs. The asset benefits from $52 million in available cash balances as of November 2017, well above expected annual capital spending of roughly $1 million to $2 million. No additional borrowing for capital-related projects is expected over the near term.

Back-Loaded Debt Structure - Debt Structure: Stronger (Senior); Midrange (Subordinate and Second Subordinate)
ACTA's debt structure is fixed-rate and largely back-loaded, with about 38% of total outstanding debt in the form of capital appreciation bonds. The lower debt structure score of ACTA's two subordinate liens reflects the liens' subordinated position within the overall debt structure, weaker structural features, and reliance on shortfall advances to meet obligations post fiscal 2026 unless additional restructuring occurs.

Financial Profile:
ACTA benefits from solid senior full-term rating case average debt service coverage ratios (DSCR) of 2.4x, and adequate first subordinate and second subordinate full-term average DSCRs of 1.5x and 1.3x, respectively (including the port's contingent obligations and ACTA's administrative costs). Notably, minimum rating case project life coverage ratios (PLCR) are higher at 3.5x senior, 2.4x first subordinate, and 1.8x all-in, demonstrating potential financial relief provided by ACTA's 10 year tail. Overall, ACTA's coverage ratios are slightly higher than Fitch's indicative guidance for ports, representing Fitch's view that additional financial cushion is necessary to offset ACTA's increased volume and price risk. Rating case year five leverage (including contingent obligations and administrative costs) is adequate for the senior and first subordinate lien at 5.9x and 9.0x but elevated on an all in basis at 12.5x. Higher leverage is mitigated by ACTA's lack of capital needs, which should allow for progressive deleveraging through final maturity.

PEER GROUP:
In comparison to 'A' category rated ports within Fitch's portfolio, ACTA has a lower percentage of minimum annual guaranteed revenues but higher senior coverage levels, representing additional cushion to offset ACTA's lower degree of revenue stability.

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

--Sustained throughput underperformance not adequately offset by rate increases, resulting in ongoing dependency on shortfall advances.
--Material changes in the credit quality of the two port counterparties, or an inability of the railroads serving ACTA to cover O&M.
--Material changes in federal policy which negatively affects trade with Asia, and correspondingly, ACTA's TEU throughput.

Future Developments That May, Individually or Collectively, Lead to Positive Rating Action
ACTA's increasing debt service profile and dependence on revenue growth to avoid shortfall advances makes upward rating migration unlikely.

CREDIT UPDATE

Performance Update

ACTA's TEUs declined 4.9% in fiscal 2017 (ended June 30), largely reflecting cargo disruptions at POLB following the August 2016 bankruptcy of Hanjin, one of the largest shippers serving the port. However, TEUs for fiscal 2018 year to date (first 6 months through December 2017) show a robust recovery of 12.7% over the same period a year prior. SPB ports have also seen strong growth of 9.0% for the same period. Management projections anticipate that volume will increase by roughly 9% to 10% for fiscal 2018. ACTA's financial metrics are expected to remain in line with its current ratings.

Use fee and container charges declined by 0.7% in fiscal 2017, with the CPI-linked rate increase of 2.2% effective Jan. 1, 2017 somewhat offsetting the effect of declines in TEU throughput on revenues. Results for fiscal 2018 year to date through November indicate an increase in revenues of 7.9%, buoyed by the rise in TEUs for the same period, as well as an additional inflationary rate increase of 3.1% effective Jan. 1, 2018. Management is currently projecting for Use Fees and Container Charges to come in at $107.3 million for fiscal 2018, an increase of 4.5%.

Administrative costs increased in 2017, reflecting rising personnel costs including salary and benefit packages, as well as other administrative expenses. Management notes that certain costs which have previously been charged to capital (consultant and legal fees) are now accounted for as operating costs, as the original Construction Funds have been exhausted. Fiscal 2018 is expected to see continued increases in administrative expenses, reflecting a one-time salary adjustment for six employees and related increases in benefits packages, as well as accounting for certain costs previously charged to capital as operating expenses.

In fiscal 2017, Fitch-calculated senior DSCR (including contingent obligations, net of administrative costs) fell to 2.1x, a slight decrease relative to fiscal 2016. Total Fitch-calculated DSCR for fiscal 2017 grew to 1.5x due to lower annual debt service on the subordinate and second subordinate lien. Fitch-calculated senior leverage rose slightly to 7.7x, driven by lower cash flow available for debt service in 2017 and relatively flat debt outstanding. For similar reasons, total Fitch-calculated leverage also increased slightly to 14.6x. Fitch expects metrics to improve slightly in 2018 as pledged revenues improve, annual debt service remains relatively flat, and debt continues to amortize.

Fitch Cases
Fitch's base case assumes 2% TEU growth for inbound containers and 1.5% growth for empties, coupled with inflationary rate increases of 2%, and inflationary administrative cost growth of 2%. Fitch's rating case assumes 1.5% TEU growth, rate increases at the minimum threshold of 1.5%, and 2.5% administrative expense growth. Fitch's base case analysis yields full-term DSCRs and year five leverage of 2.8x and 5.3x senior, 1.7x and 8.1x first subordinate, and 1.4x and 11.2x second subordinate, respectively. Fitch's rating case analysis yields full-term DSCRs and year five leverage of 2.4x and 5.9x senior, 1.5x and 9.0x first subordinate, and 1.3x and 12.5x second subordinate, respectively. PLCRs are at least 50 basis points (bps) higher than full-term DSCRs on all liens.

Fitch's breakeven analysis indicates that in order to breakeven to 1x DSCR while exhausting all available cash reserves, annual revenue growth would have to decline by 11.2% on the senior lien, decline by 0.2% on the first subordinate lien, and grow at a modest 2.0% on the second subordinate lien. In Fitch's view, the aforementioned percentages demonstrate that all liens have a very low dependence on growth when considering available contingent obligations of the ports. However, breakeven percentages decline substantially when excluding the port's contingent obligations. Under this scenario, no growth would be required for senior lien, 4.7% growth would be required on the first subordinate lien, and 5.9% required on the second subordinate lien.

While current metrics are considered adequate for their respective ratings, both Fitch's base and rating case require shortfall advances in order to meet obligations through debt maturity as a result of ACTA's back-loaded debt service obligations. Furthermore, avoiding shortfall advances on all liens would require revenue growth of at least 5.9% to breakeven, which may not be feasible. Credit quality could be compromised to the extent the authority becomes dependent on shortfall advances to meet obligations. However, Fitch views positively the long tail currently provided by the use permit and the presence of call options within ACTA's debt structure, which should provide for sufficient financial relief via a refunding or restructuring transaction if necessary.

Security
Bondholder security includes the pledged revenue stream and all other monies held by the trustee except for the M&O fund and the reserve account, both of which are for purposes of operating and capital maintenance of the corridor. Pledged revenues consist primarily of the volume assessment charges payable by the railroads and debt service shortfall advances payable by the ports. Shortfall advances from the ports are subordinate to their own costs and debt obligations. A use and operating agreement among ACTA, the ports and the railroads governs the volume assessment of charges.

Contact:

Primary Analyst
Emma Griffith
Senior Director
+1-212-908-9124
Fitch Rating, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Anne Tricerri
Associate Director
+1-646-582-4676

Committee Chairperson
Scott Zuchorski
Senior Director
+1-212-908-0659

Media Relations: Sandro Scenga, New York, Tel: +1 212-908-0278, Email: sandro.scenga@fitchratings.com.

Additional information is available on www.fitchratings.com

Applicable Criteria
Ports Rating Criteria (pub. 23 Feb 2018)
https://www.fitchratings.com/site/re/10021628
Rating Criteria for Infrastructure and Project Finance (pub. 24 Aug 2017)
https://www.fitchratings.com/site/re/902689