Moody's
INVESTORS SERVICE

Rating Update: Moody's affirms Aa3 rating of Maryland Transportation Authority's Transportation Facility Revenue Bonds; outlook is stable

Global Credit Research - 21 Dec 2012

Approximately $2.3 billion of rated debt outstanding

MARYLAND TRANSPORTATION AUTHORITY
Toll Facilities
MD

Opinion

NEW YORK, December 21, 2012 --Moody's Investors Service has affirmed the Aa3 rating of the Maryland Transportation Authority's Transportation Facilities Projects Revenue Bonds. The outlook is stable.

RATINGS RATIONALE

The Aa3 is based on the essentiality of the authority's road network; strong historical and projected debt service coverage ratios (DSCRs); demonstrated ability and willingness to raise tolls to support capital projects and conservative financial practices and capital program management. The stable outlook reflects better than expected elasticity to implemented toll increases, which if seen with future planned increases, could produce financial metrics consistent with current levels despite increased debt service levels and decreased liquidity as a result of capital projects.

LEGAL SECURITY: Bonds are secured by a pledge of net revenues from seven of the authority's eight toll facilities. The bonds are also secured by a cash-funded debt service reserve sized at the lesser of maximum debt service, 125% of average debt service or 10% of the principal amount of the bonds being issued. The authority's rate covenant requires net revenues to be at least the sum of 1.2 times annual debt service and 100% of the amount required to be deposited in the maintenance and operations reserve account. The additional bonds test requires the rate covenant to be met on a 5-year prospective basis.

The authority has a statutory debt limit of $3 billion.

INTEREST RATE DERIVATIVES: None.

STRENGTHS:

* Long history of strong demand for the authority's multiple, essential and established transportation facilities in well-developed, affluent and slowly growing service area.

* Consistently high debt service coverage ratios (DSCRs) and ample financial margins, though coverage will be reduced as outstanding debt is amortized and operating expenses increase

* Strong liquidity levels representing more than one year of operating expenses, though balances will be reduced to a minimum $350 million as the large capital improvement program is funded

* Demonstrated willingness and independent ability to raise tolls when needed with projected minimal traffic impact. Toll rates remain relatively low despite doubling of commercial tolls in 2010 and one additional expected rate increase in July 1, 2013 (part of approved three part rate increase adopted September 2011)

CHALLENGES

* Modest amount of planned future debt, and total debt outstanding limited by statute to $3 billion

* Possible, though limited, cost increases for capital projects completion

* The indenture allows for funds to flow out of the system, when authorized by the authority. From 2002 to 2007 the authority made annual (fixed) payments to the Maryland Department of Transportation (MDOT), but has not made

payments since then

Outlook

The stable outlook is stable based on our expectation that the authority will be able to maintain its strong financial profile as it implements its large, mostly non-debt financed capital improvement plan (CIP) and that traffic levels may outperform current projections of elasticity in the face of toll increases.

What could change the rating - UP

Significant and sustained higher-than-projected traffic levels and toll revenues that increase DSCRs above 3.0 times while maintaining current levels of liquidity could put upward pressure on the rating.

What could change the rating - DOWN

Greater declines in traffic and revenue levels than assumed in the authority's base case forecast combined with significantly higher debt financing of the CIP could place downward pressure on the rating. A sustained decline in the DSCR below the targeted 2.0 times in conjunction with other unfavorable developments would exert downward pressure on the rating.

DETAILED CREDIT DISCUSSION

SYSTEM FACILITIES PROVIDE ESSENTIAL TRANSPORT LINKS IN STRONG, STABLE ECONOMY

The authority's tolled assets cover a densely populated, high income service area and include the John F. Kennedy Memorial Highway (JFK), a 50-mile stretch of Interstate 95 (I-95) between Baltimore and the Maryland-Delaware border; three bridges crossing the Potomac River, the Chesapeake Bay, and the Baltimore Harbor and two tunnels carrying I-95 and I-895 under the Baltimore Harbor. The authority also operates and collects tolls on the Hatem Bridge, which crosses the Susquehanna River, but these revenues are not pledged to bondholders. An eighth facility, the Intercounty Connector (ICC) construction has completed 3 of 5 contracts (the majority of the scope of the project) and is estimated to come in about $175 million under budget. The current MSA unemployment rate of 6% is the lowest among the top 10 MSA.

In September 2011 the authority approved a series of toll increases to be implemented in phases. The first increase became effective on November 1, 2011; the second on January 1, 2012 and the third will be implemented on July 1, 2013. In 2009 the authority increased commercial toll rates by 50% and effective July 2009 the authority made several changes in commuter toll plans and added various service fees, including a $1.50 monthly electronic (EZPass) maintenance fee. Traffic and revenues for FY2012 exceeded the projected levels by 4.1% and 2.1%, respectively, demonstrating lower elasticity to toll increase than forecasted levels on legacy facilities. Traffic and revenue on the new ICC have tracked closely to forecasted levels. The authority projects that traffic will decrease by 1.4% in FY2013 and 5.8% in FY2014 before returning so modest growth thereafter. The traffic decreases are based on elasticity assumptions used to forecast FY2012 results. However, revenues are forecast to rise by 10.3% in FY2013 and 32.4% in FY2014 due to the planned toll increases. No toll increases after 2014 are included in forecast models.

The increased revenue from rate increases was needed to mitigate the impact of higher expenses in FY2012. Expenses net of depreciation increased from $165 million to $187 due to the new operations of the ICC, a transfer of certain maintenance costs to the operating budget instead of capitalizing the expenses, and a return to meeting budgeted expenses after years of under-running expense budgets. Expense levels are projected to remain elevated due to the revised accounting practices and full scope of the ICC. However, long term forecasts project operating expenses to increase at 5% annually, which is above historical increases.

Debt service coverage on a bond ordinance basis fell from 5.02 times in FY2011 to 2.74 times in FY2012, largely driven by a significant increase in debt service. Under the authority's base case scenario, which utilizes the aforementioned conservative demand elasticity and operating expense increases, DSCRs are expected to reach 3.24 times in FY2014 before declining expense growth outpaces traffic growth. Liquidity remained strong in FY2012 at 965 days. The authority has plans to draw down on unrestricted cash balances to fund the capital improvement programs over the forecast period. The authority retains minimum unrestricted cash target balances of $350 million, which by 2020 would equate to roughly 360 days based on the operating expense projections. Assuming an unlikely combination of multiple stress scenarios, including no traffic growth on the existing system, slower than forecast ramp-up of the ICC project as well as $600 million of increased capital costs, coverage would decline to 1.63 times in 2018, without any additional adjustments to toll rates.

LARGE CAPITAL PROGRAM WITH MODEST DEBT FINANCING, MEGA PROJECTS NEARING COMPLETION

The authority's 2013 through 2018 Consolidated Transportation Plan (CTP) identifies $2.264 billion in projects, including $222 million for the ICC completion; $249 million for the JFK highway and $1,792 million for system-wide improvement and maintenance projects. Plan funding is expected to come primarily from authority capital funds and cash flow ($1.770 billion), and only $494 million in additional bonds.

The ICC is a 17.5-mile, tolled, limited access facility outside of Washington, DC, connecting I-270 (via I-370) in Gaithersburg to I-95 and US 1 south of Laurel and linking Montgomery (rated Aaa, negative outlook) and Prince George's (rated Aaa, negative outlook) counties. SHA is managing the construction of this now $2.393 billion project (down from a budgeted cost of $2.56 billion). The roadway is open to traffic over the 16 miles from I-370 to I-95 ; the remaining 1.5 mile segment from I-95 to US1 will be open in 2014. All major construction contracts are completed or under construction.

The authority is an independent agency, with autonomous rate-setting authority, however the secretary of the state department of transportation (MDOT) also serves as chairman of the authority's 8-member board. The two agencies work together to address state-wide transportation needs and this high level of coordination benefits the authority as it undertakes capital projects. Until 2007 the authority had made annual payments of $43 million to MDOT for mass transit projects, which it is permitted to do per its bond indenture. Moody's notes that the authority does not currently plan to reinstate the transfers given the large amount of cash flow needed to complete the ICC and system-wide capital projects.

KEY INDICATORS:

Facility type: established, multi-asset, state-wide combined bridge and highway system

Toll transactions, FYS 2011-2012: -0.7%

Toll revenues, FYS 2011-2012: 19.5%

Debt service coverage: 2.74

Debt per roadway mile: $41,893

Debt per transaction: $26.55

10-year/5-year AAG total toll revenue: 7.4%/5.7%

10-year/5-year AAG passenger transactions: 0.1%/-0.5%

Debt outstanding: $2.3 billion

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METHODOLOGY SCORECARD FACTORS:

Factor 1 - Asset Type: Aa

Factor 1 - Operating History: Aaa

Factor 1 - Competition: Aa

Factor 1 - Service Area Characteristics: Aaa

Factor 2 - Annual Traffic: Aa

Factor 2 - Traffic Profile: Aa

Factor 2 - Five-Year Traffic CAGR: Baa

Factor 2 - Ability and Willingness to Increase Toll Rates: Aa

Factor 3 - Net Revenue DSCR: aa

Factor 3- Debt/Operating Revenue: Ba

Factor 4 - Capital Needs: A

Factor 4 - Limitations to Growth: A

Scorecard Outcome Before Notching: Aa3

Notching Factors

-0.5 Notch for open loop

1.0 Notch for more than 720 Days Cash on Hand

Scorecard Outcome: Aa3

The principal methodology used in this rating was Government Owned Toll Roads published in October 2012. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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