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Philadelphia, Pennsylvania Philadelphia International Airport; Airport; Joint Criteria

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Credit Profile		
US$285.585 mil arpt rev bnds (Philadelphia International Airport) ser 2010A due 06/30/2040		
Long Term Rating	A+/Stable	New
US$270.905 mil arpt rev rfdg bnds (Philadelphia International Airport) ser 2010D(AMT) due 06/30/2041		
Long Term Rating	A+/Stable	New
US$55.45 mil arpt rev rfdg bnds (Philadelphia International Airport) ser 2010C(AMT) due 06/30/2018		
Long Term Rating	A+/Stable	New
US$25.01 mil arpt rev rfdg bnds (Philadelphia International Airport) ser 2010B due 06/30/2015		
Long Term Rating	A+/Stable	New
Philadelphia, Pennsylvania		
Philadelphia International Airport, Pennsylvania		
Philadelphia (Philadelphia Intl Arpt)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has assigned its 'A+' rating to Philadelphia, Pa.'s airport revenue bonds series 2010A and revenue refunding bonds series 2010B, C, and D, issued for Philadelphia International Airport (PHL). At the same time, Standard & Poor's affirmed its 'A+' rating on the airport's previously issued parity airport revenue bonds, of which approximately $1.1 billion remain outstanding. We also affirmed our 'AAA/A-1+' rating on the airport's parity variable-rate demand bonds series 2005C, of which $168.6 million remain outstanding. The outlook is stable.

The 'AAA/A-1+' rating reflects the application of joint criteria (assuming low correlation) of Standard & Poor's underlying rating (SPUR) on the airport (A+) and the direct-pay, irrevocable letter of credit provided by TD Bank N.A. (AA-/Positive/A-1+).

The ratings reflect our assessment of the airport's relatively large and stable origin and destination (O&D) market, strong competitive position within the region, generally good historical enplanement trends, and a manageable overall debt burden. We believe offsetting this is a dependence on US Airways Inc. (B-/Negative/--) for approximately 67% of enplaned passengers and nearly all connecting traffic (43% of total passengers), a rising airline cost structure, and relatively weak total fixed charge debt service coverage. Our downside sensitivity analysis shows that the airport has the financial resources to absorb lower passenger levels, assuming US Airways remains largely committed to the market. However, if US Airways were to eliminate most of its service, we could lower our rating.

Although PHL's total fixed charge debt service coverage levels has eroded due to a significant drop in non-airline

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revenues (primarily parking), we expect financial margins will be stable or improve. The airport's relatively diverse service area economy allowed it to experience smaller declines in activities levels than many other large hub airports in the U.S. Although the service area economy experienced the recession across almost all industries, it outperformed the nation as well as many of the largest metropolitan areas in terms of employment growth. The service area's diverse economy and the strong presence of less cyclical sectors provide the airport with a relatively less volatile, more stable economic base for air travel demand relative to other areas.

The 'A+' SPUR also reflects our view of PHL's:

- Large O&D market, supported by a relatively stable economic base, which spans 11 counties across Pennsylvania, New Jersey, Delaware, and Maryland. It provides a good base for local air travel demand that in fiscal 2010 totaled an estimated 8.7 million O&D enplaned passengers, or approximately 57% of the 15.2 million total;
- Generally resilient air travel demand due to a strong competitive position as a result of limited competition from other major airports and the presence of low-cost carrier service by Southwest Airlines Co. (BBB/Watch Neg/--); and
- A manageable debt burden, at $81 per enplaned passenger for fiscal year year-end 2010 (June 30) that increases to approximately $101 after this proposed bond issue.

We believe offsetting credit weaknesses include the airport's:

- Relatively high carrier concentration and moderate exposure to connecting passengers--with US Airways and its affiliated commuter carriers representing about 67% of fiscal 2010 total enplanements and nearly all connecting passengers, which were about 43% of total enplanements in fiscal 2010;
- Rising airline cost structure and a debt burden that could increasing significantly over the long term as a result of the airport potentially debt financing a large portion of its estimated $5.35 billion capacity enhancement program (CEP); and
- Relatively weak total fixed charge debt service coverage levels (Standard & Poor's-calculated) for a large-hub residual airport.

The proceeds from the 2010A bonds will help fund approximately $250 million in capital costs for airport's $335 million 2010 project, which includes $127 million of terminal projects, $100 million of airfield projects, and $53 million of other projects. The proposed series 2010B, C, and D bond proceeds will refund all or a portion of the airport's 1997A, 1998A, and International Terminal Bonds. Bond proceeds will also fund a deposit to the airport's parity sinking fund reserve account and pay costs of issuance.

We believe PHL has maintained an adequate unrestricted cash position that has provided 193 days' cash on hand, on average, for fiscals 2007-2009. As of Aug. 31, 2010, the airport had an unrestricted cash position of $86.7 million, which equals 156 days' cash on hand based on airport's fiscal 2011 operating budget.

We have assigned PHL a Debt Derivative Profile (DDP) of '1' on a scale of '1' to '4', with '1' representing the lowest risk. The overall DDP score indicates that airport's swap portfolio is minimal risk. The DDP score incorporates one floating-to-fixed-rate swaption that JPMorgan Chase Bank, N.A. (AA/Negative/A-1+) exercised June 15, 2005. The swap has a notional amount of $168.6 million and synthetically fixes 100% of the airport's 2005C bonds, resulting in a net variable-rate percentage of 0%. The 2005C bonds represent the only variable-rate debt outstanding.

Outlook

The stable outlook reflects our expectation that PHL's large O&D market and strong competitive position will provide generally good enplanement trends, allowing the airport enterprise to maintain stable and improved financial margins. While the airport can withstand some weaker passenger levels, significant declines would likely result in a downgrade if PHL does not maintain its liquidity position or financial margins. We do not expect to raise the ratings during the next two years due to the airport's potentially significant debt needs longer term and weaker margins.

Airport Description

The City of Philadelphia operates PHL and the Northeast Philadelphia Airport, a small general aviation airport that operates at a loss. They comprise the airport system, which the city's Division of Aviation operates. According to Airports Council International data, in 2009, the airport ranked 18th in the nation in passengers, ninth in aircraft movements, and 14th in cargo tonnage. PHL is a major connecting hub for US Airways that, along with its affiliated commuter carriers, represent about 67% of fiscal 2010 total enplanements, and nearly all of the airport's connecting traffic. Southwest Airlines is the second leading carrier, representing 11% of enplanements in fiscal 2010.

Airline Operations And Competition

Airport management does not expect recent airline mergers to have a material affect on passenger levels. In fiscal 2010 Delta Air Lines Inc. and Northwest Airlines Corp., which began operating under a single operating certificate in December 2009, had a combined enplanement market share of 7.0%. In August 2010, the department of justice approved the merger of United and Continental that had a combined enplanement market share of 5.6% in fiscal 2010. We do not expect the recent merger between Southwest and AirTran will have a significant negative effect on the airport's passenger levels. Southwest had an 11% enplanement market share in fiscal 2010, while AirTran's market share was 1.9%. The only overlapping route that Southwest and AirTran have at the airport is to Orlando, where both operate four daily flights.

PHL benefits from the lack of nearby competing facilities--there is no major airport within a one-hour drive. Baltimore/Washington International Airport (102 miles to the southwest) and Newark Liberty International Airport (106 miles to the northeast) are the primary competitors. Since 2004, when Southwest initiated service in Philadelphia, the airport's competitive position has improved. As a result of the airline's presence, average airport airfares have decreased, stimulating air travel demand. For fiscal 2005, the first full year of Southwest's service, originating passenger numbers increased 24%, while average domestic airfares decreased 19%. Due to the recession and reductions in Southwest service, originating passenger levels declined 4.7% in fiscal 2008 and 7.5% in fiscal 2009. Despite this, the number of originating passengers at Philadelphia has exceeded that at Baltimore since fiscal 2005. In fiscal 2009 originating passengers totaled approximately 8.8 million while Baltimore/Washington International totaled approximately 8.2 million.

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Bond Provisions

Securing the bonds are net project revenues; amounts payable to the city under a qualified swap; and all amounts on deposit in, or credited to, certain aviation funds. Project revenues include all revenues from occupants and users of the airport system. Net project revenues are net of net operating and maintenance expenses. Net operating and maintenance expenses are operating and maintenance expenses net of interdepartmental charges, which are subordinate to debt service. A portion of PFCs are pledged to pay debt service for the 2001A and 1998B bonds. A portion of PFCs will also be pledged to pay debt service for the 2010D bonds.

Since July 1, 2007 (the beginning of fiscal 2008), revenues and costs related to the outside terminal area (OTA) and overseas terminal are part of project revenues. Before fiscal 2008, PHL secured its airport revenue bonds with net project revenues excluding OTA and oversea terminal revenues. We view the changes to the general airport revenue bond (GARB) ordinance and new airline agreement favorably because they should improve coverage and make additional funds available for debt service. However, revisions to subsequent airline agreements or future amendments to the general ordinance that would detract from these enhancements would be a credit concern.

Finances

The airport's financial margins eroded in fiscals 2009 and 2010 as a result of declines in originating passengers and relatively flat connecting passenger levels and rising debt service expenses. Total fixed charge coverage (Standard & Poor's-calculated) declined steadily to about 0.9x in fiscal 2010 from 1.2x in fiscal 2008. Total fixed charge coverage is budgeted 1x for fiscal 2011. Excluding interdepartmental charges, coverage declined to 1.8x from about 2.3x from fiscals 2008 to 2010 and is a budgeted 1.9x for fiscal 2011. All coverage calculations include the portion of PFC revenues on which the city has pledged to pay debt service on bonds issued to finance PFC-eligible projects.

OTA and oversea terminal revenue has been lower than previously forecast due to lower-than-expected originating passenger levels and a reduction in the use of airport's parking facilities. Net OTA revenues totaled almost $11 million in fiscal 2009, then dropped significantly to $119,000 in fiscal 2010 due mainly to a reduction in net parking revenues, which accounted for approximately 77% of gross OTA revenues in fiscal 2009. Net parking revenues decreased approximately $2.3 million in fiscal 2009 and $7.6 million in fiscal 2010, while originating passengers declined 7.5% in fiscal 2009 and 1.4% in fiscal 2010. This notable decline in parking revenues was due, in part, to the airport experiencing total fixed charge coverage (Standard & Poor's-calculated) drop below 1x in fiscal 2010. Net OTA revenues are budgeted to total $7.7 million in fiscal 2011 and range from $5.2 million-$6.6 million from fiscals 2012-2015. A 2009 forecast showed net OTA revenues gradually increasing to about $24.4 million in fiscal 2013 from about $11.4 million in fiscal 2008.

Approximately 18,800 on-airport parking spaces are provided in garages and surface lots, while private operators run about 17,000 parking spaces off airport property. In fiscal 2009, the Division of Aviation and the Philadelphia Parking Authority converted airport property for parking, providing about 800 additional public spaces. The most recent change to parking rates took effect Aug. 1, 2008. The airport expects to increase parking rates again Nov. 1, 2010. Such rate increases will provide a projected $1.2 million in additional recurring revenues per year. There are other near-term non-airline revenue enhancement initiatives that management projects will provide $940,000-$1.4 million in additional recurring revenues per year. Other initiatives that are currently under development include privilege fees for off-airport rental car and parking operators, increasing taxi and limousine fees, and leasing existing

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fuel farm to airline consortium. These other initiatives could initially provide the airport with $2.2 million in additional recurring revenues per year. Only the added revenue from the November 2010 parking rate increases is assumed during the forecast period.

Nevertheless, PHL projects that including revenues and costs allocated to the OTA and changes under the new airline lease agreement will allow it to accumulate funds available for debt service, which it forecasts will rise to $80 million in fiscal 2015 from $55 million in fiscal 2010. It projects that these funds alone will cover estimated annual debt 0.43x-0.56x during the forecast period. Based on forecasts, we expect total fixed charge coverage (Standard & Poor's-calculated) to range from about 1.00x-1.08x; including the estimated combined balance of funds available for debt service, coverage is no lower than 1.48x. Excluding interdepartmental charges (which are subordinate to debt service), coverage ranges from 1.82x-1.93x during the forecast period; and including the estimated combined balance of funds available for debt service, coverage is no lower than 2.33x.

We view PHL's airline cost structure as moderately high levels and its debt load manageable for a large-hub airport. Management expects the cost structure to increase to more than $13.00 per passenger in fiscals 2014 and 2015 from an estimated $9.73 in 2010. Based on an estimated 15.2 million enplanements for fiscal 2010, debt per enplanement is approximately $81, $101 after the 2010A bonds. If the airport were to also issue the $165 million bond issue planned in 2011 along with the series 2010A bonds, debt per enplanement increases to a manageable $112. The proceeds from the 2011 GARBs issue are to finance a $150 million land acquisition. Management has no other new-money debt plans through fiscal 2015.

Capital Program Could Stress The Ratings

PHL's long-term capital needs could pressure the rating depending on how the capital program is phased in and financed. The airport's long-term capital program is being refined and updated as part of the Master Plan and National Environmental Policy Act processes. In August 2010, the Federal Aviation Administration (FAA) published a final environmental impact statement in which it selected a preferred alternative for the airport's CEP. Such preferred alternative includes a third-parallel east-west runway, extension of two existing runways, enlarging the existing terminal complex, relocating several off-airport facilities, developing a centralized ground transportation center, and constructing an automated people mover for transport of passengers between terminals and parking facilities that would also interface with the existing commuter rail line. CEP costs are an estimated $5.35 billion and the total period for the phased construction would be approximately 13 years (2013-2025). The FAA expects to issue a record of decision by the end of 2010. In 2009, at the FAA's request, PHL prepared a preliminary analysis of expected funding sources for this preferred alternative. This preliminary analysis showed airport revenue bonds providing more than $5 billion in funding or more than 80% of CEP project costs. Such analysis assumed management would pay a portion of the GARB debt service with $218 million in airport improvement program (AIP) grants and available PFC funds.

The project costs and CEP funding could be materially different from this preliminary analysis. To advance components of the CEP, PHL will need to obtain approvals from city council and the airlines. Under the majority-in-interest provisions, the airport is not able to advance various components without signatory airline approval. The airlines and the airport place the highest priority on the airfield-specific CEP initiates because they provide the majority of the program's financial and operational benefits to the airlines in terms of reducing aircraft delays and the greatest potential for receiving AIP grant funding. The preliminary analysis showed airfield projects

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representing 17% of the total CEP project costs.

Generally Solid Air Traffic Levels

We believe PHL has experienced generally good air travel demand historically. The large O&D market, US Airways' continued commitment to operate a major hub at the airport, limited competition from other airports, and Southwest's expansion have contributed to the airport's strong growth in enplanements. In fiscals 2004 and 2005, enplanements increased 7.8% and 18.4%, respectively, resulting in enplanement levels surpassing pre-September 2001 highs in fiscal 2004. From fiscals 2006-2008 enplanement growth slowed, increasing only 0.5% in fiscal 2006, 1.8% in fiscal 2007, and 1.3% in fiscal 2008. An 11.5% increase in connecting traffic in fiscal 2008 helped offset the 4.7% decline in originating passengers. However, total enplanements declined 4.3% and 1.1% in fiscals 2009 and 2010 as a result of capacity reductions from record jet fuel prices in the summer of 2008 (the beginning of fiscal 2009) and the recession. More specifically, originating enplanements declined 7.5% in fiscal 2009 and 1.4% in fiscal 2010, while connecting passengers increased 0.3% in fiscal 2009 and declined 0.7% in fiscal 2010. Enplanements might be stabilizing. For the two months ended Aug. 31, 2010, enplanements declined 1.8% relative to the same period the previous year. Passengers enplaned for the month of August was almost the same as in August 2009. The airport consultant's report include a base case forecast that assume enplanements increasing 2.7% in fiscal 2011 and 2.6% in 2012, then 2.4% to 2.5% per year from fiscals 2013-2015. Although we consider the forecast aggressive given recent enplanement trends, we expect management will take the necessary steps to maintain stable or improved financial margins.

The consultant's report also included a stress test that assumes a 29% reduction in total enplaned passengers to 11.1 million in fiscal 2012 as a result of US Airways drastically reducing connecting service effective July 2011. From fiscals 2013-2015, it assumes enplanements will increase 7.2%, 7.6%, and 3.1% in fiscals 2013, 2014, and 2015, respectively, as a result of other airlines replacing service. The test assumes the number of originating enplanements to be similar to the number under the base case, but the number of connecting passengers is significantly lower. Under this stress test, costs per enplaned passenger peaks at $17.18 in fiscal 2012, then ranges from $16.28 to $16.88 from fiscals 2013-2015. Indenture coverage under this sensitivity drops to a low of 1.49x, or about 1.04x based on our calculation excluding revenues from the previous year and other available fund balances. Our downside sensitivity analysis shows that PHL has the financial resources to absorb lower passenger levels, assuming US Airways remains largely committed to the market. However, if the airline were to eliminate most of its service, we could lower the rating on the airport bonds, absent assurances that other airlines would quickly replace most of US Airways' routes.

Related Criteria And Research

- USPF Criteria: Airport Revenue Bonds, June 13, 2007
- Criteria: Joint Support Criteria Update, April 22, 2009
- USPF Criteria: Municipal Swaps, June 27, 2007
- USPF Criteria: Debt Derivative Profile Scores, March 27, 2006

Ratings Detail (As Of October 13, 2010)

Philadelphia, Pennsylvania

Philadelphia International Airport, Pennsylvania

Ratings Detail (As Of October 13, 2010) **(cont.)**		
Philadelphia (Philadelphia International Airport)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Philadelphia (Philadelphia International Airport) (ASSURED GTY)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Philadelphia (Philadelphia Intl Arpt)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Philadelphia (Philadelphia Intl Arpt) VRDB ser 2005C		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Long Term Rating	AAA/A-1+	Affirmed
Philadelphia Auth for Indl Dev, Pennsylvania		
Philadelphia International Airport, Pennsylvania		
Philadelphia Auth for Indl Dev (Philadelphia Arpt Sys)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Philadelphia Auth for Indl Dev (Philadelphia Arpt Sys) (MIRROR BONDS)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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