



Fitch Upgrades NC Turnpike Auth's Sr Rev Bonds to 'BBB'; Assigns 'BBB' to Sr Revs and TIFIA Loan

Fitch Ratings - New York - 31 October 2019:

Fitch Ratings has upgraded to 'BBB' from 'BBB-' North Carolina Turnpike Authority's (NCTA) approximately \$665 million of outstanding senior lien toll revenue bonds. In addition, Fitch has assigned 'BBB' ratings to approximately \$378.3 million of Triangle Expressway system senior lien revenue bonds and an approximately \$501.5 million subordinated Transportation Infrastructure Finance and Innovation Act (TIFIA) loan. The Rating Outlook for both the bonds and the TIFIA loan is Stable.

RATING RATIONALE

The upgrade reflects the Triangle Expressway's robust traffic and revenue growth ahead of expectations since opening in 2013 and the strong financial metrics associated with the expected financing of the Complete 540 project. Under Fitch's rating case scenario, which includes the Complete 540 project, post ramp-up total coverage averages 1.7x through 2038 (2.0x through the life of the senior debt), which is stronger than Fitch's prior coverage ratio expectations at the time of the initial rating for the Triangle Expressway.

The rating reflects the expressway's continued strong ramp-up and the Complete 540 expansion project's commuter-based traffic profile, supported by an expanding service area with strong population and economic growth. The rating is further supported by a commitment from the North Carolina Department of Transportation (NCDOT) to fund operating, maintenance and rehabilitation costs, if toll revenues are insufficient, strengthening the bonds' gross pledge. NCTA benefits from legal rate-making flexibility, but due to limited operating history, price sensitivity to increasing toll rates has not yet been adequately tested. Management has taken steps to reduce a sharply escalating debt service profile, though debt back-loading pressures NCTA's financial flexibility. Complete 540 will be supported by a construction completion guarantee from NCDOT during the construction phase.

KEY RATING DRIVERS

NCDOT Completion Guarantee - Completion Risk: Stronger

Project construction is viewed to be straightforward, primarily comprising the design and construction of a 17.1 mile new toll-road facility consisting of six toll lanes. The design-build (DB) contracts for the three projects are fixed-price and date-certain, with the DB contractors for the projects made up of joint ventures of experienced construction firms backed by adequate performance security packages. Design of all three projects began earlier in 2019, with groundbreaking expected to occur in late 2019. In Fitch's view, the relatively straightforward nature of the construction, coupled with the construction completion guarantee from NCDOT, mitigates completion risk. Performance and payment bonds and liquidated damage payments for delays further mitigate completion risk.

Strong Market, Continued Growth - Revenue Risk (Volume): Midrange

Triangle Expressway and the planned Complete 540 extension will serve as a major alternative to congested toll-free roadways and also as a key route to the main employment center in the region, Research Triangle Park (RTP). Traffic on the existing expressway continues to show strong growth through the ramp-up period. Ample economic activity in the service area should contribute to future traffic growth, with the addition of two parkway interchanges on the existing expressway leading to continued ramp-up until 2023. However, with the limited number of toll roads in the area, there still exists the potential for sensitivity to annually increasing toll rates, given uncertainty as to overall demand and perceived value of time savings.

Rate-Making Flexibility Available - Revenue Risk (Price): Stronger

NCTA has flexibility to increase toll rates without any additional legal or regulatory approvals. The expressway has a set annual rate increase schedule through 2035, with rates increasing somewhat above inflation. NCTA maintains the ability to increase rates above the schedule. However, given the expressway's short life to date, there is uncertainty as to whether support exists for additional rate increases above the expressway's pre-determined rate schedule, if needed.

Gross Pledge Supports Asset - Infrastructure Development and Renewal: Stronger

The existing expressway is in new condition with low maintenance needs expected over the intermediate term and the planned Complete 540 extension is expected to have minimal initial capital needs as a brand-new facility when completed in fiscal 2024. Capex will be required over time to keep the road viable and NCDOT pledges to cover the expressway's operating, maintenance and rehabilitation expenses should toll revenues be insufficient. An independent engineer is required to perform annual inspections, supporting asset preservation. The expressway has sufficient capacity to support NCTA's long-term traffic forecast.

Back-loaded, Fixed-Rate Debt - Debt Structure: Midrange

NCTA's overall capital structure consists of fixed-rate amortizing debt with no refinance risk, though annual debt obligations escalate from 2019 to maximum annual debt service (MADS) in 2049, including expected Complete 540 debt. Rate covenants are adequate, requiring toll increases to meet forward-looking minimum debt service coverage ratios (DSCRs) of 1.3x and 1.1x on senior and total subordinate debt, respectively. Structural reserves are sufficient with a reserve fund surety on the existing senior lien bonds. The senior lien debt service reserve fund (DSRF) is sized to 50% of the lesser of (a) 10% of principal amount of the bonds, (b) MADS, or (c) 125% of the average annual principal and interest requirements with respect to the bonds. The TIFIA loan DSRF will be sized to 100% of the lesser of three test. The expected TIFIA loan can spring to senior parity debt upon

occurrence of a bankruptcy related event, supporting a lack of differentiation in attribute scoring between liens. TIFIA benefits from a deferability provision that provides additional payment flexibility.

Financial Profile

Continued strong growth on the existing expressway through ramp-up has led to senior-lien DSCR of 2.3x for fiscal 2019 (unaudited), or 1.7x on all debt including the 2009 TIFIA loan (refunded in December 2018) and reserve funding requirements. Fitch's rating case, which incorporates the expected debt for Complete 540, produces an average total DSCR (senior and TIFIA) of 2.1x over the forecast period from the first year of opening through the life of the senior debt. It is Fitch's view that, while dependent on growth, there is sufficient coverage cushion and liquidity support from the NCDOT-backed O&M and R&R guarantees to offset slower-than-expected growth.

PEER GROUP

Once stabilized, the expressway's closest peers would include similar stand-alone projects such as Colorado's E-470 Public Highway Authority (E-470, A/Stable) and San Joaquin Hills Transportation Corridor Agency (SJHTCA, BBB/BBB-/Positive). Triangle Expressway and its peers are all considered to be congestion reliever roadways in strong corridors that face competition from non-tolled alternate routes. The existing expressway's tolls, at a moderate \$0.20/mile for passenger cars, are more favorable than those of its peers, ranging from \$0.30-\$0.45/mile; however, the peers have greater franchise strength as they have substantially longer operating history.

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action:

- Maintenance of solid financial metrics with total DSCR of at least 1.8x in Fitch's rating case for a sustained period;
- Continued NCDOT support and maintenance of the gross revenue pledge for any future financings;
- A track record of low demonstrated elasticity of demand with respect to rate increases.

Developments That May, Individually or Collectively, Lead to Negative Rating Action:

- An unexpected negative shift in operating performance resulting in rating case total DSCR of less than 1.6x for a prolonged period;
- Reluctance by the authority to increase toll rates above the approved rate schedule as needed;
- Reduced support for the expressway by the State of North Carolina.

TRANSACTION SUMMARY

NCTA expects to issue \$378.3 million in series 2019 senior lien revenue bonds to finance, in part, the costs of land acquisition, design, construction and equipping of Complete 540 - Phase 1, consisting of the extension of the Triangle Expressway for approximately 17.1 miles from NC 55 Bypass in Apex to I-40. The senior toll revenue bonds are fixed rate and fully amortizing with final maturity in 2055.

The authority also expects to enter into the 2019 TIFIA Loan Agreement with USDOT, pursuant to which the authority will borrow a principal amount of up to \$501.5 million. Proceeds of the 2019 TIFIA Loan, when drawn upon, will be used to finance a portion of the costs of Complete 540 - Phase 1. The closing of the 2019 TIFIA loan is a condition to the closing of the series 2019 bonds.

CREDIT UPDATE

Traffic and revenue performance on the Triangle Expressway continues to be very strong through the ramp-up period, outperforming projections. Robust revenue growth is driven by a higher percentage of video tolling than initially expected, the toll rate of which is approximately 50% higher than electronic tolling. Fiscal 2019 toll transactions are up approximately 8.7% YoY to 55.7 million. Fiscal 2019 (unaudited) toll revenues were up approximately 7.4% YoY to \$52.6 million. While traffic growth is still strong, growth rates have begun to temper from prior years as the Expressway reaches the end of its ramp-up period.

Construction of Phase 1 is divided into three projects with two construction grouping, though each project has a separate DB contract. Design of Complete 540 - Phase 1 began in 2019 with groundbreaking expected to occur in late 2019. The Complete 540 project has a construction completion guarantee from NCDOT. The construction completion assurance agreement mitigates cost overruns in the event construction costs exceed those specified in the DB contract. The obligation of NCDOT in regards to renewal payments and construction cost overruns is to be funded from amounts available in the State Highway Fund or the State Highway Trust Fund. Each such payment is subject to appropriation by the state and the availability of amounts in such fund.

FINANCIAL ANALYSIS

Fitch Cases

The forecast in the Fitch Base and Rating Case was developed by applying annual growth rates to historical Triangle Expressway revenue, along with assumptions outlined below in regards to the new Complete 540 segment. The base and rating case both assume the annual revenue growth rates for the Triangle Expressway component as assumed in the previous NCTA surveillance review.

Fitch's base case assumes sponsor traffic and revenue assumptions for Complete 540, as prepared by CDM Smith, but assumes a 12-month construction delay, a lower annual inflation rate of 2.0%,

and an annualization factor of 280 applied to the transaction and revenue impacts of Complete 540. Gross toll revenues increase at a CAGR of 3.8% from 2028 (post ramp-up) through 2049. The 10-year DSCR (post ramp-up) averages 2.0x, while coverage through the life of the senior debt (2020-2055) averages 2.3x. Given the project debt's back loaded nature and the accreting principal amount of the CABs, leverage is initially high and averages 7.0x for the first 10 years after ramp-up.

Fitch made a number of adjustments from the sponsor's traffic and revenue forecast in developing the Fitch Rating Case. The rating case assumes an 18-month construction delay and an extended ramp-up period of four years under the rating case (three-year ramp-up in sponsor case). Increased revenue leakage rates are applied to the first five years of Bill-by-Mail revenue associated with Complete 540. Fitch also assumes a 10% decrease in value of time applied to/from zones in the Complete 540 Phase 1 corridor and a 50% reduction of induced demand on Triangle Expressway. Additional assumptions include annual inflation rate of 2.0% throughout the forecast period and an annualization factor of 280 applied to transaction and revenue associated with Complete 540. Gross toll revenues increase at a CAGR of 3.6% from 2029 (post ramp-up) through 2049. The 10-year DSCR (post ramp-up) averages 1.7x, while coverage through the life of the senior debt (2020-2055) averages 2.0x. Leverage remains elevated and averages 8.7x for the first 10 years after ramp-up. Fitch notes debt service coverage ratios during the first few years of the assumed opening timeframe for the Complete 540 project are low, around 1.3x, but are driven by a number of the aforementioned conservative assumptions.

SECURITY

The senior bonds are secured by a gross lien on revenue of the expressway. The TIFIA loan is secured by a lien on revenues after the payment of the senior lien bonds. TIFIA can spring to senior parity debt upon occurrence of a bankruptcy related event. Significant support is provided to both the bonds and the overall system by NCDOT's covenant to fund operating, maintenance and capital costs in the event expressway revenues are insufficient.

Asset Description

Triangle Expressway, North Carolina's first modern toll road, is an 18.8-mile all-electronic toll road that comprises the partially complete outer loop around the greater Raleigh area from I-40 in the north to the NC-55 Bypass in the south. The expressway is formally located in Wake and Durham counties and extends south from the NC-147/Interstate 40 interchange in Research Triangle Park to Northern Wake Expressway, and then northeast to the Northern Wake Expressway (NC-540)/NC-54 interchange and to the south to the NC-55 Bypass in Holly Springs.

The Complete 540 Southeast Extension is a proposed greenfield project that will extend the existing and operating Triangle Expressway at its current southern terminus near Holly Springs by approximately 17.1 miles to a junction with I-40 south of Raleigh. Phase 1 of the project would substantially complete the 540 outer loop around Raleigh up to the I-40/US 70 interchange and would also link the towns of Apex, Cary, Clayton, Garner, Fuquay-Varina, Holly Springs and Raleigh.

In addition to connecting these towns and cities, the project is also anticipated to ease congestion on area roadways, including I-440, I-40, N.C. 42, N.C. 55 and Ten-Ten Road. The facility is expected to open to traffic in mid-2023.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS		
ENTITY/DEBT	RATING	PRIOR
North Carolina Turnpike Authority (NC)		
North Carolina Turnpike Authority (NC) /Senior Lien Toll Revenues/1 LT	LT BBB Upgrade	BBB-
North Carolina Turnpike Authority (NC) /Subordinate Lien Toll Revenues/1 LT	LT BBB New Rating	WD

Additional information is available on www.fitchratings.com

Applicable Criteria

Rating Criteria for Infrastructure and Project Finance (pub. 27 Jul 2018)
Toll Roads, Bridges and Tunnels Rating Criteria (pub. 30 Jul 2018)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

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