S&P Global Ratings

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Summary:

North Carolina Turnpike Authority; Toll Roads Bridges

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Credit Profile		
US$499.46 mil triangle expwy sys sr ln tpk rev BANs ser 2020 due 02/01/2024		
Long Term Rating	BBB/Negative	New
North Carolina Tpk Auth toll rds & br (AGM)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Tpk Auth toll rds & br (AGM)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Tpk Auth toll rds & br (AGM)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed

Rating Action

S&P Global Ratings assigned its 'BBB' long-term rating to North Carolina Turnpike Authority's (NCTA) Triangle Expressway proposed $499.5 million senior-lien turnpike revenue bond anticipation notes (BANs), series 2020. At the same time, S&P Global Ratings affirmed its 'BBB' long-term rating and underlying rating (SPUR) on NCTA's revenue bonds outstanding and Transportation Infrastructure Finance and Innovation Act (TIFIA) loan. The outlook is negative.

The negative outlook reflects the severe and ongoing disruption associated with the COVID-19 pandemic and contraction of the global and U.S. economies that is likely to negatively affect the authority's operating and financial performance over the near-to-intermediate term. For additional information, see "Ratings Outlooks On U.S. Transportation Infrastructure Issuers Revised To Negative Due To COVID-19 Pandemic," published March 26, 2020, on RatingsDirect.

The rating on the BANs reflects our view of the authority's long-term credit characteristics, as well as its ability to access the TIFIA to take out these notes. Under the already executed TIFIA loan, amounts on deposit in the capitalized interest account, and gross receipts secure the 2020 BANs.

A pledge of the expressway's receipts secures bondholders. The rate covenant requirement is that revenues in each fiscal year must equal at least 130% of the long-term debt service requirements for the senior-lien debt. In addition, revenues must equal 110% of the long-term debt service requirements on the senior-lien, subordinate, and TIFIA debt for each fiscal year; and the necessary deposits to the senior, subordinate, and TIFIA reserve accounts. NCTA can issue additional senior-lien bonds if it complies with its rate covenant. In addition, the authority must show that forecast revenue in each fiscal year is at least 140% of the debt service requirement with respect to all senior-lien debt and the proposed debt issuance; and that the revenues are at least equal to 130% of the debt service requirement with respect to all senior-lien and subordinate-lien debt, the TIFIA debt outstanding, and additional debt; and the required deposits to the senior, subordinate, and TIFIA reserve accounts are met. Bondholders also benefit from a debt service reserve fund of $34.9 million on the senior-lien bonds funded with surety policies.

Credit overview

The rating reflects our view that management will implement measures to adapt and moderate impacts from reduced travel, and that we believe forecast financial metrics will remain consistent with the current rating. However, a material and sustained decline in toll revenues and traffic as a result of the COVID-19 outbreak and associated effects could result in a downward rating action if we believe the authority's financial metrics will be diminished for longer than we estimate. For more information, see "Activity Estimates For U.S Transportation Infrastructure Show Public Transit And Airports Most Vulnerable To Near-Term Rating Pressure," June 4, 2020, and "U.S. Economic Update: A Recovery At Risk As COVID-19 Surges," July 22, 2020.

The rating is also based on our opinion of the toll road's strong enterprise risk profile and adequate financial risk profile. Our enterprise risk profile determination incorporates this toll road operating in a relatively large metropolitan area that provides important links within the Raleigh-Durham region, with historically strong traffic demand for a relatively new facility. Our financial risk profile determination incorporates debt service coverage (DSC) metrics that we expect will be pressured but remain at a level we consider adequate, supported by the strong state support for operation and maintenance (O&M) expenses, if needed. Our financial risk profile assessment also considers the Triangle Expressway System's history of consistently exceeding forecasts, although uncertainty remains as a result of COVID-19.

We believe the system's overall market position reflects a toll road operating in its service area that provides important links in the Raleigh-Durham metropolitan region, offset by what we view as a high overall toll structure. Leading into the COVID-19 outbreak, fiscal year-to-date transactions on the expressway through February 2020 were up 8% compared with the same period in 2019. However, quarantines, remote working, mobility restrictions, and other associated effects of the pandemic-induced economic disruption resulted in severe drops in traffic and revenue beginning in March 2020. Total system transactions continue to be affected, with August transactions and revenues down approximately 37%. We note that NCTA has approved 2%-3% rate increases every year, which is not expected to change; this provides predictability and removes potential difficulties associated with rate-setting processes although the road's exposure to competition from free alternative routes could result in dampened demand. However, NCTA has a record of achieving its financial and operational goals, and maintains strong cash reserves. In addition, there is strong state support. The North Carolina Department of Transportation, through its Highway Transportation Fund, has agreed to cover any cost overruns, as well as replenish the O&M reserve fund and the renewal and replacement fund.

Our financial risk profile assessment considered both historical performance, and pro forma figures, which are based on management's forecasts related to the additional debt to fund the Complete 540 Phase 1 project. The pro forma data reflect our expectations of the increased debt burden; anticipated rising annual debt service obligations; aggregate debt outstanding, including the TIFIA loan and BANs; and assumes increases in demand and related revenue growth. The COVID-19 impacts include revenue estimates remaining below fiscal 2019 levels until fiscal 2022, with the net effect of revenues being down approximately $19 million in fiscal 2021 materially worsening DSC in the near term. There is risk associated with rising debt service requirements that rely on strong annual growth in revenues, transactions, and tolls to meet base-case projections of DSC, particularly with the new tolled segment having uncertain traffic levels. However, actual results have exceeded forecasts on the operational segments and we believe that, while dampened in the short term, transactions will resume their positive trajectory, albeit from a lower base, and over time return to historical growth rates.

The Triangle Expressway System extends from the interchange of Interstate 40 (I-40) and NC Highway 147 on the north end to the NC Highway 55 (NC 55) Bypass near Holly Springs, N.C., on the south end, for a total of 18.8 miles. The road also extends the planned and partially complete Outer Loop around the greater Raleigh area. Travelers use a limited-access, six-lane, high-grade facility from I-40 to the NC 55 Bypass near Holly Springs, reducing congestion on the heavily used NC 55. The expressway also improves access to the Research Triangle Park and other employment centers. The initial plan of the Complete 540 project will be to extend the expressway to I-40 southeast of Raleigh. The Complete 540 Phase 1 project is on-time and on-budget with approximately $336 million spent (representing 26% of the plan of finance budget), and $91 million of contingency available.

Key credit weaknesses, in our opinion, are:

- Exposure to potentially prolonged weak or unpredictable toll-road activity as a result of COVID-19 outbreaks and lingering associated effects (such as the pandemic-induced recession, shifting travel restrictions, stay-at-home and social distancing restrictions, or behavioral changes with respect to travel), making effective financial budgeting and planning challenging; and
- A moderately aggressive debt service schedule that relies on steady traffic and increased toll rates on a single asset to meet escalating annual requirements.

Key credit strengths, in our view, are the authority's:

- Liquidity reserves in the general fund of approximately $63.9 million as of June 30, 2020, and the strong state support to replenish the O&M reserve fund and the renewal and replacement fund if needed;
- Extremely strong service area economic fundamentals, which include favorable income levels and economic activity as measured by GDP per capita but recent increases in unemployment associated with impact of the pandemic-induced recession; and
- Very strong management and governance that has established a record of managing and operating its assets. Management conservatively forecast the initial Triangle Expressway ramp-up period, and we expect this strong oversight and prudent governance will continue through the Complete 540 project.

Environmental, social, and governance factors

Our rating incorporates our opinion regarding the health and safety risks posed by the COVID-19 pandemic, which we view as a social factor in our environmental, social, and governance framework that is resulting in significant operating and financial pressures for NCTA. We analyzed the authority's risks related to environmental and governance factors, and consider them to be in line with our view of the standard for the toll road sector. We will continue to evaluate these risks as the situation evolves.

Negative Outlook

Downside scenario

We could lower the rating if we believe that traffic and revenue will fall materially below forecasts, suggesting a weaker market position or lower net revenues that pressure DSC and debt to net revenues.

Return to stable scenario

We could revise the outlook to stable within the next two years if toll activity and revenue trends improve and grow at levels sufficient to support the increasing debt service requirements and O&M expenses as forecast.

Credit Opinion

S&P Global Ratings acknowledges a high degree of uncertainty about the evolution of the pandemic and its effect on the economy and transportation-related activity levels. The consensus among health experts is that the pandemic may now be at, or near, its peak in some regions but will remain a threat until a vaccine or effective treatment is widely available, which might not occur until the second half of 2021. We are using this assumption in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

The U.S. economy has begun what looks to be a long, difficult journey to recover from its pandemic-induced slump. With consumer spending proving largely resilient through the summer of 2020 (helped by federal fiscal stimulus) and unemployment--while still notably high--softening a bit more than S&P Global Economics had forecast, third-quarter GDP is poised for a steeper rebound than many market participants expected. S&P Global Economics expects a 29.5% bounce in third-quarter U.S. GDP (6.7% annualized rate), although that will only partially offset the massive losses in the first half of the year. Our current economic forecasts anticipate ending 2020 at a negative 4.0% real GDP growth rate and rebounding to a slower growth phase heading into 2021 with 3.9% estimated for next year, down from 5.2% in June's economic forecast and weaker than our previous 2021 estimate of 6.2%. The unemployment rate declined to 8.4% in August from its post-1947 record high of 14.75% (in April 2020); however, we don't expect the unemployment rate to reach its pre-pandemic level until mid-2024. Our economic forecasts and macro credit implications associated with the pandemic assume a vaccine or effective treatment is widely available in the second half of 2021. As this sluggish recovery unfolds, three big risks remain: no coronavirus vaccine yet available as the country heads into flu season; a lack of new fiscal stimulus; and trade tensions with China on the rise. (See "Economic Research: The U.S. Economy Reboots, With Obstacles Ahead," Sept 24, 2020.)

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of September 29, 2020)		
North Carolina Tpk Auth toll rds brs		
Long Term Rating	BBB/Negative	Affirmed

Ratings Detail (As Of September 29, 2020) (cont.)		
North Carolina Tpk Auth toll rds brs (AGM)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Tpk Auth toll rds brs (AGM) (SEC MKT)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Tpk Auth toll rds & br (ASSURED GTY)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Tpk Auth triangle expy sys sr lien (AGM)		
Unenhanced Rating	BBB(SPUR)/Negative	Affirmed
North Carolina Turnpike Auth (Complete 540 Phase 1 Proj)		
Long Term Rating	BBB/Negative	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.