RATING ACTION COMMENTARY

Fitch Rates San Francisco International Airport (CA) Revs 'A+'; Outlook Stable

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Fitch Ratings - Austin - 13 Jan 2022: Fitch Ratings has assigned an 'A+' rating to the Airport Commission's, City and County of San Francisco, CA, San Francisco International Airport (SFO) approximately $761 million series 2022A, B, and C second series revenue bonds. Fitch has also affirmed the 'A+' rating on approximately $7.9 billion of parity SFO second series revenue bonds. The Rating Outlook for all of the bonds is Stable.

RATING RATIONALE

The rating reflects SFO's strong operational and financial performance within the normally healthy, yet competitive air trade market in the San Francisco Bay Area. The airport's fully residual airline agreement and proven management team provide a solid framework for stable and competitive results; however, its elevated leverage profile and additional borrowing needs create some pressures on the rating.

While SFO continues to face challenges stemming from the coronavirus pandemic, ongoing actions to manage revenues, costs and debt together with the airport's liquidity position and the award of federal assistance grant funds, are all likely to preserve the airport's sustainable fiscal profile. Leverage peaked above 20x due to the pandemic and will remain elevated as SFO progresses with its capital needs, falling to around 12x by 2026 in Fitch's coronavirus rating case. Cost per enplanement (CPE) averages around $23-$24, excluding

fiscal 2022. These results are reasonable for an international gateway airport and should remain competitive relative to peers and the 'A+' rating level.

KEY RATING DRIVERS

STRONG OPERATIONS, SOME CONCENTRATION - Revenue Risk (Volume): Stronger

SFO serves as a major international gateway airport with a consistently strong 67% market share of passenger traffic within the San Francisco region under normal operating conditions. The airport has a well-balanced traffic profile, with around 80% origination and destination (O&D) traffic and the remainder being a mix of domestic and international connecting traffic. Still, enplanements were down nearly 30% to 20.6 million in fiscal 2020 and fell to just 6.9 million in fiscal 2021, with the coronavirus pandemic expected to impact the traffic base for the next several years.

United Airlines Inc. (United; B+/Stable) maintains a sizable presence at SFO, with around 46% share of the passenger market. United's share has remained relatively constant since 2010 despite its increased seat capacity as growth at SFO has also been driven by the increasing presence of low-cost carriers and service expansion by foreign-flag airlines.

FAVORABLE RATE-SETTING FRAMEWORK - Revenue Risk (Price): Stronger

The current airline use agreement (AUL), extended through fiscal 2023, is fully residual and provides for strong cost recovery with respect to all operating and debt service requirements. Airline charges more than doubled in fiscal 2021 to around $60 due to coronavirus impacts; however, CPE should migrate below $30 by 2023 even in a conservative recovery scenario.

LARGE, DEBT-FUNDED CAPITAL PLAN - Infrastructure Development/Renewal: Midrange

The current capital improvement plan (CIP) is modular and has been scaled back to $6.0 billion from $7.8 billion, with several projects delayed due to the coronavirus. Airport capital needs are well managed and the $5.4 billion current total for the Ascent Program has been contractually committed and is not subject to cost escalation. While the Terminal 3 West modernization is temporarily suspended, recently completed and planned projects are considered necessary to adequately serve the airport's growing user base. Despite the active CIP of $6 billion, SFO's financial projections conservatively include another $2.5 billion in future issuance to fund the full $7.8 billion program through fiscal 2025.

STABLE DEBT PROFILE - Debt Structure: Stronger

SFO has a predominantly fixed rate, fully amortizing debt structure with sufficient covenants and reserves. Management is proactive in seeking opportunities to defease debt, lower interest rate costs through refundings, and fix out variable rate debt, eliminating the need for associated swaps. However, annual debt service obligations will rise and leverage will only return to pre-pandemic levels by the end of the forecast period given the expected new money issuances.

FINANCIAL PROFILE

SFO's debt level is high at nearly $8 billion as of fiscal year-end 2021 and contributes to the airport's high fixed-cost structure. The airport's pre-pandemic net debt-to-cash flow available for debt service (CFADS) ratio is similar to that of peer large-hub airports. Additional borrowings beyond the 2022 issuance to support capital spending could cause debt metrics to temporarily remain slightly elevated, but they should remain reasonable for an international gateway with stronger assessments for both revenue risks (volume and price).

The airport has a strong liquidity position (Fitch calculated 452 days cash on hand [DCOH] for fiscal 2021) and stable coverage levels, demonstrating it can adequately meet its debt service obligations. Fitch forecasts the debt service coverage ratio (DSCR) to remain around 1.4x through fiscal 2026, including permitted transfers (1.1x without).

PEER GROUP

SFO's peers include Los Angeles International Airport (LAX; AA/AA-/Stable), Miami International Airport (A/Stable), and Atlanta International Airport (AA-/AA-/Stable) given their similar prominence as large-hub, international gateway airports. All also have elevated leverage related to large capital needs in support of on-going operations. Behind LAX, SFO benefited from the second strongest enplanement growth in the five years prior to the pandemic. LAX also benefits from the highest DSCR given its hybrid AUL. ATL benefits from the largest pre-pandemic enplanement base and lowest cost structure, though CPE will likely be stressed at all airports in the near-to-medium term given the effects of the coronavirus.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A continued period of material traffic declines in line with or worse than the coronavirus downside case that result in an unsustainably high CPE and materially weaker financial position;

--Post-pandemic, a larger capital program size or additional borrowings leading to sustained leverage above 12x;

--Changes in the airport's traffic profile given the sizable presence of United and the presence of competing airports in San Jose and Oakland.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Upward rating migration is unlikely at this time given SFO's elevated leverage and potentially large additional borrowing needs as traffic recovers.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

TRANSACTION SUMMARY

SFO is expected to issue the series 2022A, B, and C bonds to refund outstanding CP balances previously issued for the CIP; to refund certain previously issued bonds; to pay cost of issuance, make reserve deposits, and fund capitalized interest. The refunding is anticipated to generate approximately $37 million of NPV savings with cashflow savings of $155 million front-loaded over fiscals 2022-2023 to provide near-term relief, while enplanements are impaired from the impact of the coronavirus.

CREDIT UPDATE

For fiscal year end 2021 (June 30), enplanements were down 76% from fiscal 2019. Deeply depressed traffic levels persist into fiscal 2022, such that enplanements are down 49% for

the first four months (through October). However, traffic recovered to 66% of 2019 levels for the month of October, led by stronger performance in domestic traffic as well as an uptick in international traffic. Some variability in the pace of recovery over fiscal 2022 is possible given the effects of the Omicron variant on passenger levels, but should fall within the ranges of Fitch' sensitivity cases.

Despite its slower recovery, Fitch views SFO as an airport with an important role in the national aviation system and a favorable coastal geographic location to support its standing as a prominent international gateway. A pre-pandemic five-year CAGR for 2014-2019 of 4.5% highlights the strength and desirability of the underlying air service area and the 80% O&D traffic levels add stability to volume levels. SFO also continues to enjoy a dominant market share in the Bay Area.

SFO remains especially important to its dominant carrier, United (46%). SFO is United's fifth busiest hub based on scheduled departing seats and plays an important role in United's system as a domestic connecting hub and international gateway. Over the last five years, United has launched service to more international destinations from SFO than from any other hub and has repositioned international equipment from LAX to SFO. Further, United has invested significant capital in SFO and continues to partner with SFO on future capital improvements.

The airport has updated its currently active CIP to $5.95 billion, up slightly from the $5.7 billion at last review, but still down notably from $7.8 billion pre-pandemic as SFO right-sizes the program given pandemic volume losses. Projects totalling $1.6 billion remain suspended based on decisions made in 2020. SFO has spent $5.0 billion on the Ascent Program, which remains on budget. Approximately $5.4 billion (100% of the active portion of Ascent) of aggregate project dollar value is contractually committed and not subject to cost escalation. Suspended elements of the CIP will be restored as dictated by growth as SFO takes advantage of the modular nature of the plan and continues to reassess future CIP scope as recovery evolves.

Fiscal 2021 debt service coverage, taking into account permitted contingency fund transfers of approximately $167 million, $58 million of reimbursed capitalized interest, $295 million of federal aid to offset operating expenses, operating expense reductions, and greatly reduced debt service obligations, increased to nearly 1.7x from just under 1.5x in 2020. On a stand-alone basis, excluding contingency rollover funds, coverage was 1.1x. This coverage level is below performance in recent years but is not unusual given the pandemic

and SFO's residual rate-setting methodology. Looking forward, management forecasts DSCR to remain around 1.4x.

SFO's airline CPE surged to more than $60 in fiscal 2021, given the shock to volume levels and passenger revenues. Management is using a combination of debt service savings from its refunding transactions, federal grants (CARES, ACRGP, and additional stimulus), PFCs, ongoing budget adjustments, and reduced CIP scope to mitigate the rates and charges impact to carriers. CPE should return to around $23 again by 2023 in Fitch's rating case, a level that is competitive for an internal gateway airport with sizeable capital needs. In total, SFO was awarded grants totaling $494.2 million, of which $29.7 million is for relief for concessionaires. SFO used $295 million to pay operating expenses in fiscal 2021 and is forecast to use the remainder ($169 million) to offset operating expenses in fiscal 2022.

The airport is closely monitoring liquidity and was able to grow its DCOH (Fitch-calculated) to 452 days for fiscal 2021. When also including cash-funded debt service reserve funds, leverage in terms of net debt-to-cash flow available for debt service, peaked to 21x, but this is largely a function of the residual agreement and greatly reduced debt service obligations together with lower operating expenses reducing the revenue needs. SFO also increased the CP program to $600 million from $500 million.

FINANCIAL ANALYSIS

Fitch Cases

Fitch regards the assumptions in the Report of the Airport Consultant as reasonable and generally in line with Fitch's views and therefore used it as an input for developing its own coronavirus rating and downside cases. Relative to the rating case, Fitch's coronavirus downside case reflects deeper traffic declines as well as prolonged recovery back to 2019 levels. Given the current economic environment due to the coronavirus pandemic and unlikely stable operating environment over the near term for SFO, Fitch's Coronavirus Rating Case is also considered the Base Case.

Fitch's rating case assumes, relative to fiscal 2019, enplanement recovery to 57% in 2022 followed by recoveries reverting the losses to 26% and 10% in fiscals 2023 and 2024, respectively, and a full recovery by fiscal 2025 with 3.5% growth for 2026. Operating expenses are informed by SFO's own scenario analysis and grow at a 6.2% CAGR for 2021-2026, excluding the $295 million and $169 million offsets to operating expenses in 2021 and 2022, respectively, from federal stimulus monies. Annual PFC utilization is also informed by management and ranges from $0 to $176 million annually. Non-airline,

passenger driven revenues move largely with enplanement fluctuations and airline revenues are calculated to ensure compliance with rate covenants under the residual AUL framework.

Results indicate a slightly weaker, but stable DSCR profile of around 1.4x (including permitted transfers), while cost per enplanement falls to $24 by 2026. Leverage remains slightly elevated with additional borrowing needs, falling to about 12x by 2026.

The downside case follows a similar methodology to the rating case, but forecasts enplanements to recover to a lesser 47% of 2019 levels in fiscal 2022 and a slower recovery trajectory such that a full recovery is not achieved until 2026. Given the fully residual AUL, coverage and leverage metrics are consistent with the rating case, but airline CPE is $2-$4 higher each year excluding 2022.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means 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 Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT ⬍	RATING ⬍		PRIOR ⬍
San Francisco (City & County) Airport Commission (CA) [Airport]			

San Francisco (City & County) Airport Commission (CA) /Airport Revenues/1 LT	LT	A+ Rating Outlook Stable	Affirmed	A+ Rating Outlook Stable

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APPLICABLE CRITERIA

Airports Rating Criteria (pub. 22 Oct 2020) (including rating assumption sensitivity)

Infrastructure and Project Finance Rating Criteria (pub. 23 Aug 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

GIG AST Model, v1.3.1 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

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