

Memorandum



CITY OF DALLAS

DATE August 27, 2021

TO Honorable Mayor and City Council

SUBJECT **Moody's Investors Service Affirmed 'A1' Rating and Stable Outlook for Love Field Airport Modernization Corp. (LFAMC) Revenue Bonds- INFORMATION**

On August 24, 2021, Moody's Investors Service (Moody's) affirmed the 'A1' credit rating and stable outlook on the outstanding Love Field Airport Modernization Corp. (LFAMC) General Airport Revenue Bonds following a review of outstanding LFAMC debt. The Moody's report states that the rating affirmation reflects the "positive credit effects provided by ample interest savings that will result from the proposed restructuring of LFAMC debt onto the city's senior lien," while "the stable outlook reflects Moody's expectations that Love Field will continue to outperform national recovery levels, that existing liquidity and remaining COVID relief grants will be sufficient to manage through the downturn, and that the proposed debt service profile that backloads debt service savings is achieved."

According to Moody's report, there are certain factors that could have a negative impact on the rating, including "net revenue DSCR [debt service coverage ratio] below 1.2x after covid relief funds are exhausted," "sustained negative enplanement trends," "a significant deterioration in the credit quality of Southwest Airlines Co. (Baa1 stable) below investment grade," and "significant capital improvement projects to address airport access without improved revenue collection." However, high exposure to Southwest Airlines Co. risk "is mitigated by Southwest's headquarters adjacent to the airport and Southwest's credit strength," which "minimizes the risks of severe cuts at the airport by the airline." Additionally, the rating "positively incorporate the economic strength of the Dallas-Fort Worth service area that mitigates the outsize exposure to Southwest Airlines Co." Moody's further explains that "the airport's low leverage compares favorably to other airports with recently reconstructed terminal facilities and expected leverage levels for airports that are currently under major terminal reconstruction."

Attached is the published report for your review. Please let me know if you need additional information.

A handwritten signature in blue ink that reads "M. Elizabeth Reich".

M. Elizabeth Reich
Chief Financial Officer

[attachment]

c: T.C. Broadnax, City Manager
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Directors and Assistant Directors

MOODY'S

INVESTORS SERVICE

Rating Action: Moody's affirms A1 on Dallas (City of) TX Airport Enterprise revenue bonds; outlook is stable

24 Aug 2021

New York, August 24, 2021 -- Moody's Investors Service has affirmed the A1 on Dallas (City of) TX Airport Enterprise \$205 million outstanding general airport revenue bonds and A2 on subordinate lien bank bonds. The bonds were issued by the Love Field Airport Modernization Corporation, TX (LFAMC) on behalf of the airport enterprise. The outlook is stable.

RATINGS RATIONALE

The A1 rating affirmation on senior lien bonds reflects positive credit effects provided by ample interest savings that will result from the proposed restructuring of LFAMC debt onto the city's senior lien, instead of being directly paid by Southwest Airlines Co. (Baa1 stable), that offset dilution of existing senior lien bondholders. Though the proposed restructuring will result in acutely reduced senior lien net revenue debt service coverage ratio (DSCR), to roughly 1.2x from the roughly 2.4x expected if the structure remained the same, the airport's total obligations will amortize more rapidly. Well above average passenger recovery at the airport and remaining covid relief funds allow principal payments to be relatively front-loaded and result in lower debt service and obligations in the medium- to long-term. The additional debt service capacity in outer years provides opportunity to layer in debt expected with the airport's modest capital plan while keeping airlines costs low and DSCR stable.

The ratings positively incorporate the economic strength of the Dallas-Fort Worth service area that mitigates the outsize exposure to Southwest Airlines Co. (Baa1 stable), the long term use and lease agreement that matures in 2028 and low leverage, inclusive of the obligations for the revenue credit, of \$149 adjusted debt per O&D enplanement in fiscal 2019. The airport's low leverage compares favorably to other airports with recently reconstructed terminal facilities and expected leverage levels for airports that are currently under major terminal reconstruction.

The ratings are constrained by the high exposure to Southwest, which accounted for 95% of enplanements in fiscal 2020 and more than any other rated airport, but that risk is mitigated by Southwest's headquarters adjacent to the airport and Southwest's credit strength. Each minimizes the risks of severe cuts at the airport by the airline. The rating is also constrained by federal limitations on Love Field's ability to grow and substantial competition from larger and relatively unconstrained Dallas-Fort Worth International Board, TX (DFW, A1 stable). However, Southwest is discouraged from serving DFW by the same federal agreement that limits Love Field's size through 2025.

RATING OUTLOOK

The stable outlook reflects Moody's expectations that Love Field will continue to outperform national recovery levels, that existing liquidity and remaining COVID relief grants will be sufficient to manage through the downturn, and that the proposed debt service profile that backloads debt service savings is achieved.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

-Sustained DSCR above 2.0x times on all obligations

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

-Net revenue DSCR below 1.2x after covid relief funds are exhausted

-Sustained negative enplanement trends

-A significant deterioration in the credit quality of Southwest Airlines Co. (Baa1 stable) below investment grade

-Significant capital improvement projects to address airport access without improved revenue collection

LEGAL SECURITY

The bonds are secured by a financing agreement between the city and LFAMC. The city will deposit net revenues of the airport system into a trust account. Bonds will be additionally secured by a cash-funded debt service reserve sized at the standard 3-prong test. An additional bonds test will apply that will require 1.25 times coverage.

PROFILE

The primary source of revenues will come from Love Field, which has 20 gates, 3 runways, and approximately 11,000 parking spaces. The airport is a primary airport for Southwest Airlines and facilitates connecting passenger flow across the Southwest system. The enterprise also operates Dallas Executive Airport, a general aviation airport on the southwest side of the city of Dallas.

METHODOLOGY

The principal methodology used in these ratings was Publicly Managed Airports and Related Issuers published in March 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1140469. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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