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Fitch Affirms Port of Houston Authority, TX ULTGOs at 'AAA'; Outlook Stable

Fitch Ratings-Austin-27 August 2013: Fitch Ratings has taken the following rating action on the Port of Houston Authority, Texas' (POHA, or the authority) unlimited tax general obligation bonds (ULTGO):

--\$731.9 million ULTGO bonds affirmed at 'AAA'.

The Rating Outlook is Stable.

SECURITY

The bonds are secured by an unlimited property tax levied on all taxable property within the authority's taxing boundaries, which are essentially coterminous with Harris County, TX (the county; ULTGO bonds rated 'AAA' by Fitch).

KEY RATING DRIVERS

LARGE AND DIVERSE ECONOMY: Energy and petrochemical manufacturing are the economic engines of the Houston regional economy, complemented by good diversification in biomedical research, healthcare, aerospace, and international trade via the Port of Houston (the port).

STRONG RECOVERY FROM RECESSION: Area job, population, and taxable value gains coming out of the national recession are quite strong. However, the economy remains susceptible to energy price changes.

STRONG FINANCIAL PERFORMANCE AND POSITION: The authority continues to exhibit good financial performance and has maintained its sizable liquidity position while investing its cashflow in capital expenditures.

PORT'S INHERENT ECONOMIC IMPORTANCE: The Port of Houston is one of the nation's largest maritime ports, ranking second among all U.S. ports in total tonnage. The port's shipping and trade activities support a significant number of jobs and economic activity throughout the region and the state.

LARGE CAPITAL PLAN: The authority's forward-looking capital improvement plan (CIP) positions it for continued pre-eminence as a major national port, with expansion to its cargo and ship capacity needed to accommodate an anticipated increase in demand.

ABOVE-AVERAGE DEBT BURDEN: The capital intensive nature of port operations and large number of overlapping taxing entities bring the overall debt burden to above-average levels, and principal payout is slow. Debt levels will likely remain elevated but within a range acceptable for the high rating.

RATING SENSITIVITIES

PORT OPERATIONS: A material shift in the currently strong operating metrics and financial position of the port could affect the authority's ULTGO rating. The Stable Outlook reflects Fitch's view that such shifts are unlikely over the near term.

DEBT PROFILE: An increase in overall debt levels beyond current expectations could also lead to a change in the rating.

CREDIT PROFILE

The authority is the local sponsor of the 52-mile Houston Ship Channel, and owns and operates the public terminals of the Port of Houston. The authority's large and diverse tax base encompasses Harris County, including the city of Houston. Harris County's population, estimated at 4.2 million, makes it the largest county in Texas and the third largest in the nation.

LARGE AND DIVERSE TAX BASE COTERMINOUS WITH HARRIS COUNTY

Energy and petrochemical manufacturing remain the major determinants of employment and tax base growth for the area, although the immense Houston MSA economy has also diversified into biomedical research, healthcare, aerospace, and international trade (via the port). The area is home to 26 Fortune 500 corporate headquarters.

The industry diversity has also helped offset job losses associated with the merger of Continental Airlines with United Airlines and the recent and planned NASA-related layoffs resulting from the end of the space shuttle program and the federal sequestration. In addition, the diversity between up-stream (exploration & production) and down-stream (refining & chemical manufacturing) users of oil & gas provides some stability during price swings of these commodities.

Net job gains in the Houston MSA continue to outpace those of many other large U.S. cities coming out of the recession, led by the energy and construction sectors. Regional employment registered a notable increase of 2.7% in the 12-month period ending in June 2013, and the local unemployment rate of 6.8% for the month was down from 7.5% in the same period last year and is consistent with the state average and below the U.S. rate (7.8%). The metro population continues to expand at an annual rate of nearly 2%, in line with state growth trends and double the U.S. average.

The authority's taxable assessed value (TAV) has resumed good growth following a one-year

recessionary decline in 2011, climbing 1% in 2012 and 5% in 2013. The top 10 taxpayers make up only 5.5% of TAV, although many are oil and gas firms.

POSITIVE MARGINS AND STRONG CASH POSITION

Liquidity remains very high; the authority concluded fiscal 2012 with unrestricted cash and cash equivalent balances at \$236.9 million or over one-year of cash-on-hand. Cash balances remain comfortably above management's informal minimum of \$50 million, inclusive of a \$35 million contingency reserve. Port operating margins have been strong if somewhat volatile, declining to the 20% range during the economic downturn, but have averaged 28% since fiscal 2006. The port improved its margin to 36% in fiscal 2012.

General cargo tonnage revenues have averaged 1.8% annual growth over the last five years, which is notable as this includes a large 21% decline in 2008 commensurate with the economic downturn. Bulk revenues have decreased slightly by an annual average of 0.7% over the same period. Since 2010, general cargo has resumed strong annual growth while bulk has shown less recovery. Property taxes are levied only to the extent necessary to pay debt service on voter-authorized ULTGO bonds.

Authority management is expecting to generate \$35.5 million of net income in fiscal 2013 based on year-to-year results through June, which compares favorably to the adopted budget's net income of \$33.8 million. Tonnage statistics through June show general cargo tracking essentially equal to 2012 traffic and bulk cargo up 16% year-over-year, countered by auto units down 22% year-over-year.

Forecasts indicate total annualized operating revenues of \$252 million, up 8% from 2012 revenues. On the spending side, budgeted headcount was reduced by 3% from 2012 as part of management's right-sizing efforts for staffing, and currently filled positions equal 93% of budgeted positions. Fitch views fiscal 2013 projections as realistic given the district's historical

track record of good budget-to-actual results.

ELEVATED DEBT BURDEN; VERY LARGE CIP TO BE CASH- AND DEBT-FUNDED

Overall debt ratios are elevated at 5.9% of market value (MV) and \$5,603 per capita. The port's debt portfolio consists entirely of ULTGO debt, the repayment of which is slow at only 30% retired in the next 10 years.

The authority is in the midst of funding its sizable capital improvement program to build new freight and ship terminals and to deepen the channels into its Bayport and Barbours Cut container terminals to accommodate larger ships. The authority's capital needs are being driven to a degree by increased demand for the port resulting from the expansion of the Panama Canal that should be completed by 2015 (delayed from 2014) - the port is one of the closest major ports in the Gulf of Mexico to the canal.

The port's five-year CIP calls for total spending of just over \$1 billion and will be funded with a combination of cash and debt. The port plans to spin off between \$77 million and \$90 million of annual cashflow for capital expenditures. Debt plans include the use of a \$300 million revolving credit facility secured by port (non-tax) revenues in late fiscal 2014 and additional debt (GO or port revenue debt) in fiscal 2016. Fitch expects that management will maintain its prudent cash cushion targeted at a minimum of \$50 million to \$75 million. Additionally, some of the capital projects are demand-driven and can be reduced or eliminated if growth in cargo does not materialize, and Fitch views the authority's successful implementation history as a credit positive.

The authority's exposure to retiree liabilities has been significantly diminished by the closure of its well-funded defined benefit pension plan to staff hired after Aug. 1, 2012, and the proactive establishment of an asset trust in fiscal 2011 for other post-employment benefits (OPEB) for retiree healthcare. The closed pension plan is funded at 93% as of the most recent Dec. 1, 2012

valuation using the plan's 7.25% discount rate (estimated to be 90% funded when Fitch uses a more conservative 7% discount rate). The OPEB trust had a \$16 million cash balance to conclude fiscal 2012, relative to the \$56 million unfunded liability, which equals a nominal 0.01% of full MV.

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In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, National Association of Realtors.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria' (Aug. 14, 2012);

--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

Applicable Criteria and Related Research:

[Tax-Supported Rating Criteria](#)

[U.S. Local Government Tax-Supported Rating Criteria](#)

Additional Disclosure

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