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Research Update:

Halifax Port Authority 'A+' Rating Affirmed On Strong Financial Performance; Outlook Stable

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Research Update:

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Overview

- We are affirming our 'A+' long-term issuer credit rating on Halifax Port Authority (HPA) on continued strong financial performance.
- The rating reflects the authority's stand-alone credit profile, which we assess at 'a-', and a "moderately high" likelihood of support from the government of Canada.
- The stable outlook reflects our view of the HPA's prudent financial management of its capital program to date and our expectation that it will maintain strong financial metrics with debt service coverage ratios of about 15x as per our base-case scenario.

Rating Action

On Aug. 6, 2015, Standard & Poor's Ratings Services affirmed its 'A+' long-term issuer credit rating on the Halifax Port Authority (HPA). The outlook is stable.

Rationale

The rating reflects our view of the HPA's stand-alone credit profile (SACP), which we assess at 'a-' on what we view as healthy operating and financial performance. The ratings also reflect our opinion of a "moderately high" likelihood that the federal government would provide extraordinary support in the event of financial distress, which results in a two-notch uplift to the rating.

In accordance with our criteria for government-related entities (GREs), our view of the HPA's moderately high level of support reflects our assessment of the "limited" link with the federal government because ports operate as nonshare capital corporations, with general roles and responsibilities set out in the Canada Marine Act with little involvement by the federal government in day-to-day operations. We also base this on our assessment that the role of the HPA is "very important" to Canada because ports provide essential infrastructure that is strategically important to Canada's international trade and effectively hold a monopoly position in their respective regions.

The SACP reflects Standard & Poor's view of the following factors:

- The HPA's strategic location on the east coast of North America, with its natural deep harbor and supporting infrastructure, which give it a competitive advantage as a first-in and last-out port for Southeast Asia

container traffic traveling through the Suez Canal;
- The authority's strong business position and natural advantages that have made it Canada's fourth-busiest container port after Vancouver; Montreal; and Prince Rupert, B.C. The HPA's natural advantage of ice-free harbor result in it being one of only two ports on the east coast able to attract and service the larger postpanamax and super-postpanamax vessels;
- Our view that, as a landlord port, the authority has a fairly stable revenue stream compared with that of some peers. In 2014, total revenues rose modestly by 1.0%, compared with a noteworthy 10.3% the previous year. Moderate increases in berthage and wharfage offset declines in harbor dues and cruise revenues resulting in revenue stability. In addition, we attribute the stability of the HPA's revenue base to the significant share of its 2014 revenues from fixed-revenue streams;
- The HPA's strong financial profile as reflected in relatively low debt, which we expect will peak in 2015 to fund moderate capital spending requirements before beginning to decline. Nevertheless, in our view, despite the increase, the authority's debt burden will remain low relative to that of peers. Standard & Poor's expects that the HPA will remain well-beneath its C$75 million borrowing limit in the medium term. In addition, in our base case scenario, we expect HPA to record a healthy DSCR of about 15x in 2015 and then improving thereafter as its debt is repaid;
- The authority's exposure to risks inherent in a cyclically driven sector and potentially having to offset declines in its revenues from unexpected losses in shipping lines calling on the port. As well, the HPA faces strong competitive pressures from other East Coast container ports such as the Port of Montreal and the Port Authority of New York and New Jersey. Cargo volumes of 400,063 twenty-foot equivalent units (TEUs) in 2014 declined by about 9.5% compared with those of the previous year. Results for the first half of 2015 reflect somewhat reduced volumes, as TEUs to date have decreased about 4.5% compared with that of the same period in 2014 as a result of the harsh winter in North America, Europe, and the North Atlantic. We believe mitigating this risk is the relative stability from the HPA's diversified revenue sources such as rental revenues from land holdings and other lines of business as well as its strategic plan to enhance relationships with the end users of shipping lines; and
- Operational risks inherent in the authority's dependence on a single rail line -- Canadian National Railway Co.

Liquidity

The HPA's liquidity position is adequate, in our opinion. The authority typically relies on its cash flow from operations to fund its capital program. As a result, cash balances have been what we view as low. As of Dec. 31, 2014, the HPA had cash balances of about C$146,000. Nevertheless, the HPA has access to a revolving bank facility with a maximum limit of C$45 million, of which almost C$15 million was available at year-end 2014. Through a combination of cash balances and external liquidity available through the undrawn balance of the line of credit, the authority had sufficient liquidity to cover about 247 days of operating expenses.

Outlook

The stable outlook reflects our view of the HPA's prudent financial management to date and our expectation that it will not issue significantly more debt in the next two years than it assumes in its current capital plan. We also expect that the authority will continue to record moderate cargo and revenue growth in the two-year outlook horizon and that, as per our base-case scenario, it will also continue to produce strong annual DSCR of about 15x despite its debt peaking in 2015.

Although unlikely in the next two years, if the government increases the strength or durability of its relationship with its port authorities through revised regulation that leads to significantly more oversight, we could revise the link between the federal government and HPA to strong, leading to an upgrade. In addition, we do not expect an upgrade in the near term given the expected, albeit moderate, debt issuance and the inherent volatility of the cyclical sector in which the HPA operates. Conversely, although we believe it is unlikely, material weakening of the authority's financial risk profile as reflected in a material and sustained narrowing in its DSCR to less than 5x because of a significant deterioration in total revenues could result in a negative rating action.

Related Criteria And Research

Related Criteria

- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria: Port Facilities Revenue Bonds In The U.S. And Canada, March 19, 2014

Ratings List

Rating Affirmed

Halifax Port Authority
 Issuer credit rating   A+/Stable/--

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