MOODY'S
INVESTORS SERVICE

CREDIT OPINION
12 February 2016

Update

Hawaii (State of) Port Facility

Update: Moody's affirms A2 on Hawaii Port Facility's senior lien revenue bonds; Outlook is stable

Contacts

Kurt Krummenacker 212-553-7207
VP-Sr Credit Officer/ Manager
kurt.krummenacker@moodys.com

Chee Mee Hu 212-553-3665
MD-Project Finance
cheemee.hu@moodys.com

Christopher Yared 212-553-2998
Associate Analyst
christopher.yared@moodys.com

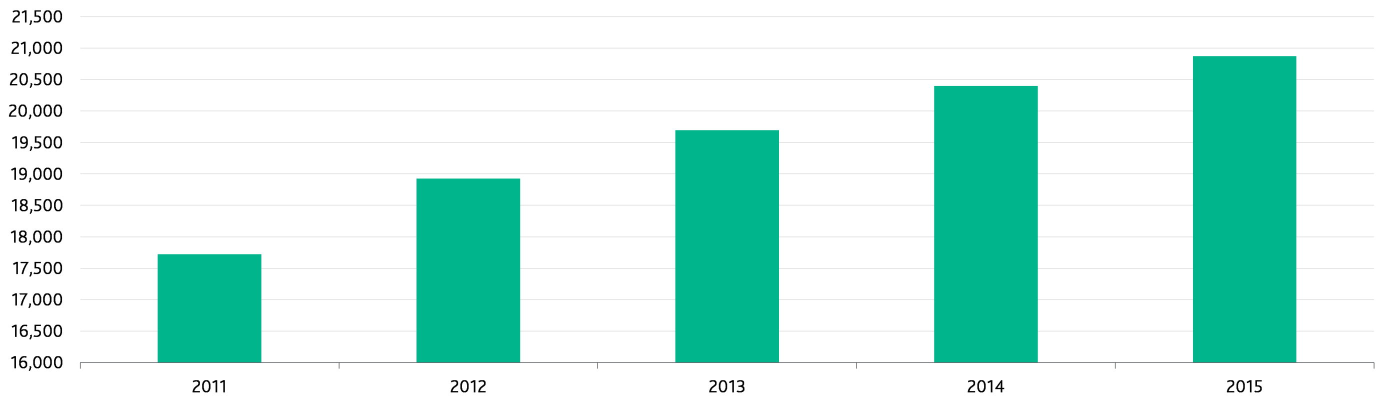
Summary Rating Rationale

Moody's Investors Service has affirmed the A2 rating on all series of the State of Hawaii's Port Facility senior lien bonds totaling $368.7 million. The rating outlook is stable.

The A2 rating is based on the harbor system's near-monopoly position in providing port services for seaborne cargo and cruise passengers into the state and among the state's islands, the solid debt service coverage projected from recently increased tariff rates, and the history of volatile cargo and cruise passenger levels. A growing Hawaiian economy should continue to drive demand for goods shipped through the harbor system. The system expects to issue a sizable amount of debt in the 2016 time frame to fund its new capital improvement program, but we believe the incremental effect on debt service coverage ratios and leverage metrics is mitigated by the substantial liquidity position of the port.

The system's proposal to reduce the debt service reserve fund (DSRF) requirement to 50% of maximum annual debt service and the fulfillment of that requirement with sureties is a credit weakness. The system's proposed change to the DSRF requires consent from 100% of bondholders, which is not expected before 2017. The provision will change the DSRF requirement to 50% of the maximum annual debt service requirements from the lesser of average annual debt service or the maximum amount allowable by the tax code. Moody's believes this change materially reduces bondholder protection for instruments issued under the 1997 Certificate that governs the division's revenue bonds and will make the credit more sensitive to other changes in credit strength.

Exhibit 1
Total Cargo Tonnage ('000)



Source: Moody's Investors Service

Credit Strengths

» Strong monopoly position and highly essential asset to island economy that derives revenues from cargo, shipping containers, and cruise passengers

» Debt service coverage ratios above 2.0 times, though we expect coverage levels to fall slightly as a result of upcoming bond offer

» Tariff increases over the past several years have led to a substantial increase in liquidity providing financial flexibility to manage operational and financial risks

» Strong cargo and container growth since 2011 driven by demand from a growing Hawaiian economy

Credit Challenges

» Exposure to potential volatility due to economic concentration in tourism and concentration in largest shipping line (Matson Navigation Company 43% of FY2015 cargo)

» Debt service reserve requirement is being reduced to 50% of MADS once 100% of bondholders consent to the change

» Flow of funds permits outflow to State of funds in excess of 150% of coming year's requirements, though outflows have been limited in recent years

Rating Outlook

The stable outlook reflects our expectation that container volumes and revenues will remain flat or grow near the 3% scheduled annual tariff increase. We expect future borrowing will only mildly affect debt service coverage ratios which are strong at over 2.0 times.

Factors that Could Lead to an Upgrade

» Significant and sustained higher-than-projected operating revenues due to increased volumes or rate increases, with resulting higher net revenue coverage sustained materially 2.0 times for all debt

» Continued strong liquidity

Factors that Could Lead to a Downgrade

» Decline in liquidity ratios

» Decline in total debt service coverage by Moody's net revenue calculation sustained below 1.75x

Key Indicators

Exhibit 2

HAWAII (STATE OF) PORT FACILITY

	2011	2012	2013	2014	2015
Total Cargo Tonnage ('000)	18,817	19,082	19,842	20,395	20,871
Debt Outstanding ($'000)	419,971	410,547	396,828	382,221	366,872
Debt to Operating Revenues (x)	4.9	4.0	3.5	3.2	3.0
Days Cash on Hand (days)	1,142	1,095	1,142	1,373	1,700
Senior Lien Debt Service Coverage By Net Revenues (x)	1.59	2.05	1.95	2.36	2.50
Total Debt Service Coverage By Net Revenues (x)	1.45	1.84	1.78	2.13	2.25

Source: Moody's Investors Service

Recent Developments

Hawaii's economy has experienced significant growth driven by low oil prices, which both lowers the cost of goods shipped to the island, and increases tourism as flights are cheaper. Even amid a global slowdown driven by reduced growth in China and other developing Asian countries, Hawaii has seen solid growth at the port with operating revenues increasing 1.5% from 2014 to 2015, while operating expenses decreased by 1.5% over that same time frame. Moody's rates the state of Hawaii Aa2 with a positive outlook owing to strong construction activity throughout the state, high levels of tourism and hotel occupancy, low unemployment, and renewed federal military spending.

The system's capital improvement plan calls for the issuance of about $250 million around April 2016, which will go to fund a new container terminal at the Kapalama Military Reservation. The project is expected to be completed by 2019 and will add 80 additional acres of land-side facilities and provide the harbor system with redundant systems to mitigate the effect of natural disasters. Phase 2 is expected to begin in 2018 with an additional $200 million needed for the project; current plans anticipate funding sources to include liquidity on hand as well as a future bond offering.

Detailed Rating Rationale

Revenue Generating Base

The commercial harbors that make up the harbor system consist of ten harbors on six islands. The Harbors System is essential to the Hawaiian economy as 80% of goods imported or exported from the state travel through the system. The system is self-sustaining and is authorized to impose rates and charges sufficient to cover its operating and maintenance expenses as well as debt service costs.

The Harbors Modernization Plan (HMP) is a set of system-wide projects to improve and expand port infrastructure throughout the state. The largest HMP project by size, the new container terminal at Kapalama, will improve container transfer efficiency in Honolulu Harbor. The project is expected to cost $450 million inclusive of a $250 million bond issue. Other key projects include the $47 million construction of an inter-island terminal pier, which is commencing construction in February 2016, as well as Pier 35 building and site improvements, which will complete construction in February 2016 with the tenant expected to move in by March 2016. The New Kumau Street Extension project, which cost $6.2 million has been completed along with Pier 2 Terminal Improvements at Kawaihae Harbor, an $8.5 million project.

Financial Operations and Position

Revenue levels continue to improve albeit at a lower rate as the new tariff rates have all been implemented save for a 3% annual escalation going forward. FY 2015 showed increases in operating revenues of 1.5%, while operating expenses decreased 1.5% over the same period. The tariff increases have bolstered debt service coverage to over 2.25 times in 2015, based on Moody's net revenue coverage calculation. Coverage is expected to drop slightly with the additional planned bond issuance in Q1 2016.

The division's cash balances remain a key stabilizing factor for the rating. Days cash on hand jumped from 1,373 days at the end of FY 2014 to 1,700 in FY 2015, representing $204.5 million in unrestricted cash and cash equivalents. During the year, the system generated almost $40 million of cash, which considerably added to the system's liquidity position. Moody's believes strong liquidity is an important credit consideration for the system given the volatility of cargo levels and the proposed decrease in the debt service reserve requirement discussed above layers an additional need for liquidity at the current rating level.

Cargo tonnage and volume have exhibited a steady recovery. Container volume and total cargo tonnage showed improvement with increases of 7.2% and 2.3%, respectively in FY 2015. Pipeline throughput increased 5.7%, while cruise passengers fell 12%; however, the fall reflects a change in procedure for how passengers are counted. Moody's expects volumes to remain stable and trend primarily with the recovery of the state economy.

Including the portion of state GO debt that the harbor system is legally obligated to pay, the system has $369 million of debt outstanding and is contemplating an additional bond issue in Q2 2016 of $250 million. While this sizable increase in leverage will weigh on the system's financial flexibility, we expect a strong Hawaiian economy combined with a sound liquidity position to offset the risk of lower financial metrics.

In 2015, debt service coverage was 2.25 times on a Moody's net revenues basis. We expect coverages to slightly decrease as a result of the new Q2 2016 offering such that coverages will likely fall closer to 1.75 times.

LIQUIDITY

Liquidity has increased rapidly in recent years as tariff increases pushed revenues higher, while operating costs were generally flat. In 2015, liquidity as measured by days cash on hand increased to 1,700 days from 1,373 days the year prior mainly due to increased cash from operations. The system forecasts continued strong cash flows and liquidity, though it does expect to use some of its available funds for future capital expenditures.

Debt and Other Liabilities

DEBT STRUCTURE

Total System Debt Outstanding of $368,715,970 is comprised of the following series, including a portion of general obligation debt issued by the state of Hawaii, for which the port is responsible paying debt service.

Series 2004B - $17,775,000

Series 2006A - $74,710,000

Series 2007A - $36,000,000

Series 2010A&B - $186,620,000

Series 2013 (unrated) - $22,435,000

State of Hawaii General Obligation debt payable by the Harbor System - $31,175,970

All of the debt is fixed-rate. Debt service payments are flat through 2023, and decline substantially thereafter; however, an anticipated bond sale in April 2016 is expected to extend the authority's flat debt payments for several years. All bonds outstanding today will mature by 2041.

DEBT-RELATED DERIVATIVES

None.

PENSIONS AND OPEB

The financial impact of unfunded and OPEB obligations of this issuer are minor and thus not currently a major factor in our assessment of its credit profile.

Management and Governance

The Hawaii Department of Transportation is one of 18 principal executive departments of the state of Hawaii tasked with maintaining and operating transportation facilities of the state, which includes the state's harbors. Through the Harbors Division, the Director of the Department of Transportation oversees the financial and operational management of the state's ten ports. The director is appointed by the governor and confirmed by the State Senate. Directors serve four-year terms coterminous with the governor's term.

Legal Security

The bonds are special limited obligations of the state, payable solely from the Harbor Special Fund, into which the State is obligated to deposit revenues after accounting for operating and maintenance expenses. Moody's notes the open flow of funds allows the state to transfer excess revenues to the state general fund, but these transfers have been immaterial in recent years.

The bonds are secured by a 100% MADS debt service reserve fund, which is expected to step down to a 50% MADS reserve fund upon either refunding or maturity of the Series 2004B and Series 2006A bonds. The debt service reserve is funded in cash apart from the reserve for the Series 2010A&B bonds, which is funded with a surety from Assured Guaranty Municipal Corporation (A2, stable). A rate covenant of 125% of debt service and an additional bonds test of 125% debt service coverage provide further security to the bonds.

Use of Proceeds

Not applicable

Obligor Profile

The Harbors System is responsible for running ten commercial ports on six islands throughout the state. The authority is charged with the operations and maintenance of these facilities.

Methodology Scorecard Factors

OTHER CONSIDERATIONS: MAPPING TO THE GRID

The grid is a reference tool that can be used to approximate credit profiles in the U.S. Public Power Electric Utility industry in most cases. However, the grid is a summary that does not include every rating consideration. Please see the Public Port Revenue Bonds Methodology for more information about the limitations inherent to grids.

The actual rating of A2 differs from the scorecard indicated rating of A1 due to the sizable debt issue expected in 2016 to fund the container terminal at the Kapalama Military Reservation. The project is expected to substantially increase debt service and tighten the port’s financial flexibility on a forward looking basis.

Exhibit 3

Factor	Subfactor	Score	Metric
1. Market Position	a) Port Size (Operating Revenues) (000s)	A	123,209
	b) Quality of Service Area and Competition	Aaa	
	c) Operational Restrictions	Aa	
2. Diversity and Volatility	a) Financial Revenue Variation (5-year operating revenue CAGR)	Aaa	
	b) Customer Diversity	B	
3. Capital Program	a) Capital Needs Requiring Leverage	B	
4. Key Credit Metrics	a) Net Revenues DSCR (3 year avg)	Aa	2.27
	b) Debt to Operating Revenue (3 year avg)	A	3.22
Notching Considerations		**Notch**	
	1 - Tax Support for Operations	0	
	2 - Liquidity- Cash to Debt	0	
Scorecard Indicated Rating:		**A1**	

Source: Moody's Investors Service

Methodology

The principal methodology used in this rating was Public Port Revenue Bonds published in December 2013. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

REPORT NUMBER 1011767

MOODY'S
INVESTORS SERVICE