MOODY'S
INVESTORS SERVICE

CREDIT OPINION
31 March 2021

Rate this Research

Contacts

Kathrin Heitmann +1.212.553.4694
VP-Senior Analyst
kathrin.heitmann@moodys.com

Kurt Krummenacker +1.212.553.7207
Senior Vice President/Manager
kurt.krummenacker@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Port Authority of Guam

Update to credit analysis

Summary

The Port Authority of Guam (Baa2 negative) is the sole commercial port in Guam, handling around 90% of the territory's imported cargo, including a significant portion of military cargo. Leverage is low (2.9x adjusted debt to operating revenue in fiscal 2019) and liquidity remains strong. The port remained fully operational during the coronavirus pandemic. We expect that the authority will maintain healthy credit metrics with debt service coverage (DSCR) around 2.0x in fiscal year 2020 and close to 2.0x in fiscal year 2021.

Constraining credit factors include the small scale, high customer concentration, exposure to weather-related events, the linkages to the credit quality of the Government of Guam and a high fixed cost base as an operator port.

Credit strengths

» Monopoly position as the sole commercial port in Guam

» Stable cargo trends despite coronavirus restrictions

» Low leverage

» Solid liquidity

Credit challenges

» Small scale of operations and high customer concentration

» High fixed cost base

» Linkages to the Government and risk of slow recovery in tourism arrivals and economic activity as result of the coronavirus

» Execution of capital plan on budget and continued focus on maintenance

Rating outlook

The negative rating outlook reflects our assessment of the linkage between the port authority and the financial health and stability of the Government of Guam (Ba1 negative).

Factors that could lead to an upgrade

» Sustained volume growth that supports Moody's net revenue DSCR above 2.0x

» Diversification of the port authority's customer base

- Visibility that the port authority will complete the capital program on time and on budget and will maintain capital equipment in a state of good repair
- Days cash on hand maintained above 500 days on a sustained basis
- Improvement in the government's financial position and liquidity

Factors that could lead to a downgrade

- Erosion of the government's financial position and liquidity or deteriorating local economic conditions that would negatively impact the authority's financial flexibility
- Loss of a material customer
- Moody's net revenue DSCR below 1.5x
- Liquidity levels falling to around 225 days cash on hand on a sustained basis

Key indicators

Exhibit 1
Port Authority of Guam

	2015	2016	2017	2018	2019
Operating Revenues ($'000)	48,448	52,549	50,753	54,330	55,236
Debt Outstanding ($'000)	18,385	19,833	21,210	71,445	70,125
Adjusted Debt ($'000)	87,534	88,422	113,319	159,230	160,040
Adjusted Debt to Operating Revenues (x)	1.81	1.68	2.23	2.93	2.90
Total Days Cash on Hand (days)	210	312	314	415	403
Total Debt Service Coverage by Net Revenues (x)	6.90	7.26	4.27	2.71	2.44

All ratios are as defined and as adjusted by Moody's Investors Service.
Source: : Moody's Investors Service, Audited financial statements Port Authority of Guam

Profile

The Port Authority of Guam operates the Jose D. Leon Guerrero Commercial Port of Guam, the only commercial port in Guam. The port has a cargo terminal, industrial terminal, six cargo handling berths, cargo handling equipment and numerous support buildings and facilities. The authority generates all of its revenue from tariffs charged to its customers. The Public Utilities Commission (PUC) of Guam needs to approve tariffs since 2009. The port authority handles more than 90% of the island's total imports and around 30% of military-related cargo.

Detailed credit considerations

Revenue generating base

Operating revenue remained fairly stable during coronavirus pandemic

Cargo trends fluctuate with economic activity in Guam. However, the coronavirus pandemic had limited impact on PAG's cargo tons and operating revenue in fiscal year 2020, ending September 30, 2020. PAG processed 85,143 containers similar to fiscal 2019. Unaudited preliminary operating revenue declined by a modest 1.6% to $45.3 million and total revenue was around $54.7 million in fiscal year 2020. Management maintained good cost control in fiscal year 2020 and was able to generate positive net income. Trends have remained favorable throughout January 2021.

Continued military construction on projects in Guam will support future cargo volumes. Nevertheless, the coronavirus pandemic has brought tourism activity in the territory to a standstill and a prolonged decline in tourism activity could cause financial stress at the government level and a reduction in economic activity. We note positively that the territory is making substantial progress in vaccinating its population and is targeting a reopening of the economy in May/June of this year.

Revenue from container volumes represent around 80% of the port authority's operating revenue. Transshipments represent around 30% of total containers and total TEU but less than 10% of operating revenue. Transshipments tend to be more volatile than containers destined for the local market because of competition from other Micronesia islands. Break-bulk cargo includes automobiles, steel, cement, rebar and pipes, asphalt and aggregate. Liquid bulk mostly relates to petroleum, which can be subject to volatility because of fluctuating fuel prices and fuel demand.

New tariff plan currently under development

The port authority is currently in the process of updating its Master Plan and feasibility study which will also determine the need for future tariff increases. The port authority will likely not recommend a tariff increase for the next fiscal year. The authority's good operating performance in fiscal 2020 amid the pandemic reduces also the need for a tariff increase to maintain solid financial metrics. Any new five-year tariff plan requires approval from the PUC.

Limited operational restrictions and high fixed cost structure as a port operator

The port faces limited restrictions to accommodate future growth related to the military build up. The port's capacity limit is around 200,000 containers and current volumes average around 100,000 containers per year.

Most of the port's operating costs are fixed which is not unusual for port authorities that operate the port in contrast to landlord ports. The high fixed cost structure supports operating margin improvements in a growth environment. However, the authority's cost structure provides less flexibility to reduce costs in a period of lower demand.

The port authority has demonstrated good cost control in fiscal year 2020 and year-to-date fiscal year 2021. Unaudited results as of September 30, 2020 show that general and administrative expenses came in 1.5% below the prior year and 8.2% below budget.

Sole commercial port in Guam

The port authority is the sole commercial port in Guam, handling around 90% of the territory's imported cargo and a significant portion of military cargo. Competition from other smaller ports in Micronesia only applies to a small volume of volatile transshipment cargo. The port of Guam is the only port in the Micronesia region that has the infrastructure and equipment required to service container vessels with a capacity of up to 4,000 TEUs (twenty-foot equivalent units). Load factors on ships to Guam tend to be around 50% and 4,000 TEUs vessels are not required. Other ports in the region have more limited infrastructure, cranes and container handling equipment but attract transshipments through competitive pricing.

Small scale of operations and high customer concentration

With around $55 million of operating revenue in 2020, the port is of small scale, and smaller container and transshipment vessels service the port compared to other rated US ports. Customer concentration is high. The two major customers represent around 66% of total operating revenue and Matson, Inc. is the largest customer. The port is vulnerable to a loss of a single customer or an unexpected decline in volumes. Guam's reliance on shipping operations as an island nation mitigates its high customer concentration.

US based and international carriers that deploy cargo ships between the US mainland or Asian markets and Guam service Guam. Carriers with service routes between Guam and the US mainland are exempt from certain US requirements of the Jones Act: these carriers do not need to use US built ships. However, vessels must be US flagged and employ US crew members. Matson is the only carrier serving the port that is fully compliant with the Jones Act and also uses US built ships.

Financial and operational performance

DSCR will stay close to 2.0x in 2021

The authority estimates that it had an indenture DSCR of 1.7x as of January 31, 2021. We expect that the indenture DSCR was still above 2.0x in fiscal 2020 (2.3x in fiscal 2019).

Bondholders benefit from a pledge on net revenue after operating and maintenance expenditures but before contributions to other reserve funds and the bonds have a statutory lien on revenue. The revenue pledge however, excludes around 16% of operating revenue including crane surcharge revenue, facility management fees and marina revenue. Moody's net revenue DSCR calculation, which we base on the consolidated audited financial statements, includes this portion of the operating revenue and associated expenses.

Execution of capital plan on budget and continued focus on maintenance will be critical

The authority's capital plan is financed with proceeds from the 2018 bond issuance, cash flow generation and grants. Crane surcharge revenue and facility management fees are pledged to bondholders but will be used to pay for crane maintenance fees, facility maintenance or crane-related debt service.

As of January 31, 2021, capital projects that are funded partially with the bond proceeds amount to around $55 million. However, only $2.5 million have been spent so far on these projects, partially because of lengthy procurement processes.

The authority is currently evaluating initiatives to improve efficiency of its internal procurement processes as well as the potential for additional federal grants.

Liquidity

The port authority's liquidity position remains strong, partially also because of a high amount of unspent 2018 bond proceeds.

Total cash and investments as of January 31, 2021 were around $109 million, of which $49 million is reserved for construction projects and around $2.0 million is for the debt service reserve.

The rest of the funds are for operations, crane acquisitions reserves, facility maintenance, crane related operations, operations reserves and other funds that are required in the bond indenture.

Days cash on hand excluding construction reserves and the debt service reserve fund were 403 in fiscal 2019. We estimate that days cash on hand was similar as of January 31, 2021.

Debt and Other Liabilities

The authority issued $71.445 million in 2018 Series port revenue bonds to finance a portion of the port authority's capital improvement program, fund a debt service reserve and redeem existing bank loans. The bonds are fully amortizing, have a debt service reserve funded at maximum annual debt service and a final maturity of July 1, 2048. Maximum annual debt service is around $6.5 million and average annual debt service is around $4.1 million over the life of the debt. Bondholders benefit from a rate covenant of net revenue at 1.25x debt service. Bondholders are also protected by an additional bonds test, which requires either historical or prospective debt coverage of net revenue at 1.25x maximum annual debt service and a cash funded debt service reserve sized at maximum annual debt service. Other reserve requirements include an O&M reserve fund and a renewal and replacement reserve fund.

DEBT-RELATED DERIVATIVES

None.

PENSIONS AND OPEB

The Port Authority of Guam participates in the Government of Guam Defined Benefit Plan, a single-employer defined benefit pension plan administered by the Government of Guam Retirement Fund. For fiscal 2019, the port reported a net pension liability of about $55.2 million. Moody's adjusted net pension liability (ANPL), which is based on a lower discount rate, was around $89.9 million for the same period. Adjusted debt to operating revenue including the ANPL was 2.9x (unadjusted debt to operating revenue of 1.3x) in fiscal 2019.

ESG considerations

Environmental

Overall credit exposure to environmental risks for the port sector is moderate, reflecting exposure to carbon emissions from ocean vessels, cargo handling equipment and truck or rail carriers, most of which operate diesel-powered equipment. Depending on the jurisdiction, ports can be subject to country or regional-wide control of emission standards and electrification commitments. Ports are exposed to trade flows which in turn can be influenced by environmental pressure either through changed perception from consumers (reputational damage) or tighter regulatory restrictions.

Climate change increases risk of extreme weather conditions for seaports. Over the next 10 to 20 years, the risk of sea level rise, flooding, hurricanes, wildfires, water and heat stress is likely to worsen in certain regions of the US, according to data provided by Moody's affiliate Four Twenty Seven. Ports are an essential component of US trade and economic growth, and face unique climate risks relative to other infrastructure assets given that they are largely coastal entities. If needed, larger scale adaptation and mitigation projects may require public support.

Given Guam's location, the Port Authority of Guam has a very high risk exposure to sea level rise, typhoons as well as heat stress.

Social

The port sector faces moderate exposure to social risks.

The rapid and widening spread of the coronavirus outbreak, deteriorating global economic outlook, falling oil prices and asset price declines are creating a severe and extensive credit shock across many sectors, regions and markets. The combined credit effects of these developments are unprecedented. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. We do not believe there are major unique social considerations for the Port Authority of Guam.

Governance

The authority's five board members are appointed by the governor of Guam with the advice and consent of the Legislature. The five nonsalaried directors are appointed to three-year terms. The board of directors appoints the general manager and the two deputy general managers who are responsible for maintenance, operation and development of the port and the agency's business affairs. Policy decisions of the board are carried out by the general manager and her staff. Tariffs are approved by the PUC of Guam. The port authority makes no transfers to the Government of Guam.

Rating methodology and scorecard factors

The principal methodology used in these ratings was Publicly Managed Ports Methodology published in June 2019. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

The scorecard-indicated outcome for Port Authority of Guam based on fiscal year 2019 is A3, which is above the assigned rating of Baa2.

The assigned Baa2 rating is constrained by the authority's exposure to weather-related events including typhoons; the linkages to the credit quality of the Government of Guam; and the high customer concentration.

Exhibit 2

Publicly Managed Ports Methodology

Factor	Subfactor	Score	Metric
1. Market Position	a) Port Size (Operating Revenues) (000s)	Baa	55,236
	b) Quality of Service Area and Competition	Baa	
	c) Operational Restrictions	A	
2. Diversity and Volatility	a) Financial Revenue Variation (5-year operating revenue CAGR)	Aa	4.24%
	b) Customer Diversity	Caa	
3. Capital Program	a) Capital Needs Requiring Leverage	Baa	
4. Key Credit Metrics	a) Net Revenues DSCR	Aa	2.44x
	b) Adjusted Debt to Operating Revenue	A	2.90x
Notching Considerations		**Notch**	
	1 - Tax Support for Operations	0	
	2 - Liquidity- Cash to Debt	0	
Scorecard Indicated Outcome:		**A3**	

Source: Moody's Investors Service

REPORT NUMBER 1270710

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S INVESTORS SERVICE