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Illinois State Toll Highway Authority; Joint Criteria; Toll Roads Bridges

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Credit Profile		
US$225.0 mil toll hwy sr rev bnds ser 2019B dtd 12/04/2019 due 01/01/2031		
Long Term Rating	AA-/Stable	New
Illinois St Toll Hwy Auth		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA-' long-term rating to the Illinois State Toll Highway Authority's (ISTHA or the authority) pro forma $224.1 million series 2019B toll highway revenue refunding bonds. At the same time, S&P Global Ratings affirmed its 'AA-' rating on the ISTHA's toll highway senior revenue bonds outstanding. S&P Global Ratings also affirmed its 'AA+/A-1' rating on each of the subseries of the authority's series 2007A variable-rate demand obligation bonds. The ratings on the series 2007A bonds are based on the application of our joint criteria with low correlation. The outlook is stable.

The ratings reflect the combination of the authority's very strong enterprise risk and financial risk profiles, and the ISTHA's significant near-term debt needs. Our enterprise risk profile assessment incorporates the ISTHA's strong traffic trends (despite toll rate increases) due to its important role and strategic location, and the lack of significant competition from toll-free roads. Our financial risk profile assessment considers the ISTHA's strong revenue growth from recent toll rate increases, and favorable traffic trends due to its sizable and resilient demand base historically that we expect to continue. This will allow the authority to maintain strong financial performance and a very strong capacity to manage its increasing debt service requirements, with level debt service not occurring until 2026.

The very strong enterprise risk profile reflects our view of the ISTHA's:

- Very strong market position due to the toll road's strong demand characteristics given its important role as a regional urban infrastructure provider, with critical transportation links in northern Illinois that include the deep and diverse Chicago metropolitan statistical area (MSA), despite nontolled alternatives;
- Extremely strong service area economic fundamentals, which include favorable economic activity as measured by GDP per capita, a large population base, below-average expected population growth, and average unemployment levels;
- Low industry risk relative to that of other industries and sectors; and
- Very strong management and governance, reflecting the authority's history of meeting or exceeding most operational and financial goals, detailed financial forecasts that management updates frequently to address material variances, and very capable staff that has considerable experience operating a statewide tolling agency.

The very strong financial risk profile reflects our view of the ISTHA's:

- Strong financial performance that we expect to continue due to the authority's history of strong revenue growth from its willingness and ability to increase toll rates annually and the toll road's favorable traffic trends that, in our view, will allow the ISTHA to maintain total debt service coverage (DSC; S&P Global Ratings-calculated) at or near 2x;
- Very strong debt and liabilities capacity that we expect will continue as the authority counters rising debt service requirements from additional near-term borrowings with additional revenue from toll increases, ensuring that its capacity to service its debt will not diminish; and
- Very strong liquidity and financial flexibility, based on our expectation that the ISTHA's liquidity position--972 days' cash on hand and 17% of debt in fiscal 2018--will remain near current levels; the authority plans to cash-fund portions of its capital improvement plan, which will include the drawing down of a portion of current unrestricted reserves offset by the addition of excess cash flow on an annual basis.

Tollway system net revenue secures the bonds, and post-issuance, the authority will have $6.2 billion of revenue bonds outstanding, of which $722 million (11%) is variable rate and synthetically fixed. The bond proceeds will be used to refund the authority's series 2010A-1 bonds for interest savings without extending maturity and to pay issuance costs.

The remaining debt is fixed rate. The authority has no junior-lien debt. Overall, we view the bond provisions as credit neutral. They include a 1.3x rate covenant and an additional bonds test that calls for net revenue at least at the rate covenant for 12 consecutive months of the most recent 18; any toll adjustments within the 12 months preceding the bond issuance may be retroactively applied to the full 12-month period.

The Illinois Tollway, governed by an 11-member board of directors, operates 294 miles of interstate tollways for 12 counties in northern Illinois, including the greater Chicago area. The system comprises five major routes: Tri-State Tollway (interstates 294, 94, and 80), Jane Addams Memorial Tollway (Interstate 90), Ronald Reagan Memorial Tollway (Interstate 88), Veterans Memorial Tollway (Interstate 355), and the recently opened Illinois Route 390. The Tri-State accounts for about 46% of system revenue and about 45% of system transactions while the remaining three (not including the recently opened Illinois Route 390) are about evenly split.

The U.S. Court of Appeals for the First Circuit decision affirming a lower court's ruling that payment of Puerto Rico Highways and Transportation Authority's special revenue-secured debt is voluntary, and not required, during bankruptcy, has generated significant market attention. At this time, that decision is technically the only binding precedent for cases brought in the First Circuit, which does not include Illinois. In addition, we believe the authority rating is supported by significant constitutional and statutory protections that insulate the ISTHA's financial resources from related government intervention from the state of Illinois as well as our opinion of near-term credit stability with regard to the state general obligation rating.

Despite being an administrative agency of the state of Illinois, the tollway is a fully self-supporting enterprise, which derives approximately 98% of its operating revenue from the tolls and evasion recovery it collects from those who use its toll highways. Its board of directors has the authority to increase toll rates as needed. The tollway does not receive any funding from the state, and it is not dependent on state appropriations. Its finances are also separate and independent from those of the state. The authority, not the state, collects toll revenue, and then is required to transfer that revenue to the state treasurer, who is then responsible, at the authority's direction, to pay ISTHA expenses as they become due and to submit funds to the trustee to satisfy ISTHA bond-related payments and deposits required under the indenture. In this case, however, the state treasurer is the legal custodian, and the authority's revenue is not comingled with any other state funds or money. Furthermore, there are strong statutory, constitutional, and other legal protections that should prevent the state from diverting tollway revenue for nontollway purposes. While the state could become motivated to take steps to rewrite, eliminate, or even ignore such protections in times of severe financial distress, we believe the likelihood of this happening is remote since our forward-looking view on the state is reflected in our current stable outlook. However, if the state's financial situation materially weakens it could cause downward pressure on the ISTHA's ratings since, in our opinion, the likelihood of the state diverting ISTHA revenue for non-ISTHA purposes increases.

Outlook

The stable outlook reflects our expectation that, over the next two years, the ISTHA will continue to manage its operations and capital program effectively while maintaining DSC levels near 2x.

Downside scenario

Although unlikely, we could lower the rating during the outlook period if the ISTHA's DSC or liquidity falls materially below our expectations. In addition, we may lower the ratings or revise the outlook to negative if the state legislature attempts to weaken statutes or state constitutional provisions protecting the ISTHA or takes other actions that we believe could impair the authority's ability to operate the tollway, or the state credit rating is facing downward pressure.

Upside scenario

We also consider it unlikely that we will raise the rating within the two-year outlook period, given the authority's significant additional debt needs.

Enterprise Risk: Very Strong

Our assessment of the ISTHA's enterprise risk profile as very strong reflects the authority's extremely strong economic fundamentals, low industry risk, very strong market position, and very strong management and governance.

Economic fundamentals

The service area has extremely strong economic fundamentals, reflecting favorable income levels and economic activity as measured by GDP per capita, large population, and average unemployment levels.

We consider the economy of the Chicago MSA to be broad and diverse. Chicago, the nation's third-largest city, is a global business center and transportation hub. Its economy is very diverse, with no single industry accounting for more than 14% of the workforce. The city and its surrounding MSA have a more educated population than the nation (43.3% with some higher education compared with 38.8% for the U.S.), and also is home to a larger-than-average population aged 25-34 (14.5% compared with 13.7% for the U.S.). It is repeatedly named a top MSA for corporate relocation and boasts significant cultural attractions, with 58 million visitors in 2018. However, the Chicago MSA's economic growth has been tepid relative to those of the the U.S. and comparable MSAs, and although it remains an economic powerhouse, it is not without challenges, in our view. We anticipate the city will continue to experience positive economic growth over the medium term, albeit slower compared with that of the nation.

Market position

We consider the ISTHA to have a very strong market position. The toll system is large and diverse, in our opinion, serving 1.6 million daily drivers in the Northern Illinois area, including the Chicago MSA. It maintains and operates 294 miles of interstate tollways for 12 counties. The authority collects tolls at 28 mainline plazas and 59 ramp plazas.

The ISTHA is operating under a schedule of approved toll increases, and projections indicate it will require no further adjustments to support the additional debt associated with the Move Illinois (MI) program. In January 2012, electronic and cash toll rates on passenger cars increased approximately 87.5% although no additional passenger-car toll rate increases are scheduled. Commercial-vehicle toll rates increased 40% in January 2015, 7.1% in January 2016, and 6.7% in January 2017. Since 2018, commercial-vehicle toll rates will increase annually by an inflation-based index. For 2018, the increase was about 1.84%, and for 2019, it was about 2.25%; a 2.07% increase will become effective on Jan. 1, 2020. Each increase became effective on Jan. 1 in each year. We consider the authority's cost per mile for passenger cars below average, and its cost per mile for commercial vehicles above average, but still competitive relative to that of other tolling agencies.

Despite the rate hikes, traffic levels have performed relatively well, in our view. More specifically, total annual traffic, as measured by toll transactions, increased 1.2% to 1.0 billion in 2018 following an increase of 7.0% to 997.3 million in 2017. Transactions rose 5.7% in 2016, 5.2% in 2015, and 2.7% in 2014. In 2018, the system exceeded its previous historical peak for revenue set the previous year. Transaction trends for both passenger cars and commercial vehicles were favorable in 2018; passenger-car transactions increased 0.6% while commercial transactions grew 5.2%.

Management

The authority's management and governance is very strong, in our view, reflecting the ISTHA's strategic positioning, risk management and financial management, and organizational effectiveness. The ISTHA has demonstrated over a long period, an ability to manage its large-scale capital programs while maintaining key financial metrics at high levels.

The tollway has an 11-member board, including the state's governor and secretary of transportation, who serve as ex officio members. The chairman and directors are appointed by the governor and serve four-year terms; no more than five of the members may be from one political party. We view the ISTHA's governance structure as credit neutral.

Financial Risk: Very Strong

Our assessment of the authority's financial risk profile as very strong reflects the toll system's strong financial performance, very strong debt and liabilities capacity, and very strong liquidity and financial flexibility. Our financial profile risk assessment considered pro forma figures, which reflect the first full year of level debt service in 2026 incorporating the effect of remaining debt issuances to fund the MI program. Our financial profile assessment also considered the ISTHA's financial policies, which we consider credit neutral.

Financial performance

The strong financial position reflects S&P Global Ratings-calculated coverage. Historically, DSC has been below 3x (ranging from about 2.4x to 2.7x from fiscal 2015 to fiscal 2018). We expect the authority's financial performance to remain strong. Fiscal 2018 operating revenue increased to $1.5 billion compared with $1.4 billion in fiscal 2017. In addition, management has an internal goal of maintaining at least 2.0x DSC although this is not codified. Projections include the additional debt issuances needed over the remainder of the MI program through 2026, and the base-case scenario demonstrates DSC at a low point of 2.21x in 2026, which is based on forecast assumptions that we believe are reasonable and achievable.

Debt and liabilities

We assessed the ISTHA's debt and liabilities capacity as very strong, as the authority counters rising debt service requirements from additional borrowings with additional revenue from toll increases, ensuring that its capacity to service its debt will not diminish.

In 2011, the ISTHA approved the 15-year, $12.15 billion MI program, which began the following year. In April 2017, the board of directors agreed to expand the original reconstruction of the Central Tri-State Tollway by $2 billion, bringing the program's estimated capital investments to $14.3 billion, the budget for which is currently $14.2 billion. The program addresses a mix of system preservation and expansion. The authority has issued $3.1 billion in revenue bonds to date to pay part of the program's cost. The ISTHA expects to fund the rest with proceeds from additional debt and funds on hand. We expect the authority will issue additional senior revenue bonds of approximately $500 million in 2020, approximately $1.2 billion from 2021 to 2022, and approximately $700 million from 2023 to 2024.

Illinois' pension plans are some of the worst funded in the nation and remain its largest source of long-term pressure and a significant fixed cost. Substantially all of the authority's employees participate in the State Employees' Retirement System of Illinois (SERS), a single-employer, public employee defined-benefit pension plan. As of fiscal 2018, the SERS' fiduciary net position (assets) provided a 34.5% funded ratio, slightly higher than the 33.4% funded ratio in fiscal 2017, based on Governmental Accounting Standards Board measurement standards. Improved funding reflects strong investment returns, with the fund achieving actual returns greater than the assumed rate of return. The portion of the state's total pension liability and other postemployment benefit (OPEB) liability allocated to the authority, as of June 30, 2018, totaled $882.5 million and $140.1 million, respectively. While the ISTHA's combined allocation is nominally high, we consider it manageable in comparison with the authority's unrestricted liquidity position, which currently totals $1.1 billion. Due to the state's relatively low funded ratios, we expect the authority's pension and OPEB costs to increase in the future, but we also expect the authority to adjust its toll rates and other charges to raise the additional revenue needed to cover future cost increases and maintain its historically strong DSC in excess of 2x. To the extent that the authority were to not do so, leading to a material decline in coverage and increase in overall pension and OPEB costs as a percentage of the ISTHA's total budget, we would view this as credit negative.

Liquidity and financial flexibility

The ISTHA has had what we consider a very strong liquidity position in recent years, with the balance sheet for the 2018 audit indicating unrestricted cash and investments at $1.07 billion, or 972 days' cash on hand and 17% of debt outstanding. Although we expect the authority will use some of its current unrestricted cash reserves to fund the capital program, we expect this will be offset by the additional excess cash flow from operations and allow the authority to maintain liquidity at or near levels that we would consider very strong.

The ISTHA is party to five swaps among various counterparties. As of Sept. 30, 2019, each swap had a negative value--not in the authority's favor--with a collective estimated mark-to-market valuation of negative $152 million. The ISTHA's swap portfolio, in our opinion, poses low contingent liquidity risk. More specifically, the authority is not required to post collateral under any one of its swap agreements and the ratings-based termination triggers--'BBB' from any credit rating agency--that would require a termination payment is more than two notches from the current rating. Furthermore, in the event that the ratings-based threshold were to be triggered, we believe the authority has a robust liquidity position to make any potential terminal payments. We also consider the contingent liquidity risk exposure from the series 2008A-1b direct purchase manageable given the authority's very strong liquidity position.

Ratings Detail (As Of October 22, 2019)		
Illinois St Toll Hwy Auth toll hwy var rate sr priority rev bnds ser 2007-A1A dtd 11/01/2007 rmktd dtd 3/18/2011 due 07/01/2030		
Long Term Rating	AA+/A-1	Affirmed
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Illinois St Toll Hwy Auth toll rds br (BAM) (SECMKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Illinois St Toll Hwy Auth toll rds br (BAM) (SECMKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Illinois St Toll Hwy Auth (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Illinois St Toll Hwy Auth (BAM) (SECMKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Illinois St Toll Hwy Auth toll hwy sr priority VRDB 2008A1-A2		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Long Term Rating	AA/A-1/Stable	Current
State Toll Highway Authority, Variable Rate Senior Priority Revenue Bonds, Series 2007 A-1B		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Long Term Rating	AA+/A-1	Affirmed
State Toll Highway Authority, Variable Rate Senior Priority Revenue Bonds, Series 2007 A-2D		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Long Term Rating	AA+/A-1	Affirmed

Many issues are enhanced by bond insurance.