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The rating game

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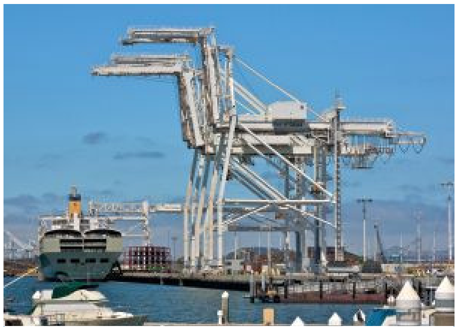
Ratings take the guesswork out of port financials, as Barry Parker discovers



The Port of Oakland comes in with an “A+” rating, raised from “A” in September, 2012. Credit: Jay Galvin

The views of New York’s harbour are spectacular from the downtown offices of Standard & Poor’s Ratings Services (S&P), in lower Manhattan - where the ratings agency hosted a roundtable discussion on the US Transportation ratings in the public finance sector.

The watery backdrop provided a perfect setting for the US ports presentation, given by Todd Spence, an S&P director, who was also the primary analyst on the S&P RatingsDirect report *Port and Port Infrastructure Ratings Move With The Economic Tide*.

The publication’s title belies the nuanced nature of analysing a port’s finances; yes, a rising tide lifts most boats, but, as the authors point out, “the port sector depends, to a large degree, on the economies of the regions they serve” and that “regional pockets can counter global economic trends”.

In all, S&P rates 29 US ports; which range from two entities rated “AA” (solidly in the ‘investment grade’ category), down to one rating at “BB” (just below ‘investment grade’). The ratings are clustered around “A+” and “A”, squarely within the investment grade bracket.

However, reflecting the underlying economic situation, the ratings are anything but static. One of Mr Spence’s charts showed that upgrades (improvements in ratings) far outnumbered downgrades during good economic times; from 2005 to 2008, two downgrades were dwarfed by 11 upgrades. Conversely, during 2009 to 2011, four issues were downgraded while two saw improved ratings.

Pacific performance

Lately, trans-Pacific trade flows have held their own; indeed, the two “AA” rated US bond issuers are entities linked to the ports at Long Beach and Los Angeles. Port of Tacoma debt has an “AA-” rating while strength in the Pacific Rim has also benefited the Port of Oakland which comes in with an “A+” rating, recently raised from “A” in September, 2012. Oakland is an important container port, with multiple terminals, and interfaces with two large Class-1 railroads: BNSF and Union Pacific.

Earlier this year, the outlook for Alabama State Port Authority’s dock facility revenue bonds was raised from BBB+/Stable to BBB+/Positive, reflecting the possibility of an improved rating in the months ahead. Mr Spence explained to *Port Strategy*: “ASPA had declining activity levels in 2009 and 2010 which resulted in lower financial margins. Cargo activity increased in 2011 and financial metrics increased to levels similar to pre 2009 levels leading us to revise the outlook to positive (debt service coverage over 2x in 2011 and expected to be over 2x in 2012).” He added that: “The rating applies to outstanding bonds totalling approximately $388m as of September 30, 2011 (Series 2006A&B, 2006D, 2008A and 2010).”

The debt service ratio, an important metric for revenue bonds, is computed by dividing net operating income by the total debt service payments required during a year. Facilities of ASPA include a mix of intermodal container terminals, drybulk and liquid bulk terminals. The port at Mobile is a regional rail hub, served by five Class-1 railroads.

A recent addition is the ThyssenKrupp steel plant in Calvert, Alabama, about 50 miles north of Mobile; some $95m was raised by the ASPA in 2008-2009 to partially fund construction of a terminal at Pinto Island (very near to downtown Mobile), for handling imports of steel slabs that are barged to the steel mill and then processed into finished products at the plant. The $102.6m raised through the 2010 bond issue (divided into portions maturing in 2030, 2035 and 2040) was used, mainly, to retire $50m and $45m , that had been raised in 2008 and 2009, respectively.

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Rating winner

In describing the ratings change at Oakland (raised from “A/Positive” to “A+/Stable”), Mr Spence said: “The ratings were raised on the senior and intermediate lien revenue bonds. The upgrade reflected improved financial performance as management implemented a financial plan that reduced expenses, increased unrestricted cash balances and the port's capital improvement plan was scaled back.”

He also explained the situation at Oakland, where the borrowing entity’s remit extends beyond the seaport, adding that: “The bonds are backed by all revenues of the port for which the marine port accounts for 51% of revenues the airport accounts for 45% of revenues and the real estate division accounts for 4%. The ratings apply to all outstanding senior and intermediate lien revenue bonds.”

As noted in Mr Spence’s presentation: “Large ports tend to have strong competitive positions and are vital to national and local economies.” Typically, such ports tend to have ratings ranging from “A” to “AA”, and are primarily container handling facilities providing national, as well as local transportation services. S&P offers: “In our view, the large ports serve a critical role in the national local and transportation infrastructure system.” The large ports are also well positioned financially, with “an excellent cash position and…strong debt service coverage”.

Moving down the scale to medium (generally in the “A” category) and smaller ports (generally with ratings of “BBB”), the higher end includes “large, efficient intermodal operators” while the lower end includes what S&P describes as “less traditional maritime enterprises with market specialties”.

Some risks

The ports at the smaller end have “a concentration in commodity mix”. These commercial characteristics translate into the ports’ financial visage; the medium ports are characterised as having “generally solid finances” but they “face some economic risks and often tied to smaller economies”. According to S&P, their brethren in the small ports category “have a susceptibility to cash flow erosion from the loss of one or two tenants”.

S&P’s analysts are also closely attuned to the carrier and cargo environments, presenting “volatile transportation costs, particularly fuel costs, for all modes - maritime, barge, rail and trucking - which could alter the economics of the logistical decisions of global shipping players”.

Like everyone in the ports business, eyes are on developments in Panama, and the expansion of the Canal, where “significant work is left to be completed in the schedule’s remaining two years, which could result in delays”. Impacts on specific ports are hard to predict, with S&P acknowledging, in its RatingsDirect report, that: “At this time, it is difficult to gauge the impact of the opening of the canal.”

In the face of all these unknowns and ‘what-if’s?’, one very practical suggestion emerged during the presentation, with Mr Spence noting that privatisation deals, in the form of a long term lease to a private operator, offer stability and eliminate the risk from shifting volumes.

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Long Beach and Los Angeles house two “AA” rated US bond entities Credit: Burce Perry

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