CREDIT OPINION
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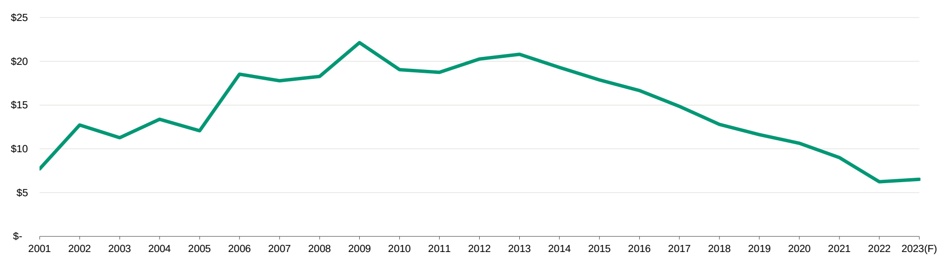
Alaska (State of) Airport Enterprise

Update following upgrade to Aa3

Summary

The credit profile of Alaska Airport Enterprise (AIAS or system, Aa3 stable) reflects substantial airline activity, driven by Anchorage's (ANC) position as the second-largest cargo airport in the US per Airports Council International; the continued reduction of debt, which has positioned the system among the lowest levered among our rated airports on a debt to net revenue basis; and the long-term residual airline agreement that mitigates risk related to cargo operations and provides visibility to capital spending. Counterbalancing these credit strengths, AIAS presents good but average liquidity and enplanement levels are constrained by the characteristics of its service area, which is exposed to the cyclicality of natural resource extraction industries and sustained population loss.

Exhibit 1
AIAS has substantially reduced its leverage due to debt reduction and high activity levels
Debt to certified maximum gross takeoff weights



Source: AIAS

On March 4, we upgraded the system's bond rating to Aa3 from A1. We also revised the outlook to stable from positive.

Credit strengths

» ANC is the second largest cargo airport in the US and a major trans-loading point for international air cargo

» ANC has a dominant position in O&D passenger air travel and is the gateway between Alaska and the lower 48 states

» Good liquidity, low leverage, and comprehensive cost recovery under full residual airline agreement in place through 2033

Credit challenges

- Alaska's domestic economy remains challenged in terms of performance and prospects
- Air cargo use is predominantly transient, technical in nature
- Moderately elevated adjusted net pension liability (ANPL)

Rating outlook

The stable outlook reflects our expectation of continued strength in cargo and passenger trends and strong financial flexibility, supported by a comprehensive residual cost recovery airline agreement, low leverage, a cash funded capital plan, and adequate liquidity.

Factors that could lead to an upgrade

- Substantial improvement in market position that results in sustained increase in cargo and passenger activity levels
- Improvement in operating margins or debt reduction that on a sustained basis results in days cash on hand above 600, debt to net revenue below 4x and net revenue debt service coverage above 2x

Factors that could lead to a downgrade

- Sharp deterioration in market position that results in sustained reduction in cargo and/or passenger activity levels
- Decline in operating margins or incremental debt that on a sustained basis results in days cash on hand below 500, debt to net revenue above 7x and net revenue debt service coverage below 1.25x

Key indicators

Exhibit 2
Key indicators for Alaska International Airports System

	2018	2019	2020	2021	2022
Cargo (millions of pounds)	24,040,796	24,312,650	26,704,201	31,673,675	34,076,649
Total enplanements ('000)	3,318	3,405	2,649	1,740	3,084
Debt outstanding ($ millions)	375,535	346,545	333,370	319,440	243,805
Debt to Net Revenues (x)	5.4x	5.48x	4.87x	6.73x	7.42x
Total DSCR by net revenues	2.24x	2.07x	2.3x	1.68x	1.92x
Total DSCR (bond ordinance)	2.16x	2.07x	2.55x	1.79x	1.98x
Days cash on hand	507	551	577	786	537

Source: AIAS, Moody's Ratings

Profile

Alaska International Airports System (AIAS) is comprised of two airports, Ted Stevens Anchorage International Airport (ANC) located three miles from downtown Anchorage, and Fairbanks International Airport (FAI), located five miles from central Fairbanks. Both airports provide passenger and cargo facilities and services, and each has a sea plane base for general and light aviation adjacent to and operated as part of the airport.

Per Airports Council International ANC ranked as the third busiest air cargo hub globally, and as the second busiest air cargo hub in North America, in 2022. Both ANC and FAI airports act as the diversionary airport for the other, with FAI being a full-service diversionary airport providing carriers reliability. Cargo operations contribute roughly two thirds of revenue. ANC (2.7 million) and FAI (0.541 million) served a combined 3.2 million passenger enplanements in fiscal 2022, compared to a combined 3.4 million –

2.82 million at ANC and 0.58 million at FAI – in fiscal 2019. ANC's cargo position is durable given the flight stage length for air travel between Asia and North America and its high diversity of air cargo carriers that reduces dependence on any individual carriers operating strategy.

AIAS is an enterprise fund of the State of Alaska and is managed by the Alaska Department of Transportation and Public Facilities.

Detailed credit considerations

Revenue Generating Base

Dominant market position

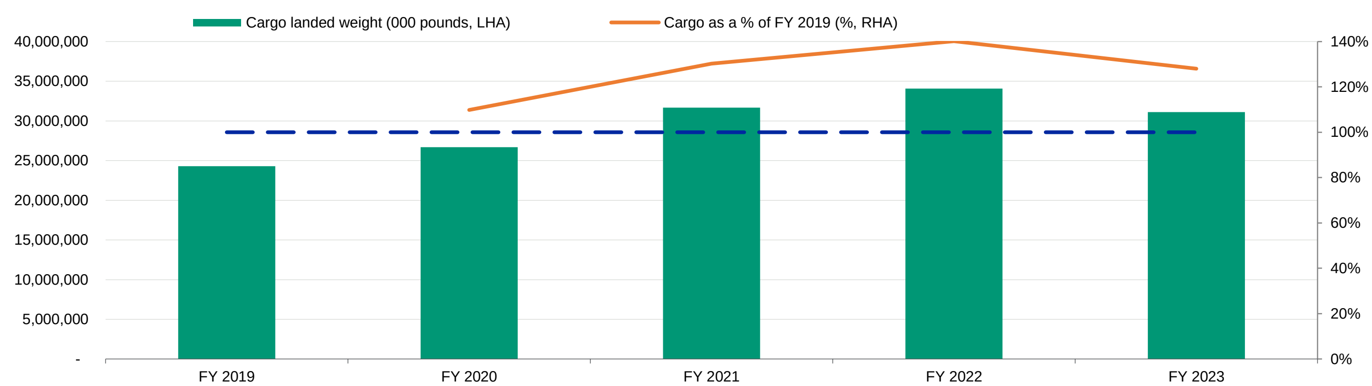
While per the Federal Aviation Administration (FAA) ANC is a medium hub and ranks as the 59th largest passenger airport in the US, it is also the largest air cargo airport in the nation. The system derives roughly two thirds of its revenue from cargo activity, therefore the impact of passenger enplanements is moderate. Located on the great circle route and equidistant to major markets in Asia, Europe and the US and Mexico, ANC is a major refueling point and sorting and transfer hub for domestic and international carriers: an estimated 80% of trans-Pacific cargo flights stop at ANC for refueling, cargo transfer or shift change of crew. ANC has consistently maintained its market share.

AIAS's dominant cargo position is fortified by regulatory exemptions that support the efficient flow and transfer of cargo, such as the ability of a foreign airline to transport cargo between US destinations under a single itinerary if (and only if) an interline connection is made in Alaska.

The airport's overall activity level is substantial and it has demonstrated to be resilient to the pandemic. In fiscal year ending June 30, 2022, e-commerce and on demand delivery models favored AIAS, with the highest landed weight in the airports' history registered that year. In fiscal 2023, cargo activity slowed down versus fiscal 2022, but it was still very strong, around 30% higher than in fiscal 2019.

Exhibit 3

Cargo activity continues to be stronger than pre-pandemic



Source: AIAS

In terms of passenger air travel, the system remains well positioned as it operates two of the busiest airports in the state of Alaska, a state in which air travel is essential for both intra-state and inter-state mobility. While a majority of leisure visitors continue to access the state by cruise or marine highway transport, air travel remains a dominant mode due to the physical expanse of the state and the limited connectivity afforded by the road network.

ANC continues to recover relatively well from the pandemic. As of fiscal 2023, AIAS enplanements were at 96% of the levels registered in fiscal 2019, which recorded the highest enplanement levels of the airport's history. AIAS expects full recovery in fiscal 2024 and flat growth thereafter. On a long term basis, AIAS enplanement levels are constrained by the characteristics of its service area, which is exposed to the cyclicality of natural resource extraction industries and sustained population loss.

Long term full residual airline agreement supports cost recovery and mitigates volatility

Further supporting AIAS resiliency to cargo and enplanement volatility, the enterprise renewed its residual airline agreement, now valid until 2033. The residual ratemaking is key to managing risk associated with the sizeable non-native cargo operations and provides visibility to planned capital spending.

The new agreement does not present significant changes versus the previous one. Per the agreement, each fiscal year rates and fees are reviewed and adjusted to ensure that revenues are sufficient to meet operations and maintenance expenses, capital investment plan (CIP) costs, debt service and other funding requirements. Midway through the fiscal year, if the projection of annual revenues made at that time is greater than 5%, more or less, than the initially budgeted requirements for the fiscal year, the agreement allows for the State of Alaska Department of Transportation and Public Facilities (DOT&PF) to adjust the rents, fees and charges. If at any time during the fiscal year AIAS projects that annual revenues will not be sufficient to cover the AIAS total revenue requirement, the agreement also allows DOT&PF to immediately adjust landing fees. Substantive investment projects are subject to airline majority in interest balloting. Annual escalation rate for the pre-approved capital projects is seven percent for the first half of the term and will be adjusted per the agreement for the second half.

Financial Operations and Position

Strong financial flexibility to manage volume declines

As the US economy grows at a more moderate pace in calendar 2024 - we anticipate 1% GDP growth in 2024- we expect cargo volume growth to slow down as well. Cargo was impacted significantly during the 2008 recession, falling nearly 30% from peak to trough over several years. We view the current cargo level as still unusually elevated and vulnerable to further retrenchment if economic conditions deteriorate. Cargo accounts for a significant share of total airline revenue for the system, and is key to helping absorb pressure on rates and charges for passenger airlines. Nevertheless, we view that AIAS is well positioned to manage lower activity.

The strong growth in overall activity through COVID has enabled the system to further deleverage and increase liquidity. Even if cargo activity reverts back to trend as COVID-induced demand for goods eases, we think debt will continue to decline and cost pressures will remain comparatively modest.

Also, the very strong market position implies an ability to sustain a higher passenger airline CPE if needed. We note the airport continues to target a roughly $8 CPE that we view as reasonable . CPE has been stable over the last decade and should remain so going forward as debt service was lowered with the 2021 refunding, no new debt is anticipated, pay-go capital spending is expected to be modest and the system's operating footprint is not materially changing.

AIAS has been generating sound debt service coverage ratios – at or above 1.5x in each of the last six fiscal years (fiscal 2016-2022) – in part because it collects revenues for capital projects in rates and charges, in addition to having conservatively managed its debt service. Fiscal 2022 DSCR was 1.9x. Once the federal relief funds are depleted, we expect the enterprise to adjust rates accordingly to ensure a DSCR of at least 1.25x as proscribed in the extended airline use and lease agreement.

Liquidity

AIAS is well positioned to deal with a downturn in cargo thanks to its adequate liquidity, including approximately $60 million of remaining COVID relief grants available to support rates and charges in fiscal 2023 and fiscal 2024 and a low level of debt service. The $60 million of COVID relief grants are complemented by $130 million of unrestricted cash of fiscal 2022, relative to around $20 million of debt service and about $40 million of pay-go capital spending in each of the next two years.

AIAS has solid liquidity for an airport with a residual rate-making framework, typically holding over 500 days cash on hand. The airport had 537 days cash on hand in fiscal 2022 versus 786 in fiscal 2021. The reduction partially reflects the contribution of unrestricted cash toward debt reduction in fiscal 2022. The system additionally had $60 million of COVID relief grants remaining entering fiscal 2023, which it will use in fiscal 2023 and 2024 to support rates and charges.

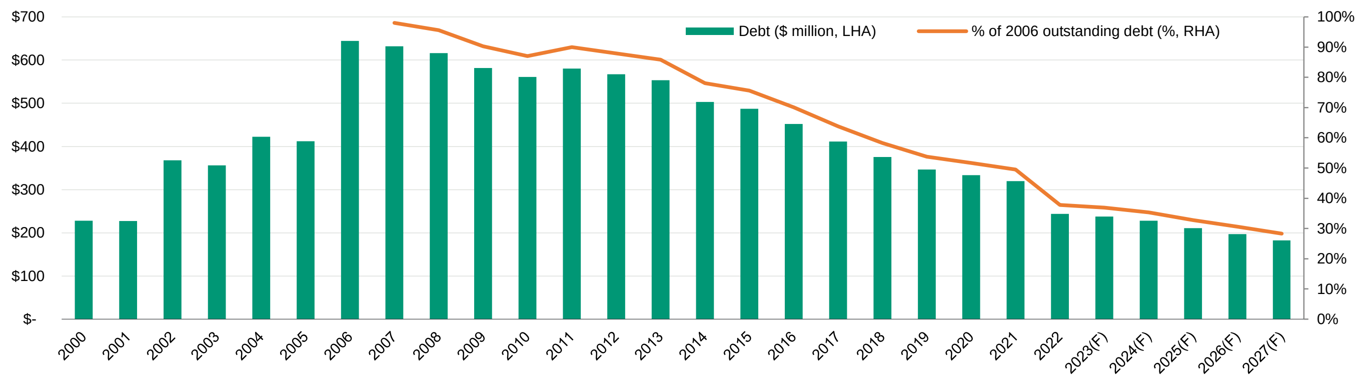
Debt and Other Liabilities

Low leverage supports credit profile

We expect AIAS to register debt to net revenue between 4x and 6x, below other airports in the Aa3 rating category with stronger service areas and higher enplanement levels. AIAS's low leverage levels among similarly rated peers is supported by its consistent debt reduction and substantial activity volumes. AIAS has progressively reduced its outstanding debt, a trend that we expect to continue as the enterprise's current CIP will not require additional debt.

Exhibit 5

AIAS has consistently reduced its outstanding debt



Source: AIAS

Legal security

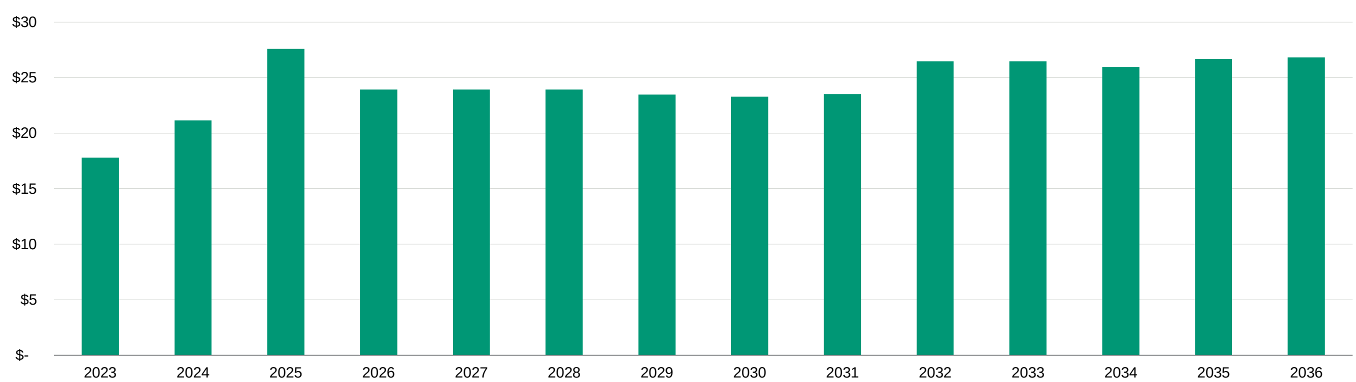
Senior lien on net revenues of the airport system. The debt service reserve has a standard three-prong test for all parity debt. A reserve requirement of approximately $25.3 million is entirely cash funded.

Debt structure

The system has a favorable debt structure. Near-term debt service is lower than typical as the system front-loaded savings with the 2021 refunding transaction, but the long-term trajectory remains relatively level through final maturity in 2036. All of the system's debt consists of fixed rate, fully amortizing long term bonds.

Exhibit 6

Debt service profile ($ million)



Source: AIAS

Debt-related derivatives

None.

Pensions and OPEB

The system has a moderately large adjusted net pension liability. The system recorded a net pension liability of $54 million in fiscal 2022. With Moody's standard adjustments to reported pension data, we calculate an adjusted net pension liability (ANPL) of $199 million in fiscal 2022. The main difference between the net pension liability and Moody's ANPL is the rate used to discount the pension liability for the fiscal year 2022 reporting period, which was 7.38% for the system and 2.84% for Moody's.

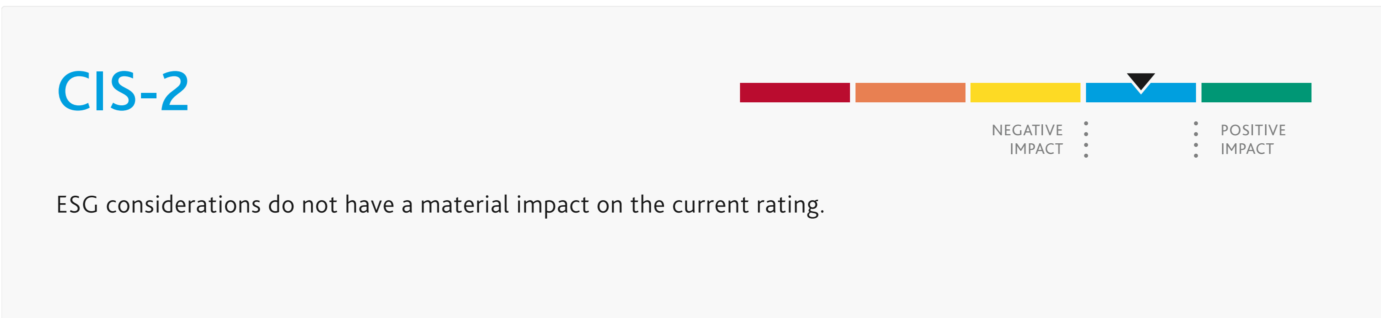
Nearly all full-time employees of the system participate in the State Public Employees' Retirement System (PERS), a cost sharing defined benefit pension plan. Over 60% of airport system employees fall within the Tier IV plan, established for employees entered after fiscal 2006, which provides a defined contribution benefit. The preponderance of employees under Tier IV will temper future pension expense and position the airport more favorably as the legacy defined benefit liability is amortized.

ESG considerations

Alaska (State of) Airport Enterprise's ESG credit impact score is CIS-2

Exhibit 7

ESG credit impact score



Source: Moody's Ratings

Alaska Airport Enterprise, AK's ESG credit impact score of **CIS-2** indicates that ESG considerations have a limited impact on the rating.

Exhibit 8

ESG issuer profile scores

Source: Moody's Ratings

Environmental

The airport system is exposed to carbon transition risks. The system is exposed to evolving decarbonization policies around the globe and regulations that may increase operating costs for airlines and result in higher costs that reduce the demand for air freight or travel. The desire by some to reduce carbon emissions may lead to reduced travel, in particular, corporations seeking to reduce their carbon footprints. The State of Alaska also faces more acute carbon transition risk than most other states, given its reliance on the oil extraction industry.

Social

Levels of social risk related to the linkage between carbon transition and demographic and societal policies are lower in the US than in other regions given the geographically dispersed nature of the country and the lack of viable rail alternatives.

Governance

Exposure to governance risk is limited. Federal Aviation Administration regulation of US airports tightly restricts the use of funds generated at US airports to aviation purposes and essentially eliminates the possibility that a municipal owner could extract value from the airport at the expense of bondholders. The airport system is an enterprise fund of the state and is managed by the Alaska Department of Transportation and Public Facilities.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The Aa3 assigned rating is two notches above the A2 scorecard indicated outcome. The assigned rating reflects the strength and benefit of the cargo business, which contributes materially to revenue, reduces operating and capital expenses for passenger airlines, and increases diversity for the overall enterprise.

The scorecard is a reference tool that can be used to approximate credit profiles in the airport sector in most cases. However, the scorecard is a summary that does not include every rating consideration. Please see the Publicly Managed Airports and Related Issuers methodology published in February 2023 for more information about the limitations inherent to scorecards.

Exhibit 9

Publicly Managed Airports and Related Issuers
As of fiscal year 2022

Regional Position:	**Regional**		
Rate Making Framework:	**Residual**		
Factor	**Subfactor**	**Score**	**Metric**
1. Market Position	a) Size of Service Area (millions)	Baa	0.4 million
	b) Economic Strength and Diversity of Service Area	A	
	c) Competition for Travel	Aaa	
2. Service Offering	a) Total Enplanements (millions)	A	3.1 million
	b) Stability of Traffic Performance	Baa	
	c) Stability of Costs	A	
	d) Carrier base (Primary Carrier as % of Total Enplanements)	Baa	67.5%
3. Leverage and Coverage	a) Net Revenue Debt Service Coverage Ratio	Aa	1.92x
	b)Debt + ANPL per O&D Enplaned Passenger	Ba	$146
		Notch	Metric
4. Liquidity	Days Cash on Hand	0	537
5. Connecting Traffic	O&D Traffic	0	2% connecting
6. Potential for Increased Leverage		0	
7. Debt Service Reserves		0	
Scorecard Indicated Outcome:		A2	

Source: Moody's Ratings

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