MOODY'S INVESTORS SERVICE

New Issue: **MOODY'S ASSIGNS A2 TO SAN DIEGO AIRPORT SUBORDINATE LIEN REVENUE BONDS; AFFIRMS A1 SENIOR LIEN AND STABLE OUTLOOK**

Global Credit Research - 13 Sep 2010

AUTHORITY HAS $470 MILLION REVENUE BONDS OUTSTANDING AFTER THIS ISSUE

Airport
CA

Moody's Rating

ISSUE		RATING
Airport Revenue Bonds, Subordinate Series 2010A		A2
Sale Amount	$260,215,000	
Expected Sale Date	09/01/10	
Rating Description	Revenue	
Airport Revenue Bonds, Subordinate Series 2010B		A2
Sale Amount	$27,670,000	
Expected Sale Date	09/01/10	
Rating Description	Revenue	
Airport Revenue Bonds, Subordinate Series 2010C (Federally Taxable)		A2
Sale Amount	$135,815,000	
Expected Sale Date	09/01/10	
Rating Description	Revenue	

Moody's Outlook Stable

Opinion

NEW YORK, Sep 13, 2010 -- Moody's Investors Service has assigned an initial A2 rating to the San Diego County Regional Airport Authority Airport (SDCRAA) Subordinate Airport Revenue Bonds, Series 2010 and affirmed the A1 rating on the senior airport senior revenue bonds. The rating outlook is stable.

RATINGS RATIONALE

The rating is based on the airport's stable origination and destination (O&D) base in the second largest city in California; a relatively strong service area economy; diversified carriers and fairly stable traffic through the recession; and strong historical and forecasted debt service coverage and liquidity. The rating also considers the authority's large capital program and its impact on future debt service and operating costs, as well as some possible operational disruptions during construction.

LEGAL SECURITY: Net general airport revenues. Rates and charges are set to provide revenues that are at least 110% of annual subordinate lien debt service and 125% of annual senior lien service. The authority's indenture requires debt service deposits from revenues to be made to the trustee only five days prior to the payment due date rather than in monthly installments, which Moody's considers a weakness. However, this weakness is offset by the authority's healthy liquidity and monitoring practices.

INTEREST RATE DERIVATIVES: None.

STRENGTHS:

*Strong Origination & Destination (O&D) airport serving San Diego economy which has been experiencing steady population growth. In FY 2010 approximately 96% of enplanements were O&D passengers

*Diversity of air carriers serving the airport. Approximately 20 airlines serve the airport with low cost carrier Southwest Airlines (Senior Unsecured rating Baa3) comprising over 37.7% of airport enplanements in FY 2010

* Under the traffic consultant's base case forecast debt service coverage remains strong and costs per enplaned passenger are forecasted to remain competitive despite the significant increase in debt

CHALLENGES:

*Sizable capital program of over $1.21 billion to address rehabilitation and capacity enhancements to be funded primarily debt financed (708%) with airport revenue bonds. Some potential disruptions to operations could occur during construction, though these are mitigated by the majority of construction outside of secure areas

*Long-term capacity limitations allow little room for expansion. The airport has a single runway and a curfew on flights, which cannot operate depart between 11:30 PM and 6:30 AM

*Several airports within approximately 2 hours driving time, including LAX (rated Aa3), Long Beach (A2), John Wayne (Aa3), and Ontario (A2) pose some competition, though traffic congestion in the area limits competition

*The authority's indenture requires debt service deposits from revenues to be made to the trustee only 5 days prior to the payment date rather than in monthly installments, though this is mitigated by the authority's strong liquidity position

MARKET POSITION/COMPETITIVE STRATEGY: RELATIVELY STABLE O&D MARKET SERVED BY DIVERSE CARRIERS; CAPACITY CONSTRAINTS POSE CHALLENGES

The authority derives significant credit strength from the diversity of carriers serving its relatively stable O&D base, accounting for 96% of enplanements. Of the roughly 20 airlines serving the airport Southwest Airlines (rated Baa3) accounted for over 37.7 % of enplanements in FY 2010, with United and Delta ranking second and third largest, at 10.9% and 10.7% of total enplanements, respectively. Fares reportedly remain competitive due to both the number of carriers and the presence of low cost airlines serving the San Diego market.

San Diego County (issuer rating Aa1), located on the Mexican border, is one of the most populous counties in California with approximately 3 million residents. Despite the significant loss of housing values in the current recession the county's strong rating continues to be based on a diverse economy, based in defense, technology industries, trade and tourism. The city of San Diego is rated Aa3. The diversity of the county's economy has helped to move it into recovery according to Moody's Economy.com. The economic recovery is expected to strengthen in 2010 due to growth in tech and defense-related industries. Wealth levels in the county are quite varied, ranging from higher income coastal cities to lower income border communities. The county's historic position as a naval center tends to dampen median income levels, but is a positive credit factor as it continues to expand and provide stability and support population growth. The number of naval vessels stationed in San Diego is expected to more than double to 83 by 2014.

OPERATING PERFORMANCE: DEBT SERVICE COVERAGE REMAINS STRONG BUT IS SCHEDULED TO DECLINE AS DEBT IS ADDED

Though down from 5.625 times in FY 2008, the unaudited senior lien debt service coverage ratio (DSCR) was a strong 3.98 times in FY 2010, which is significantly above the 1.25 times debt service coverage ratio required by the bond indenture. However, the new subordinate lien and all-in DSCRs are forecasted to be considerably lower as Green Build and CIP debt comes on line. Under the base case midpoint forecast, which combines the a base case with a slower economic recovery scenario, minimum DSCR for subordinate bonds is 2.0 times and 1.58 times for total debt service. The midpoint forecast prepared by the authority's traffic consultant assumes enplanements will grow at an average annual rate of 2.8% from 2010 through 2016, which Moody's believes may be optimistic. Though this growth rate is lower than the 4.3% growth achieved during an expansion period from 2002 to 2008, it is lower higher than the 2.1% achieved during a longer-term period (1990-2010) that included periods of economic contraction as well as expansion. Under the slower economic growth scenario the forecast yields 2% average growth, subordinate DSCR of 1.865 times and all-in DSCR of 1.5039 times. In Moody's view failure to achieve these minimum coverage levels could place negative pressure on the subordinate lien rating.

The airport currently derives approximately 42% of its operating revenues from the airlines, in the form of landing fees, building rentals and security surcharges and this is forecasted to rise to 47% by 2016, which is above average compared to similarly rated airports (26.3%). Airline costs per enplaned passenger (CEP) at the airport were $6.71 in FY 2010 , which is close to Moody's median of $6.26 for A1 rated airports. The CEP is forecasted to rise to $10.72 by 2016 under the assumed base enplanement growth scenario.

Total FY 2009 unrestricted cash and reserves equal roughly 1.6x of long-term bonds and outstanding commercial paper (CP). Moody's calculates the authority's FY 2009 days' cash on hand at 385 days, which is below the Moody's median for A1-rated airports of 443 days. Unaudited FY 2010 results show a significant improvement to 537 days cash, primarily due to reimbursement of costs from PFCs and a CP draw.

Under a new 2009 through 2013 airport use and lease agreement the airport calculates landing fee rates based on a cost center residual approach and assesses terminal rents using the compensatory rate-setting method. The new agreement phases in a "commercial compensatory" rate methodology, which allows the airport to increase its recovery of terminal costs from 45% to over 65% by FY 2013. The agreement also maintains the authority's strong gate control and utilization provisions. The forecast assumes that the current rates and charges methodology remains in place after expiration of airline use and lease agreement in 2013.

CAPITAL PROGRAM: LOW DEBT AND RELATIVELY STRONG LIQUIDITY EXPECTED TO CHANGE AS NEW CAPITAL PROJECTS ARE FUNDED

Long-term CEP while currently very low at $6.71 in FY 2010, is forecasted to rise to $10.72 by FY 2016 with the addition of $438 million GARB debt for the $865 million Green Build program and $109 million GARB debt for the $377 million five-year capital improvement plan (CIP). In addition to the GARB debt, funding sources include passenger facility charges (PFCs) ($178 million) and federal grants ($142 million), authority funds ($210.7 million) as well as on-going use of the authority's $250 million commercial paper (CP) authorization. The Green Build program includes 10 new gates, a dual-level access roadway, a new aircraft parking apron and taxi lane, expanded concessions areas as well as security improvements. The program has a reasonable 7.5% program contingency and completion is scheduled for mid-2013. The CIP includes landfill remediation and access improvements, expansion of Terminal 2 East facilities, taxiway improvements and various other infrastructure upgrades.

BACKGROUND

The authority became operational in January 2003, after separating from the San Diego Unified Port District. The authority is governed by a nine-member board of directors representing all areas of the county and appointed by city mayors and county supervisors, plus three ex officio non-voting members. Members serve three-year terms and may be reappointed.

The authority pays the port district $1 per year in rent for the airport footprint (through 2069 or when the airport ceases to operate on the property) and leases adjacent properties at fixed fees. The airport has only one runway (9,400 feet long) and a single full-length taxiway. It has limited land available for expansion (660 acres) and is bordered by San Diego Bay, residential and commercial development, Interstate 5, and a Marine Corps training center. Nearby development and noise concerns have resulted in a departure curfew between 11:30 PM and 6:30 AM.

Moody's expects that the physical constraints of the existing airport will continue to pose limitations on the airport's ability to expand. While the Green Build program will add gates and aircraft parking positions, the single runway continues to be a limiting factor. In addition, construction-related disruptions as the Green Build is implemented could divert some traffic to neighboring airports. There are several airports within approximately 2 hours driving time, including LAX (rated Aa3), Long Beach (A2), John Wayne (Aa3), and Ontario (A2) which provide some competition.

Outlook

The rating outlook on the authority's revenue bonds is stable, reflecting Moody's expectation that the regional economy and significant population base will continue to support sustained demand for air service and that the capital program will be completed as budgeted. The stable outlook is also based on Moody's expectation that the authority will meet forecasts and that debt will be structured as currently planned.

What Could Change the Rating - UP

Better than forecasted traffic and revenues which improve debt service coverage ratios and liquidity levels could have a positive credit impact.

What Could Change the Rating - DOWN

Lower than forecasted traffic and revenue or higher than expected debt needs that weaken debt service coverage ratios as well as delays in completing the Green Build Program could put negative pressure on the ratings.

KEY INDICATORS

Type of Airport: O&D

Rate-making methodology: Hybrid (Cost center residual airside and compensatory terminal)

FY 2010 Enplanements: 8,453,996

FY 2010 vs. FY 2009 Enplanement growth: -1%

FY 2009 vs. FY 2008 Enplanement growth: -9.1%

5-Year Enplanement CAGR 2005-2009: 0.6%

% O&D vs. Connecting, FY 2010: 96%

Largest Carrier by Enplanements, FY 2010 (share): Southwest (37.7%)

Unaudited Airline Cost per Enplaned Passenger, FY 2010: $6.71

Unaudited Bond Ordinance Debt Service Coverage, FY 2010 3.98x

Utilization Factor, FY 2009: 2.66x

FY 2010 Outstanding Debt: [2]

Airport Revenue Bonds, $41.27.3 million

CP: $164 million (of $250 million authorized)

[1] Including outstanding commercial paper.

Related Ratings: San Diego G.O. Aa3; San Diego County Aa1 Pension Obligations

[1] Including outstanding commercial paper.

[2] Before current issue.

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The last rating action on the airport was on March 15, 2010, when we affirmed the A1 rating on the airport's revenue bonds.

RATING METHODOLOGY

The bond ratings were assigned by evaluating factors believed to be relevant to the credit profile of the issuer such as i) the business risk and competitive position of the issuer versus others within its industry or sector, ii) the capital structure and financial risk of the issuer, iii) the projected performance of the issuer over the near to intermediate term, iv) the issuer's history of achieving consistent operating performance and meeting budget or financial plan goals, v) the nature of the dedicated revenue stream pledged to the bonds, vi) the debt service coverage provided by such revenue stream, vii) the legal structure that documents the revenue stream and the source of payment, and viii) and the issuer's management and governance structure related to payment.

REGULATORY DISCLOSURES

Information sources used to prepare the credit rating are the following: parties involved in the ratings, public information, confidential and proprietary Moody's Investors Service's information, confidential and proprietary Moody's Analytics' information.

Moody's Investors Service considers the quality of information available on the credit satisfactory for the purposes of assigning a credit rating.

MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

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