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Summary:

Kansas Turnpike Authority; Toll Roads Bridges

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Long Term Rating	AA-/Stable	Current

Rationale

S&P Global Ratings' long-term rating on the Kansas Turnpike Authority's (KTA) toll revenue bonds outstanding is 'AA-'. The outlook is stable.

Net revenues of the authority secure the toll revenue bonds. Net revenues include toll revenues and rental income from turnpike concessionaires. A common debt service reserve funded to 125% of average annual aggregate debt service provides additional liquidity to bondholders.

KTA has approximately $113 million of toll revenue bonds outstanding. The authority has no direct-purchase obligations, variable-rate debt, or swaps outstanding.

Credit overview

The rating reflects our view of KTA's very strong enterprise and financial risk profiles. We expect recovering overall traffic levels, very strong liquidity, a low debt burden, minimal capital needs, and actions by management post-pandemic to mitigate the effects of somewhat reduced passenger traffic levels will allow the authority to maintain financial metrics and flexibility consistent with a very strong financial risk profile.

Our enterprise risk profile assessment reflects our opinion that the turnpike is an important link in the state and regional economy, as well as a mature toll road. More specifically, the 236-mile Kansas Turnpike, operated by KTA, is the only toll road in the state that faces little competition from toll-free alternative routes and is a key economic link across the U.S. Midwest, connecting to strategic arterial routes in Missouri to the east and Oklahoma to the south. The 41-mile eastern portion to Topeka is a section of U.S. Interstate 70. The rest extends from Topeka to the state's southern border, through Wichita, and includes an 82-mile portion of U.S. Interstate 35. Due to effects of the pandemic, changes in commuting patterns, and an increase in online shopping, from fiscal years 2019-2021, passenger car traffic steadily declined to about 28.1 million from about 33.8 million, while commercial vehicle traffic increased to about 5.5 million from about 5.1 million because of an increase in consumer spending and demand for goods. For fiscal 2021, traffic (including discounts and adjustments) totaled 33.8 million (88% of fiscal 2019), while toll revenues (including discounts and adjustments) totaled $121.5 million (98% of fiscal 2019). KTA's relatively good revenue performance reflects favorable commercial vehicle traffic trends, rebounding passenger traffic levels, and an increase in passenger car violation revenue. As a result of the difference between discounted electronic and higher cash toll rates, transponder usage among commercial vehicles increased to 78% from 73% from fiscal years 2019-2021. As a result, KTA collected less commercial vehicle toll revenue in fiscal 2021 than fiscal 2019, though fiscal 2021 commercial vehicle transactions were higher than fiscal 2019.

Our financial risk profile assessment reflects our evaluation of fiscal 2021 audited results, fiscal 2022 estimated results, 2023 budgeted figures, and an updated toll revenue and traffic forecast. We expect that KTA will maintain strong debt service coverage (DSC) in line with historical levels (2.2x in fiscal 2021, S&P Global Ratings-calculated). Improving traffic levels and declining debt service requirements have helped the authority maintain financial metrics consistent with pre-pandemic levels. KTA has no plans to increase toll rates until cashless tolling is fully implemented in fiscal 2025 to offset an anticipated $20 million decline in toll violation revenues. The authority selected a vendor for the roadside toll collection system and work began on the 42 toll zones and the new back-office system. Although KTA may need to issue debt in five-to-10 years to fund capital improvement projects, we believe it should maintain an extremely strong debt capacity as its EBIDA (S&P Global Ratings Calculated) remains relatively steady or improves as its existing debt amortizes. Despite historically relying on cash reserves rather than debt to fund its capital needs, KTA has maintained a very strong overall liquidity position that we expect will continue. Fiscal year ended June 30, 2021 unrestricted cash balance totaled $163.5 million, equating to approximately 626 days' cash on hand (S&P Global Ratings Calculated) and about 145% of debt outstanding, exceeding KTA's 400 days' cash on hand minimum liquidity policy target. As of June 30, 2022, the authority had an unaudited unrestricted cash and investments balance of about $167 million, equating to about 598 days' cash on hand based on fiscal 2022 budgeted expenditures of approximately $102 million (S&P Global Ratings-calculated). Because the authority uses the modified approach to reporting infrastructure assets, a part of the operating expenses (on a generally accepted accounting principles basis) include preservation expenses, which are cash expenses paid from operating cash flow. As a result, we include preservation expenses in our calculations of DSC, EBIDA, and days cash on hand.

The authority's estimated toll revenues (including discounts and adjustments) for fiscal 2022 totals about $133 million, which is 6.3% higher than budgeted and 6.5% higher than fiscal 2019. Its fiscal 2023 budget assumes toll revenues of $140.5 million and total traffic of 36.3 million or about 96% of fiscal 2019 traffic levels, which we consider reasonable. The fiscal 2023 budget accounts for motorists' response to higher gasoline prices and lower commuter traffic levels. We expect KTA will continue to monitor traffic as fuel prices increase nationally given the strong correlation between changes in vehicle miles traveled and fuel prices and evolving commuter traffic patterns.

KTA is currently in the early stages of developing a tolling plan for when it transitions to all-electronic (i.e., cashless) toll collection in 2024. It last increased toll rates in February 2002, when it did so for transponder and cash customers by 2% and 12%, respectively. Although the authority anticipates that it will fund its all-electronic toll collection system projects with cash reserves, we expect the overall liquidity position to remain very strong.

Key credit strengths, in our view, are the turnpike's:

- Very strong market position, reflecting its role as an important economic link across the U.S. Midwest with limited competition from toll-free routes and generally stable overall traffic trends during previous economic downturns;
- Strong coverage levels (around 2x, per our calculations) and very low debt burden (debt-to-EBIDA below 5x) that we expect to remain so because of declining debt service requirements, a manageable capital improvement

program (CIP), and no additional, new-money toll revenue debt at this time;

- Very strong liquidity position, with an unaudited cash and investments balance of about $167 million as of fiscal year ended June 30, 2022, equating to 598 days' cash on hand (S&P Global Ratings-calculated) that we expect will remain so as a result of steady revenue performance from recovering and normalizing passenger traffic levels, relatively good commercial traffic trends, and limited use of cash reserves to pay for CIP project costs; and
- Very strong management and governance, with a conservative approach to financial and capital planning and track record of achieving financial and operational goals.

Key credit weaknesses, in our opinion are:

- Economic cyclicality, gasoline price shocks, and construction delays associated with the turnpike's preservation, modernization, and enhancement needs; and
- Potential for passenger toll traffic to fall below pre-pandemic levels due to remote work and telecommuting trends.

The stable outlook reflects our expectation that recovering and normalizing traffic levels and limited new-money debt needs will allow KTA to maintain financial metrics consistent with a very strong financial risk profile.

Environmental, social, and governance

We analyzed KTA's environmental, social, and governance (ESG) risks and opportunities relative to its market position, management and governance, and financial performance and determined that all are neutral in our credit rating analysis. Although the turnpike's revenue performance was initially affected by activity declines due to health and safety restrictions during the pandemic, which we view as a social factor, this risk is abating and we do not view it as a material credit factor.

Stable Outlook

Downside scenario

We could lower the rating if coverage declines materially, weakening KTA's overall financial risk profile assessment.

Upside scenario

We could raise the rating if we believe KTA can maintain coverage, per our calculations, at levels we consider very strong (above 3x) on a sustainable basis.

Credit Opinion

S&P Global Ratings believes that currently, economic momentum will likely protect the U.S. economy from recession in 2022. But, with supply-chain disruptions worsening as the weight of extremely high prices damages purchasing power and aggressive Federal Reserve policy increases borrowing costs, economic effects are likely in 2023. Our U.S. GDP growth forecast is 2.4% for 2022 and 1.6% for 2023 (compared with 2.4% and 2.0%, respectively, in May 2022) and, while our baseline signals a low-growth recession, we believe the likelihood of a contraction or technical recession are rising--to 40% (35%-45% band). The wider band reflects increased uncertainty over the Russia-Ukraine conflict. Supply-chain disruptions, worsened by the Russia-Ukraine conflict and the China slowdown, remain the largest stumbling block for the U.S. economy. As inflation expectations become more entrenched, extreme price pressures will likely last well into 2023. We expect the unemployment rate, at 3.6% in May and just over its pre-pandemic level, will remain near that rate until early 2023 before rising to top 4.3% by the end of 2023 and climb over 5.0% by the end of 2025 as the economy slows. The Federal Reserve is now likely to push rates from zero at the beginning of the year to 300 basis points by year-end and reach 3.50%-3.75% by mid-2023. It will keep monetary policy tight until inflation decelerates and nears its target in second-quarter 2024. We expect the Fed will start to cut rates in third-quarter 2024. Our lower GDP and inflation forecasts for 2023 and 2024 reflect this more aggressive policy stance (see "Economic Outlook U.S. Q3 2022: The Summer Of Our Discontent," published June 27, 2022, on RatingsDirect).

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022