

PENNSYLVANIA TURNPIKE UPDATE

JANNEY FIXED INCOME RESEARCH

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Pennsylvania's Auditor General questions solvency of PA Turnpike Commission, but alarm is overstated.

We believe that PTC has adequate resources and revenue to continue supporting its debt.

- PA Auditor General expresses concern about impact of PTC's annual \$450 million payment to state.
- We believe the annual payment has been factored into rating agency and other analysis.
- The essential purpose of the toll road system and PTC's demonstrated willingness to increase toll rates as needed translate into a strong issuer and well secured bonds.

500 MILES OF TOLL ROAD

In recent comments, Pennsylvania's Auditor General said that the Pennsylvania Turnpike Commission (PTC) is in danger of becoming insolvent and may default on debt because of an ongoing obligation of PTC to pay the state \$450 million each year. The PTC CEO responded by saying that "the continued existence of the Turnpike Commission is not in jeopardy, as he alleges, because the PTC has developed a sound, fiscally responsible approach to meet all of its financial obligations, including the \$450 million annual payments."

Under provisions of 2007 legislation, PTC is required to make annual payments to the state to be used to fund non turnpike transportation projects. Initially payments were \$900 million per year, to be financed by toll revenues from expected conversion of I-80, across northern Pennsylvania, into a toll road. Approval for the conversion was not forthcoming, so an agreement was reached to cut the annual payment to \$450 million. As the Auditor General noted, turnpike finances would be stronger if this annual obligation was eliminated, but the payment amount has been well factored into rating agency and other analyses.

Considering a 10% January 1, 2012 toll increase on cash transactions, we believe that PTC has adequate resources and revenue to continue supporting the bonds. Moody's has a negative outlook on its ratings for the various PTC issues based on expectations that debt will continue to grow, with issuance of up to \$5.3 billion in new senior debt in the next 10 years.

Pennsylvania Turnpike Has More Than \$7.5 Billion in Bonds Outstanding

Bond Type	Bonds Out (5-31-11)	Ratings	Revenue Source
Toll Revenue Senior	\$3,004 MM	Aa3/A+/A+	Secured by toll revenues. Sr DSC 3.55 times, Sub coverage is 1.78 times (Fitch).
Toll Revenue Subordinated	\$3,077 MM	A3/A-/A-	
Toll Revenue Subordinated 3rd lien - Motor License Fund Enhanced	\$402 MM	Aa3/NR/AA	3rd lien on revs plus ability to draw on Motor License Fund if revs insufficient. DSC 1.2 times before MLF backing.
Registration Fee	\$436 MM	Aa3/A/AA-	Revenues from motor vehicle registration fees. PTC receives first \$28 million collected annually from total revenue stream of \$200 million per year.
Oil Franchise Tax Senior	\$669 MM	Aa3/AA/NR	Revenue from taxes on wholesale gas and diesel sales.
Oil Franchise Tax Subordinated	\$132 MM	A2/A+/NR	

Source: Janney Fixed Income Strategy, Moody's, S&P, Fitch and PTC Annual Report

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After a decline in 2009, traffic on the 500 mile system increased in FY 2010 and 11. Linking the Ohio turnpike in the west and the New Jersey turnpike in the east, the Pennsylvania turnpike is an essential and busy roadway. PTC raised toll rates as needed in the past. Fitch notes that “traffic has demonstrated relatively low elasticity through toll increases since 2005.”

PTC benefits from some diversity of revenue sources to support bonds, with a variety of issue types, but about 80% of PTC debt is supported by toll revenue. The impact of future debt issuance must be closely watched, and it would be favorable to see PTC’s obligation to make large payments to the state either diminished or eliminated, but the essential purpose of the toll road system and PTC’s demonstrated willingness to increase toll rates as needed translate into a strong issuer, and well secured bonds.

The impact of future debt issuance must be closely watched.

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