S&P Global
Ratings

Research

Research Update:

Irish Airport Operator daa PLC Rating Raised To 'A' On Sovereign Upgrade; Outlook Stable

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Rating Action Overview

- Following our upgrade of Ireland to 'AA-' from 'A+', we believe Ireland's government has an increased capacity to support state-owned airport group daa PLC (daa), if needed.
- We continue to believe there is a moderately high likelihood that daa would receive timely and sufficient extraordinary support from the government.
- Our stand-alone credit profile (SACP) on daa remains 'a-', after the Commission for Aviation Regulation (CAR) released the final determination to set aeronautical charges at an average of €7.87 for the next regulatory period 2020-2024, up from €7.50 in the draft determination.
- Therefore, we are raising our long-term issuer and issue credit ratings on daa to 'A' from 'A-', and our short-term rating to 'A-1' from 'A-2'.
- The stable outlook reflects our expectation that daa will maintain weighted average S&P Global Ratings-adjusted funds from operations (FFO) to debt between 20% and 30% in the 2020-2024 price control period. The credit metrics will be constrained by lower aeronautical charges while the company completes significant investments.

Rating Action Rationale

Our revised issuer credit rating (ICR) on Irish airport operator daa to 'A' from 'A-' follows our upgrade of Ireland, to 'AA-/A-1+' from 'A+/A-1' (see "Research Update: Ireland Upgraded To 'AA-/A-1+' From 'A+/A-1' On Prudent Policies and Vigorous Growth; Outlook Stable," published Nov. 29, 2019). We also raised our short-term rating on daa to 'A-1' from 'A-2'.

At the same time, our ratings on daa reflect our expectation of a moderately high likelihood of extraordinary state support from Ireland, and daa's SACP, which we continue to assess at 'a-'.

In October 2019, CAR released its decision to set Dublin Airport charges at €7.87 (in real terms) per passenger on average during the regulatory period starting Jan. 1, 2020 and ending Dec. 31, 2024. The annual aeronautical charges cap will increase to €8.32 in 2024 from €7.50 in 2020 (in real terms), compared with €7.50 in the draft determination issued in May 2019 (see "Irish Airport Operator daa PLC Outlook Revised To Stable On Expected Lower Tariffs; 'A-' Rating Affirmed," published July 3, 2019). The regulator also increased the weighted average cost of capital (WACC) to 4.2% (pre-tax) in 2020-2024, from the 4.0% proposed under the draft determination, to reflect risks related to delivery of the €2.4 billion expansion during the period. Despite the final determination's slightly more favorable terms, we continue to expect FFO to debt to deteriorate to within the 20%-30% range, down from 58.7% in 2018.

In addition, we still expect daa's aeronautical and commercial revenue will be insufficient to cover its highest-ever investment program, which will result in negative discretionary cash flow (DCF) over the period and deterioration of the credit metrics. The extent of credit metrics' deterioration will depend on the pace of air traffic growth, which in daa's view is likely to soften in response to the macroeconomic slowdown in Europe, a potential Brexit-related disruption, and a prolonged grounding of the Boeing 737 Max aircraft. The 737 Max situation has led to a reduced traffic-growth forecast for Ryanair, Dublin Airport's largest airline, which in 2018 served 42% of the airport's passengers.

Outlook

The stable outlook on Irish airport operator daa reflects our view that we expect the company to maintain S&P Global Ratings-weighted average adjusted FFO to debt in 2020-2021 between 25% and 30%. The credit metrics will be constrained by the lower aeronautical charges in the 2020-2024 price control period, and daa completing significant investments. As daa generates more than 30% of its traffic from the U.K., the annual growth in passenger volumes will likely slow down to low single digits in response to macroeconomic slowdown in Europe, a potential Brexit-related disruption, and a prolonged grounding of the Boeing 737 Max aircraft.

Downside scenario

We would lower the SACP to 'bbb+' and ICR to 'A-' if we were expecting daa's weighted average adjusted FFO-to-debt ratio to fall below 20%.

Upside scenario

While daa continues to benefit from a moderately high likelihood of extraordinary state support, we would raise the ICR if we expected S&P Global Ratings-adjusted FFO to debt sustainably above 35% throughout 2020-2024, while completing significant investments. We could also increase the SACP to 'a' if we were expecting daa to maintain a weighted average adjusted FFO-to-debt ratio above 30% on sustainable basis, although this would have no impact on the ICR, which would remain 'A'.

Company Description

daa owns and engages in the development, operation, and management of airports in Ireland. It operates the two largest airports in the country, Dublin and Cork, which together welcomed 33.9 million passengers in 2018. Dublin Airport is the key gateway for Ireland, accounting for more than two-thirds of all air travel to Ireland, or 31.5 million passengers, in 2018. In 2018, Dublin Airport generated 66% of daa's revenue and 94% of its EBITDA. The company is also involved in airport-related activities, duty-free shopping, property development, and car parks. Through its wholly owned subsidiary Aer Rianta International, daa operates airport retail businesses in the Middle East, the Americas, New Zealand, and Cyprus, and holds minority stakes in other airports (a 20% stake in Dusseldorf airport in Germany and an 11% stake in Paphos and Lanarca airports in Cyprus).

Our Base-Case Scenario

Our base case for 2019-2023 assumes:

- Traffic growth at a rate slightly lower than Ireland's real GDP growth, which we forecast to increase by 5.8% in 2019 and 2.7% in 2020 and 3.0% 2021. Traffic volumes to increase by 4.0%-4.5% in 2019, slowing to about 1.0%-1.5% annually on average between 2020 and 2023.
- Aeronautical charges in Dublin Airport of €7.87 per passenger on average in 2020-2024 in real terms, or €7.6-€9.0 in nominal terms, following the regulatory reset. Tariff to benefit from an additional €0.26 per passenger once the runway is complete. We index nominal aeronautical charges to the consumer price index (CPI), which we forecast will increase by 1.0% in 2019, 1.4% in 2020, and 1.5% in 2021.
- Domestic commercial revenues (retail, property and concessions, car parking, and other) to increase proportionally with traffic and Irish CPI growth.
- International activities to grow proportionally with the GDP growth and CPI growth of the respective regions. The international revenue is generated primarily from Cyprus, New Zealand (Auckland), Middle East, and North America.
- Costs to be a function of passenger numbers and the CPI. Payroll to increase at a slightly higher rate than CPI, because we assume wage inflation of 2.5% over the forecast period. Materials and services costs to increase in line with passenger number growth and CPI growth. Overall, operating costs of about €620 million-€650 million in 2019, rising to about €740 million-€770 million in 2024.
- About €2.4 billion capital expenditure (capex) over 2019-2024, including €320 million for the construction of the North Runway and other investments at Dublin Airport. We expect an outlay of €200 million-€250 million in 2019, increasing to €350 million-€450 million in each of 2020 and 2021.
- Dividend distributions of 30% of the previous year's net income, equal to €30 million-€40 million per year.

Based on these assumptions, we arrive at the following credit measures:

- Adjusted EBITDA of €310 million-€330 million in 2019, declining to €250 million-€300 million annually in 2020-2021.
- FFO to debt of 50%-60% in 2019, falling to 27%-32% on average over 2020-2022, before declining further toward 22% in 2023.
- Debt to EBITDA of 1.3x-1.7x over 2019 and increasing to about 3x-4x in 2023.
- Negative DCF of €150 million-€250 million in each year from 2020 through 2023, reflecting higher capex.

Liquidity

We view daa's liquidity as strong. We estimate that sources of liquidity in the 12 months to Sept. 30, 2020 will exceed uses by more than 1.5x, and that liquidity coverage in the following 12 months will be more than 1.0x.

In our view, daa should be able to withstand substantially adverse market circumstances over the next 24 months, while still having sufficient liquidity to meet its obligations. This view is supported by our expectation that sources of cash will exceed uses, even if forecast EBITDA declines by 30%, and that the company will be able to absorb high-impact, low-probability events without refinancing. In our view, management exercises prudent risk management, and has ensured that the company has maintained continued strong liquidity, in particular ahead of construction of the North Runway. daa has a high standing in the credit markets, and its debt documents remain favorable with very limited clauses and covenant protections, which include a change of control clause.

We expect daa's principal liquidity sources for the 12 months to Sept. 30, 2020 will include:

- Surplus cash and liquid investments of about €350 million;
- Availability of €300 million under the revolving credit facility that expires in November 2022, and a €350 million European Investment Bank (EIB) loan signed in June 2019, available to June 2022; and
- Cash flows from operations of about €250 million-€260 million.

We expect principal liquidity uses over the same period will include:

- Debt maturities of about €40 million-€50 million;
- Capex of about €320 million-€340 million; and
- Dividends of about €40 million-€50 million.

Government Influence

We view daa as a government-related entity. It is 100% owned by the Irish government and is a strategic asset for Ireland. In our view, there is a moderately high likelihood that Ireland (AA-/Stable/A-1) would provide timely and sufficient extraordinary support to daa in the event of financial distress. This reflects our assessment of daa's:

- Important role for Ireland, owing to the company's strategic role in relation to air access and general economic development in Ireland; and
- Strong link with the Irish government. We understand that the Irish government is not considering the privatization of Dublin Airport, because of its strategic value to the state. Nevertheless, we anticipate that the independent regulatory regime, established under the Aviation Regulation Act 2001, would be the primary source of financial support to daa. It is government policy that daa should operate on a commercial basis.

Issue Ratings - Subordination Risk Analysis

Capital structure

As of December 2018, daa held EIB loans of about €190 million. daa Finance PLC, the subsidiary, held the remainder of the group's financial debt, which included about €213.8 million in loans from the EIB and about €400 million of notes listed on the Irish Stock Exchange. daa guarantees this debt.

The rating on the €612 million of unsecured debt issued by daa Finance PLC is the same as the long-term ICR on daa, because the debt benefits from a corporate guarantee.

Ratings Score Snapshot

Issuer Credit Rating: A/Stable/A-1

Business risk: Strong

- Country risk: Low Risk
- Industry risk: Low Risk
- Competitive position: Strong

Financial risk: Modest

- Cash flow/Leverage: Modest

Anchor: a

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: a-

Government support: A

- Sovereign rating: AA-/Stable/A-1+
- Likelihood of government support: Moderately high (+1 notch)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global

Corporate Issuers, Dec. 16, 2014

- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | Industrials: Key Credit Factors For The Transportation Infrastructure Industry, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Research Update: Ireland Upgraded To 'AA-/A-1+' From 'A+/A-1' On Prudent Policies and Vigorous Growth; Outlook Stable, Nov. 29, 2019
- Industry Top Trends 2020: Transportation Infrastructure, Nov. 21, 2019
- Irish Airport Operator daa PLC Outlook Revised To Stable On Expected Lower Tariffs; 'A-' Rating Affirmed, July 3, 2019
- ESG Industry Report Card: Transportation Infrastructure, June 3, 2019
- daa PLC, Jan. 10, 2019

Ratings List

Upgraded

	To	From
daa PLC		
Issuer Credit Rating	A/Stable/A-1	A-/Stable/A-2
daa PLC		
Senior Unsecured	A	A-
daa Finance PLC		
Senior Unsecured*	A	A-

*Guaranteed by daa PLC.