TAX-EXEMPT CREDIT PERSPECTIVES: TOLL ROAD BONDS

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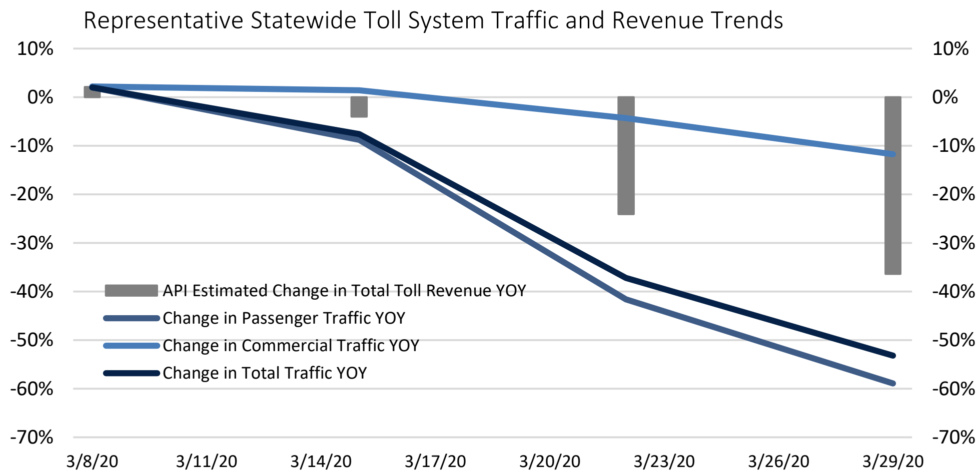
What are Toll Road Bonds?

Toll Road bonds are municipal revenue obligations issued by transportation agencies or related municipal authorities to fund highways, bridges or tunnels. Unlike General Obligation bonds, Toll Road bond issues are dependent on dedicated user fees, not diverse revenue sources. As a result, the highly unusual and abrupt drop in revenue resulting from a prolonged curtailing of national economic activity is raising concerns about near-term credit fundamentals.

How Has This Sector Been Impacted by the Economic Environment?

Bond disclosure reveals the extent of recent Toll Road revenue declines. Year-over-year data reported by authorities in Florida, Illinois, Pennsylvania and New York State, among other states, suggest that total highway traffic fell in the vicinity of 25-35% over the 3rd week in March, with revenue declines accelerating the following week. How severe the drop off remains and for how long is uncertain and largely dependent on easing of economic restrictions.



Source: Illinois State Toll Highway Authority

Is There Potential Value in the Toll Road Sector?

We feel credit analysis is ultimately a security specific exercise and see meaningful distinctions among Toll Road bond issues. Overall, we are cautious on near-term sector fundamentals and anticipate moderate downgrade risk. However, we try and build a margin of safety into all our bond holdings and proprietary stress testing indicates that certain issuers have the resources to weather a prolonged shutdown. Given recent market pressures, we are very selectively adding to Toll Road exposure when creditworthy bonds become available at attractive prices. These issuers are likely to be early beneficiaries of economic re-opening and eventual recovery.

What Credit Factors Are Important to Your Analysis?

Our assessment of a bond issuer's ability to maintain credit quality through a sustained downturn emphasizes several metrics. These determinants can help separate value from potential credit impairment.

Debt service coverage	Net operating cash flow relative to debt obligations due within the next year reveals the extent to which a cushion is available to absorb revenue declines.
EBIDA (cash flow) margin %	In a somewhat similar manner as debt service coverage, this calculation assesses operating leverage before debt expense.
Days cash on hand	This liquidity measure details the extent to which an additional layer of protection exists should declining revenue become insufficient to cover debt service and other expenses.
Commercial vehicle revenue mix	We typically prefer a higher reliance on passenger vehicles, although recent Toll Road issuer disclosure indicates that commercial traffic has declined less than passenger vehicles. Commercial vehicles also pay higher tolls, thereby helping to offset passenger vehicle traffic declines.
Service Area	We feel statewide systems are somewhat more secure as they offer geographic diversity and tend to be more essential to commercial transportation.
Credit linkage	Certain revenue bond issues are interconnected from a credit standpoint with State GOs, a factor that can either be positive or negative depending on the circumstances. Our analysis considers structural linkages of this nature.

Economic and market stress introduces credit challenges as well as value opportunities. Fundamental analysis offers invaluable insight as we look to differentiate individual bond issuers.

Accessibility and communication are important in any environment, although these attributes are especially valuable during uncertain and volatile times. Appleton Partners is committed to sharing our market and portfolio management perspectives as developments unfold. We hope these briefs are helpful and also invite you to reach out to us directly and/or visit www.appletonpartners.com/Insights for additional commentary and insights.

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