FitchRatings

Fitch Rates Hudson Yards Infrastructure Corp. (NY) Senior Revs 'A'; Outlook Stable

Ratings
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Fitch Ratings-New York-27 September 2011: Fitch Ratings has assigned a rating of 'A' to the following Hudson Yards Infrastructure Corporation's (HYIC or the corporation) senior revenue bonds:

--$1 billion, fiscal 2012, series A.

The bonds will be offered through negotiation and are expected to be delivered on or about Oct. 19, 2011. Proceeds will finance a portion of the costs of various projects undertaken to support future development of the Hudson Yards financing district, an approximate 45-square-block area in west central Manhattan.

Proceeds from the sale will fund the design and construction of an extension of the No. 7 subway line, the construction of a system of parks, public open spaces and streets in the project area, and certain property acquisition.

In addition, Fitch affirms the 'A' rating on $2 billion of outstanding senior revenue bonds.

The Rating Outlook is Stable.

SECURITY
The bonds are special obligations of HYIC payable from a combination of recurring and one-time revenues expected to be generated from development in the Hudson Yards area of Manhattan.

Recurring revenues include payments in lieu of taxes (PILOTs) under agreements between property owners in the project area and the New York City Industrial Development Agency (NYCIDA) or Metropolitan Transportation Authority (MTA); tax equivalency payments (TEPs) representing an amount equal to real property taxes; and PILOTs collected by the city if PILOT agreements are not entered into with the IDA or MTA. PILOTs flow directly to the bond trustee and TEPs must be appropriated by the city.

Bondholders are further secured by interest support payments from the City of New York, subject to appropriation, sufficient to enable the corporation to pay interest on up to $3 billion in bonds to the extent project revenues are insufficient for such purpose. The corporation will have issued $3 billion in supported bonds following delivery of the series 2012A bonds. The indenture prohibits the issuance of more than $3 billion in bonds supported by the city's interest support payments absent a city council resolution to increase the amount of interest support. The city is not obligated to pay principal on the bonds.

One-time development-related revenues include payments in lieu of mortgage recording taxes (PILOMRTs) which are made as part of PILOT agreements, district improvement fund bonus payments (DIBs) made in exchange for approval of greater density than base zoning allows, and proceeds from the sale of the transferrable development rights of the eastern railyards (up to $200 million plus interest).

KEY RATING DRIVERS
--The 'A' rating is primarily supported by New York City's commitment to the Hudson Yards project, most notably, its obligation, subject to appropriation, to pay interest on up to $3 billion of bonds if project revenues are insufficient for this purpose. Fitch rates the city's general obligation bonds 'AA' with a Stable Outlook.
--Key credit concerns center on risk inherent in a security that relies on prospective development, which could be affected negatively by delays in construction completion, competition from other development projects, and changes in the broader economy and the real estate and financial markets.
--The bonds have a nominal final maturity of April 1, 2047 and installment payments do not commence until the project has demonstrated self-support from recurring revenues. The amortization structure, in conjunction with the city's interest payment commitment, allows time for construction and development delays and the phase-out of tax incentives.
--The project area represents an attractive location for development, reflecting the city's unique role as a national and international center for commerce and culture, the project area's proximity to the city's midtown central business district, and a lack of development capacity that restrains future new office building space.

CREDIT PROFILE

NYC Credit Support
The city's interest support, in conjunction with the flexible principal repayment structure noted below, serves to underpin the current rating. The city's interest support commitment is for the life of the bonds. To take maximum advantage of this benefit, interest is subordinate to principal (to ensure all other project revenues are applied first to principal).

The mechanism for this backstop, which is laid out in an agreement between the HYIC and the city, provides that by April 1 of each year the corporation shall provide the city with the expected amount of interest support needed in the following fiscal year for inclusion in the mayoral budget submitted to city council. The request for interest support is included in the city's general debt service appropriation bill. If at any time the appropriation enacted for such fiscal year is no longer sufficient, the mayor shall take action to seek an increase in the appropriation from city council.

The city has made $157 million in grants and support payments to the corporation for fiscal years 2010 through 2012 (appropriated). The city's current financial plan assumes interest support payments of approximately $138 million in each of fiscal years 2013 through 2015 (or approximately 2% of the city's total debt service appropriation). The corporation projects the city will pay interest on the bonds through 2018.

Flexible Bond Structure
The series 2007A bonds and series 2012A bonds are structured as term bonds with a final maturity of Feb. 15, 2047. No sinking fund installments shall be scheduled until the conversion date, which is the date the corporation has certified to the trustee that net recurring revenues for each of the immediately preceding two fiscal periods equal at least 125% of maximum annual debt service (MADS) on outstanding senior bonds or 105% of MADS on all outstanding bonds. MADS is calculated assuming level or declining debt service amortization beginning in the fiscal year after conversion. Subsequent to the conversion date, the obligation of the corporation to pay sinking fund installments on outstanding bonds is only to the extent that money is available therefore.

Prior to conversion, all project revenues must be used to pay bond interest and corporation expenses. If excess revenues are available after interest has been retained for the subsequent fiscal year, revenues then pay down principal once bonds are callable. No project revenue flows to the city until after conversion, except for reimbursement for bond interest paid by the city in that fiscal year, if any.

Hudson Yards Development and Revenues
The bonds are ultimately secured by revenues expected to be generated from development in the Hudson Yards area of Manhattan. The project area is a roughly 45-square-block area from West 43rd Street, 7th & 8th Avenues, to 30th Street, 11th & 12th Avenues. In 2005 the city re-zoned this area from primarily manufacturing and low-density commercial use to allow for a medium- to high-density (office building, hotel, residential) extension of the midtown central business district. Consistent with the city's demonstrated support of the project, the NYCIDA has adopted tax incentives for the area to encourage commercial development.

Cushman & Wakefield (C&W) updated its 2006 demand and development study in conjunction with the series 2012A bond sale. The report projects demand for 50.6 million square feet (msf) of new mixed-use development in the project area. Since 2005 7.3 msf of new private residential and hotel development has been completed within the project area, yielding the corporation TEP and DIB revenue totaling $53.8 million and $85.1 million, respectively, through fiscal 2011.

The recession has delayed office development, relative to C&W's 2006 forecast, and no PILOT agreements have been entered into to date. In 2008 development rights to 11.9 msf of space presently constituting the east and west rail yards were awarded by the MTA to the Related Companies (Related). The corporation reports Related is actively marketing two proposed office towers to a number of potentially large tenants, and believes Related will announce an agreement with at least one anchor tenant before the end of the calendar year. Under this scenario the first commercial office building would be scheduled to come on-line by 2015. Recurring revenues would provide coverage to satisfy the conversion test in 2026; consistent with the series 2007 bond sale forecast.

Over the forecast period, cumulative revenue generation is greater than previously anticipated, due to the increased availability of developable space (the western rail yards were rezoned by the city in 2009 for 5.7 msf of new mixed-use development). Total recurring and non-recurring revenues through 2050 are projected at $35.1 billion and $1.8 billion, respectively, more than sufficiently supporting debt service payments on the bonds. Under one of several stress scenarios examined by the C&W report, full and timely payment still occurs even if only 29% of projected project revenues is realized. The revenue conclusions are based on certain real estate, demographic, and economic assumptions, which the C&W report concludes are reasonable.

No. 7 Subway Extension

To foster private development, the city committed to fund the extension of the #7 subway line west and south to a new station at 11th Avenue and 34th Street. The subway extension is critical to the Hudson Yards project; office building development in Manhattan is dependent on subway access, and the area is currently underserved. Upon completion of the subway extension most of the Hudson Yards will be within a 10-minute walk of a subway station.

The subway extension is the largest public infrastructure component of the Hudson Yards project, and the bulk of corporation bond proceeds are for this purpose. The corporation reports essentially all property interests required for the subway extension have been acquired and 65% of the project work is complete (including all subway tunnel excavation). Contracts have been awarded covering 90% of the project budget. The series 2012A bonds are expected to provide sufficient funds to complete the project. The extension is expected to be operational on schedule by late 2013.

Project Administration
The HYIC is a local development corporation created by the city to finance the Hudson Yards project. HYIC does not engage in the development directly, but finances the development which is managed by Hudson Yards Development Corporation (HYDC) in coordination with the city, the MTA, the New York City Economic Development Corporation (NYC EDC), and the city's Office of Management and Budget (OMB). The majority of the members of the board of directors of both HYIC and HYDC are appointees of the New York City mayor, and the staff of both organizations is largely comprised of members of OMB and former officials of the NYC EDC.

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In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, Zillow.com, National Association of Realtors, and Property and Portfolio Research.

Applicable Criteria and Related Research:
'Tax-Supported Rating Criteria', dated 15 Aug. 2011;
'U.S. Local Government Tax-Supported Rating Criteria', dated 15 Aug. 2011.

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