

THE NORTHWEST SEAPORT ALLIANCE
MEMORANDUM

MANAGING MEMBERS
STAFF BRIEFING

Item No.	2
Date of Meeting	February 4, 2021

DATE: January 28, 2021
TO: Managing Members
FROM: John Wolfe, CEO
SUBJECT: 5-Year Look Back Performance of NWSA

A. BRIEFING

This memo is intended to provide an overview of the performance of the NWSA over the past five years (2015 – 2020)

B. BACKGROUND

In 2014, the Ports of Tacoma and Seattle entered discussions under a Federal Maritime Commission (FMC) agreement to evaluate alternative approaches to manage the international marine cargo activities in the Pacific Northwest gateway. These discussions were in response to changing market conditions that included fewer shipping lines, larger ships, significant public dollar investments in cargo terminals and capacity expansion in Canadian Ports.

In 2015, the Ports of Seattle and Tacoma (HomePorts) signed an Interlocal Agreement which created the Northwest Seaport Alliance (NWSA) and approved the NWSA Charter, the foundational document that dictates NWSA governance, management and operations. The Charter was approved by the FMC and any changes to it require FMC approval. The Charter provides that the NWSA is overseen by two Managing Members (MMs), which consists of the HomePort Commissioners, each acting through their two boards. The NWSA is the first Port Development Authority (PDA) in the state of Washington.

- Ports are special purpose districts governed under RCW Title 53. A new chapter 53.57 RCW was adopted by the state to allow for the development of a PDA.
- Port powers or statutory compliance requirements did not change (ex. Maintain debt coverage requirements, statutory budget filing, environmental stewardship, public records and Open Public Meetings Act compliance)
- Marine cargo business activities included properties that were licensed for use by the HomePorts to the NWSA.

The impact on the two HomePorts was very different: the properties licensed to the NWSA by the Port of Tacoma represented approximately 85% of its revenue generating activities, while the Port of Seattle's licensed properties represented less than 20% of its overall revenue generating activities and approximately 60% of its non-airport revenues.

Two key factors contributed to these differences:

1. The Port of Seattle is a larger entity due to the airport.
2. The Port of Seattle marine cargo activities were predominantly landlord lease agreements (tenants provide majority of maintenance), while the Port of Tacoma business model is a hybrid approach which included landlord leases, crane ownership, rail yard operations and direct operation on non-containerized cargo activities (autos, breakbulk)

C. THE SHIPPING INDUSTRY ENVIRONMENT AT THE FORMATION OF THE NWSA

At the time of the formation of the NWSA, the Ports of Seattle and Tacoma were collectively the third largest trade gateway in the United States. The two Ports' marine operations were similar in size in many significant ways and only 30 miles apart.

The Ports had invested billions of dollars in their marine cargo facilities and the Ports prospered for many years in attracting cargo that generated jobs and revenue for the region. More than half the cargo that came through the Ports were bound for destinations outside of the Puget Sound region (primarily the Midwest). Such cargo was discretionary, insofar as the shippers and carriers had choices about which ports and routes they used to offload their cargos. If the Ports couldn't retain this discretionary cargo, the Ports, terminal operators and communities that had invested heavily in these terminal facilities would suffer.

The reasons for the formation of the NWSA are still valid. Those reasons include the following:

1. Increasing competition for cargo from ports all over North America has continued unabated. Competing ports on the West Coast of North America have historically competed with Seattle and Tacoma. Ports in the Gulf and East Coast, however, are emerging as new competitors because of the Panama Canal widening and they are seeking to pry away Seattle and Tacoma's market share of Midwest-bound discretionary cargo.

A major contributing factor for the formation of the NWSA was to eliminate competition between the Ports of Seattle and Tacoma to better position the ports to remain competitive on the West Coast.

2. The shipping lines have been steadily increasing the size of their vessels. This trend towards larger vessels inevitable leads to fewer vessels in use, and therefore fewer port calls. Due to this fact, the formation of the NWSA would allow major infrastructure investments to be coordinated in both the north and south harbors.
3. The shipping lines have also continued to form alliances to reduce their operating costs. Such consolidation also leads to fewer port calls as they seek to rationalize their resources. With the formation of the NWSA, it would allow approaching the customer base as a single "Gateway" rather than as individual ports, offering better solutions to the shipping lines.
4. The formation of the NWSA would combine the efforts of both ports for added political power to achieve strategic initiatives at the local, state and federal levels.

D. ACCOMPLISHMENTS

The following section provides a summary by year of the major accomplishments since the formation of the NWSA

2020 ACCOMPLISHMENTS

- Passage of HMT Reform
- Implemented an **IPI Rail Incentive program** in partnership with the BNSF targeting specific inland destinations for incremental growth. Ten (10) Ocean Carriers signed up and the program resulted in 3,718 incremental rail lifts in Q3
- Executed the **Second Lease Amendment at the West Sitcum Terminal** with SSA in support of Matson's Hawaii business relocating from Seattle to Tacoma. In addition to the 27 acres, staff renegotiated and reset the lease rate for the entire leasehold area, resulting in an additional \$4 to 5 million for the balance of the lease.
- Executed the **3rd amendment with Yang Ming** anchoring its IPI business in our gateway for a couple more years
- Partnered with WWL on new auto account - **VOLVO** - which will provide an estimated \$250,000 in revenue
- Secured **\$10.7 million Port Infrastructure Development Program grant** for Terminal 5
- **T-5 Tenant Stormwater Treatment** - Received and executed Department of Ecology Grant \$5 million; West Sitcum and WWS auto stormwater treatment systems meeting all required benchmarks
- Prevailed on summary judgment in the **W. Sitcum litigation** on two important issues: 1) the court confirmed the limited scope of the Industrial Stormwater General Permit; and 2) the court found that the Port of Tacoma did not violate its Permit. The Port has been dismissed from the lawsuit.

2019 ACCOMPLISHMENTS

- Realigned the overall customer base in the North Harbor, including securing a long-term customer and funding for redevelopment at Terminal 5.
- Authorized the construction phase of the Terminal 5 redevelopment project.
- Updated the support services agreements between the Homeports and the NWSA.
- Completed the removal of several obsolete cranes in the North Harbor.
- Entered an agreement with the Port of Seattle to utilize a portion of Terminal 46 for expansion of the Cruise business.
- Finalized the one-time membership interest affirmation.
- Finalized the NWSA Total Rewards program.
- Financial statement audit and SAO compliance audits completed with "No Findings".

2018 ACCOMPLISHMENTS

- Finalized the future management structure for the NWSA and Homeport of Tacoma.
- Completed a work space/HQ needs assessment followed by a market search for NWSA office space for staff supporting the commercial, operations, and support functions.
- Completed an assessment associated with developing a total rewards program including an implementation plan.
- Implemented a clean truck compliance program.

2017 ACCOMPLISHMENTS

- First financial statement audit and SAO compliance audits were completed with “No Findings”.
- Completed the phase 1 work associated with the Work space needs assessment.
- Completed the public procurement to retain a resource to conduct the Total Rewards assessment and implementation plan.
- Documented the processes and work flows associated with the Lease Administration for the NWSA.
- Documented alternatives for a post transition organization model.

2016 ACCOMPLISHMENTS (YEAR ONE)

- Integrated the customer facing and operations teams into the NWSA.
- Created the initial NWSA budget including support service agreements with the Homeports.
- Created financial statement preparation and accounting processes and controls in support of the NWSA.
- Established segregated Public Records processes for the NWSA.
- Established an NWSA Audit Committee.
- Obtained Washington Court of Appeals Ruling that Federal Shipping Act pre-empts state OPMA laws, which preserves NWSA ability to hold FMC meetings, if needed.
- Authorized a long-term lease extension, terminal improvements and the purchase of new cranes at the Husky terminal in the South Harbor.

E. NWSA 5-YEAR FINANCIAL HISTORY

- a. Provided by PowerPoint presentation

Item No.:

Date of Meeting: February 4, 2021

5-Year Look Back of NWSA

Name: David Morrison
Title: Chief Financial Officer



THE NORTHWEST
SEAPORT ALLIANCE

SEATTLE + TACOMA

Summary: Why was the NWSA formed in 2015?

- The Ports of Seattle and Tacoma were competing with the other West Coast gateways, and the Panama Canal widening expanded the competition to the Gulf and East Coast Ports. The Ports felt that by combining our efforts, we would be in a stronger position to maintain international container market share.
- Eliminate any form of competition between the Ports of Seattle and Tacoma with all types of cargo in order to:
 - ▶ Address under-utilized terminal capacity.
 - ▶ Justify terminal investments in each harbor that could handle larger vessels.
 - ▶ Point to greater job growth and economic development within each County.
 - ▶ Maintain sustainable financial return on investments.
- Leverage the political strength of the two Ports working together at the local, state, and federal levels of government to advance our gateway initiatives.
- Approach the marketplace as a single gateway, providing higher levels of service to our customers.
- The Alliance was formed to balance the regional value of jobs and economic activity with finance and environmental sustainability.

NW Seaport Alliance Scorecard

September 30, 2020



CARGO VOLUME

	2019 Total	2020 YTD Actuals	2020 Budget
<u>Containers (TEUs)</u>			
International	3.1 M	1.9 M	3.3 M
Domestic	0.7 M	0.5 M	0.7 M
Break Bulk (Metric Tons NH & SH)	246 K	217 K	306 K
Autos (Units NWSA & POT)	156 K	109K	160 K



JOB CREATION

	2019 Total	2020 YTD Actuals	2020 Target
ILWU Hours	4.7 M	2.7 M	4.7 M



FINANCIAL RETURNS

\$ in millions

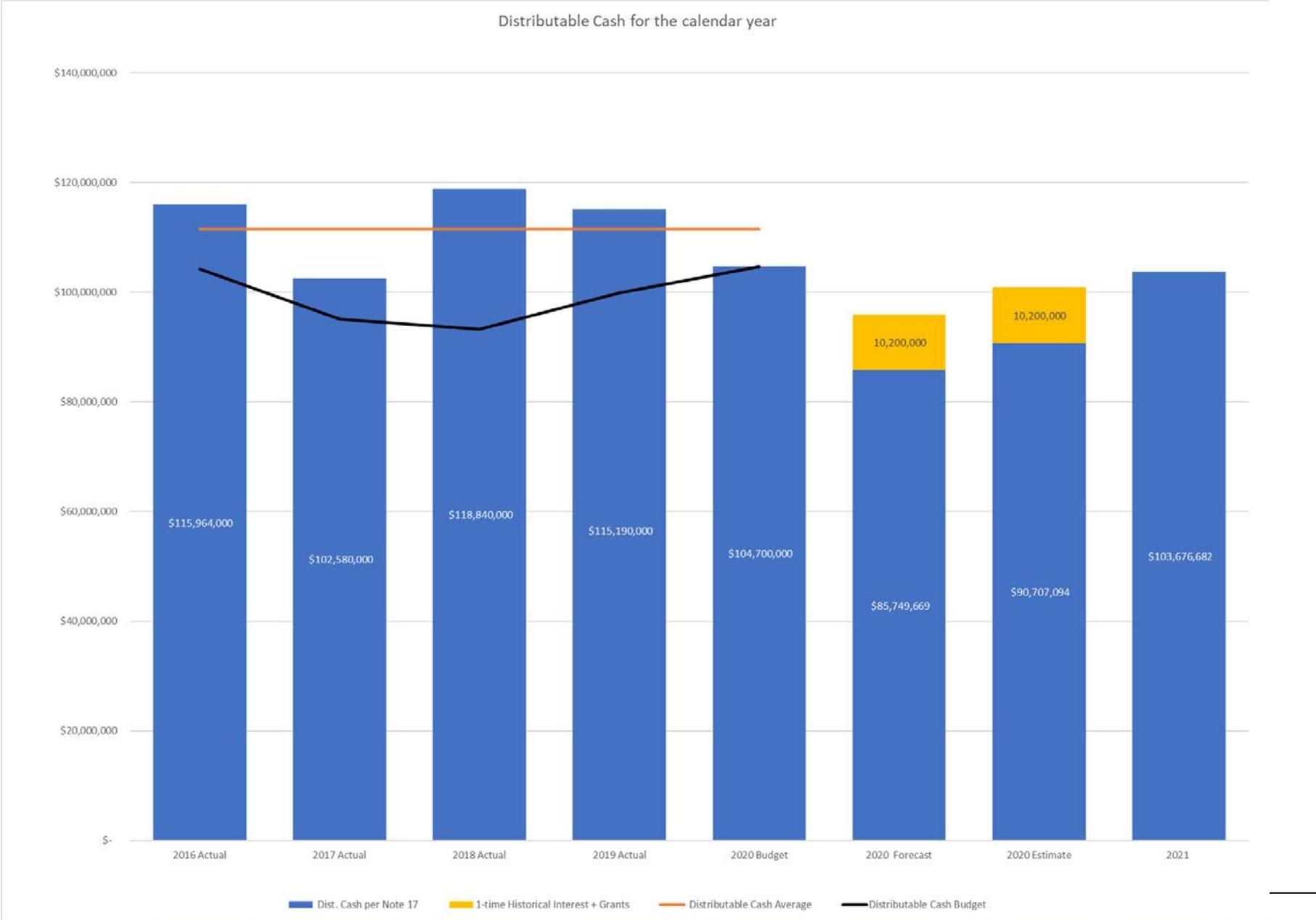
	2019 Total	2020 YTD Actuals	2020 Total Budget
Operating Income <i>(Before GASB 87 Adjustment & Depreciation)</i>	\$105.8	\$71.8	\$97.6
Return on assets	7.1%	5.7%	5.8%



ENVIRONMENTAL STEWARDSHIP

	2019 Results	2020 Actuals	2020 Target
Water Quality (Improve Source Control)	195 Acres	Total 79 Acres: NIM - 22, NIM N. - 12 E. Sitcum - 14, Maint. Shop - 3, EB1 - 6, SIM - 22	65 Acres
Air Quality (Reduce Greenhouse Gas Emissions)	15% Terminals; Executed Fuel Efficiency Plans	15% Terminals; Executed Fuel Efficiency Plans	36% Container Terminals Executed Fuel Efficiency Plans

Distributable Cash



Business Case (2015 to bond rating agencies)

- **Container shipping business is dynamic and competitive**
- **Recent changes include**
 - ▶ Shipping alliances that influence routing and pricing
 - ▶ Growth in ship size that requires facility changes
 - ▶ Economic downturn that has reduced volumes
 - ▶ Lack of national coordination on facility investments that results in over capacity
 - ▶ Panama Canal widening to be completed 2016
- **Puget Sound Ports Position**
 - ▶ #3 gateway in U.S (in 2015)
 - ▶ Good intermodal connections and overall shipping time from Asia
 - ▶ Existing terminals too small for ultra-large ships
- **Strategic Response: Ports of Tacoma and Seattle form an alliance to manage facilities**
 - ▶ Coordinate customer relationships
 - ▶ Improve capacity utilization
 - ▶ Rationalize strategic investments
 - ▶ Combine forces to leverage political influence

Canadian competition in 2015

- Factors making Canada a significant competitive threat
 - ▶ HMT
 - ▶ National health care impact on Canadian labor
 - ▶ Rail Rates
 - ▶ US / Canadian Dollar exchange rate
 - ▶ Canadian National Freight Strategy

- Both ports are losing share to Canadian 2015

POT and POS Customer Competition Examples

- 2008-2009 Time Frame: Maersk moves from APMT terminals to T46
- 2008-2009 Time Frame: NYK Blair Hylebos Terminal Development
- 2012 Grand Alliance moves to POT
- 2014 APL released from T5 agreement

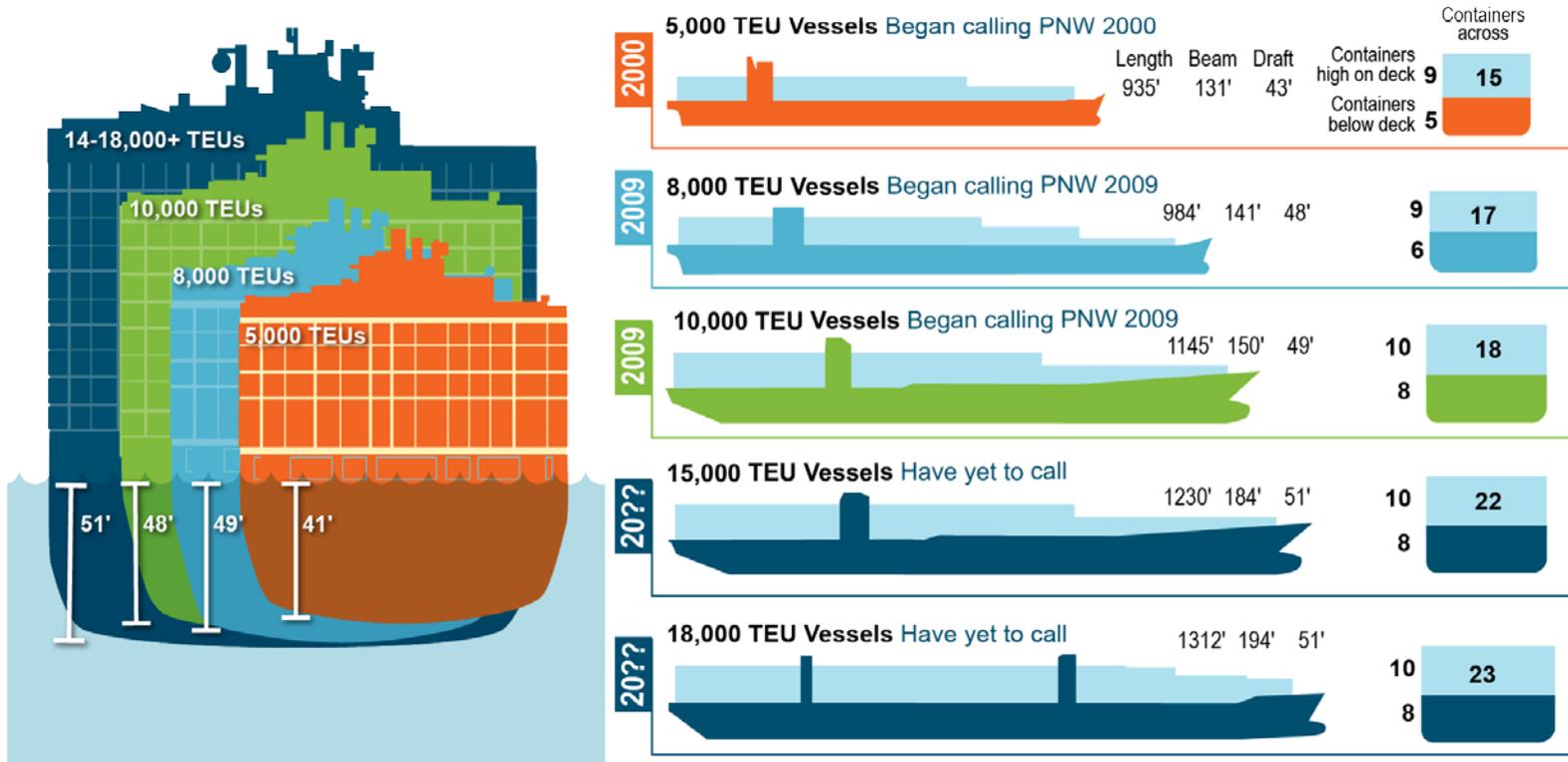
What if the NWSA was not formed in 2015

- The two home ports would have competed for container customers to justify either the rebuilding of Husky or the rebuilding of T5.
 - ▶ Both home ports may have built their respective terminals to expand big ship capability
- AWC and WWL auto and breakbulk businesses were up for renewal and the two home ports could have competed for that business as well
- The new ocean carrier alliances would have the ability to play the two ports against each other for better rates resulting in lower financial returns for the two home ports

Competition with All North American Ports

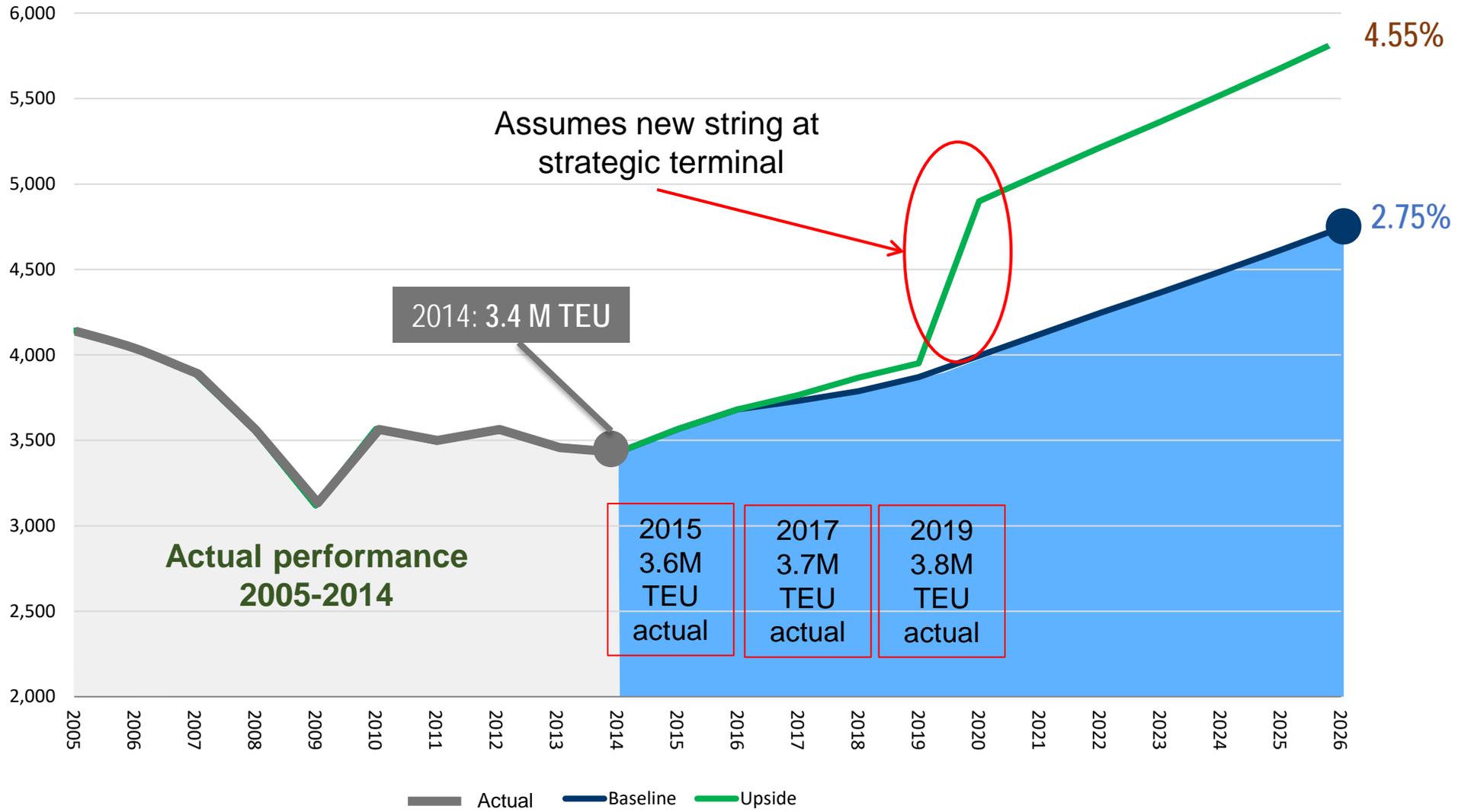


Need to Accommodate Larger Ships



Ports Have an Opportunity to Attract New Business with Strategic Investments

Seaport Alliance TEU History and Comparison of Baseline and Upside Forecasts



Gateway Optimization

Achieve 70% Utilization and double volume by Investing in strategic terminals and diversifying uses of other facilities

CURRENT

- ≈ 43% Utilization
- 3.4m TEU (3m Int'l)
- Current Acreage: 1080 acres (Int'l container)

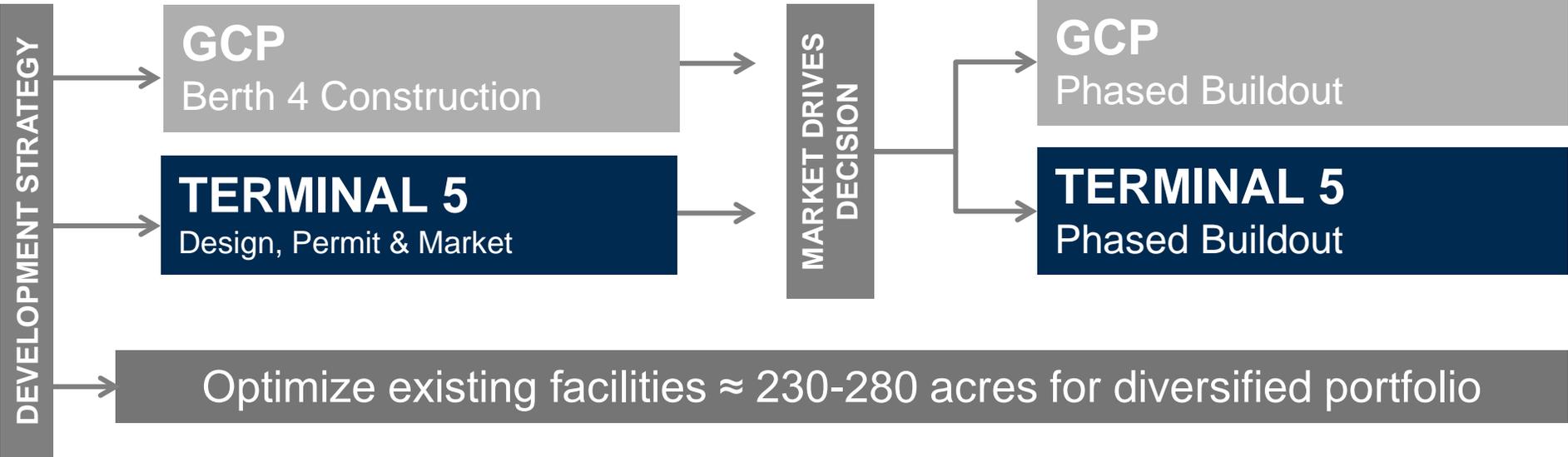


VISION 2025

- 70% Utilization
- 6m TEU (5m Int'l)
- Optimal Acreage: 800-850 acres (Int'l container)
- Terminal 5 and GCP re-developed as strategic terminals

IMMEDIATE

NEAR TERM



Rationale & Objectives

The Northwest Seaport Alliance Objectives

- Adopt a regional approach to promote marine cargo activity and enhance customer service with:
 - ▶ unified management structure for marine cargo terminals
 - ▶ unified business retention and recruitment activities
 - ▶ coordinated operations and planning of future capital investments
 - ▶ improved alignment of customer needs with terminal capabilities
- Optimize utilization and value of existing marine cargo assets
- Maintain market share, supporting job opportunities in the Puget Sound region
- Achieve overall financial returns to enable reinvestment and to provide revenue to each Port
- Provide bondholder protection and support the Ports of Seattle and Tacoma bond obligations

Equal and Committed Partners

- Commissioners from both Ports are fully committed to the goals of The Northwest Seaport Alliance and are driven by shared business interests and values
- Negotiations have been characterized by significant trust and cooperation
- Ports have collaborated previously, including the Northwest Ports Clean Air Strategy

Financial Forecasts (2015)

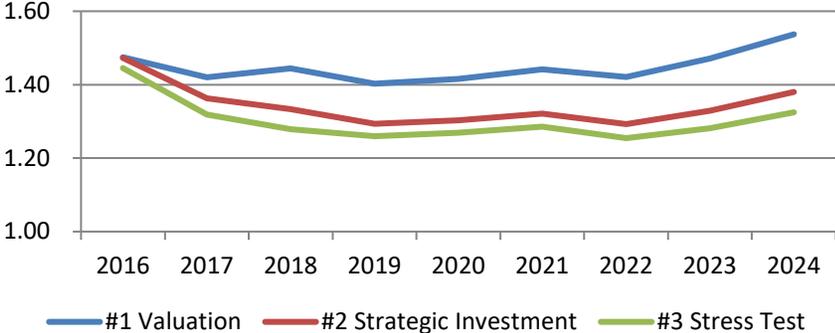
- Each Forecast contains
 - ▶ The Northwest Seaport Alliance income and capital investment
 - ▶ Port of Tacoma rate covenant calculation
 - ▶ Port of Seattle rate covenant calculation
- Scenario 1: Valuation Scenario (2015 state w/out T5 and Husky redevelopment)
 - ▶ Income based on the valuation exercise
 - ▶ Includes revenues from interim uses not associated with a lease agreement
 - ▶ Includes renewal and replacement capital
- Scenario 2: Strategic Terminal Development Scenario
 - ▶ Same as Valuation Scenario plus
 - ▶ Incremental revenues and capital spending associated:
 - Re-development of T-5 for mega ships
 - Re-development of T-4
- Scenario 3: Stress Test
 - ▶ Same as Strategic Terminal Development Scenario except
 - ▶ No revenues associated with interim uses at other terminals are included

Note: Scenarios 2 and 3 do not include any mitigation measures to improve financial results
Mitigation could include reducing or delaying capital investments or using alternative funding sources

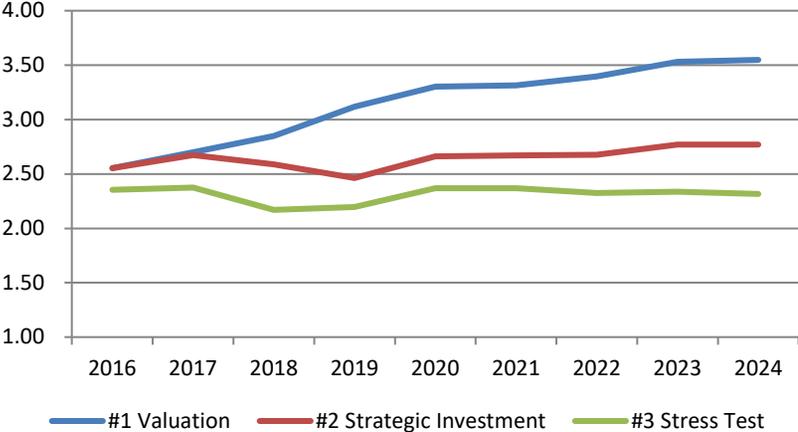
Summary of Scenarios Ten Year outlook (2015)

	#1 Valuation	#2 Strategic Investment	#3 Stress Test
Revenue Assumptions	Based on valuation analysis includes Lease revenues and interim revenues at facilities not under lease	Valuation analysis plus re-development of Terminals 4 & 5 Revenues reflect new lease agreement at T-5 and repurposing of T-46, new cranes and wharf at T4 and new lease at T7	Strategic Investments with reduced revenues Same as #2, no interim revenues are assumed at T5 or replacement revenue at T7
Alliance Capital Spending (\$ mil.)	\$166.3	\$736.5	\$736.5
POT - New Debt (\$ mil.)	-	109.3	162.1
POS - New Debt (\$ mil.)	-	349.8	424.2

**Port of Seattle
Aggregate Coverage Forecast**



**Port of Tacoma
Fully Diluted Coverage**



Moody's feedback (2015)

D. Moody's Rationale

Scenario 1

The benefits of cooperation on each port's financial position will offset the additional governance risks brought on by the alliance. Both ports will have a stronger competitive position benefiting from reduced competition in the Puget Sound, improved negotiating position with counterparties, improved ability to compete with other seaports, and greater political influence. In the short term the Port of Tacoma bondholder will be in an initially weaker position as it currently maintains the competitive advantage of stronger container facilities, but this advantage would not likely be maintained over the long-term. The alliance will add risks from a more complex governance structure as it will be committed to two separate boards, tax bases, and bond indentures. This elevates the alliance's exposure to greater political influence on operating, financing, and capital decisions.

S&P feedback (2015)

With respect to all three scenarios presented to Ratings Services, the Alliance should be beneficial to both the Port of Seattle and Port of Tacoma for promoting development and utilization of included port assets. The creation of the Alliance should have minimal impact on the Port with respect to net revenues from port activities and should not impact the rights of existing bondholders. We assume that cash will be distributed to each port on a timely basis and will not impact existing bondholders. We note that the Alliance will not issue debt directly and that each port will fund its obligation related to the Alliance with debt on parity with each respective port's existing revenue bond debt.

2016-2019 Charter Model vs Net Cash (Distributable cash less capital investment)

- The original charter model created by Martin and Associates included capital spending along with operating cash flows.
 - ▶ The original charter model excluded \$33M for upgrades to Husky for either crane improvements or other terminal improvements and included \$1.5M/year in revenue reductions for the impairment of T4
 - T4 wharf was being dismantled and removed due to environmental contamination
- To compare the actual performance to the charter model, actual results must be adjusted to remove the investments in Husky and T5 which were decisions made after the formation of the NWSA
- The original charter model had T5 at 50% of Seattle Container Terminal lease rate. The subsequent revaluation resulted in a payment of up to \$32M from the POS to the NWSA. The Comparison provided is against the original charter model of March 2015

2016-2019	Net Cash 2016-2019 \$M	Notes
Charter model	\$366	
Actual	\$368	Excluding T5 and Husky upgrade investments