



## Research: No Credit Impact on Transport for London From Longer-term Funding Deal

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LONDON (Standard & Poor's) July 29, 2004--Standard & Poor's Rating Services said today its issuer credit ratings on Transport for London (TfL; AA/Stable/--), a functional body of the Greater London Authority, are unaffected by its recently announced funding agreement with the U.K. central government. The agreement sets out increased grant levels over the next five years and confirms TfL's flexibility to raise substantial new borrowings over this period.

The funding agreement confirms the strong relationship between the U.K. government and TfL. By agreeing to the five-year deal, the government has entered into an unprecedented arrangement with TfL, both in terms of access to new borrowing from the wider debt markets and the length of the underlying five-year financial arrangements. The agreement sets out increases in grant income of about £200 million to £300 million (\$364 million-\$547 million) each year, so that annual grant levels received by TfL will be up to about £2.5 billion per year until the financial year ending March 31, 2010. The government has made this five-year agreement in recognition of the benefits of long-term funding arrangements such as greater certainty for the funding of capital projects. It has been agreed that the government will review the funding arrangement in 2006, with a view to increasing TfL's grant allocation levels, if the level of overall settlement from the spending review at that time is positive.

"Although this agreement is not a legally binding commitment, it is a strong indication of the government's intention over the medium term," said Standard & Poor's credit analyst Robert Robinson. "Moreover, the secretary of state has confirmed his intention to review grant allocation in the event of unforeseen expenditure pressures for TfL."

In addition to the above, the government has stated its support for the Mayor of London's intention to borrow in support of TfL's investment objectives. Under the Prudential borrowing code, TfL has the flexibility to raise up to £3 billion of new direct borrowing over the five-year period covered by the funding agreement. No decision has yet been taken on the amount (or type) of borrowing required. If the borrowing flexibility is used to take on a significant amount of debt, then this would be the first time TfL would have a material amount of direct debt on its balance sheet. TfL's credit ratings will be key to any new debt issuance.

TfL has other obligations, but no significant direct-debt obligation. Its main obligation is as guarantor of 95% of the London Underground public private partnership debt in the event of project default. This obligation is supported by a letter of comfort from the government, which sets out the government's

intention to provide TfL with additional resources in the event TfL has to honor its obligation.

"Significant new borrowing by TfL could put pressure on its financial profile," said Mr. Robinson. "We expect TfL to provide clear plans as to how its resources would be used to support debt-related payments."

Under the Prudential Code, local authorities such as TfL are not allowed to pledge security or securitize specific future revenue streams in support of debt. Against this background, TfL will need to demonstrate its capacity to meet debt-payment obligations.

The five-year funding agreement and the borrowing flexibility are in part intended to help TfL meet the cost of transport infrastructure development in support of London's 2012 Olympic bid.

TfL is currently amending its business plan in light of the funding agreement and revised expenditure priorities. Proposals for borrowing will be identified as part of this process, and Standard & Poor's expects the final business plan to eliminate any funding gap. (TfL's previous business plan had an annual funding gap of nearly £1 billion.)

"We will evaluate the business case for an increase in debt when specific proposals are made, and assess any impact this may have on TfL's current 'AA' long-term credit ratings," concluded Mr. Robinson.

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