

## Transport for London

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# Transport for London

## Major Rating Factors

### Strengths:

- Predictable and supportive institutional framework, reflecting significant central government support.
- TfL's dominant position as a transport provider in the Greater London area.
- Very positive liquidity position, supported by access to the Public Works Loan Board.
- Financial management is very positive for the rating.

### Issuer Credit Rating

AA+/Stable/A-1+

### Weaknesses:

- High tax-supported debt levels, at about 150% of consolidated operating revenues by 2015.
- Exposure to risks associated with its large investment plan, particularly Crossrail.

## Rationale

The ratings on Transport for London (TfL) reflect the predictable and supportive institutional framework within which it operates and our view of the significant, ongoing central government support that it receives, as well as the likelihood of further extraordinary support if required.

TfL benefits from a dominant position in the provision of urban transport services in the Greater London area. This supports its very strong demand profile, which demonstrates a long-term growth trend and resilience to economic downturns.

TfL's liquidity position is very positive for the rating, and is supported by its strong cash reserves and its access to the Public Works Loan Board (PWLB), which would provide timely liquidity support if needed. We also consider that TfL's financial management is very positive for the rating.

Constraining rating factors include TfL's high tax-supported debt levels, which we expect to reach about 150% of consolidated operating revenues by 2015. We consider that TfL is exposed to risks associated with its investment in large projects, especially in Crossrail, a major new railway link being built in London.

TfL is a functional body of the Greater London Authority (GLA; AA+/Stable/--) and is responsible for implementing the mayor's transport strategy in London. The authority operates through a multiyear funding agreement with the central government and the Department for Transport. Within this framework, however, TfL enjoys a good degree of operational and financial flexibility.

TfL is funded by revenues generated via fares and fees and by government grants (both operational and capital). In our opinion, the central government has demonstrated its commitment to ensuring that TfL has stable funding, as outlined in the funding agreement that expires at the end of financial year 2015. Although government grant has reduced and is in line with the U.K. government's austerity drive, TfL has made strategic operational cost reductions and has rephased some of its capital expenditure to maintain its financial strength.

TfL provides a complex portfolio of transport services, through a large number of subsidiaries that together comprise the TfL Group. For the purposes of our analysis, we focus on the group as a whole. In our opinion, TfL has demonstrated a strong budgetary performance over several years, posting operating balances above 18% of consolidated operating revenues in the period 2010-2012. Over 2012-2015, we expect TfL's operating performance to remain strong, supported by fare increases and structural cost saving. A strong operating performance is essential to funding ongoing capital investments.

TfL has an extensive investment plan for 2013-2015--amounting to about £11.6 billion. This may lead to an average forecasted deficit after capital accounts of about 6% of total adjusted revenues by 2015.

One of the key priorities of TfL's investment plan is Crossrail, a £14.8 billion investment, expected to be in operation in 2018. The project is primarily funded by the U.K. Department for Transport (DfT), the Greater London Authority (GLA; AA+/Stable/--), and TfL itself. So far, construction has proven to be largely on track and well within budget.

We forecast that TfL's tax-supported debt will reach about 150% of consolidated operating revenues by 2015, as a result of its considerable investment plan. Although direct debt is likely to increase significantly, we expect the ratio of tax-supported debt as a percentage of consolidated operating revenues to increase marginally because of the forecasted growth in consolidated operating revenues.

During the London 2012 Olympics, TfL will be responsible for managing the extended operations of the public transport and road system. We understand that all related infrastructure projects have been completed on time and to budget.

### **Liquidity**

We consider that TfL's liquidity position is very positive for the rating; cash and short-term investments amount to about £0.8 billion (after Standard & Poor's haircuts). This is equivalent to about 43% of estimated annual debt service, including financial leases and commercial paper, for financial year 2012-2013. Excluding commercial paper and financial leases, this would be equivalent to about 181% of estimated annual debt service. TfL also has access to about £200 million in committed liquidity facilities, if required.

Because TfL is a local government entity, it has access to the government-funded PWLB, subject to the guidelines in the U.K. Prudential Borrowing Framework of 2004. We consider that TfL's access to PWLB provides a valuable source of external liquidity.

TfL's treasury policy is conservative, and designed to mitigate risk. For this reason, it invests its cash mainly in U.K. Treasury bills and gilts, as well as money market funds rated at the 'AAA' level.

We exclude from TfL's liquidity analysis an additional £1.4 billion of liquidity, which is only available to Crossrail. TfL cannot use these funds to service its debt.

## **Outlook**

The stable outlook reflects our expectations that TfL will maintain a good budgetary performance and marginally increase its tax-supported debt levels as a percentage of consolidated operating revenues. We also expect TfL to maintain a very positive liquidity position over the rating horizon.

We could consider upgrading TfL following a reduction of its debt burden and increasing flexibility on fare charges. We might also consider upgrading TfL if stronger support from the central government or the DfT were to mitigate risks and contingent liabilities associated with its capital-intensive business.

Although unlikely, we could downgrade TfL if its budgetary performance were to deteriorate significantly to below 10% of adjusted operating revenues, following a considerable worsening of its multiyear funding agreement with the central government. In our downside case, we would expect TfL to commit to its current investment plan, despite the weaker operating performance, leading to tax-supported debt levels rising to well above 170% of consolidated operating revenues within the rating horizon.

## Comparative Analysis

For the purpose of this comparative analysis, we compare TfL with other transport providers that we rate across the world, rather than with other LRGs in the U.K., which differ from TfL due to the nature of the services provided.

Unlike other public transport providers that we rate in Western Europe, TfL is a local government entity rather than a company owned by shareholders. For this reason, it benefits from the strength of the U.K. institutional framework and from a close link with the central government.

Other rated transport companies in Western Europe, such as Rheinbahn AG (AA-/Stable/A-1+) in Germany, or Consorcio de Transportes de Bizkaia (A/Negative/A-1) in Spain or ATAC Spa. (BBB+/Negative/A-2) in Italy, operate under periodically revised service contracts and formula-based funding allocations, and do not benefit from a close funding relationship with the central government, as TfL does.

Despite its close ties with the central government, TfL does not benefit from formal guarantees for its financial obligations, as is the case for Societe des Transports Intercommunaux de Bruxelles (AA/Negative/A-1+), the public transport company of Bruxelles, whose financial obligations are guaranteed by the Region of Brussels-Capital.

With about £9 billion of total revenues, TfL's revenue base is significantly larger than that of its peers in Western Europe. TfL is for this reason mostly comparable with some transport authorities in the U.S., such as the New York Metropolitan Transportation Authority (MTA; A/Stable/--) or the Chicago Transit Authority (CTA; A/Stable/--).

These large transportation authorities play an essential role in their local economies and serve their populations through a complex portfolio of transport services, in vast metropolitan areas, such as New York City, Chicago, and Greater London. This translates into similar funding frameworks, largely based on financial support from other tier governments, such as the New York State and New York City in the case of MTA, and the U.K. central government for TfL. Compared with the MTA and CTA, however, TfL benefits from a direct access to liquidity through the PWLB, which underpins its closer link with the central government, and represents a prompt source of external liquidity.

**Table 1**

TfL: Peer Comparison							
	TfL*	Sytral	Smtc Grenoble	Rheinbahn AG	STIB	CTB	ATAC Spa
Issuer credit rating	AA+/Stable/--	AA-/Stable/--	A+/Stable/A-1+	AA-/Stable/A-1+	AA/Negative/A-1+	A/Negative/A-1	BBB+/Negative/A-2
Country	U.K.	France	France	Germany	Belgium	Spain	Italy

**Table 1**

<b>TfL: Peer Comparison (cont.)</b>							
Rating methodology	LRG	GRE and LRG for the stand-alone credit profile (SACP)	GRE and LRG for the stand-alone credit profile (SACP)	GRE and Corporate for the Stand alone credit profile (SACP)	GRE	GRE	GRE
Related Government	Greater London Authority	Urban Community of Lyons and Department of Rhône	Communauté d'agglomération de Grenoble and Departement of Isère	City of Dusseldorf directly 5%, and through a holding company 95%	Brussels-Capital (Region of)	Bizkaia (Historical Territory of) and Basque Country (Autonomous Community of)	Rome, City of
Issuer credit rating on the related government	AA+/Stable/--	Not rated	--/--/A-1+ for Communauté d'agglomération Grenoble Alpes Métropole	Not rated	AA/Negative/--	A/Negative/A-1 and A/Negative/--	BBB+/Negative/--
Link with the controlling government	N.M.	Very strong	Integral	Very strong	Integral	Integral	Integral
Role to the controlling government	N.M.	Critical	Critical	Critical	Critical	Critical	Critical
Likelihood of extraordinary support from the government	N.M.	Extremely High	Almost certain	Extremely high	Almost certain	Almost certain	Almost certain

**Peer Comparison - Financial Summary - 2011**

	<b>TfL*</b>	<b>Sytral</b>	<b>Smtc Grenoble</b>	<b>Rheinbahn AG</b>	<b>STIB</b>	<b>CTB</b>	<b>ATAC Spa</b>
Total revenues (mil. £)	9070	514.8	158.8	220.1	633.3	136.5	862.8
Total transfers (% of total revenues)	54.0	24.5	37.9	18.6	67.4	43.0	50.6
Fare revenues (% of operating revenues)	51.4	28.0	16.5	71.6	39.8	56.5	N.A
Fare revenues (% of network operating expenditures)	67.1	55	33	80	43	72	N.A
Lease-adjusted debt (at year-end)	8,170	991.9	542.4	217.9	180.2	416.2	N.A
Direct debt (% of operating revenues)	95.7	203.6	351.3	99.0	39.2	361.9	40.9
Direct debt/operating balance (x)	5.3	6.4	13.9	N.M.	5.1	35.6	N.A
Interest (% of operating revenues)	4.8	10.2	12.0	4.4	1.4	10.0	1.5
Debt service (% of total revenues)	25.4	24.6	24.0	10.2	9.8	26.5	2.7

**Table 1**

TfL: Peer Comparison (cont.)							
Service area population	7,684,700	1,300,000	400,000	1,015,000	1,100,000	1,100,000	2,500,000

Ratings on April 25, 2012. \*TfL--Transport for London (2012 data). STIB--Société de Transports Intercommunaux de Bruxelles. CTB--Consorcio de Transportes de Bizkaia. LRG--Local and regional government. GRE--government-related entity. N.M.--Not meaningful.

## Institutional Framework

Standard & Poor's views the U.K. institutional framework for local and regional governments (LRGs) as one of the strongest systems globally. Under our criteria, we assess the U.K.'s framework as "predictable and supportive," and have assigned it a score of 1 (the highest) on a scale of 1 to 6. This is based on our view of its high degree of transparency, accountability, and predictability, as well as the supportive role of the U.K. government (see our system report "Public Finance System Overview: U.K. Local and Regional Governments," published on April 5, 2011 for additional information).

Reforms affecting U.K. local and regional governments (LRGs) are ongoing, and in time will determine changes to their financial and operating profiles. As part of the 2012 budget, the central government announced that TfL should receive some funding from the locally retained share of London's business rates, to support future investment levels. We understand that the proposal is at an initial stage and will follow developments in this regard (see "Sector Reforms Are Unlikely To Damage U.K. Local And Regional Governments' Strong Creditworthiness In The Short Term," published on March 23, 2012).

## Economy

### London's strategic importance for the U.K. economy

With a population of 7.6 million, London is the largest metropolitan area in the U.K. and represents the most important economic hub of the country. GDP per capita accounted for £34,800 in 2010 (\$55,800), about 68% higher than the U.K. average. Moreover, London accounts for more than 20% of the U.K. aggregate GDP, and, as such, is the major contributor to the U.K. economy.

The central government has a strong incentive to sustain London's economy. For this reason we believe that TfL should enjoy support from the U.K. government over the long term, as transport infrastructure represents one of the key assets supporting economic growth.

### Growing demand for urban transport and resiliency to economic cycles

Demand for TfL transport services in the Greater London area is strong, and has been growing over a number of years, as testified by TfL's long-term ridership statistics. This is mainly due to TfL's dominant position as an urban transport provider in London. In our view, the strong and gradually increasing demand for TfL services represents an important stabilizing factor for revenues from fares, which account for about 50% of TfL's total revenues.

We believe that the 10% increase in population growth, forecast for Greater London in the next decade, will support TfL's demand levels in the long term. Passenger journeys have proven to be resilient to the economic cycles (see table 2). We note that following the economic downturn, in 2009/2010 passenger journeys have reduced marginally, by 0.3%, following a 2.2% reduction in underground journeys. In the same period, GDP per capita decreased in London by 2.6%, which indicates that passenger's demand is relatively inelastic to the economic cycle,

thereby stabilizing revenues from fares.

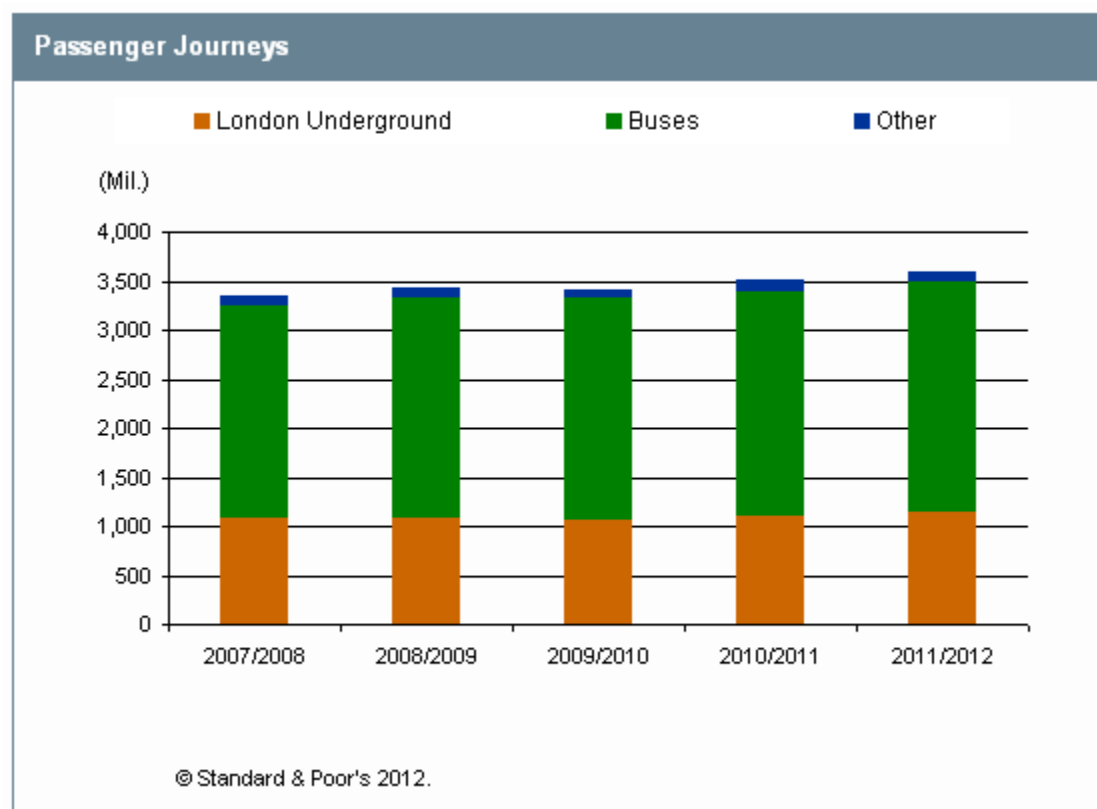
**Table 2**

<b>Economic Growth and Transport Demand Indicators</b>				
	<b>2009</b>	<b>2010</b>	<b>2011e</b>	<b>2012f</b>
<b>Economic Indicators (Annual Growth Rate %)</b>				
U.K. GDP/capita	(5.0)	1.9	0.6	0.4
<b>TFL Passenger Journeys (Annual Growth Rate %)</b>				
London Underground	1.6	(2.2)	3.9	3.6
Buses	3.3	0.4	1.4	2.2
Docklands Light Railway	(1.5)	4.5	13.0	10.3
London Tramlink	3.8	0.0	3.7	3.6
Total	2.6	(0.3)	2.5	2.8

f--Standard & Poor's forecast based on Tfl figures. e--Standard & Poor's estimate based on Tfl figures.

In 2010/2011, passenger growth for underground services recovered and is expected to grow by an additional 3.6% for 2011/2012 (see chart 1). Moreover, we note that the number of passenger journeys is expected to increase, supported by the overall capacity increase of Tfl's infrastructure.

**Chart 1**



## Financial Management

### Management is experienced and innovative

In our view, TfL's management is a rating strength. TfL is a functional body of the GLA, both of which are chaired by the Mayor of London. TfL benefits from a close link with the U.K. central government and the DfT, given its strategic role for London's economy.

In May 2012, Boris Johnson was re-elected as mayor of the Greater London Authority for the next four years. We believe that this will ensure continuity in TfL's strategy as we expect no material change to TfL's business plan, updated in December 2011, and close cooperation between TfL and the GLA to continue--increasing operating efficiency at both entities.

TfL's executive management is experienced, with a track record of successfully delivered projects, and has been able to deal effectively with significant emerging challenges such as the integration of Metronet and Tube Lines PPPs within TfL. In 2011, TfL repurchased £1.2 billion of Tube Lines notes, funding it through the issuance of commercial paper. Debt management is prudent and sophisticated, and supported by a very conservative treasury management strategy and the use of derivative instruments, for interest hedging purposes.

TfL's management is continuing with its "Project Horizon" strategy to simplify TfL's organizational structure and reduce the structural cost base. As part of this process, management is reorganizing TfL's operations into two single divisions, the Rail and Underground Division that will absorb the Docklands Light Railway (DLR) and cable car services, and the Surface Transport Division (see table 2), that will mainly incorporate street, bus, and river services.

**Table 3**

TfL Business Organization	
Rail and Underground Division	Underground (Tube) and related maintenance services, Docklands Light Railway, Overground, Tramlink, Cable car
Surface Transport Division	London Buses, London Streets, London River Services, Congestion Charging, Cabs Licensing

### London Olympic and Paralympic Games 2012

London will host the Olympic and Paralympic Games in the summer of 2012. We recognize that TfL has effectively delivered all required projects on time and to budget. During the Games, we expect TfL to experience a peak in demand, particularly on the DLR and Jubilee Line. However, we understand that management has put all measures in place to ensure satisfactory levels of network efficiency during this period. We do not consider the Olympic and Paralympic Games will have any material repercussion on TfL's financial performance and consequently on its credit profile.

## Budgetary Flexibility

### Fare increases are limited for 2012

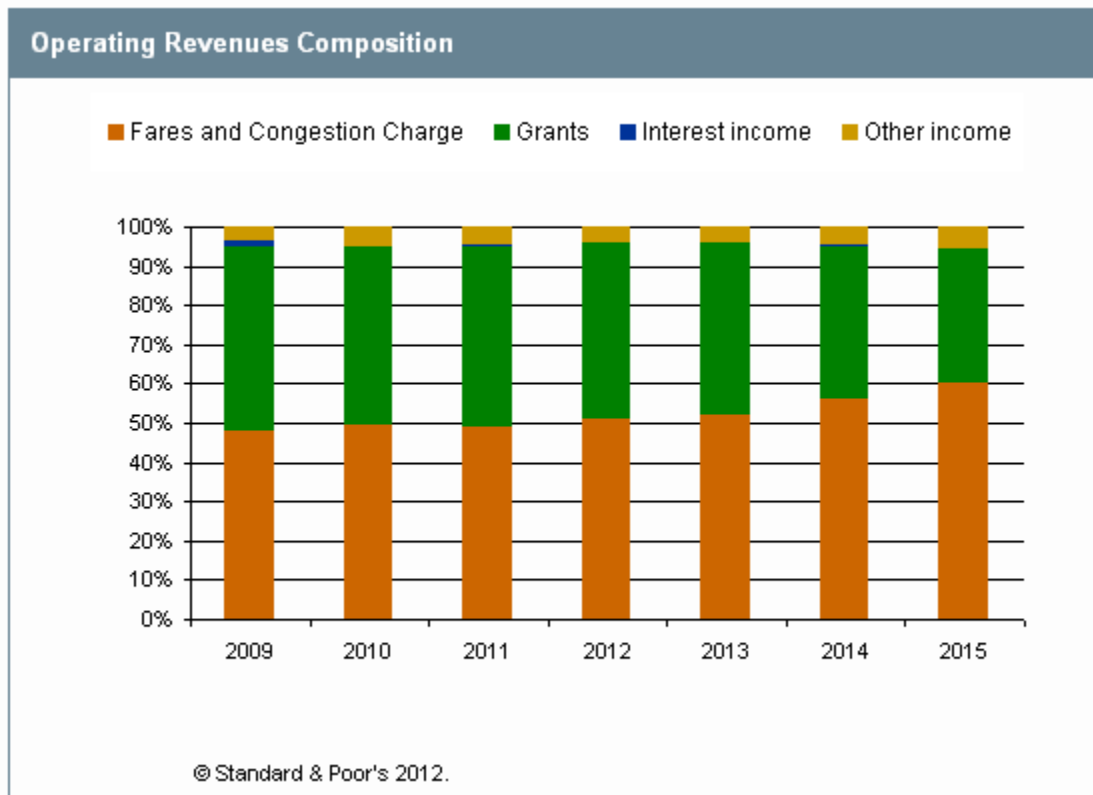
In November 2011, TfL announced that fares for 2012 would be capped at Retail Price Index (RPI) +1%, down from RPI +2%. We believe that the revision of TfL's fares increase to RPI +1% does not represent a reduction in TfL's operating flexibility within the rating horizon, and consider it likely that from 2013 on, fares might increase by RPI +2%, as outlined in TfL's business plan.

TfL's revenues from fares and congestion charges account for about 50% of consolidated operating revenues. Fare



revenues form 80% of this income, whereas congestion charging fees account for about 20%.

**Chart 2**



Fares will gradually play a more significant role in TfL's operating profile, representing about 60% of consolidated operating revenues by 2015 (see chart 2), whereas grants are predicted to reduce further, following the most recent funding agreement with the central government, which has reduced planned levels of general grants.

In theory, due to the price-inelastic demand for its services, we believe that TfL's ability to raise fares would only be limited by the politically sensitive nature of fare increases. For this reason we believe that, in case of further funding reductions from the central government, TfL might be able to increase fares above currently planned levels.

**Changes to the funding framework might affect revenue flexibility**

In our base case, we assume that the central government will not significantly reduce funding to TfL, as part of the current agreement, before 2015. However we believe that some changes might occur to the composition of this funding.

We note that the 2012 budget from the U.K central government announced that TfL might receive funding from a locally-retained share of London business rates. Business rates in Greater London are collected by the boroughs, and at the moment there is no clarity on the amount of funding TfL may receive, or if these funds will be additional or replace grants from the central government: we consider the latter more likely. We will follow reforms to business tax rates closely as we believe that they might be subject to a degree of volatility, which would affect TfL's revenue flexibility and budgetary performance. We anticipate that government measures, particularly through the introduction of a safety net mechanism, will address this volatility, similar to its plans for other LRGs.

### **TfL's asset base provides additional revenue flexibility**

We believe that TfL has a considerable asset base that could provide additional revenue flexibility either by way of asset sale income or by increasing the return on retained assets.

On one hand, TfL plans to dispose of some assets, worth about £340 million, during 2013-2015 to finance its investment plan. On the other hand, it has recently revised its asset management strategy with the objective of increasing revenues generated from its asset base. This includes buildings, parking facilities, retail shops, and other properties.

### **Strong expenditure flexibility, supported by TfL's ability to postpone capital investment if required**

TfL's operating expenditure profile is relatively flexible, as demonstrated by the success of the cost-saving program it set up to compensate for the planned reduction in grants over 2012-2015.

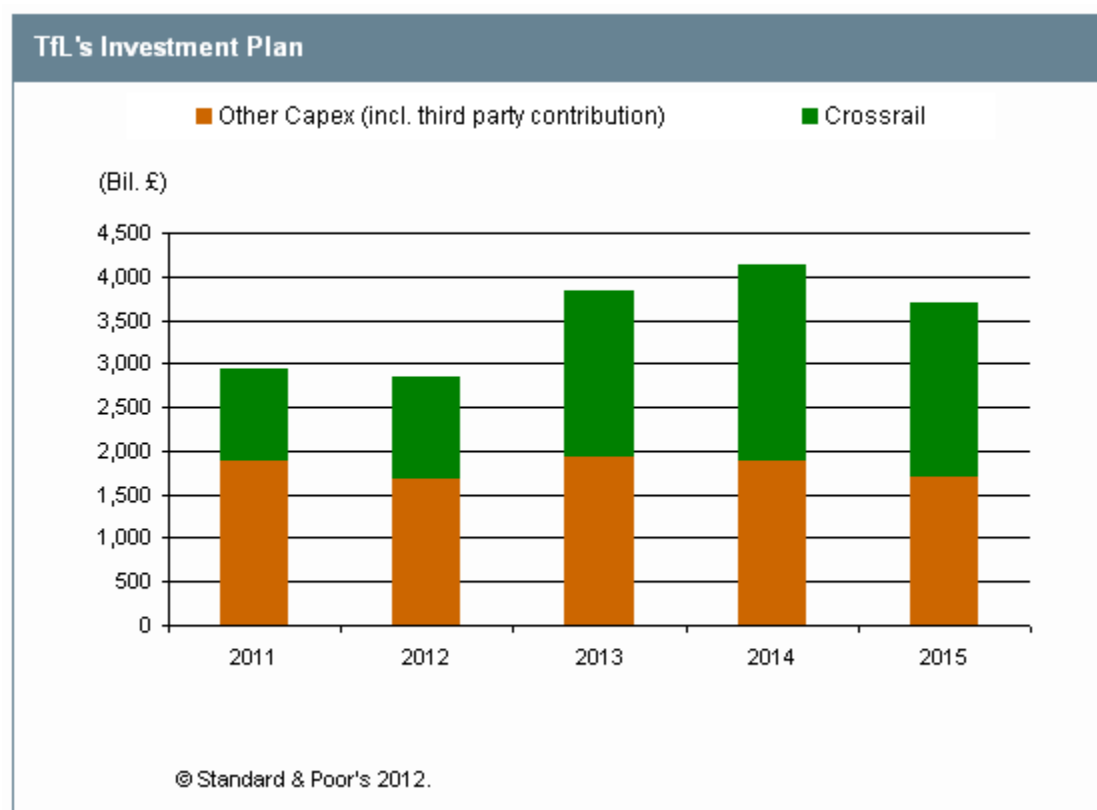
The £3 billion cost saving measures include the rationalization of the operating expenditure profile and the re-profiling of some investments. TfL will enjoy additional funding from the central government in compensation for the general grant reduction.

In 2011, TfL was able to deliver £630 million in savings, or about 11.7% of its adjusted operating expenditure. Its acquisition of Tube Lines contributed to the operating expenditure reduction, giving rise to the release of provisions and write-backs of £145 million. We believe that TfL will be able to successfully deliver targeted operating expenditure reductions, as demonstrated by its positive track record.

TfL enjoys significant capital expenditure flexibility given the capital intensive nature of its business. As demonstrated recently, TfL is able to postpone some line upgrades and other major projects if required.

TfL's investment plan amounts to about £11.6 billion over 2013-2015, or an annual average of 37% of total adjusted expenditure. This includes Crossrail's capital expenditure, which will amount to £6.1 billion over 2013-2015. We believe that, except for Crossrail and some other investments, TfL likely has considerable flexibility in its remaining £5.5 billion investment programme. As part of the funding agreement with central government, TfL has explicitly committed to deliver on other investments as planned, but some of the programme is still uncommitted (potential upgrades to the Bakerloo and Piccadilly lines for example) (see chart 3).

Chart 3



## Budgetary Performance

### A sound operating performance

TfL's cash budgetary performance is sound, as demonstrated by strong average operating margins at about 19% of adjusted operating revenues for 2009-2012.

In our analysis of operating balances we include, as part of TfL's consolidated operating revenues, all grants that TfL receives (excluding ring-fenced grants provided for Crossrail). We believe that TfL has a strong degree of autonomy regarding how its grants are allocated for both operating and capital-related activities.

We expect TfL to post annual average operating performance of more than 13% of consolidated revenues for 2013-2015, supported by average yearly fare increases at 2% above RPI. Over the rating horizon, TfL's revenue structure will change significantly, following the grants reductions laid out in the Comprehensive Spending Review 2010. Fare increases, coupled with an effective structural cost reduction plan, will help compensate for the overall reduction in grants. We forecast grants will decrease to £2.5 billion in 2015, from £3.3 billion in 2011. As a result, we expect fares to account for about 63% of consolidated operating revenues, compared to about 50% in 2011 (see chart 2).

**Table 4**

<b>TfL Budgetary Performance Forecast</b>					
(%)	2011	2012BC	2013BC	2014BC	2015BC
Op. Balance/Adj. Op Rev (%)	25.2	18.1	17.1	13.6	9.5
Balance after capex/Tot. Adj. Rev (%)	1.7	1.1	-3.4	-9.2	-13.5
Tax supported debt to consolidated operating revenues (%)	134.4	129.7	130.2	138.0	151.3

In our base case, we believe that operating costs will remain relatively stable following TfL's forecast cost reduction and its cost base aligning with inflation levels. We believe that deviations to the base case are relatively unlikely and would mainly be the consequence of commodity-price volatility. We consider the impact of rising commodity prices would be negligible for the rating, at this time.

### **A considerable investment plan, leading to moderate deficits after capital accounts**

TfL's investment plan is considerable, leading to an average deficit after capital accounts of about 6% of total adjusted revenues in 2012-2015.

In the calculation of TfL's margins after capital accounts, we include both capital revenues and investments that are related to Crossrail (TfL's main investment). About 53% of TfL's investments until 2015 will be for Crossrail, whereas 47% will be used to fund a diversified portfolio of investments to improve existing infrastructure capacity.

### **Crossrail is on track and within budget**

Crossrail is a £14.8 billion (P95) major rail project for the London metropolitan area. It is TfL's largest project, and will provide a fast urban train system that connects Heathrow and Maidenhead to the West London, Essex, and South East London. It is expected to increase the capacity of urban transport by 10%, diverting some of the current tube passengers to its train services.

We view the project as very complex, both operationally and financially. Crossrail is of strategic importance for the Greater London area. For this reason, it is regulated by a specific project agreement between TfL and the Department of Transport. TfL is the sole shareholder of Crossrail Ltd. (CRL) and is responsible for taking the project through to completion, scheduled for December 2018.

The project is co-funded from several sources, including: £5.2 billion of DfT grants, £7.1 billion of TfL funds, and £2.5 billion of other funding sources.

The £7.1 billion contribution classified as TfL funding (see table 5) includes a grant from the GLA for £4.1 billion. The GLA's contribution is mainly funded through its borrowing (£3.5 billion), supported by supplementary business rates revenues. A Business Rates Supplement (BRS) of 2p has applied since April 2010 to business properties with a rateable value of more than £50,000 in the Greater London area. TfL manages Crossrail's cash through the sponsor funding account and provides funding to Crossrail Ltd. according to an agreed funding schedule.

**Table 5**

<b>Crossrail Funding Scheme</b>	
(Mil. £)	TfL Funding (%) of total funding
<b>From London Boroughs</b>	
Developer Contributions	300
Community Infrastructure Levy	300

Table 5

<b>Crossrail Funding Scheme (cont.)</b>		
<b>From GLA</b>		
GLA Borrowing backed by Business Rates Supplement	3,500	
Business Rates Supplement (Borrows)	600	
<b>From TfL</b>		
EIB Corporate Loan to TfL	1,000	
Other TfL borrowing	1,000	
Sale of Surplus Land and Property	444	
Total TFL Funding	7,145	48%
<b>DFT Funding</b>		
BAA Plc	230	
CoL	250	
Dft Grant	4,700	
Total DFT Funding	5,180	35%
<b>Other Funding</b>		
Network Rail Surface Works and Other	2,500	17%
Total Funding	14,825	100%

Source: Standard & Poor's estimates based on TfL figures.

TfL's funding commitment for Crossrail, included in its core contribution of £2 billion (see table 5), will partly come from additional debt. TfL has limited its borrowing, along with its subsidiaries, to a maximum of £1.9 billion from 2011 to 2014.

So far, capital expenditure is £66 million lower than budget. This variance reflects a lower spend on direct construction costs, which has also been due to delayed procurement schedules and contract start dates. We also understand that key contracts for the project including station and tunnelling works have been awarded, while contracts for rolling stock are yet to be awarded.

### Debt burden expected to grow marginally over the rating horizon

We expect TfL's cumulated deficits over the rating horizon (until 2015) to be funded by about £1.8 billion in borrowing. As a result, debt is forecast to slightly increase in absolute terms over the life of the business plan. However, debt as a percentage of consolidated operating revenues is likely to grow only marginally because of the forecast growth in consolidated operating revenues. In this context, interest payments including financial leases are forecast to remain below 7% of operating revenues, mainly due to the relatively long debt amortization profile.

As of March 2012, TfL's tax-supported debt amounted to £9.7 billion, or 130% of consolidated operating revenues (see table 5). Tax-supported debt includes about £7.1 billion of direct debt, £1.0 billion of financial leases, and about £1.5 billion in guarantees, which TfL provides to its subsidiary companies.

About £2.7 billion of TfL's direct debt (as at March 2012) is sourced from the government-funded PWLB, and is predominantly at fixed rate, thereby significantly reducing interest rate risk. About £1.9 billion is funded by commercial paper and about £600 million by TfL bonds. We expect TfL's debt burden to increase to about £11 billion by 2015, or 150% of consolidated operating revenues. We expect TfL's borrowing to be funded by a diversified range of sources, including PWLB, commercial loans, commercial paper, and potentially bonds.

**Table 6**

<b>TfL--Tax-Supported Debt Levels At March 2012</b>	
<b>(Mil. £)</b>	
<b>Direct Debt</b>	
Tube lines	74
Commercial Paper	1,860
PWLB	2,725
European Investment Bank	1,572
Floating Rate Notes	300
TfL Bonds	600
Direct Debt Total	7,131
Financial Leases	1,039
<b>Guarantees*</b>	
CityLink (Connect PFI)	502
Canary Wharf Properties (Crossrail) Ltd (Canary Wharf station)	500
QW Rail Leasing Ltd	290
Powerlink (Power PFI)	168
Other	55
Total Guaranteed Debt	1,515
Total Tax-supported Debt	9,685

\*Source: Standard & Poor's estimates. Some minor doublecounting between Financial Leases and Guarantees are possible.

### Reducing exposure to guarantees

In respect of subsidiary companies' contracts, £1.5 billion is the most that TfL has to guarantee in theory. However, we understand that the actual amount may vary depending on unforeseen contractual costs.

In 2011, guarantees for PFI contracts for the City Airport (CARE) and Woolwich Arsenal (WARE) extensions ceased being relevant, as TfL acquired the two PFI subsidiaries. Following the acquisition, TfL prepaid £260 million in companies' commercial loans. Prior to the acquisition, debt service for CARE and WARE was funded indirectly through periodic fees paid to the concession companies.

### Limited exposure to pension liabilities and derivatives

TfL has about £1.2 billion in unfunded pension liabilities (based on 2010 valuation), through a benefit scheme that it manages directly. We understand that TfL is planning to absorb the deficit by 2020. According to our criteria, pension liabilities represent a debt-like obligation, which is excluded from tax-supported debt.

Unlike other local authorities, the TfL Act of 2008 allows TfL to enter into derivatives for hedging purposes. TfL therefore makes use of derivatives to hedge interest rate volatility and currency risk, and may hedge commodity risk in the future. As of March 2012, TfL has outstanding interest rates derivatives with a notional amount of about £2.0 billion and currency swaps for a notional amount of £10.7 million.

## Contingent Liabilities

In our opinion, TfL's contingent liabilities are moderate and are mainly related to its significant investment plan, particularly with regard to Crossrail.

### Crossrail's Project Development Agreement protects TfL from major cost overruns

Crossrail's Project Development Agreement caps TfL's financial exposure to the project in case of significant cost overruns, thereby protecting TfL's credit profile.

The "Project Development Agreement" includes several review phases (or "intervention points"), which could help TfL identify potential cost overruns in advance and put timely correction mechanisms into place. If costs were to overrun significantly, under certain conditions TfL could exercise its right under a put option--an agreement it has with Dft--which would transfer the project ownership back to Dft. Despite this agreement, we believe that in the case of significant cost overruns or project delays Dft and TfL would likely cooperate to complete Crossrail's construction, eventually re-working the funding agreement of the project.

### Acquisition of PFI concessions reduces contingent liabilities going forward

TfL acquired the PFI contracts for CARE and WARE following its reassessment of the financing arrangements in 2011. TfL has identified significant long-term savings from running the projects in-house rather than through separate PFI subsidiaries. In our opinion, the acquisition of the two PFIs reduces TfL's exposure to litigation risk related to the projects, although we view this risk as marginal. Currently, TfL has five other outstanding PFI transactions (see table 7).

**Table 7**

TfL: List Of PFIs	
Docklands Light Railway (DLR) Greenwich	Design , Build and Operate DLR extension
British Transport Police (Underground)	Police infrastrucure for Jubilee line and long-term policy strategy for Underground
Power	Electricity supply (management and procurement)
Connect	Communication systems for Tube
AI3 Thames Gateway	Design, Build, Finance and Operate AI3

**Table 8**

Transport for London Financial Summary (Standard & Poor's Forecast)														
(Mil. £)	Standard & Poor's Downside Case				Standard & Poor's Upside Case				Standard & Poor's Base Case				Actuals	Actuals
	2015f	2014f	2013f	2012e	2015	2014	2013	2012	2015	2014	2013	2012	2011	2010
<b>Operating revenues</b>														
Fares and Congestion Charge	3604	3677	3752	3829	4646	4302	4059	3829	4433	4221	4020	3829	3543	3272
Grants	2503	2962	3371	3345	2503	2962	3371	3345	2503	2962	3371	3345	3305	3001
Other income	414	372	334	296	414	372	334	296	414	372	334	296	351	337
Adjusted operating revenues	6521	7011	7457	7470	7563	7636	7764	7470	7350	7555	7725	7470	7198	6609
<b>Operating Expenditure</b>														
Operating costs	6994	6536	6109	5709	5525	5542	5490	5424	6058	5940	5823	5709	4931	5273
Debt Interest (including leases)	780	740	459	361	408	392	368	348	457	438	397	361	408	421
Group Items & Pension Adjustments	134	154	181	45	134	154	181	45	134	154	181	45	47	100
Adjusted Operating Expenditure	7907	7431	6749	6115	6067	6088	6039	5816	6650	6531	6402	6115	5386	5793
Operating balance	-1386	-419	708	1355	1496	1548	1725	1654	700	1024	1324	1355	1813	816

**Table 8**

<b>Transport for London Financial Summary (Standard &amp; Poor's Forecast) (cont.)</b>														
<b>Capital Revenues</b>														
Crossrail	1693	2068	2059	1560	2032	2482	2471	1872	1693	2068	2059	1560	1222	172
Asset sales	0	0	0	40	74	143	123	40	74	143	123	40	50	60
Adjusted Capital Revenues	1693	2068	2059	1600	2106	2625	2594	1912	1767	2211	2182	1600	1272	232
Total adjusted revenues	8214	9079	9516	9070	9669	10261	10358	9382	9117	9766	9907	9070	8470	6841
<b>Capital Expenditure</b>														
Capital Expenditure (incl. third-party contrib.)	1700	1889	1937	1673	1530	1700	1743	1506	1700	1889	1937	1673	1885	2183
Crossrail	3983	2655	1770	1180	2002	2247	1904	1180	2002	2247	1904	1180	1052	694
Adjusted Capital Expenditure	5683	4544	3707	2853	3532	3947	3647	2686	3702	4136	3841	2853	2937	2877
Total adjusted expenditures	13590	11975	10456	8968	9599	10035	9686	8502	10352	10667	10243	8968	8322	8671
Balance after capital accounts	(5,376)	(2,895)	(940)	102	70	226	671	880	(1,235)	(901)	(335)	102	147	(1,830)
<b>Debt burden</b>														
Total Direct Debt	13080	8867	6750	7131	5741	5851	5955	6251	8785	8018	7574	7131	6350	4125
Total Guarantees	1515	1515	1515	1515	1515	1515	1515	1515	1515	1515	1515	1515	1897	2289
Financial Leases	817	897	971	1039	817	897	971	1039	817	897	971	1039	1427	3035
Total Tax-Supported Debt	15412	11278	9236	9685	8073	8263	8441	8805	11117	10430	10060	9685	9674	9449
<b>Liquidity</b>														
Free cash & Liquid assets (after S&P haircut)	327	409	682	718	765	765	765	765	765	765	765	765	783	718
Committed bank lines	200	200	200	200	200	200	200	200	200	200	200	200	200	200
Free Cash & Liquid assets (after S&P haircut) and committed bank lines	527	609	882	918	965	965	965	965	965	965	965	965	983	918

Downside Case, Upside Case, and Base Case represent Standard & Poor's opinion of forecasted scenarios that might lead to a downgrade, an upgrade, or a stable rating. Forecasted scenarios may differ from the forecasts published by the rated entities. e--Estimate. N.A.--Not available.

**Table 9**

<b>Transport for London Key Ratios</b>														
<b>(Mil. £)</b>	<b>Standard &amp; Poor's Downside Case</b>				<b>Standard &amp; Poor's Upside Case</b>				<b>Standard &amp; Poor's Base Case</b>				<b>Actuals</b>	<b>Actuals</b>
	<b>2015f</b>	<b>2014f</b>	<b>2013f</b>	<b>2012e</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>
<b>Economy</b>														
GVA/Capita USD (thousands)	59.1	57.8	56.8	56.3	59.1	57.8	56.8	56.3	59.1	57.8	56.8	56.3	56.1	55.8
<b>Budgetary Flexibility</b>														
Mod rev/Adj Op rev (%)	55.3	52.4	50.3	51.3	61.4	56.3	52.3	51.3	60.3	55.9	52.0	51.3	49.2	49.5



**Table 9**

<b>Transport for London Key Ratios (cont.)</b>														
Adj. Capex/Tot Adj. Exp (%)	41.8	37.9	35.5	31.8	36.8	39.3	37.7	31.6	35.8	38.8	37.5	31.8	35.3	33.2
<b>Budgetary Performance</b>														
Op. Balance/Adj. Op Rev (%)	(21.3)	(6.0)	9.5	18.1	19.8	20.3	22.2	22.1	9.5	13.6	17.1	18.1	25.2	12.4
Balance after capex/Tot. Adj. Rev (%)	(65.4)	(31.9)	(9.9)	1.1	0.7	2.2	6.5	9.4	(13.5)	(9.2)	(3.4)	1.1	1.7	(26.7)
<b>Liquidity</b>														
Free Cash & Liquid Assets/Debt Service (%)	17.4	22.2	36.8	31.2	50.5	51.2	43.4	33.4	48.9	49.6	42.7	33.2	39.0	155.0
Free Cash & Liquid Assets & Com. Liq. Facilities / Debt Service (%)	28.0	33.1	47.6	39.9	63.7	64.6	54.8	42.2	61.7	62.6	53.9	41.9	48.9	198.2
<b>Debt Burden</b>														
Tax supported debt to consolidated operating revenues	236.4	160.9	123.9	129.7	106.7	108.2	108.7	117.9	151.3	138.0	130.2	129.7	134.4	143.0
Interest / Adjusted op rev	12.0	10.6	6.2	4.8	5.4	5.1	4.7	4.7	6.2	5.8	5.1	4.8	5.7	6.4
Unfunded pension liabilities / adj op. revenues	18.4	17.1	16.1	16.1	15.9	15.7	15.5	16.1	16.3	15.9	15.5	16.1	18.1	19.7

Downside Case, Upside Case and Base Case represent Standard & Poor's opinion of forecasted scenarios that might lead to a downgrade, an upgrade, or a stable rating. Forecasted scenarios may differ from the forecasts of the rated entities. E--estimate. N.A--Not available.

**Table 10**

<b>Summary Of Published Rating Factor Scores</b>	
<b>Institutional Framework</b>	<b>Predictable and supportive</b>
Financial Management	Very Positive
Liquidity	Very Positive
Indicative Credit Level	AA+
Overriding factors	None

<b>Ratings Detail (As Of June 1, 2012)</b>	
<b>Transport for London</b>	
Issuer Credit Rating	AA+/Stable/A-1+
Commercial Paper	A-1+
Senior Unsecured	AA+
<b>Issuer Credit Ratings History</b>	
03-Dec-2010	AA+/Stable/A-1+
20-Sep-2010	AA/Watch Pos/A-1+
29-Mar-2010	AA/Stable/A-1+

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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