

### Research Update:

## Transport for London CP Program Assigned 'A-1+' Rating; 'AA/A-1+' Issuer Ratings Affirmed; Outlook Stable

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## Research Update:

# Transport for London CP Program Assigned 'A-1+' Rating; 'AA/A-1+' Issuer Ratings Affirmed; Outlook Stable

## Overview

- We are assigning an 'A-1+' short-term rating to the £2 billion commercial paper program of Transport for London (TfL; AA/Stable/A-1+).
- We are also affirming the 'AA' long-term and 'A-1+' short-term ratings on TfL.
- The stable outlook reflects our expectation that TfL will continue to have a positive relationship with the U.K. government (AAA/Negative/A-1+), which could lead to additional support in the event of financial stress.

## Rating Action

On July 1, 2010, Standard & Poor's Ratings Services assigned its 'A-1+' short-term rating to the £2 billion commercial paper program of Transport for London (TfL; AA/Stable/A-1+). The rating on the program is directly linked to the short-term rating on TfL. At the same time, we affirmed the 'AA' long-term and 'A-1+' short-term ratings on TfL. The outlook is stable.

## Rationale

The notes to be issued under the commercial paper program will be direct obligations of TfL, and hence they are directly linked to the TfL issuer credit rating. TfL ultimately plans to refinance its commercial paper through longer-term borrowing from the capital markets and the U.K. Public Works Loan Board (PWLB), part of the U.K. government's Debt Management Office. We understand that TfL is legally bound to remain within its prudential borrowing limits, which are set by the Mayor of London as required under legislation, and hence would be able to refinance 100% of any outstanding commercial paper from the PWLB. (In the unlikely event that this changed, we would reconsider the rating.) As further back-up, we understand that TfL intends to have a combination of cash and overdraft facilities totaling £450 million at any one time, comprising more than 2x the commercial paper maturing within any 3-day period.

The rating on TfL continues to reflect its positive relationship with the central government, the critical nature of its services for London and therefore the U.K. economy, and its financial flexibilities. The rating is constrained by the risks and debt associated with its substantial capital plans, and the fiscal challenges facing the U.K. (AAA/Negative/A-1+).

The rating on TfL has not been adversely affected by the acquisition of the Tube Lines Group, for the reasons outlined in the bulletin "No Change To Transport for London Rating Following Planned Acquisition Of Tube Lines," published on May 17, 2010. Although there will be a slight increase in TfL's exposure to capital cost overruns as it increases its direct responsibility, we believe this will be readily compensated for by an increase in autonomy and hence expenditure flexibility.

TfL is responsible for nearly all public transport functions in London. It operates through a number of subsidiaries, the largest of which is London Underground Ltd., which together comprise the TfL Group. For the purposes of our analysis, we have focused on the group as a whole. TfL is also a functional body of the Greater London Authority (GLA; AA+/Stable/--).

TfL enjoys an extremely strong business position and a near-monopoly over London's public transport and the associated fares. In addition, approximately half of its revenues come from government grant, via the Department for Transport (DfT). Although the fiscal challenges facing the U.K. government may present some uncertainty over the level of future grant for TfL, and has already reduced the grant for 2010/11 by £108 million, we believe that the U.K. government will continue to act in a highly supportive manner, given the importance of TfL's services both for London and the U.K. economy.

Although there are risks and uncertainties associated with TfL's investment program, its substantial size--£13.5 billion (excluding works associated with Crossrail and the former Tube Lines PPP) from 2010/11 to 2017/18--allows considerable flexibility to defer, reduce, or cancel individual projects. TfL also has responsibility for Crossrail, a £15.9 billion major rail project for London and the southeast of England. Should the start-up costs of Crossrail overrun beyond the contingency provision, TfL's financial obligations are in effect capped under an agreement with DfT, thereby protecting TfL's credit standing.

### **Liquidity**

TfL has a sufficient level of liquidity, with cash and short-term investments (exc. those earmarked for Crossrail) at £0.8 billion, or 13.5% of estimated operating expenditures, as at June 2010. TfL also has access to undrawn overdraft facilities of £200 million. In addition, it has ready access to the government-funded Public Works Loan Board (PWLB), assuming TfL remains within its prudential borrowing limits. (PWLB's role is to lend to local authorities and other prescribed bodies, and it has a policy and track record of lending to local authorities such as TfL within two days of any legitimate application.) We understand that the combination of TfL's cash position and its potential access to the PWLB is forecast by TfL to cover any outstanding commercial paper by at least 1.5x during the financial year ending March 31, 2011.

## Outlook

The stable outlook reflects our expectation that TfL will continue to have a positive relationship with the U.K. government, which could lead to additional support in the event of financial stress. In the unlikely event that we believed such support would not be forthcoming, or if debt were to increase substantially more than planned, pressure might be put on the rating.

Any positive rating action is likely to be contingent on greater clarity around TfL's medium-term grant settlement, the extent of any increased flexibility relating to the acquisition of Tube Lines, and our view of the U.K. government's credit standing.

## Related Criteria And Research

- Methodology And Assumptions: Rating International Local And Regional Governments, Jan. 5, 2009

## Ratings List

### New Rating

Transport for London Commercial Paper	A-1+
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### Ratings Affirmed

Transport for London Issuer Credit Rating	AA/Stable/A-1+
Senior Unsecured	AA

### Additional Contact:

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