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Fitch Affirms Transport for London at 'AA'; Outlook Stable Ratings

09 Feb 2010 6:45 AM (EST)

Fitch Ratings-London/Barcelona/Frankfurt-09 February 2010: Fitch Ratings has today affirmed Transport for London's (TfL) Long-term foreign and local currency ratings at 'AA', respectively, and its Short-term foreign currency rating at 'F1+'. The Outlooks on the Long-term ratings are Stable.

The ratings reflect TfL's importance to the economic development of the greater London area and ongoing strong government support through direct grant funding. However, the ratings also take into account TfL's ambitious capital spending plan, including the Crossrail project, and the entity's limited revenue flexibility.

Despite the projected decline and flatness in tube and bus usage respectively, the Stable Outlook reflects the political visibility of TfL, as set out in the government's spending review, and the expected patronage recovery as reflected in TfL's updated business plan. Although TfL expects to undertake a considerable increase in leverage to fund capital expenditure, Fitch believes that government support will remain strong and this is a key factor in the Stable Outlook.

TfL's dependence on indirect central government support is a positive rating factor. Central government grants accounted for around an average 40% of its total revenue over the past four years. Further evidence of government support is the extraordinary funding of GBP1.7bn received to compensate TfL for the exercise of the put option by the providers of finance to Metronet, which TfL had to repay. TfL subsequently acquired Metronet's undertakings.

Tube and bus usage has been negatively affected by the UK economic slowdown and TfL forecasts that usage will remain flat in the bus network and decline in the tube network in the next two-to-three years. Nevertheless, the projection is that tube patronage will start rising from 2012 and that bus network usage will begin increasing by 2013. However, TfL's business plan does not forecast a decline in fare revenue as the rise in ticket prices (retail price index + 2%) and cost savings identified will compensate for the stagnation in patronage in the near term.

TfL's ambitious capital expenditure plan has resulted in a moderate increase in financial debt. However, debt increases further if obligations under the private-public partnership (PPP) projects are added. The business plan indicates additional direct debt of about GBP5.2bn during the period, bringing total indebtedness to GBP8.4bn by FY18. Due to the considerable increase in leverage, direct and indirect government support will become increasingly important to the ratings.

The Crossrail project will be an important investment for TfL, and is expected to cost about GBP15.9bn, with additional off-balance-sheet financing of GBP1.5bn, part of which will be funded by TfL. Although the project will create some risk for TfL, particularly if there is a cost overrun, there are sufficient safeguards in place (such as the put option to the central government) to cap TfL's liabilities at a pre-determined level. Fitch will monitor the execution cost of the project against projections.

TfL, which reports to London's mayor, is a functional body of the Greater London Authority . It was created in 2000 and took over all responsibilities for buses and other transport functions in London from the government. Its remit includes roads and bridges, buses, the Docklands Light Railway, river services and taxis. London Underground Limited was passed to TfL in July 2003.

Applicable criteria, "Revenue-Supported Rating Criteria", dated 29 December, 2009, and "Ratings of Non-US Public Finance Entities", dated 1 September, 2009, are available at www.fitchratings.com.

Contacts: Fernando Mayorga, Barcelona, Tel: +34 93 323 84 00; Guido Bach, Frankfurt, + 49 69 768076 111.

Media Relations: Peter Fitzpatrick, London, Tel: + 44 (0)20 7417 4364, Email: peter.fitzpatrick@fitchratings.com.

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