

## Fitch Revises Outlook on BAA Funding's Bonds to Stable on Equity Injection Ratings

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Fitch Ratings-Paris/London-23 November 2009: Fitch Ratings has today revised the Outlook on BAA Funding Limited's (BAA) class A and B bonds, issued under its GBP50bn multi-currency debt issuance programme, to Stable from Negative. The agency has simultaneously affirmed the class A bonds at 'A-' and class B bonds at 'BBB'.

The rating action reflects BAA's recent announcement regarding a financial optimisation plan which primarily consists of a GBP500m equity injection into BAA Funding's capital structure.

The plan will be implemented in two phases. The first phase represented a GBP260m equity injection which has already been implemented. The second phase is a monetary contribution of GBP200m from shareholders, on a pro-rata basis to their stakes, which the respective boards have now formally approved. This cash, together with GBP40m from FGP Topco Limited and BAA Airports Limited, is expected to be injected into the London airports in January 2010. Funds will be used to prepay swap coupons during 2010-2012, which will alleviate the cash debt service for these years and enhance debt coverage ratios with a short-term orientation, as well as to deleverage and prepay, or cancel, out-of-the-money swaps, with a longer term orientation.

Fitch believes the first step of remedial action undertaken by shareholders supports the revision of the rating Outlook to Stable.

The agency had previously stated that the Outlook on BAA's bonds could be revised to Stable if traffic staged a robust recovery in the coming six months, which is now unlikely, or if BAA's shareholders took remedial actions to offset the drop in debt coverage levels to the extent that the Fitch-calculated post-maintenance interest cover ratio (PMICR) would reach 1.5x-1.6x for class A and 1.2x-1.3x for class B. The latter has now happened, and Fitch has accordingly revised the Outlook to Stable.

The coverage ratios have been improved by the remedial action, although they take into account a more conservative updated business plan. The updated plan includes lower traffic forecasts which better reflect the recent economic downturn. By lowering this expectation, the updated business plan also reduces the risk of underperformance.

There is still a risk that market fundamentals deteriorate further and an economic recovery takes longer than BAA expects to occur, although Fitch believes this possibility is moderate as positive growth in traffic has returned in recent months and because Heathrow airport has been fairly resilient through the crisis.

The equity injection restores financial flexibility until the next regulatory re-set, which determines the price cap on aeronautical tariffs from April 2013 to March 2018, and will rebase the revenue flow on the actual level of passengers by an appropriate tariff increase. Fitch continues to believe that there is always an embedded risk in regulatory resets, an important unknown variable being the cost of debt that the regulator (CAA) will allow for in the tariff which is notably a function of the assumptions retained by the regulator in terms of gearing and the proportion of index-linked debt.

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