12 AUG 2022

Fitch Affirms High Speed Rail Finance (1) Notes at 'A-'; Stable Outlook

Fitch Ratings - London - 12 Aug 2022: Fitch Ratings has affirmed High-Speed Rail Finance (1) PLC's senior secured notes and programme ratings at 'A-' with Stable Outlook. The issuer is the funding vehicle for HS1 Limited, which is the operator of the only high-speed railway in the UK.

RATING RATIONALE

HS1 benefits from a robust operating profile and the critical nature of the railway connection between the UK and continental Europe. Domestic volumes are substantially underpinned by the UK government, which mitigates the risk and support stability of cash flows in the medium term. We view demand for international traffic as robust in the long term, despite being significantly affected by the Covid-19 pandemic at present. We currently assume demand to substantially recover by FY27 (ending in March 2027) from the pandemic shock.

Tariffs are based on RPI-linked investment recovery charges and a pass-through of operating costs. HS1 outsources most operations and maintenance (O&M) to an experienced operator. Debt is fully amortising and secured, with minimal exposure to interest-rate risk.

This, together with a robust debt service coverage ratio (DSCR) profile averaging 1.6x under the updated Fitch Rating Case (FRC), supports HS1's 'A-' rating with Stable Outlook.

KEY RATING DRIVERS

Highly Stable Volumes; Volume Risk: 'Stronger'

The UK government guarantees around 95% of pre-Covid-19 domestic train paths as part of the underpinned volume scheme, making domestic revenue effectively availability-based. International volumes are based on dominant Eurostar train services from London to the continent.

RPI Link, Costs Pass-Through; Price Risk: 'Stronger'

The concession framework allows HS1 sponsors to recover their invested capital including debt through an RPI-linked investment recovery charge, which represented around 71% of EBITDA in FY22. Unlike most regulated assets in the UK, this is not subject to periodic regulatory review. The RPI revenue swap mitigates the risk of low inflation, as HS1 will receive cash flows at a fixed growth while the payable portion will accrete as per realised RPI.

The operations, maintenance and renewal costs (OMRC) component of revenues is designed to meet the majority of HS1's operating, maintenance and renewal costs, and is subject to benchmarking and review every five years. The OMRC charges can also be 'reopened' before the five-year review cycle under certain circumstances, such as where traffic is +/- 4% the forecasts presented at the beginning of the control period. HS1 initiated a volume reopener in December 2020, and the new calculated OMRC was agreed in February 2021. HS1 will reopen the OMRC calculation again by the end of this year.

Full Outsourcing to an Experienced Operator; Operating Risk: 'Stronger'

The majority of O&M is outsourced to a subsidiary of Network Rail Infrastructure Finance Plc (AA-/Stable), the leading rail infrastructure operator in the UK, which guarantees the subsidiary's obligations.

The concession and operating agreements are not strictly 100% back-to-back, and in contrast to standard private finance initiative (PFI) concessions there is a limited universe of replacement operators. However, Fitch believes HS1's ability to periodically request renegotiations of the terms of the operating agreement mitigates these risks. HS1 also benefits from a substantial pass-through of liabilities to train-operating companies.

High Visibility on Capex; Infrastructure Development & Renewal Risk: 'Stronger'

HS1's infrastructure is well-maintained and has consistently outperformed requirements and expectations. Major maintenance services are largely the responsibility of the operator, while HS1's responsibilities are limited and predictable. Forward-looking escrow arrangements in respect of track-and-station capex provide high visibility of renewal costs. The five-year concessionaire's review of asset conditions is expected to prevent HS1 incurring unexpected handover liabilities at concession maturity.

Solid Debt Structure; Debt Structure: 'Stronger'

The rated debt is senior secured and fully amortising, with more than 95% of the current outstanding debt either at fixed or swapped interest rates. A dedicated 12-month liquidity facility within the ring-fenced group, together with covenanted lock-up and default ratios, provide strong creditor protection. The amortisation of legacy swaps' crystallised mark-to-market value is fixed and reflected in the debt service coverage ratio (DSCR) metric.

As of end-July 2022, HS1 had a fully undrawn its GBP125 million liquidity facility as well as most of its GBP80 million working capital facility.

Financial Profile

Under FRC, HS1's DSCR profile is robust, averaging 1.6x from FY23 until FY40, with a minimum DSCR of 1.4x in FY24. Despite the short-term deterioration, its credit metrics maintain buffer against our negative sensitivity trigger.

PEER GROUP

Channel Link Enterprises Finance Plc (CLEF; rail/transportation, BBB/Stable) has the same catchment area as HS1's international traffic. CLEF has lower DSCR than HS1 and a 'Midrange' debt structure. We view HS1 as stronger than CLEF in terms of lower expected volatility in revenue, as well as lower operating costs and infrastructure renewal costs, which explains the two-notch difference in their ratings.

Given the stable revenue profile and metrics, HS1 compares well with Meridian Hospital Company PLC (hospital PFI concession), whose bond is rated 'A-'/ Stable with an average DSCR of 1.5x. Meridian benefits from 100% availability-based revenues, which underpin a 'A-' rating despite having a lower DSCR than HS1's 1.6x.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/ downgrade:

-Material underperformance of FRC, resulting in an average DSCR below 1.45x

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-An upgrade is unlikely as we believe that HS1 could raise additional debt

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

TRANSACTION SUMMARY

The high-speed rail line connects London's St Pancras International station to high-speed commuter services throughout Kent, and international passenger destinations in Europe, mainly Paris and Brussels, via the Channel Tunnel.

CREDIT UPDATE

Train Paths

HS1's train paths during FY22 continued to be impacted by travel restrictions, but on a cash flow basis this is mitigated by the robust contractual protections of the underpin scheme. While the number of train paths run in FY22 were 69% of pre-pandemic levels, actual paths billed were 78%.

In particular, the number of domestic train paths timetabled for May 2022 to December 2022 continues to be below the underpin arrangement of 1,024 paths per standard week. As such, the concessionaire is relying on timely payments from the Secretary of State, Department for Transport, in accordance with the concession agreement, which helps to absorb cash flow depletion.

International train paths are recovering from the plunge seen as a consequence of Covid-19. Demand responded swiftly to the lifting of travel restrictions with annualised Eurostar train paths reaching close to 80% of 2019 levels in June 2022.

Train Operating Companies (TOCs)

We do not expect recent changes to the domestic operator in FY22 to affect HS1's performance. In October 2021, London South-Eastern Railways' 'LSER' direct award was not extended and the government operator of last resort, South-East Trains Limited (SET), took over the service - a procedure that ensures the government requirement to maintain continuity of passenger rail travel.

Similarly, we do not expect the merger of Eurostar with Thalys to negatively impact HS1's operations.

FINANCIAL ANALYSIS

The FRC reflects our conservative assumptions over the management case on both international and national train path growth, with an aggregate 2% CAGR from FY22 to FY40. Under our FRC we expect total train path to be substantially back to FY20 levels by FY27 for both domestic and international paths. O&M as well as power and station charges are substantially passed on to TOCs, resulting in no exposure to cost overruns or margins pressures.

HS1 DSCR profile remains robust under the FRC, at an average of 1.6x. The minimum DSCR is 1.4x, reflecting Fitch's expectation of an improvement in the performance of HS1. Despite a weakening in the short term, its credit metrics maintain a buffer against out negative sensitivity trigger.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
High Speed Rail Finance (1) PLC					
• High Speed Rail Finance (1) PLC/Debt/1 LT	LT	A-	Affirmed		A-

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		

RATINGS KEY	OUTLOOK	WATCH
STABLE		◘

Applicable Criteria

Infrastructure & Project Finance Rating Criteria (pub.20 Jul 2022) (including rating assumption sensitivity)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Third-party Model, v (20 July 2022)

Additional Disclosures

Solicitation Status

Endorsement Status

High Speed Rail Finance (1) PLC	UK Issued, EU Endorsed

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