S&P Global
Ratings

RatingsDirect®

Transaction Update: High Speed Rail Finance (1) PLC

Primary Credit Analyst:
Rachel C Goult, Paris (33) 06-2009-1284; rachel.goult@spglobal.com

Secondary Contact:
Luisina Berberian, Madrid +(34) 91-788-7200; luisina.berberian@spglobal.com

Table Of Contents

Table Of Contents (cont.)

Transaction Update: High Speed Rail Finance (1) PLC

Credit Rating(s)	
Senior Secured	
£246.5 mil 1.566% index-linked bnds due 11/01/2038	
Local Currency	A-/Stable
£610 mil 4.375% bnds due 11/01/2038	
Local Currency	A-/Stable

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

Transaction Description

U.K.-based special-purpose entity High Speed Rail Finance (1) PLC (HSRF1) is a finance vehicle for HS1 Ltd. (HS1, the project operating company; not rated), the operator of the U.K.'s sole high-speed rail line. HS1 operates under a 30-year concession agreement with the U.K. Secretary of State through December 2040 and is regulated by the Office of Rail and Road (ORR), an independent U.K. regulator. HS1 is responsible for the operations, maintenance, and renewal of the track and associated infrastructure, along with the four railway stations served by the route, which it subcontracts to Network Rail High Speed (NRHS) under a fixed price agreement through 2047. The rail line, which connects St. Pancras International station in London with the Channel Tunnel boundary in south-east Kent, provides track access to domestic and international high-speed traffic, plus a small quantity of freight traffic. HS1 has been in operation since 2007.

HSRF1's debt facilities comprise £610 million rated senior secured fixed-rate bonds and £246.5 million rated senior secured index-linked bonds (£268 million outstanding on Sept. 30, 2018), both due Nov. 1, 2038. The other senior project debt in the secured ring-fenced operating group comprises a £98 million seven-year bank facility due March 31, 2022 (£78 million outstanding on Sept. 30, 2018), issued by HS1, and a total of £879 million private placement notes due between March 2028 and December 2039 issued by High Speed Rail Finance PLC (HSRF; not rated). All senior secured debt ranks pari passu.

Transaction Summary

High Speed Rail Finance (1) PLC -- Debt

(Mil. £)	Issued by	Debt quantum issued	Outstanding as of September 2018	Maturity	Interest rate	Amortizing starts	Comments
Nominal bonds	HSRF1	610	610	Nov. 1, 2038	4.38%	April 2028	
Index linked bonds	HSRF1	247	268	Nov. 1, 2038	1.57%	April 2029	
Seven-year bank debt	HS1	98	78	March 31, 2022	Libor + 0.85%	April 2017	Fixed through interest rate derivatives at 2.35% al in rate

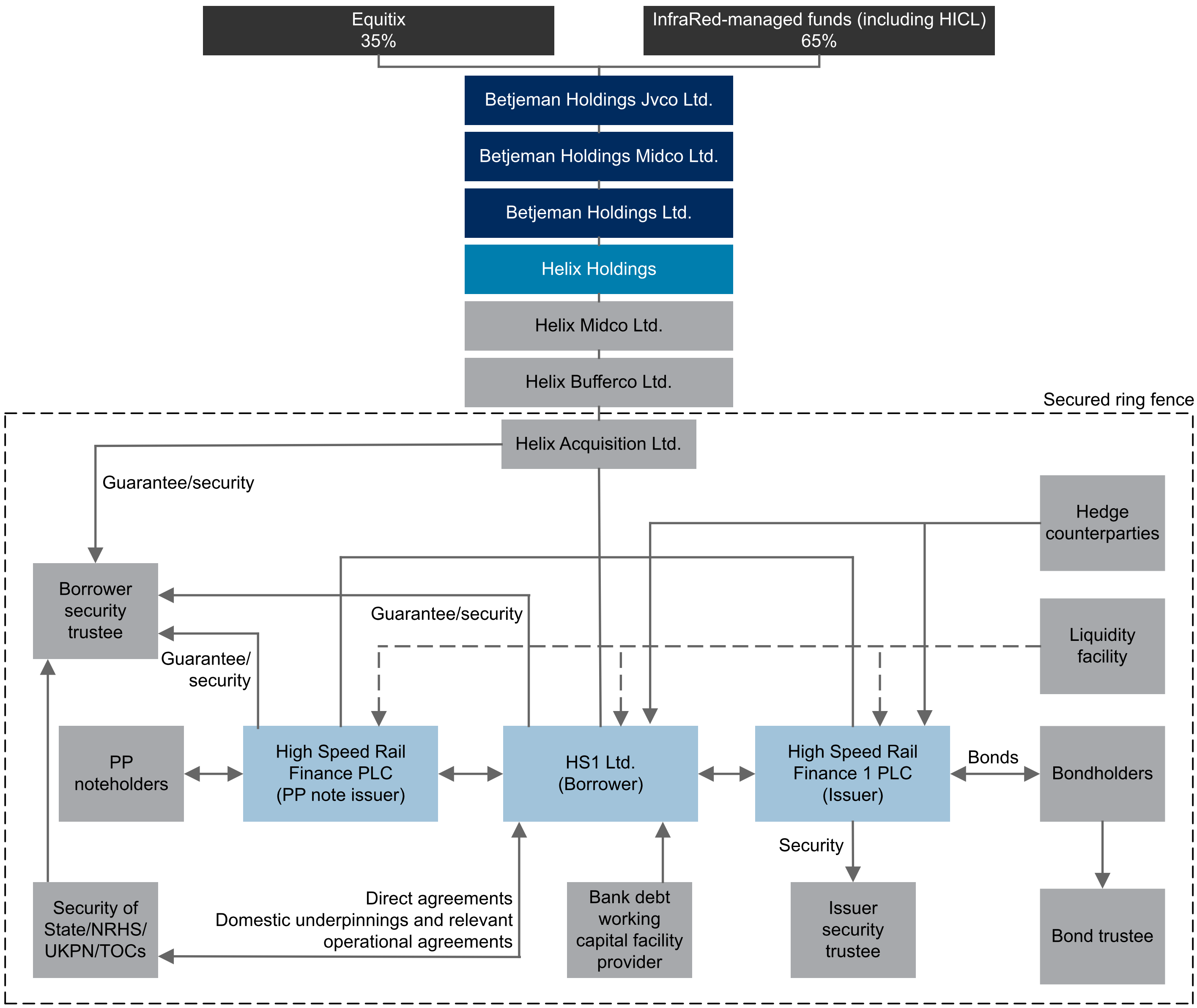
High Speed Rail Finance (1) PLC -- Debt (cont.)

(Mil. £)	Issued by	Debt quantum issued	Outstanding as of September 2018	Maturity	Interest rate	Amortizing starts	Comments
Private Placement 1	HSRF	340	340	March 30, 2028	3.79%	April 2021	Debt is US$550 million, fixed in GBP with cross currency swap.
Private Placement 2	HSRF	117	117	March 31, 2031	4.21%	April 2027	
Private Placement 3	HSRF	58	58	March 31, 2031	Libor + 1.64%	April 2027	
Private Placement 4	HSRF	50	50	March 30, 2036	4.72%	April 2028	
Private Placement 5	HSRF	184	184	Dec. 31, 2039	2.30%	April 2019	
Private Placement 6	HSRF	130	130	March 31, 2039	2.81%	Bullet	
Total		1,833	1,835				

HS1's secured ring-fenced operating group is ultimately owned by a consortium of funds managed by Equitix Investment Management Ltd. (35%), and third-party funds managed by InfraRed Capital Partners Ltd. (65%) following their acquisition of the group in September 2017. The £500 million of holding company (HoldCo) debt issued at Betjeman Holdings Ltd. at the time of the acquisition sits outside of the ring-fenced operating group and is fully subordinated to the senior secured debt.

Chart 1

High Speed Rail Finance (1) PLC -- Transaction Structure



NRHS--Network Rail (High Speed). UKPN--UK Power Networks. TOCs--Train operating companies.

Rationale

Our 'A-' long-term issue rating on HSRF1's debt reflects our view of the project's operations-phase stand-alone credit profile (SACP), which we assess at 'a-'. The project entered into operations in 2007, and hence there is no construction risk.

Operations-phase SACP: 'a-'

The project's operations continue to exhibit strong operational and safety performance. Financial performance is robust and in line with our expectations, underpinned by HS1's transparent and supportive regulatory framework. We consider HS1's transparent and supportive regulatory framework helps to protect the project from any potential negative financial impact of Brexit.

The 'A-' rating continues to reflect the following strengths:

- The project has a strong competitive position as the sole high-speed rail connection between London and Continental Europe, via Eurotunnel.
- The majority of the project's revenues (about 90%) come from highly stable, regulated track and station related charges that are inflation-linked and paid by the two train operating companies (TOCs): the domestic train operator, The London & South Eastern Railway Ltd. (LSER; trading as Southeastern); and the international train operator, Eurostar International Ltd (EIL).
- The U.K. Secretary of State underpins domestic rail services, which in our view mitigates the project's exposure to domestic market risk. Furthermore, the project could, if required, fully cover its debt service based on revenue from the domestic agreement alone.
- The project's market exposure to international routes is mitigated by the obligation for train paths to be booked up to 12 months in advance and paid for quarterly in advance, irrespective of whether the service is run. The same advanced booking and payment requirement applies to domestic and freight services. There is robust demand for EIL services. We therefore assess market risk as very low.
- Regulated revenues are supplemented by income from unregulated retail, car parking, and commercial operations, which make up about 10% of total revenues. We do not factor in nominal revenue growth of nonregulated activities in our rating.
- The project continues to deliver strong operational performance in terms of safety and track availability.
- HS1 passes the majority of the cost of operations through to the track users. The track user charges are paid quarterly in advance of scheduled train services and include a fixed investment recovery charge (IRC), plus a regulated operations, maintenance, and renewals charge (OM&RC) to cover the cost of the operations, maintenance, and renewal of the project's track infrastructure. Power and station usage charges are also applied. In addition to the option for an in-control period reopener, the regulated OM&RC is reviewed every five years by the ORR and allows for virtually full cost pass-through.
- HS1 has limited exposure to capital expenditure (capex) and places the renewal component of the OM&RC and of the station use charge paid by the TOCs into escrow accounts to cover the renewal of the track and the four stations.
- The capital structure of the secured ring-fenced group is predominantly fixed-rate debt. The only floating debt is the £58 million index-linked U.S. private placement tranche C maturing in March 2031, in addition to the £65 million working capital facility (which HS1 draws and repays periodically over a financial year). A portfolio of swaps largely mitigates the remaining interest rate and currency exposure.
- At the time of the new shareholder acquisition, HS1 put in place a £58 million 3.14% revenue retail price index (RPI) swap (settled twice a year) to lock in a minimum inflation increase on the underpinned domestic revenues.
- The senior secured debt benefits from a cash distribution covenant set at an annual debt service coverage ratio

(ADSCR) of 1.20x.

- The project is supported by adequate liquidity in the form of a 12-month debt service reserve facility.
- The project demonstrates robust financial performance under our base case, with a minimum ADSCR of 1.49x and average ADSCR of 1.63x. HS1's reported DSCR for March 2018 was 2.21x. This, combined with the relatively simple operations of the asset, very low market risk, and a strong competitive position, results in a preliminary operations-phase SACP of 'a-'.
- As a result of the contractual protections, the project is strong under our downside scenario, leading us to factor in a one-notch positive adjustment to our assessment of the preliminary operations-phase SACP.

The rating also reflects the following weaknesses:

- The project is exposed to revenues from international train paths, which have shown some deterioration in the past, with the impact of larger trains, terrorist attacks in France and Belgium and, potentially, the Brexit vote being contributing factors. The continued uncertainty around these factors has led us to adopt prudent assumptions in our base-case and downside-case analysis, under which the 'A-' rating continues to be supported.
- The amortization of the debt is relatively back-ended for a project reliant on growth assumptions, with amortization of the majority of facilities not starting until at least 2027. The December 2016 debt issuance shortened the concession tail to one year from two years, and includes a bullet repayment of £130 million in December 2039. We reflect this weakness by applying a one-notch negative debt adjustment.
- Despite HS1's November 2017 security trust and intercreditor deed amendment to offset the revenue RPI-linked income of the revenue RPI swap against operating cash flows, we continue to treat net swap payments as scheduled debt service, in line with our project finance criteria. Consequently, a prolonged period of materially high inflation could weaken the financial ratio profile under our analysis, particularly toward the back end of the concession. Finance performance under our base-case and downside-case assumptions is not impacted, however.
- The rail line requires relatively complex maintenance services. However, we think this risk is largely offset by the subcontracting of these services in full the NRHS under a fixed-price agreement until 2047, beyond the term of the debt, which is subject to price adjustment every five years.
- The rating on the project's debt is weak-linked to the ratings on the operational and financial counterparties, but none of these counterparties' ratings is currently a rating constraint.

Transaction Structure

- Parent linkage: Delinked
- Structural protection: Neutral

Liquidity

We assess the project's liquidity as neutral. The project maintains a 12-month liquidity facility agreement through March 2040 equal to the forthcoming 12 months of scheduled debt service (principal and interest, including amortization and interest of the offsetting swaps). In addition, the project maintains a £65 million working capital facility through March 2020 that is more than sufficient to meet its working capital needs. We assume that the project will readily renew or replace the working capital facility at its maturity.

For the maintenance of the assets and replacement capex, the project maintains escrow accounts, into which it places the renewals component of the regulated revenues. The cost-pass-through nature of these charges largely mitigates life cycle risk. The combined balance on these escrow accounts stood at £110 million in the financial year ending March 30, 2018, and we forecast that this will rise to about £120 million at the end of the current control period in March 2020.

Outlook

The stable outlook on HSRF1's debt reflects our view that the project will continue to deliver strong operational performance and benefit from a supportive and stable regulatory regime. The outlook also factors in the project's strong competitive position as operator of the sole high-speed train route connecting the U.K. to Continental Europe, as well as our view that the minimum ADSCR of at least 1.4x under our base case is sustainable. The rating on HSRF1's debt is supported by the project's strong contractual structure, including advance train path reservation and payment by train operators and an agreement guaranteed by the U.K. government underpinning domestic train paths. These factors help to provide performance resilience against stressed operating conditions.

Downside scenario

We could lower the rating on HSRFI's debt if the project's financial profile weakened, causing the minimum ADSCR to fall below 1.4x or a weakening of performance under our downside scenario. This could occur because of operational underperformance or long-term reduced demand for international train paths resulting, for example, from the impact of Brexit or terrorist events. A prolonged period of materially high inflation could also lead to deterioration in the project's financial performance under our ADSCR calculation, which treats the net revenue RPI swap payments as scheduled debt service, although we view such a scenario as unlikely.

We could also lower the ratings if the project becomes exposed to additional counterparty risk. Revenue counterparty risk could increase, for example, through the weakening of the credit quality of existing or new train operators. Financial counterparty risk could heighten as a result of a downgrade of swap counterparties or working capital facility providers to below the project debt rating level, or if the project incurs additional exchange-rate risk due to the issuance of a further tranche of foreign currency-denominated debt with a lower-rated swap counterparty.

Upside scenario

A positive rating action is unlikely, in our view, without further significant improvement in our base-case projection of the minimum ADSCR, assuming no counterparty rating constraint. For us to consider an upgrade, we would need to observe a minimum ADSCR of about 1.80x, or a restructuring of the debt repayment profile to make it less back-ended.

Operations-Phase Base-Case And Downside-Case Assumptions

Base-case assumptions

Our base-case forecasts for train paths, operating costs, and macroeconomic assumptions for 2018-2040 are:

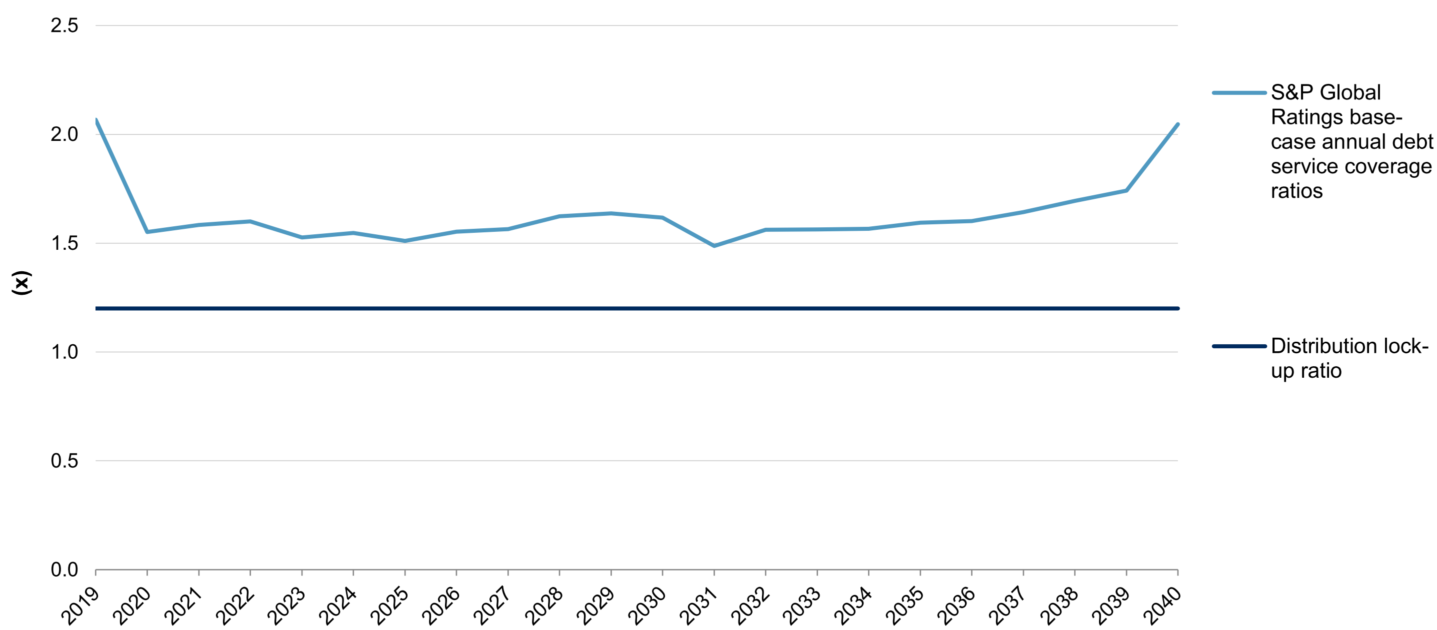
- International train paths: 17,780 total services in the year to March 2019, and flat at 18,000 through to March 2024. Linear total growth of 4,000 train paths thereafter, through the end of the concession. This profile reflects the tough operating conditions facing international traffic demand in the short term in light of larger train sizes, terrorist events in France, and the potential impact of the Brexit vote. Our medium-term growth forecast models the introduction of new services by EIL or a new operator to existing or new destinations, such as Amsterdam or Frankfurt.
- Domestic train paths: Flat demand of 55,575 train paths per year.
- Freight train paths: Flat at 800 train paths per year.
- Spot train paths: Flat at 130 train paths per year for both domestic and international operators.
- Unregulated revenue from retail and carparks: £36 million in March 2019; zero nominal growth thereafter.
- Operating costs: In line with management's forecast, with cost pass-through of OM&RC, power, and station costs.
- Retail Price Index: In line with S&P Global Ratings' latest forecasts: 3.5% for 2018, 3.1% for 2019, 3.0% for 2020, and 3.9% for 2021. We assume inflation of 3.4% in 2022-2026, 3.1% in 2027-2031, and 3.0% growth thereafter.
- A recessionary period between 2035 and 2039, designed to replicate the stress experienced in 2008-2009 and in line with the assumptions in the peer project, Channel Link Enterprise Finance PLC.
- Corporate tax rate: 19% for 2017-2019, and 17% from 2020.
- Interest income: None, in line with our ADSCR calculation.
- To ensure comparability in our cash flow analysis, we assume that the liquidity facility is fully drawn and the reserve account is cash funded.

Base-case key metrics

- Minimum ADSCR: 1.49x in March 2031
- Average ADSCR: 1.63x
- The minimum forecast ADSCR remains above 1.40x, which supports a preliminary SACP of 'a-' given the project's operations-phase business assessment (OPBA) of '4'.
- Chart 2 shows the profile of our forecast base-case debt service coverage ratios.

Chart 2

High Speed Rail Finance (1) PLC -- Base-Case ADSCR



ADSCR--Annual debt service coverage ratio. Source: S&P Global Ratings.

Downside-case assumptions

- International train paths: Flat at 18,000 total train paths, plus two three-year shocks starting in 2021 and 2035. The shocks reflect the impact of an incident, such as a tunnel fire, resulting in partial temporary tunnel closures with 20% capacity constraint in two consecutive semesters. Steady traffic recovery to pre-stress 18,000 train paths levels in the fourth year.
- Domestic train paths: Train paths at the underpin level (53,000 train paths per year).
- Freight train paths: No change from our base case, plus three-year train path shocks in 2021 and 2035 (as per international train paths).
- Spot train paths: None.
- Unregulated revenue: 20% below our base case.
- Unregulated costs: 20% above our base case.
- Retail Price Index: 1 percentage point below our base case for the five years (2018-2022). Thereafter, in line with the base case (including the recessionary period between 2035 and 2039).

Downside-case key metrics

- The project performs strongly under our downside-case scenario, supported by the 12-month debt service reserve facility. The minimum base-case ADSCR remains above 1.2x at all times, supporting a downside assessment of 'aa'.
- We incorporate a one-notch positive adjustment to the preliminary SACP to reflect the project's strong financial performance under the downside-case scenario. This is a reflection of the contractual agreement that supports domestic revenues and protection afforded to HS1 by the revenue payment mechanism, along with our expectations that international demand will not decline materially from current levels.

Financial Performance

The IRC, which totaled £170 million in the year to March 2018, up from £163 million in the year to March 2017, drives the majority of HS1's cash flows. HS1 recorded a 4.3% year-on-year IRC increase, despite a decrease in international train paths. This figure reflects the inflation-linked nature of the IRC, as well as to the end of the IRC discount on the Brussels route. The train path reduction stemmed from the introduction of larger trains, as well as from weaker performance of the international TOC, EIL, which experienced a tough operating environment following terrorist attacks in France and Belgium, thereby reducing passenger volumes. HS1 recorded an historic DSCR of 2.21x for March 2018, which was above the budget of 2.16x and significantly above the 1.20x cash distribution lock-up covenant.

Operations Update

The OPBA of '4' remains unchanged and reflects our view of the project's transparent and supportive regulatory framework that helps to mitigate operational risk and, combined with a strong competitive position and very low market risk, leads to a strong operational performance. None of the operational developments that have occurred over the past year affects our assessment of the project's operational risk profile.

Operational developments

HS1 has performed well over the period since our last review. Performance for the year to date is robust, driven by strong Eurostar growth. We expect Eurostar services for the year to March 2019 will reach more than 18,000 train paths, up 4% on the previous year and in line with our long-term international train path forecast. This performance is a substantial turnaround from the decline in Eurostar train paths recorded in the year to March 2018.

Other events in this period include the delay of the domestic franchise contract renewal and the CP2 (the regulatory control period running from April 1, 2015, to March 31, 2020) OM&RC rate reopener, neither of which have had a material effect on HS1's performance. Domestic train service levels are stable and HS1 continues to deliver a high level of track safety and availability performance. HS1 has also promptly dealt with one-off service interruption issues.

Nonregulated services--predominantly station retail and car parks--continue to perform strongly and boost cash flow available for debt service. We do not factor growth of these services into our base-case analysis.

Turnaround in international train path performance

The Eurostar Paris to London route is operating well, supplemented by services to other international stations and French regional routes, such as Marseille. Eurostar launched new services to Amsterdam in April 2018, running two return journeys per weekday and one return journey per weekend day. Juxtaposed border controls (whereby border control takes place before boarding rather than upon arrival after disembarkation), which are a key competitive advantage over air travel, are bilateral agreements between the British, French, and Belgian governments, rather than EU law, and are therefore unlikely to be affected by the Brexit vote.

No near-term rating impact of the Brexit vote

In our opinion, HS1 is relatively well protected--particularly in the short term--against the potential impact of Brexit, which could lead to a change in train path demand from both domestic and international traffic.

HS1 receives quarterly, advance revenue receipts from TOCs, based on the pre-agreed annual timetable (the First Working Timetable [FWT]). These inflation-linked charges help to protect HS1 from short-term train path fluctuations, as demonstrated in the year to March 2018. The current FWT covers the period from January 2019 to June 2019, which includes the 30 March 2019 U.K.'s scheduled departure from the EU. The FWT starting in December 2018 will set train paths for mid-May to December 2019--this provides HS1 with even more certainty prior to U.K.'s departure from the EU in March 2019. Therefore, unlike many companies, HS1's cash flow volatility exposure is mitigated for at least one year. It is also less exposed to the potential disruptions that could occur immediately after Brexit.

Over the longer term, HS1 could be exposed to a reduction in international train paths if border and immigration changes harm the flow of business or leisure bookings. That said, the potential move of businesses out of London and into Europe could lead to a demand for increased train services to Europe by U.K. business travelers, thereby offsetting any reduction in traffic from the U.K. to Europe. Regarding tourists, both the U.K. and European governments have indicated that they would like to preserve the free flow of people for short-period trips.

It is unlikely that Brexit will materially affect the number of domestic train paths. Even if the U.K.'s economy were to shrink to such a level that the population's movements around the U.K. decreased, domestic train paths are underpinned by the U.K. government and cannot fall below 53,248 train paths per year, as per our downside-case assumptions.

OM&RC reopener

The OM&RC reopener clause also provides HS1 protection against train path reduction that could occur, for example, as a result of Brexit. The reopener helps HS1 mitigate volume risk by permitting it to reset the OM&RC based on a lower assumed train path amount. This was demonstrated earlier in the year when HS1 instigated the reopener following a decline in international train paths above the 4% OM&RC reopener threshold for the CP2. The rate review resulted in revised OM&RC rates being implemented for both domestic and international train paths from April 1, 2018, albeit these were largely offset by a decline in the domestic OM&RC rates due to the higher number of domestic train paths being run compared with the CP2 assumptions. The OM&RC reopener's overall financial impact on HS1 has been limited.

Stable domestic services

Domestic train paths remain relatively stable and we do not anticipate any material interruption to result from the new franchise award. LSER franchise award is underway, although this has been delayed from the initial award announcement expected in the third quarter of 2018. In the meantime, the government has granted LSER a direct agreement, under which LSER is required to deliver business as usual until the new franchise is awarded. We expect the new Southeastern franchise award will cover an eight-year period, through mid-2027, with a one-year extension option available at the Department For Transport's discretion. We have seen the replacement of a number of domestic TOCs in the U.K. in the past, as seen when LSER took over its current franchise in 2014, or following various TOC failures in the U.K. since 1994. These replacements have typically resulted in immediate remediation with the continued timely, full payment of access charges.

We maintain our flat base-case demand of 55,575 train paths throughout the concession. Our forecast is slightly below the 55,793 figure as of March 2018.

Nonregulated activities demonstrate strong performance

HS1's nonregulated retail and car-parking income, which directly affects cash flow available for debt service, continued to increase in the year to March 2018, reaching £35 million. HS1 forecasts continued growth in the year to March 2019. Growth is driven largely by retail activities at St. Pancras, but also by car parking at the Ebbsfleet and Stratford stations. The assumption of nominal revenue growth from nonregulated activities does not affect our rating. Revenue from nonregulated activities only represents 11% of total revenue, with the train IRC reaching £170 million in the year to March 2018.

Group developments

Keith Ludeman, the former Group CEO of Go-Ahead Group plc, succeeded Rob Holden as HS1 chairman in September 2018. Keith is an experienced chairman and senior board member, having served as non-executive director of companies such as Network Rail Ltd. Hence, we do not expect the board change to hinder the project's governance or performance. The operational management team remains unchanged, with Dyan Crowther and Mark Farrer both in their second years as Chief Executive Officer and Chief Financial Officer, respectively. HS1 continues to deliver strong operational and safety performance under the management team's guidance.

On Sept. 7, 2017, there was a change in the ultimate shareholders of the secured ring fenced group, when the shareholders, Ontario Teachers' Pension Plan and Borealis Infrastructure, sold 100% of their shares. The new shareholder structure comprises a consortium of funds managed by Equitix Investment Management Ltd. (35%), and third-party funds managed by InfraRed Capital Partners Ltd. (65%). The secure project company is ring-fenced from the activities and credit quality of the shareholders, and hence the sale does not affect the rating on HSRF1's debt. We have not seen, and do not anticipate, a change in the strategic direction of the regulated business. The £500 million of new HoldCo debt issued at the time of the acquisition sits outside of the ring-fenced operating group and is fully subordinated to the senior secured debt. The £58 million revenue RPI swap (settled twice a year) issued by Betjeman Holdings Ltd. was transferred to HS1 following the completion of the shareholder acquisition. A small portion of the HoldCo debt proceeds were used to prepay £19.6 million of the £98 million bank facility at HS1, which we have factored into our financial analysis with minimal effect on ratios.

Counterparties

We weak link the project's debt rating to the credit quality of counterparties that take material risks and potentially expose the credit of the project to the risk of the counterparty failure. A material counterparty is one that significantly affects the timeframe or cash available to service debt through the construction and/or operation of the project (see "Project Finance Construction And Operations Counterparty Methodology," published Dec. 20, 2011).

Revenue Counterparties

HS1's revenue comprises approximately 90% regulated revenue and 10% nonregulated revenue. The nonregulated revenue is generated by multiple station retail units and car park users and there is not, in our opinion, a rating dependency on any individual nonregulated customer.

HS1 regulated revenues are generated by two TOCs: LSER and EIL. We view the project's exposure to the IRC counterparties as material and our analysis to assess the dependency of HS1 to these counterparties adopts a rating to principles approach, using our criteria "General Criteria: Principles Of Credit Ratings," published Feb. 16, 2011, in conjunction with our "Project Finance Construction And Operations Counterparty Methodology," published Dec. 20, 2011. Under the rating to principles approach we determine the overall revenue counterparty credit quality by calculating the weighted average creditworthiness of the two revenue counterparties in proportion of their regulated revenue contribution. The revenue counterparty credit quality under this approach does not constrain the debt rating.

The regulated revenue comprises the fixed IRC, the OM&RC, and the qualified station expenditure charges (QX). HS1 passes the OM&RC and QX charges through to the train operators and therefore it is the IRC, which represents about 55% of total revenues under our base case, that drives HS1's profitability and cash flow performance.

The majority of the IRC (approximately 70%) is provided by the domestic TOC and is directly guaranteed by the U.K. government under the agreement put in place in January 2015. Furthermore, the U.K. Department for Transport maintains step-in arrangements that would enable it to take over a failing domestic TOC and directly operate its service. We therefore view the domestic TOC as a material and irreplaceable counterparty, with credit quality in line with see the U.K. government (unsolicited, AA/Negative/A-1+).

All remaining IRC revenues come from the international train operating company, EIL, which we consider to be a material--but replaceable--counterparty. Due to the strategic nature of the route, we expect that another service provider would continue to operate the international route, if required, without material interruption to the service. Cash flow interruption would be limited by the protection afforded by the 12-month debt service reserve and the advanced payments for train paths. Our view of EIL's credit quality has weakened in recent months due to its challenging operating environment exacerbated by terrorism and uncertainty regarding Brexit.

Operations counterparties

We consider the O&M counterparty, NRHS, to be irreplaceable and weak link the project's debt rating to the credit quality of NRHS, which is not a rating constraint. NRHS retains performance risk and the responsibility for safety under railway regulation, in line with the operator's role in transport projects. NHRS's payment and performance obligations benefit from a guarantee granted from its parent company, Network Rail Infrastructure Ltd. (Network Rail). Network

Rail is funded by the debt program of Network Rail Infrastructure Finance PLC, which is a government-related entity and rated in line with the rating on the U.K. government.

U.K. Power Networks (UKPN) operates the electricity distribution infrastructure and supplies electricity under a finance lease agreement (through to 2057). The electricity distribution market is wide in the U.K. and we believe that UKPN could be replaced if necessary, without material disruption. We therefore do not weak link the project's debt rating to the credit quality of UKPN.

Financial Counterparties

Swap counterparties. The ratings on the project debt are weak-linked to the ratings on the swap counterparties, as the terms of the swap do not fulfill our criteria requirements for collateral and timely replacement. The project's hedging policy states that HS1 may enter into swaps with counterparties rated 'A-' or above and that the swap counterparty is committed to taking corrective action when its rating falls below investment grade. The agreement does not, however, require the counterparty to post collateral or provide a timely replacement. The replacement language in the swap agreement is therefore not compliant with our criteria (see "Counterparty Risk Framework Methodology And Assumptions," published June 25, 2013, on RatingsDirect). The project maintains interest rate and cross-currency swaps with a number of rated counterparties: National Australia Bank, BNP Paribas, Bank of Nova Scotia, Royal Bank of Canada, and Lloyds Bank. We rate all of these entities one notch higher than HSRF's debt and therefore they do not constrain the project's debt rating. Should the rating on any of the entities fall below the issue rating, we would assess the fallout from this counterparty failing to fulfill its obligations under the swap.

Bank account, liquidity and working-capital facility providers. The 12-month forward-looking liquidity facility is provided by three financial counterparties: National Australia Bank, Bank of Nova Scotia London Branch, and BNP Paribas. The terms of the liquidity facility require that we rate the counterparties at least 'BBB' and that, should the rating of any counterparty fall below this level, HS1 must replace it within 60 days. The replacement period is in line with the required remedy period stipulated in our criteria to support transactions rated at 'A-'.

Similarly, the terms of the account bank agreement require the account bank to be rated at least 'BBB-' or to be replaced within 60 days. Assuming that the definition of 'days' is 'calendar days', our criteria requires the account bank to be rated at least 'BBB-' to avoid constraining our 'A-' rating.

The ratings on the project debt are weak-linked to the ratings on the six £65 million working capital facility providers, each of which provides £10.8 million: The Royal Bank of Scotland, Lloyds Bank, Canadian Imperial Bank of Commerce, Scotiabank (Ireland), BNP Paribas, and Export Development Canada. We rate these entities one notch higher than HSRF's debt, with the exception of RBS and Scotiabank (Ireland). We believe that the size of the facility is in excess of requirements and hence we can exclude these two weakest financial counterparties without affecting the liquidity position of the project. Hence, the ratings on the working capital financial counterparties do not constrain the rating on the project's debt rating.

Other Modifiers Update

There are no other modifiers that have an impact on the rating.

Rating Score Snapshot And Peer Comparison

The closest peer for HSRF1 is Channel Link Enterprise Finance PLC (CLEF), which we rate one notch lower at 'BBB+'. CLEF has a weaker minimum DSCR (1.4x) than our 1.49x base case for HS1. Unlike HSRF1, CLEF does not have the protection of U.K. government-guaranteed revenues, nor does it receive advanced payments from any of its revenue counterparties.

Operations-Phase SACP (Senior Debt)

- Operations-phase business assessment: 4 (1=best to 12=worst)
- Preliminary operations-phase SACP: 'a-'
- Downside analysis: 'aa' (+1 notch)
- Debt structure: Negative (-1 notch)
- Liquidity: Neutral (no impact)
- Comparable ratings analysis: Neutral (no impact)
- Operations-phase SACP: 'a-'

Modifiers (Senior Debt)

- Parent linkage: Delinked (no impact)
- Structural protection: Neutral (no impact)
- Senior debt issue rating: 'A-'

Related Criteria

- Criteria - Corporates - Project Finance: Key Credit Factors For Road, Bridge, And Tunnel Project Financings, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Transaction Structure Methodology, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Operations Methodology, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Framework Methodology, Sept. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Financial Institutions - Banks: Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Criteria - Structured Finance - General: Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Criteria - Corporates - Project Finance: Project Finance Construction And Operations Counterparty Methodology, Dec. 20, 2011
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Bulletin: U.K.-Based HSRF And HSRF1 Debt Ratings Unaffected By Sale Of Indirect Holding Company, Helix Holding Ltd, Sept. 12, 2017
- New Issue: High Speed Rail Finance PLC, Dec. 15, 2016
- Research Update: High Speed Rail Finance New Senior Secured Debt Rated 'A-'; Outlook Stable, Dec. 15, 2016

Additional Contact:
Infrastructure Finance Ratings Europe; InfrastructureEurope@spglobal.com