AA Intermediate Co Ltd - Investor Report

This is the Investor Report for the year ended 31 January 2021 which we are required to deliver pursuant to paragraph 6 of Part A of Schedule 3 of the Common Terms Agreement.

All figures in the commentary below are as per the AA Intermediate Co Limited statutory accounts, post adoption of new IFRS accountings standards such as IFRS 16 and IFRS 9. We note that the ratios below the commentary in respect of the Group's debt covenants are calculated after reversing the impact of such GAAP changes as required by the covenant documents.

General Overview

The business is characterised by stable and predictable revenue streams, strong operating margins and high cash conversion.

The business is focused on delivering the highest possible standards of customer service, quality products, stable and predictable profits, strong operating margins and high cash conversion. The Group continued to demonstrate all of these qualities in the financial year:

- We attended 3.0 million breakdowns in the year ended 31 January 2021, and the AA remains the market leader with c. 40% of the Consumer market, c. 60% of the manufacturer segment, c. 60% of the UK's largest fleet and leasing companies and around half of the AVA banking segment.

- Trading EBITDA decreased by 6% to £322 million in the twelve months ended 31 January 2021 (2020: £341 million).

- Trading EBITDA margin remained steady at 35% in the twelve months ended 31 January 2021 (2020: 35%).

- Cash flow from operating activities before tax and exceptional items of £281 million (cash conversion: 87%) for the year ended 31 January 2021 and £336 million (cash conversion 99%) for the year ended 31 January 2020.

- Total Net Debt to EBITDA of 8.4 x and Total Class A Net Debt to EBITDA at 6.5 x as at 31 January 2021.

Further information is available at www.theaacorporate.com/investors and within the AA Limited Annual Report and Financial Statements.

Regulatory and business update

On 25 November 2020, the board of directors of Basing Bidco Limited, a newly formed joint venture company indirectly owned in equal shares by (i) funds advised by TowerBrook Capital Partners (U.K.) LLP or its affiliates and (ii) private equity funds managed by Warburg Pincus International LLC or its affiliates, agreed with the board of directors of AA Limited (the AA Intermediate Co Limited group's ultimate parent undertaking), the terms of a recommended cash acquisition pursuant to which Bidco would acquire the entire issued and to be issued ordinary share capital of AA Limited. The Acquisition was completed on 9 March 2021 and AA Limited's ordinary shares were de-listed from the London Stock Exchange on 10 March 2021. AA Limited was re-registered as a private company on 17 March 2021. As part of the Acquisition, the Consortium made an alternative offer to shareholders enabling them to transfer their ownership to the new structure resulting in an interest of 16% in Bidco and the AA Limited group transferring to these shareholders.

As reported in the prior year financial statements, the former Executive Chairman, Bob Mackenzie, who was dismissed for gross misconduct on 1 August 2017, had on 6 March 2018 issued a claim for substantial damages against AA Limited, its subsidiary (Automobile Association Developments Limited) (together, 'the Companies') and personally against a number of their directors (existing and former) and the former Company Secretary.

In November 2018, Mr Mackenzie's claim against all the directors and the former Company Secretary was dismissed in full and he was ordered to pay their costs to be assessed by the Court if not agreed. The majority of Mr Mackenzie's claim arises from his exclusion from a share option scheme which, in any event, lapsed for all participants without any payment in June 2019. However, Mr Mackenzie subsequently issued an amended claim which included a new claim for personal injury allegedly suffered as a result of stress arising from his role as CEO and Chairman.

The Companies have filed a full defence in relation to Mr Mackenzie's amended claim and, after further discussion with external counsel, the Companies decided to apply for a strike-out application in relation to the entirety of Mr Mackenzie's claims against them. This application was filed in May 2020 and the Companies attended an application hearing in March 2021 in respect of this. The Court reserved its judgement after the strike out application hearing and as of the date of this document the judgement is still awaited. Therefore, the Board assumes for the purpose of these financial statements that Mr Mackenzie will proceed with the claim against the Companies but maintains that it is not necessary for the Group to make a financial provision as it expects the defence will prevail.

The insurance industry has seen significant activity from the FCA in the areas of pricing practices, vulnerable customers and product value considering COVID-19. The AA has worked collaboratively with the FCA in responding to the 'Dear CEO' letters and data requests sent out to intermediaries. The FCA's Pricing Practices final rules have now been published. These rules confirm the requirements to ensure renewal prices offered are no higher than the equivalent new business price as well as requiring firms to assess fair value of the products they sell. The FCA's recent pricing practices final rules may have a material impact on the motor and home insurance market in the UK for both insurers and insurance intermediaries, which could lead to a disrupted market. The rules come into force at the end of 2021 and we will continue to monitor change in market dynamics as a result of these new rules and the impact on the AA. Given recent political events, the AA continues to monitor the potential impact of Brexit on the AA's business and operations, which has previously been assessed as being minimal.

There have been no other new significant regulatory and business developments (including any highly publicised incidents) other than as described in the Annual Financial Statements.

There have been no other significant announcements/publications by the government relating to Permitted Business.

There were no changes to office holders during the year and up to the date of approval of the financial statements.

Capital Expenditure

Capital Expenditure (excluding Maintenance Capital Expenditure) in the period to 31 January 2021 included growth capital expenditure of £26m related to our Roadside and Insurance business and £13m related to digital projects.

There has been no other Capital Expenditure (excluding Maintenance Capital Expenditure) in an amount exceeding £5m (Indexed) during the period.

Financing

On 5 February 2020, the Group issued £325m of Class A8 Notes at an interest rate of 5.50% in exchange for £325m of Class A5 Notes.

On 23 April 2020, the Group announced that it had drawn down in full its £200m Senior Term Facility. The proceeds were held in escrow and subsequently released to refinance the remaining £200m Class A3 Notes on 31 July 2020.

On 29 January 2021, the Group issued £280m of Class B3 Notes at an interest rate of 6.50%. At 31 January 2021, the cash proceeds were held in a secured escrow account on behalf of the Group, its Class B Note Trustee and the Class B3 Noteholders as secured creditors. These funds could only be used for the purposes of redeeming the Group's Class B2 Notes or repaying the Class B3 Noteholders should the Class B2 Notes not have been redeemed.

On 10 March 2021, the Group refinanced the £570m outstanding Class B2 Notes using £261m cash injected as new equity from the Consortium, the £280m proceeds from the issuance of the Class B3 Notes which were released from escrow and the cancellation of £29m Class B2 Notes held directly by AA Limited.

On 10 March 2021, the Group also refinanced its Senior Term Facility, Working Capital Facility and Liquidity Facility.

Acquisitions or Disposals

On 21 May 2020, the Group completed the sale of the entire share capital of AA Underwriting Limited and Automobile Association Underwriting Services Limited for cash consideration of £5m. The combined net book value of net assets disposed of was £6m, which resulted in a £1m loss on disposal being recognised. The net outflow of cash to dispose of these subsidiaries was £1m.

Current Hedge Position

The Holdco Group has an interest rate swap in place which can be used in order to fully hedge its interest rate exposure in relation to its Authorised Credit Facilities, should it be required.

Class A 'basket' reset

As noted in the prior year, as permitted by the WBS programme, we have reset both the Minimum Capital Maintenance Spend Amount to £35 million (from £25 million) and the Maximum Finance Lease Amount to £150 million (Indexed) (from £60 million (Indexed)). This applies for the 5 financial years ending 31 January 2023.

Ratios

We confirm that in respect of this investor report dated 28 June 2021, by reference to the most recent Financial Statements that we are obliged to deliver to you in accordance with paragraph 1 (*Financial Statements*) of Part A (*Information Covenants*) of Schedule 3 (*Holdco Group Covenants*) of the Common Terms Agreement:

- the Class A FCF DSCR as at 31 January 2021 is more than 1.35; we set out the calculation below:

	Year to January 2021 £m
Operating profit before tax	53
Add back:	
Debt interest payable	138
Penalty interest payable	6
Interest payable under finance leases	2
Amortisation of debt issue costs	8
Discounts and fees in respect of financing	12
Non-cash interest expense attributable to movement in mark-to-market hedging obliga	1
Finance costs in respect of pensions	(3)
Exceptional items	4
Depreciation and amortisation	89
Difference between the pension service cost and employer cash contributions	5
Share-based payments	4
Class A Maintenance EBITDA	319
Less	
Cash tax paid	(14)
Change in working capital	2
Minimum capital maintenance spend	(35)
Class A Free cash flow	272
Class A total debt service charge	107
Class A FCF DSCR	2.5

- the amount of Additional Financial Indebtedness raised since the date of the immediately preceding Investor report and included for the Test Period ending 31 January 2021 was £Nil.

- the maximum amount of Permitted Investor Payments that may be made in the 90 days following the date of required delivery of this Compliance Certificate is £Nil, and the calculation below shows the maximum amount of Permitted Investor Payment where the ratio of Total Class A Net Debt as at the most recent Test Date to EBITDA in respect of the Test Period ending on that Test Date calculated pro forma would be 5.5:1.

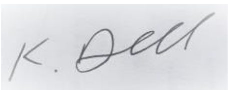
		Year to Jan-21 £m
Class A Debt:		
	Senior Term Facility	200
	Class A2 Notes	500
	Class A5 Notes	372
	Class A6 Notes	250
	Class A7 Notes	550
	Class A8 Notes	325
Less:	Cash and Cash Equivalent Investments	(119)
Total Class A Net Debt		2,078
	Permitted Investor payment	(324)
Max Class A Net Debt		1,755
Class A Maintenance EBITDA		319
Ratio of Class A Net DEBT to EBITDA		5.5

- We confirm that the Class A FCF DSCR Ratio has been calculated in respect of the Test Dates for which it is required to be calculated under the Common Terms Agreement.

We confirm that:

- no CTA Default or Trigger Event has occurred and is continuing.
- the Holdco Group is in compliance with the Hedging Policy.
- as excess cashflow for the year is £33 million, £33 million has been added to Retained Excess Cash flow.
- No dividend payment has been made out of Retained Excess Cashflow in the period since the date of the most recent Compliance Certificate;
- therefore the amount of Retained Excess Cashflow as at the date of this Compliance Certificate is £228 million; there have not been other payments made out of Retained Excess Cashflow
- we are in compliance with the Obligor Coverage Test.
- below is a list of the Material Companies as at 31 January 2021:
    - ➢ Automobile Association Developments Limited
    - ➢ Automobile Association Insurance Services Limited
    - ➢ AA Corporation Limited
- the statements set out in this Investor Report are accurate in all material respects.

Yours faithfully,



Kevin Dangerfield
Director
For and on behalf of Automobile Association Developments Limited as Holdco Group Agent
28 June 2021