AA Intermediate Co Ltd - Investor Report

This is the Investor Report for the year ended 31 January 2022 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 3.1 million breakdowns in the year ended 31 January 2022, and the AA remains the market leader with c. 40% of the Consumer market, c. 55% of the manufacturer segment, over 65% of the UK's largest fleet and leasing companies and over 60% the AVA banking segment.

- Trading EBITDA increased by 1% to £324 million in the twelve months ended 31 January 2022 (2021: £322 million).

- Trading EBITDA margin decreased by 0.2% to 34.5% in the twelve months ended 31 January 2022 (2021: 34.7%).

- Cash flow from operating activities before tax and exceptional items of £320 million (cash conversion: 99%) for the year ended 31 January 2022 and £281 million (cash conversion 87%) for the year ended 31 January 2021.

- Total Net Debt to EBITDA of 7.1 x and Total Class A Net Debt to EBITDA at 6.2 x as at 31 January 2022.

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 (BidCo), 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 (together, the Consortium), agreed with the board of directors of AA Limited (the AA Intermediate Co Limited group's 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 previously, 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 former directors and the former Company Secretary.

In November 2018, Mr Mackenzie's claim against all the directors and a 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 has now issued an amended claim which includes 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. 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 strike out hearing was held in March 2021. The strike out application was successful on all counts and all of Mr Mackenzie's claims, bar his wrongful dismissal claim which was not part of the strike-out application, were dismissed. Mr Mackenzie subsequently applied directly to the Court of Appeal and the hearing commenced on 4 May 2022 but was adjourned due to illness of one of the judges. The remainder of the hearing is being relisted and is expected to be heard in June 2022. The Board assumes for the purpose of the Intermediate Co Limited group financial statements that should Mr Mackenzie be successful in appealing the strike-out application decision then he 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 wider insurance environment has remained fluid, with the effects of the pandemic and the new General Insurance Pricing Practices (GIPP) creating a unique combination of challenges. Having delivered strong growth in the first half of the year, we evolved our stance in the second half of the year by balancing growth and profitability and ensuring robust underwriting disciplines in our underwriter in light of a particularly competitive pricing environment. During this period, we have also facilitated a smooth transition to meet the GIPP requirements by January 2022, have further strengthened our direct to consumer and cross selling activities and have further expanded footprint and capability in our insurance underwriter. The introduction of GIPP is one of the most significant changes to pricing within the UK insurance industry and has resulted in a challenging trading environment, which has been widely reported on. As we look ahead, and not withstanding the near-term disruption, we remain confident in the quality of our insurance business.

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.

The Directors who held office during the year and up to the date of signing the financial statements were as follows:

Marianne Neville, Director	
Kevin Dangerfield, Director	(resigned 12/11/2021)
Nadia Hoosen, Company Secretary	(resigned 31/05/2021)
Tom Mackay, Chief Financial Officer	(appointed 15/11/2021)
James Cox, Company Secretary	(appointed 01/10/2021)

Capital Expenditure

Capital Expenditure (excluding Maintenance Capital Expenditure) in the period to 31 January 2022 included growth capital expenditure of £32m related to our Roadside and Insurance business and £15m 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 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 refinanced its Senior Term Facility. The new £150m Senior Term Facility was drawn down immediately and used, in combination with £50m of cash, to refinance the existing £200m Senior Term Facility. The Group also agreed a new £56m Working Capital Facility, of which £46m is available for cash drawings and remains undrawn, and cancelled its existing Working Capital Facility of £60m. In addition, the Group agreed a new £160m Liquidity Facility which remains undrawn, and cancelled its existing Liquidity Facility of £165m.

On 21 July 2021, the Group issued £270m of Class A9 Notes at an interest rate of 3.25%. The proceeds of these notes were held in escrow until 1 November 2021 when they were released and used, along with a further equity injection of £100m, to redeem the £372m of outstanding Class A5 Notes.

Acquisitions or Disposals

There were no acquisitions or disposals in the year ended

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. The Group has also currently hedged 100% of forecast diesel usage for the year ended 31 January 2023 and c.50% of forecast usage for the year ended 31 January 2024.

Class A 'basket' reset

As at 31 January 2018 we 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 21 June 2022, 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 2022 is more than 1.35; we set out the calculation below:

	Year to January 2022 £m
Operating profit before tax	(4)
Add back:	
Debt interest payable	125
Interest payable under finance leases	1
Amortisation of debt issue costs	8
Discounts and fees in respect of financing	5
Non-cash interest expense attributable to movement in mark-to-market hedging obligations	(1)
Finance costs in respect of pensions	2
Exceptional items	84
Depreciation and amortisation	95
Difference between the pension service cost and employer cash contributions	30
Share-based payments	5
Less: Gain from release of Class B2 Notes	(29)
Class A Maintenance EBITDA	321
Less	
Cash tax paid	(10)
Change in working capital	44
Minimum capital maintenance spend	(35)
Class A Free cash flow	320
Class A total debt service charge	103
Class A FCF DSCR	3.1

- 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 2022 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-22 £m
Class A Debt:		
	Senior Term Facility	150
	Class A2 notes	500
	Class A6 notes	250
	Class A7 notes	550
	Class A8 notes	325
	Class A9 notes	270
Less:	Cash and Cash Equivalent Investments	(67)
Total Class A Net Debt		1,978
	Permitted Investor payment	(213)
Max Class A Net Debt		1,765
Class A Maintenance EBITDA		321
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 £nil, £nil 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 2022:
  - 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,

T. MacKay

Tom MacKay
Director
For and on behalf of Automobile Association Developments Limited as Holdco Group Agent
21 June 2022