AA Intermediate Co Ltd - Investor Report

This is the Investor Report for the year ended 31 January 2023 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 and 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 generation.

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 generation. The Group continued to demonstrate all of these qualities in the financial year:

- We attended 3.2 million breakdowns in the year ended 31 January 2023, and the AA remains the market leader with > 40% of the Consumer market, >55 % of the manufacturing segment, over 65% of the UK's largest fleet and leasing companies and over 70% the AVA banking segment.

- Adjusted EBITDA increased by 5% to £365m in the twelve months ended 31 January 2023 (2022: £347m) and Reported EBITDA (previously trading EBITDA) increased by 4% to £336m (2022: £324 million).

- Adjusted EBITDA margin decreased by 0.2% to 36.7% and Reported EBITDA decreased by 0.7% to 33.8% in the twelve months ended 31 January 2023 (2022: 36.9% and 34.5%).

- Cash flow from operating activities before tax was £252m (2022: £252m)

- Total Class A Net Debt to EBITDA was 5.8 x as at 31 January 2023 (2022: 6.2x).

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

Regulatory and business update

Following Warburg Pincus and TowerBrook Capital Partners' acquisition of the AA in March 2021, we have continued to invest in the future of the AA, whilst maintaining a deleveraging trajectory. Capital investment of £79m in FY23 (2022: £77m) has gone into core re-platforming across Roadside and Insurance, improving our digital and data infrastructure and developing new propositions for our B2B and B2C customers.

Litigation – update on Mr Mackenzie's claim:

AA Limited and Mr Robert Mackenzie are pleased to confirm that Mr Mackenzie's long-standing actions against the Group have now been settled. The terms of the settlement are confidential. The AA's new management has seen from the evidence that has been put forward during this claim that Mr Mackenzie was very ill in 2017 at the time of the incident in question and are delighted that Mr Mackenzie is reported to have now made a full recovery.

At the end of FY22, we successfully implemented changes in our pricing models in order to comply with the requirements of the FCA's General Insurance Pricing Practices (GIPP) rules, whilst continuing to drive new business volumes and increase customer value.

The Department for Business and Trade (formerly the Department for Business, Energy and Industrial Strategy) published its plans to strengthen the UK's audit, corporate reporting and corporate governance systems. The proposed measures aim to enhance accountability across the business ecosystem and increase resilience and choice in the statutory audit market. The AA has started to assess the potential impact and is making plans to respond to the expected future direction of financial reporting for in-scope firms.

The AA recognises that climate change poses a number of transitional and physical risks and opportunities for business, people and our communities. We already have a well embedded process for modelling the impact of climate change and related weather events within our Roadside Operations, to ensure we have the right resources to meet our members' needs. Over the last 12 months we have identified further key climate related risks (such as adverse weather events and energy usage), we have been developing financial modelling of the most material to our future strategy and we're embedding the management of climate-related risks into our broader risk management framework. These key activities form part of our commitments under the Task Force for Climate related Financial Disclosure's (TCFD) recommendations, which will be reported in FY24.

The Group will apply International Financial Reporting Standard 17 (IFRS 17) with effect from 1 February 2023. IFRS 17 introduces a significant change to the accounting for insurance contracts. Our impact assessment is currently ongoing (please see note 35 of the FY23 AA Intermediate Co Limited Annual report and financial statements for more details).

We are preparing ourselves for our regulator's incoming cornerstone regulation, Consumer Duty. We have an extensive programme of work in place to review our existing frameworks, structures and processes to proactively look for opportunities to improve and enhance the outcomes we deliver to our customers.

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
Tom Mackay, Chief Financial Officer

Capital Expenditure

Capital Expenditure (excluding Maintenance Capital Expenditure) in the period to 31 January 2023 included growth capital expenditure of £37m related to our Roadside and Insurance business and £16m 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 13 July 2022, the Group completed a refinancing of its A6 Notes, issuing £250m of A10 Notes at a coupon of 7.38%.

On 6 February 2023 the Group issued £400m of Class A11 Notes at an interest rate of 8.45%. The proceeds of the issuance of the Class A11 Notes were used to redeem £308m of Class A7 Notes for a cash payment of £302m on 7 February 2023 tendered by existing note holders as part of a liability management exercise. The remaining surplus cash proceeds of £98m were transferred to a mandatory prepayment account to be held for redemption of Class A7 Notes. A further £10m of Class A7 Notes were purchased from existing bond holders on 3 March 2023 and redeemed and £103m of Class A7 Notes were voluntarily repaid on 16 May 2023 and redeemed.

On 6 February 2023 the Group renewed and increased its Liquidity Facility by £15m to a total of £175m which remains undrawn and on 10 February 2023 the Group increased its Senior Term Facility by £15m to a total of £165m. The additional £15m Senior Term Facility commitments were drawn on 24 March 2023.

Acquisitions or Disposals

There were no acquisitions or disposals in the year ended

Current Hedge Position

The Holdco Group has interest rate swaps in place which are used to fully hedge its interest rate exposure in relation to its drawn Authorised Credit Facilities. The Group has also currently hedged 100% of forecast diesel usage for the year ended 31 January 2024 and 31 January 2025.

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 29 June 2023, 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 2023 is more than 1.35; we set out the calculation below:

	Year to January 2023 £m
Operating profit before tax	66
Add back:	
Debt interest payable	123
Penalty interest payable	1
Interest payable under finance leases	1
Amortisation of debt issue costs	5
Discounts and fees in respect of financing	1
Exceptional items	37
Depreciation and amortisation	99
Difference between the pension service cost and employer cash contributions	5
Share-based payments	2
Less:	
Interest receivable	(2)
Finance income in respect of pensions	(3)
Class A Maintenance EBITDA	336
Less	
Cash tax paid	(9)
Change in working capital	6
Minimum capital maintenance spend	(35)
Class A Free cash flow	298
Class A total debt service charge	103
Class A FCF DSCR	2.9

- 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 2023 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-23 £m
Class A Debt:		
	Senior Term Facility	150
	Class A2 notes	500
	Class A7 notes	550
	Class A8 notes	325
	Class A9 notes	270
	Class A10 notes	250
Less:	Cash and Cash Equivalent Investments	(99)
Total Class A Net Debt		1,946
	Permitted Investor payment	(101)
Max Class A Net Debt		1,845
Class A Maintenance EBITDA		336
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 £50m, £50m 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 £278 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 2023:
    - 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
29 June 2023