European Structured Finance
Performance Analytics

Whole Business - UK

RoadChef Finance Limited

Ratings

Class	Original Amount (GBP million)	Final maturity	Rating
A1	35	2008	BBB+
A2	133	2023	BBB+
B	42	2026	BB

Previous Ratings

Class	Original Amount (GBP million)	Final maturity	Rating
A1	35	2008	A
A2	133	2023	A
B	42	2026	BBB

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■ Summary

This transaction involved the securitisation of motorway service areas ("MSAs") located in the United Kingdom. Fitch Ratings has downgraded the ratings of the notes as indicated on the left.

The transaction raised GBP210 million in November 1998. The RoadChef Group is the third largest operator of MSAs in the UK. Fitch Ratings analysed the likelihood of repayment on the Notes based on stressed revenues derived from fuel services, catering services, retailing (including petrol forecourt), accommodation income from hotel lodges and games and other services of the group (see: www.Fitchresearch.com, *RoadChef Finance Ltd*., 22 December 1998).

The Notes were placed on Rating Watch Negative in June 2001, as Fitch Ratings was concerned with the transaction meeting its financial covenant of 1.25x DSCR when amortisation began in October 2001. Fitch Ratings found that the MSA sector was suffering from lower spend per visitor, and lower turn-in rates, compared with original estimates (see www.Fitchresearch.com, *RoadChef Finance Ltd* press release 21 July 2001).

Given the possibility of a recession during the next few years, Fitch believes there is the potential for credit risk to develop and therefore an investment grade rating is no longer warranted for the Class B Notes.

Fitch Ratings has met with the management to discuss plans for the future. The latest performance report from RoadChef, for quarter ending 23 December 2001, shows a rolling 12

Structure summary

- Financial covenant: DSCR of 1.25x
- Dividend release: DSCR of 1.50x
- Issuer level Liquidity facility of GBP25 million
- Overdraft facility of GBP6 million, undrawn at end Dec 2001
- Ancilliary facility of GBP4 million, undrawn at end Dec 2001
- Class A1 amortisation commenced in Oct 2001. Class A2 starts Oct 2009, Class B starts Oct 2004
- DSCR definition: EBITDA to Debt Service. EBITDA is earnings pre tax; all interest; amortisation of intangibles, and financing or acquisition costs; depreciation; fair value adjustments; non-operating exceptionals; asset write ups or write downs; deferred income in respect of relevant fuel agreements. Debt Service is net interest (excluding interest accrued but unpaid on loans made by the obligors to RoadChef Motorway Holdings Ltd. and MSA Acquisitions Co. Ltd.) and principal payments.

22nd February 2002

month EBITDA of GBP20.5 million, and a debt service of GBP19.5 million. RoadChef placed GBP4 million in a cash reserve account in order to maintain its 1.25x financial covenant.

In October 2001, GBP25 million of proceeds from an issue of new share capital was injected into the RoadChef Group, of which GBP 23 million of cash was transferred to the Securitisation Group. This cash will be used to finance major capital expenditure (“capex”) on three of the sites in the security group, refurbishment of all retail outlets and free flow restaurants, and a roll out of the Costa Coffee franchise across the estate.

Credit Committee Highlights

- OFT investigation concluded, but additional competitive pressures could result.
- Below anticipated debt service coverage levels.
- Growth in EBITDA of 18.9% by December 2002 required to maintain “true” DSCR at 1.25x.
- EBITDA stable rather than rising.
- Fitch believes that a higher than expected capex spend is necessary to improve and maintain the condition of MSA estates.
- Cash reserve account funded at GBP4 million to maintain financial covenant.
- Equity support forthcoming.
- Cash available and committed for capex.
- Management change, greater focus on customer service.
- Transaction has started amortising Class A1 Notes.

MSA sector overview

The MSA sector has undergone a period of significant change in recent years, with public opinion and unfavourable press coverage forcing an OFT investigation, which was completed in December 2000.

The adverse publicity and consumer pressure had already forced the three major operators, Welcome Break, Moto (formerly Granada) and RoadChef, to embark on programmes designed to improve customer service, the MSA facilities and the offering. These programmes involved high levels of capital expenditure, and the condition of MSAs has improved as a result.

The investigation found no evidence of anti-competitive behaviour or excess profits being made by the MSA operators. However, it found consumer concerns over value-for-money justified. The OFT also stated that it would seek to work with the Highways Agency and the MSA operators to try to find ways to increase competition without jeopardising safety.

The OFT inquiry and adverse press coverage has focussed the attention of MSA operators on better service and value-for-money. This inevitably has led to the need for increased capital spend on the facilities themselves and on business efficiency, for example more sophisticated IT. Generating growth in EBITDA as a result of this capex appears to be less certain than in the past. To the extent that competition increases, this may affect the ability of MSAs to increase profitability in the future.

While MSAs have demonstrated relatively stable performance in the past, they are vulnerable to downturns in the economy. During a recession, traffic growth has historically slowed, but rarely turned negative. However, whilst traffic volumes may remain relatively unaffected, Fitch believes that the turn-in rate and spend per visitor are more susceptible.

	1999	2000	2001
EBITDA to end of December (GBP million)	21.0	21.5	20.5
Year on year growth	N/A	2.3%	-4.7%
Capital expenditure (GBP million)	4.6	5.3	3.6
Debt outstanding	210.0	210.0	207.1
Debt Service 12 months to December (GBP million)	16.5	16.6	19.5

Performance

The latest performance report for quarter ending 23 December 2001, shows a rolling 12 month EBITDA of GBP20.5 million, and a debt service of GBP19.5 million. This equates to a DSCR of 1.05x, however, the documentation allows the company to place cash on deposit in a cash reserve account, which, for the purpose of the financial covenant calculation, is treated as earnings. The company has placed GBP4 million in the cash reserve, and has therefore maintained its 1.25x financial covenant.

There has been a 4.7% decrease in 12 month rolling EBITDA between December 2000 and December 2001. This is partly due to an increase in overheads, a direct effect of management's strategy to increase customer service. Spending on staff training programmes has increased, as well as other costs associated with the changes in management discussed later. Maintenance and repair budgets have been brought forward to the first half of this financial year, to ensure that the estate is improved to a large degree for the busy third and fourth financial quarters (April – September).

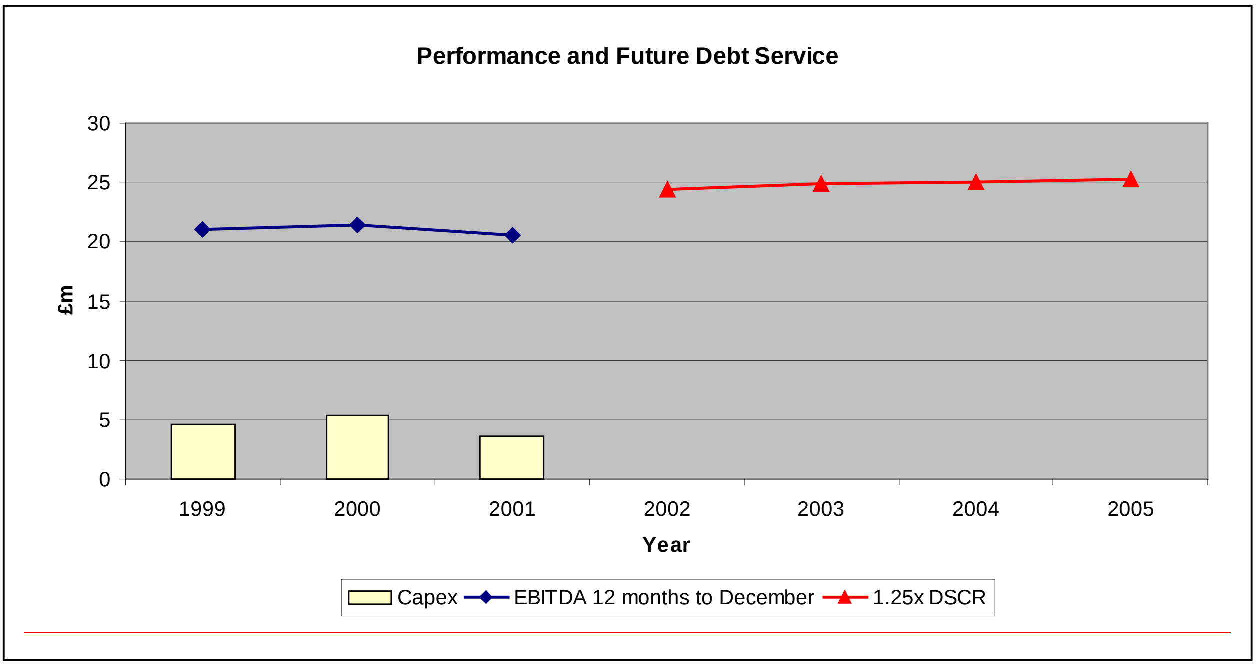
Headline sales are down 4.2% on the equivalent quarter last year, but this includes a reduction in fuel revenues due to price decreases. This is not a concern for RoadChef, as it receives a fixed amount per litre sold, regardless of the price. Fuel accounted for 66% of turnover and contributed 13% to gross profit. Sales in the higher margin areas, i.e. retail and restaurants are up 9.9% on the same period last year, with gross profit contribution up 5.9%.

The last two years have seen external market influences that have affected the MSAs either positively or adversely. The repercussions of the Hatfield rail crash in late 2000 increased car usage whilst the increase in fuel prices leading to the fuel crisis in 2000 and foot and mouth disease in 2001 reduced road traffic.

Fitch Ratings considers that the improvements being implemented at present will need to add significantly to profit to avoid the need for further equity injection, and the current levels therefore do not support our investment grade rating on the Class B notes any longer. RoadChef needs to increase EBITDA by 18.9% by December 2002 in order to achieve a "true" DSCR of 1.25x, i.e., without using the cash reserve to maintain the financial covenant. Historic performance reveals a stable EBITDA and profit, rather than an increase.

The chart below shows the stable performance for the 12 months to December for the last three years, and the uplift in EBITDA required to meet a 1.25x DSCR on the notes without posting cash on each payment date.

Management and shareholders have acknowledged the need to increase EBITDA quickly in order to avoid breaching covenants, hence the cash injection



to fund capex. However, the capex programme may cause disruption at the MSAs, which may lead to a short-term fall in profits as the programme is carried out.

RoadChef is currently cash positive, with a balance of around GBP20 million. The company is committed to spending around GBP15 million on three of its major service areas, and intends to spend more across the estate. If the required EBITDA uplift is not forthcoming, the company may have to draw down on overdraft facilities in order to make the covenant, which would create a super-senior liability, compounding the problem with the low actual DSCR but disguising this in published figures.

■ Capex

The upgrading of the RoadChef estate is necessary since the other competitor operators have already begun improving their property portfolios.

The three major capex projects are at Strensham South, Watford Gap and Rothersthorpe.

Strensham South is located on the M5 between Birmingham and Bristol. It is one of the busiest MSAs, but it is dated, and poorly designed. As a result, it under performs significantly compared with other large RoadChef MSAs. A new purposely-designed building is scheduled to open in June 2002.

Watford Gap, located on the M1 in Northamptonshire, is being redeveloped to include a Costa Coffee and increase the retail outlets on both sides of the motorway. The work is expected to be completed in May 2002.

Rothersthorpe is ten miles south of Watford Gap on the M1. RoadChef plans to increase parking and petrol facilities on both sides of the motorway, and extend the amenity buildings on both sides. The site will have Costa Coffee outlets, and upgraded retail outlets and free flow restaurants. Parking facilities will be upgraded also. This project is due to be completed in August 2002, although this may slip due to planning delays.

RoadChef intend to upgrade the retail shops and free flow restaurants on 17 sites across the estate. This upgrade is scheduled to be completed by May 2002. They intend to roll out more Costa Coffee shops, and continue the maintenance capex program.

All the sites are remaining open during the construction and upgrading programme, although there may be an effect on the EBITDA contribution caused by potential disruption to customers.

■ Management

RoadChef had a change of senior management in January 2001, with the appointment of John Greenwood, formerly CEO of the catering group Compass in the UK. Fitch Ratings view this as a positive factor, and have discussed RoadChef's strategy with senior management and the equity holder.

Management has initiatives to improve customer service at MSAs and increase operating efficiency and effectiveness. They have identified the need to improve the working environment for the staff if customer service is to improve. This change includes training and hiring programmes, and an effort to retain staff in this traditionally high staff-turnover sector.

The company has created a new role of Site Director, which replaces General Managers. The role has more responsibility, but is potentially better remunerated, with Site Directors benefiting financially from achieving performance targets. Under the Site Director is a new management structure, which management predict will result in fewer but better, focussed managers.

The long-term results of this new approach to the business may prove to be positive and indeed increase EBITDA significantly, however in the view of Fitch Ratings the immediate effect is shown in the higher overhead and lower EBITDA figure for the period ending December 2001. Fitch expects a further reduction in EBITDA during 2002, although the current capex programme may have a positive impact in the latter part of the year and into 2003. RoadChef believe they can deliver growth in EBITDA this year.

■ Conclusion

Fitch Ratings has analysed the performance of RoadChef and considered the operating environment of the MSA sector in the UK. Fitch Ratings broadly views RoadChef's capital expenditure programme, the demonstrated equity support and a change of management as positive moves for the company.

Nonetheless, the agency sees the low level of debt service coverage coupled with the uncertainty of the magnitude of uplift in EBITDA arising from the capital expenditure programme and the susceptibility of MSAs in an economic downturn as not compatible with the previous ratings of the Notes.

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Surveillance

Fitch Ratings will monitor the transaction on a regular basis and as warranted by events. Its structured finance surveillance team ensures that the assigned ratings remain, in the agency's view, an appropriate reflection of the issued notes' credit risk.

Details of the transaction's performance are available to subscribers at www.fitchresearch.com. Further information on this service is available at www.fitchratings.com.

Please call the analysts at Fitch Ratings listed on the first page of this report for any queries regarding the initial analysis or the ongoing surveillance.