S&P Global
Ratings

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Research Update:

U.K. Social Housing Association Richmond Housing Partnership Outlook Revised To Negative; 'A+' Ratings Affirmed

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Overview

- We expect that U.K.-based social housing association Richmond Housing Partnership Ltd. (RHP) will increase investment in its existing properties over the next three years.
- Together with inflationary pressure, this investment could put a greater strain on RHP's financial performance and debt metrics than we previously forecast.
- We therefore revised our outlook on RHP to negative from stable and affirmed our 'A+' long-term issuer credit rating on the group.
- The negative outlook reflects the risk that higher-than-anticipated costs, coupled with inflationary pressure, could weaken RHP's financial metrics beyond our current forecast.

Rating Action

On June 21, 2022, S&P Global Ratings revised its outlook on U.K.-based social housing provider Richmond Housing Partnership Ltd. (RHP) to negative from stable. At the same time, we affirmed our 'A+' long-term issuer credit rating on the group.

We also affirmed our 'A+' issue rating on the £275 million senior secured debt issued by RHP's funding vehicle, RHP Finance PLC.

Outlook

The negative outlook reflects the risk that higher-than-anticipated costs coupled with inflationary pressures could weaken RHP's financial metrics beyond our current forecast.

Downside scenario

We could lower the rating on RHP over the next two years if management deviates from its prudent financial policies, leading to financial metrics materially weaker than our current projections; for example, adjusted EBITDA margins remaining structurally below 20%. We also consider that this might weigh on the group's liquidity position. In addition, we could lower the rating if we thought the likelihood of timely extraordinary support from the U.K. government via RSH had decreased.

Upside scenario

We could revise the outlook back to stable if RHP improved its financial performance, such that adjusted EBITDA margins structurally exceeded 20%, while keeping debt metrics moderate.

Rationale

The outlook revision reflects our view that RHP's increased investment in existing stock, alongside general inflationary pressure, will entail higher costs than we previously expected. RHP is investing in its asset base to ensure that the properties meet fire and safety regulations. These costs will weigh on S&P Global Ratings-adjusted EBITDA margins in the next two to three years.

Under our updated projections, adjusted EBITDA margins will now structurally weaken to 21% of revenue on average over FY2023-FY2025 (financial year ending March 31), compared with 26% that we previously expected and the historical level of more than 30%. The main pressure comes from the group's investment in its existing assets, which is linked to fire safety works and additionally its target that all social housing properties should be at Energy Performance Certificate C levels by 2030. We acknowledge that investments in the group's asset base are expected to peak in FY2024, providing a gradual margin recovery thereafter. We also expect that inflation will drive up costs faster than income, and is unlikely to be fully compensated by the rent increase. This is because affordable rents in the social housing sector are increased with a lag, based on the September Consumer Price Index from the previous year.

Weaker adjusted EBITDA will also weigh on the group's debt level and interest coverage. We expect that debt to nonsales EBITDA will rise to an average of 23.5x over FY2022-FY2024, from 16.2x in FY2020-FY2022. In addition, we expect that RHP's nonsales interest coverage will weaken to an average of 1.4x during FY2023-FY2025 from 2.1x in FY2020-FY2022.

Despite the weakening financial metrics, we continue to assess RHP's management positively. The group is committed to its ambitious development plan and aims to complete 1,500 homes over the next 10 years, which would increase its existing stock by 14% should the plan be fully executed. RHP focuses on low-risk traditional housing activities, with sales exposure remaining below 10% of total revenue on average. In our view, RHP's management has strong expertise and demonstrates good adaptation capabilities, as shown by its recent revisions to the business plan that addressed multiple challenges, such as inflation and cost increases. Moreover, a large part of RHP's development program is uncommitted, which provides sufficient flexibility should further pressures arise. Besides this, RHP follows an extensive set of risk standards and internal golden rules.

RHP operates in West London (mainly Richmond), which is an area that has high demand for affordable housing units. The group's vacancy rates averaged 1.1% over the past three years, in line with the sector average. The strong demand is supported by RHP's average social and affordable rent, which is only about 45% of market rent in the areas where it operates.

We assess the regulatory framework under which registered providers of social housing in England operates as strong (for more information, see "Global Regulatory Framework Report Card

For Public And Nonprofit Social Housing Providers", published on June 8, 2021).

We believe that there is a moderately high likelihood that RHP would receive extraordinary support from the government via the Regulator for Social Housing (RSH) in case of financial distress. This provides one notch of uplift to the stand-alone credit profile. As one of the key goals of the RSH is to maintain lender confidence and low funding costs across the sector, we believe the RSH is likely to step in to try and prevent a default in the sector. The RSH has a record of mediating mergers or arranging liquidity support from other registered providers in cases of financial distress and we think this would apply to Richmond.

Liquidity

We assess RHP's liquidity position as extremely strong. We expect sources of liquidity to exceed planned uses by about 3.4x over the next 12 months. We also view RHP's access to external liquidity as satisfactory.

We expect sources of liquidity over the next 12 months will include:

- Cash flows from operations adding back noncash cost of sales of about £15 million;
- Current cash and liquid investments of just above £50 million;
- Fixed-asset sales receipts of about £2 million;
- Committed and undrawn facilities expiring beyond 12 months of about £150 million; and
- Grant receipt of about £10 million.

We expect uses of liquidity over the same period will include:

- Capital expenditure, including development spending on homes for sale, of about £60 million; and
- Interest and principal repayments of just under £10 million.

Richmond Housing Partnership--Key Statistics

	--Fiscal year ended March 31--				
(Mil. £)	**2021a**	**2022e**	**2023bc**	**2024bc**	**2025bc**
Number of units owned or managed	10,811	10,942	11,023	11,127	11,211
Adjusted operating revenue	63.9	62.4	65.5	76.6	69.5
Adjusted EBITDA	20.6	12.9	14.1	13.8	15.6
Nonsales adjusted EBITDA	20.1	12.0	13.3	11.0	15.6
Capital expense	17.2	23.9	57.5	56.7	42.5
Debt	273.3	273.2	273.0	310.0	340.0
Interest expense	7.1	8.1	8.9	9.4	10.4
Adjusted EBITDA/Adjusted operating revenue (%)	32.2	20.6	21.5	18.0	22.4
Debt/Nonsales adjusted EBITDA (x)	13.6	22.7	20.6	28.3	21.8
Nonsales adjusted EBITDA/interest coverage(x)	2.8	1.5	1.5	1.2	1.5

a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Richmond Housing Partnership--Ratings Score Snapshot

	Assessment
Enterprise risk profile	2
Industry risk	2
Regulatory framework	3
Market dependencies	2
Management and Governance	2
Financial risk profile	3
Financial performance	4
Debt profile	5
Liquidity	1

S&P Global Ratings bases its ratings on non-profit social housing providers on the seven main rating factors listed in the table above. S&P Global Ratings' "Methodology For Rating Public And Nonprofit Social Housing Providers," published on June 1, 2021, summarizes how the seven factors are combined to derive each social housing provider's stand-alone credit profile and issuer credit rating.

Environmental, social, and governance (ESG) credit factors for this change in credit rating/outlook:

- Health and safety

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, June 1, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Related Research

- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, April 22, 2022
- U.K. Social Housing Sector Borrowing Needs to Rise To Fund Investment In New Homes, March 31, 2022

- Social Housing Outlook 2022: Green Agenda Takes Root In Investment Plans, Nov. 23, 2021
- How U.K. Public Finance Sectors Fare Under Latest Spending Review, Nov. 11, 2021
- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers, June 8, 2021

Ratings List

Ratings Affirmed		
Richmond Housing Partnership		
Senior Secured	A+	
RHP Finance PLC		
Senior Secured	A+	
Ratings Affirmed; Outlook Action		
	To	**From**
Richmond Housing Partnership		
Issuer Credit Rating	A+/Negative/--	A+/Stable/--