S&P Global
Ratings

RatingsDirect®

Research Update:

U.K.-Based Social Housing Provider Bromford Housing Group 'A+' Rating Affirmed; Outlook Stable

January 23, 2020

PRIMARY CREDIT ANALYST

Celia Franch Lopez
London
+ 44 20 7176 0100
celia.franch_lopez@spglobal.com

SECONDARY CONTACT

Christopher Mathews
London
+ 44 20 7176 7115
christopher.mathews@spglobal.com

ADDITIONAL CONTACT

EMEA Sovereign and IPF
SovereignIPF@spglobal.com

Overview

- We expect Bromford Housing Group Ltd. (Bromford) to focus on delivering about 13,140 homes by 2028.
- Our view of Bromford's creditworthiness balances its very strong liquidity, exceptional asset quality, and strong debt sustainability metrics against its increasing exposure to development-for-sale activities.
- We are affirming our 'A+' long-term issuer credit rating on Bromford.
- The stable outlook reflects our view that Bromford will manage its exposure to outright and first-tranche shared ownership sales, such that they do not surpass more than one third of total revenues.

Rating Action

On Jan. 23, 2020, S&P Global Ratings affirmed its 'A+' long-term issuer credit rating on Bromford Housing Group Ltd. (Bromford). The outlook remains stable.

At the same time, we affirmed our 'A+' long-term issue rating on the £300 million senior secured bond issued by Bromford.

Rationale

The affirmation reflects our expectation that Bromford will continue to focus on the delivery of its "New Homes Plan", through which it aims to deliver 13,140 units by 2028. The group's very strong liquidity and its strategic partnership with Homes England support these development efforts.

The group has aligned its development plans with its geographic strategy in that it is targeting expansion within its existing core geographies in the Midlands and southwest of England, where most of its stock is located. We expect Bromford will rationalize its stock in areas of lower concentration.

Bromford benefits from strong demand for its properties, with voids of 0.9% and gross arrears of

3.7% as of the end of financial year 2019 (ending March 31, 2019; FY2019). This is modest compared to its local peers. However, economic conditions in its areas of operations are weaker than in other U.K. regions. According to data published by the Office for National Statistics, the average social housing rent in the Midlands and southwest is around 65% of the market rent, compared with 41% of market rent in London and 56% in the Southeast. All of Bromford's stock meets the Decent Homes Standard and the group has committed £260 million of capital and revenue maintenance over the next three years to maintain its strong asset quality.

Bromford has slightly re-profiled its development plan after receiving £66 million in grants from Homes England in FY2019. We now expect that the percentage of units developed that are allocated to outright sales will decrease from 15% to below 13%, while shared ownership will remain around 30%. We also expect the group to boost its development for social and affordable lettings tenures to 58% from 52%. Although sales account for a significant portion of the development plan, Bromford has a golden rule stipulating that it will derive no more than 30% of its total revenues from sales-related activities. We do not expect Bromford will breach this internal rule; we forecast sales revenue as a percentage of total revenue will peak at 25% in FY2022.

We expect in our base case that adjusted EBITDA margins will average 31% over the forecast period FY2020-FY2022, constrained by higher sales activities where margins are lower. Higher levels of capitalized repairs than historically and a higher proportion of revenues coming from development for sale activities will put pressure on profitability, however the CPI+1% rent settlement will boost margins compared to FY2019. The reported volatility also reflects that FY2019 was the first financial year in which Bromford operated as a fully consolidated entity, following the completion of mergers with Merlin Housing House Society and Severn Vale Housing Association.

We expect debt to increase under our base case. Bromford will draw on the £50 million private placement in FY2021, leading to debt peaking at £1.3 billion in FY2022 to enable the group's development efforts. An increase in debt, combined with an erosion in adjusted EBITDA, is likely to result in debt to EBITDA reaching 15.5x in FY2020, before receding to around 14x in FY2022. We expect a similar trend in its interest cover ratio--remaining sound at above 1.5x throughout the forecast period and strengthening to 1.8x in FY2022. We also expect Bromford will cover interest costs from social housing-generated EBITDA by 1.6x over our five-year base case.

Bromford's creditworthiness benefits from our view of a moderately high likelihood of extraordinary support from the U.K. government, through the Regulator of Social Housing, in the event of financial distress. The 'A+' rating on Bromford is therefore one notch higher than its stand-alone credit profile. Our view of a moderately high likelihood of extraordinary government support is based on Bromford's important role for the U.K. government and its public policy mandate. It is also based on the group's strong link with the U.K. government, demonstrated by the government's track record of providing credit support to the sector in certain circumstances.

Liquidity

We view Bromford's liquidity position as very strong on the back of a £300 million bond issuance completed in April 2018 and two private placements for £50 million and £100 million. Bromford inherited about £290 million of facilities from Merlin and subsequently restructured them into new revolving credit facilities, which continue to support the group's liquidity position.

Over the next 12 months, we estimate sources of liquidity will cover uses by 2.5x, supported by the group's liquidity policies and golden rules.

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

- £82 million from cash flow from operations;
- £261 million cash and liquid investments;
- £39 million from asset sales; and
- £340 million of committed undrawn facilities.

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

- £181 million of expected capital expenditure; and
- £113 million of interest and principal repayments.

Outlook

The stable outlook reflects our view that Bromford will contain its exposure to outright and first-tranche shared ownership sales, such that they do not surpass more than one third of total revenues.

Downside scenario

We could lower the rating on Bromford if its exposure to sales-related activities increases structurally above one third of total revenue. We could also lower the rating should we observe further volatility in liquidity and performance metrics, which could change our view on the group's financial policies.

The ratings on Bromford could also come under pressure over the next two years if there is renewed pressure on the sovereign credit ratings on the U.K. In addition, we could lower the rating on Bromford if we thought that the likelihood of timely extraordinary support from the U.K. government had decreased.

Upside scenario

Alternatively, we could raise the rating on Bromford if we saw a structural improvement in both its financial performance and debt profile. This would result from adjusted EBITDA margins strengthening structurally above 40% of revenue, with adjusted debt to EBITDA trending below 10x.

Key Statistics

Table 1

Bromford Housing Group Ltd. Key Statistics

	--Year ended March 31--				
(Mil. £)	**2018a**	**2019a**	**2020e**	**2021bc**	**2022bc**
Number of units owned or managed	37,914	42,268	43,208	44,427	45,619
Revenue§	215.8	251.9	254.4	261.5	303.4
Share of revenue from sales activities (%)	11.7	21.0	19.9	17.6	24.7

Table 1

Bromford Housing Group Ltd. Key Statistics (cont.)

	--Year ended March 31--				
(Mil. £)	2018a	2019a	2020e	2021bc	2022bc
EBITDA§†	74.5	75.3	77.5	82.3	95.2
EBITDA/revenue §†(%)	34.5	29.9	30.5	31.5	31.4
Capital expense†	125.9	167.2	127.5	195.0	218.2
Debt	777.5	1,186.6	1,196.6	1,180.0	1,329.2
Debt/EBITDA §†(x)	10.4	15.8	15.4	14.3	14.0
Interest expense*	31.8	42.1	51.2	51.1	53.9
EBITDA/interest coverage§†* (x)	2.3	1.8	1.5	1.6	1.8
Cash and liquid assets	106.5	232.1	175.6	59.8	81.9

§Adjusted for grant amortization. †Adjusted for capitalized repairs. *Including capitalized interest. a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N.A.--Not available.

Ratings Score Snapshot

Table 2

Bromford Housing Group Ltd.

Industry Risk	2
Economic fundamentals and market dependencies	4
Strategy and management	3
Asset quality and operational performance	1
Enterprise profile	3
Financial performance	4
Debt profile	3
Liquidity	2
Financial policies	2
Financial profile	3

S&P Global Ratings bases its ratings on non-profit social housing providers on the eight main rating factors listed in the table above. S&P Global Ratings' "Methodology For Rating Public And Nonprofit Social Housing Providers," published on Dec. 17, 2014, summarizes how the eight factors are combined to derive each social housing provider's stand-alone credit profile and issuer credit rating. For social housing providers generating more than a third of its consolidated revenues from open market sales, we also refer to the "Key Credit Factors For The Homebuilder And Real Estate Developer Industry."

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, Dec. 17, 2014

- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Global Social Housing Risk Indicators, Dec. 2, 2019
- Global Social Housing Rating Score Snapshot, Dec. 2, 2019
- Outlook 2020 On Social Housing Providers, Nov. 25, 2019
- Why Most Rated U.K. Social Housing Providers Are At Home In The 'A' Category, Dec. 3, 2019

Ratings List

Ratings Affirmed	
Bromford Housing Group Limited	
Issuer Credit Rating	A+/Stable/--
Senior Secured	A+