MOODY'S
PUBLIC SECTOR EUROPE

CREDIT OPINION
4 November 2020

Rate this Research

RATINGS

Bromford Housing Group Limited

Domicile	United Kingdom
Long Term Rating	A2
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Edward Demetry +44.20.7772.1720
Analyst
edward.demetry@moodys.com

Sebastien Hay +34.91.768.8222
Senior Vice President/Manager
sebastien.hay@moodys.com

Maylis Chapellier +44.20.7772.1429
Associate Analyst
maylis.chapellier@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

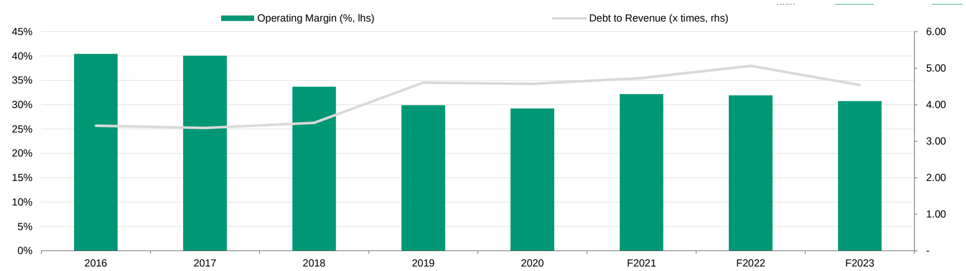
Bromford Housing Group Limited (UK)

Update to credit analysis

Summary

Bromford Housing Group's (Bromford A2 stable) credit profile reflects weakening debt metrics and interest coverage, balanced against stabilised operating margins, ample liquidity, a strong market position and a strong regulatory framework. It also incorporates our assumption of a strong likelihood that the government of the United Kingdom (UK, Aa3 stable) would intervene in the event of acute liquidity stress. We expect the coronavirus outbreak to cause ongoing operational disruption but limited credit impact.

Exhibit 1
Bromford's profitability has stabilised while debt to revenue continues to weaken



F: Forecast. Standalone pre-merger financials for FY2016-18; the merged entity's financials for FY2019-2020; the merged entity's board-approved business plan for FY2021-23.
Source: Bromford, Moody's Investors Service

Credit strengths

» Ample liquidity cover and additional borrowing capacity

» A strong market position and continued focus on core business in medium term

» Supportive institutional framework in England

Credit challenges

» Increased borrowing will weaken related metrics

» Ambitious development program, market sales exposure remains high beyond medium term adjustment

Rating outlook

Bromford's current stable outlook reflects an expectation that Bromford is well positioned in the A2 rating category in the medium term, based on our assessment of the current business plan.

Factors that could lead to an upgrade

A combination of the following could have positive rating implications: 1) operating margins returning to historic levels at or above 40%; 2) SHLIC is enhanced and maintained to 2x or above; 3) debt to revenue reducing to 3.5x.

Factors that could lead to a downgrade

Negative pressure could be exerted on the rating by one or a combination of the following: 1) SHLIC weakening materially to close to 1x; 2) growing debt above currently planned levels, with debt to revenue held at or above 5x; 3) weaker regulatory framework or a dilution of the overall level of support from the UK could also exert downward pressure on the rating.

Key indicators

Exhibit 2
Bromford Housing Group

Bromford Housing Group	31-Mar-16	31-Mar-17	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21 (F)	31-Mar-22 (F)
Units under management (no.)	29,110	29,510	38,266	43,146	43,977	44,311	44,893
Operating margin, before interest (%)	40.5	40.0	33.7	29.9	29.2	32.2	31.9
Net capital expenditure as % turnover	1.0	10.9	35.2	44.3	37.3	56.4	61.2
Social housing letting interest coverage (x times)	2.7	2.4	2.3	1.7	1.4	1.5	1.6
Cash flow volatility interest coverage (x times)	3.3	3.1	2.9	2.7	2.3	1.4	2.1
Debt to revenues (x times)	3.4	3.4	3.5	4.6	4.6	4.7	5.1
Debt to assets at cost (%)	35.3	35.2	37.7	45.3	45.9	46.0	47.3

F : Forecast. Standalone pre-merger financials for FY2016-18; the merged entity's financials for FY2019-2020; the merged entity's board-approved business plan for FY2021-23.
Source: Bromford, Moody's Investors Service

Detailed credit considerations

The credit profile of Bromford, as expressed in its A2 stable rating, combines (1) its current Baseline Credit Assessment (BCA) of a3, and (2) a strong likelihood of extraordinary support from the UK government in the event that Bromford faces acute liquidity stress.

Baseline credit assessment

Ample liquidity cover and additional borrowing capacity

Bromford's strong management practices and well-documented procedures have ensured that it has sufficient funding in place to match the funding need outlined in its business plan, which is reflected in its strong liquidity coverage. The housing association's (HA's) treasury policy continues to support ample liquidity, as it stipulates the need to keep on-hand cash covering three months rolling cash-flow (excluding uncommitted development and sales), facilities covering 18 months of expected committed and uncommitted spending, £25 million for contingency, and sufficient liquidity to cover a 20% slippage in forecast sales income. Additionally the HA's treasury policy also states that Bromford should maintain an additional £15 million buffer above its net mark-to-market position on callable stand-alone swaps, thereby providing sufficient mitigation against adverse movements in interest rates.

As a result, Bromford's liquidity cover metric remains a key credit strength in fiscal year 2020 (FY2020). At fiscal year end 2020, Bromford had sufficient available liquidity to cover 1.8x of its net two year spending requirements, and this metric is set to remain strong at 1.6x on average over the next three years. Bromford's liquidity cover is in line with A2-rated peers, despite the HA's higher level of forecast capital expenditure, which is forecast to reach 61% of turnover by FY2022.

Moreover, Bromford follows eight golden rules, one of which is to have a minimum of £100 million worth of unencumbered assets that are ready to charge to ensure further liquidity is available for the HA. Bromford enhanced its unencumbered asset position as a result of its FY2019 merger with Merlin Housing Society (Merlin) and Severn Vale Housing (SVH), growing the value of its unencumbered assets to approximately £530 million in FY2020, which would secure further borrowing of £479 million. Bromford intends to release excess security in FY2021 which should further enhance its unencumbered asset position in the near term.

A strong market position and continued focus on core business in medium term

Bromford is one of the largest HAs within the regions it operates, namely the Midlands and the West of England, with approximately 44,000 units under management in FY2020. We find that Bromford can benefit from its scale by enabling the HA to carry influence in negotiations with other key market players and provide input to local and national policy. Moreover, over 50% of Bromford's stock is located in four areas: Lichfield, Cotswold, Tewkesbury, and South Gloucestershire, further strengthening the HA's influence in these specific areas. Bromford will continue to rationalise its housing stock, through a programme of strategic asset disposal in areas where it has less presence, which deliver increased efficiencies in its stock management. Across FY2020 and FY2021, Bromford completed half of its disposal plan, which will result in a reduction of 1.8% of its stock and which will allow the HA to focus its operations to 40 local authorities, down from 51 in FY2019. The rationalisation plan will generate £16 million of gain on disposals in FY2021, with a further £28 million gains over the next 4 years.

Bromford will continue to focus on its core business of managing and delivering social and affordable housing. In line with this, Bromford exited its student accommodation business in FY2020, and the proportion of revenues core social housing letting is forecast to grow over the next two years, from 78% in FY2020 to 84% in FY2022 (FY2020 A2-rated peers median: 76%). From FY2023, social housing letting as a percentage of revenue is projected to decline to 68% as the HA plans to continue its sales programme, to cross-subsidise social housing provision. We note however that Bromford will reassess the its exposure to the cross-subsidy model, in line with the scale of grant funding it can secure.

Bromford's financial performance is expected to improve marginally to 32% in FY2021 from 29% in FY2020. While this operating margin is in line with the A2-rated peer median of 28% for the year, it remains significantly lower than Bromford's previous average of 40%, achieved between FY2015-2017. Bromford's profitability was hindered by the rent cut regime, implemented between FY2016 and FY2020, a growing cost base related to Bromford's expansion of its Neighbourhood Coaching programme (a tenants service programme which has supported rent collection and kept rental arrears low at 2% as at September 2020, but will increase in scope as Bromford's units under management grow), and its business-wide transformation programme consisting of IT and process enhancements.

Supportive institutional framework in England

The sector's credit quality will continue to benefit from the strong regulatory framework governing English HAs. The regulator maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and by undertaking biennial In-Depth Assessments (IDAs) for large and complex HAs. In response to the pandemic, the regulator adapted some aspects of its oversight temporarily, for example, extending its liquidity monitoring, briefly pausing the programme of IDAs and delaying regulatory submissions to reduce the operational burden on HAs. The regulator has a strong track record of intervention in cases of mismanagement or financial stress with powers to provide financial assistance and/or make manager appointments where there has been a breach of regulatory standards.

The operating environment for English HAs has improved under more supportive policies for social rent increases and capital grant. Following four years of social rent reductions, HAs now benefit from a return to inflation-linked rent increases from April 2020 for five years. In addition, the government has committed to increased capital grant on more flexible terms for new social housing.

Counterbalancing the improvements, we expect policy to drive increased borrowing and development risk in the sector as it responds to the government's objective to deliver a significant increase in the construction of new homes.

Increased borrowing will weaken related metrics

Bromford continues to increase its debt levels to deliver its New Homes plan, which will weaken its debt metrics and interest cover ratios over the medium term. Bromford's debt amounted to £1.2 billion in FY2020 or 4.6x revenues, following a bond issuance of £300 million in May 2018 and the amalgamation with Merlin and SVH. This compares unfavourably to the A2-rated peers median of 3.9x in FY2020. Bromford's debt level is expected to reach £1.5 billion in FY2023, or 4.5x revenues as the forecast growth in turnover is expected to offset the increase in debt.

Bromford's gearing, measured as debt to assets at cost, is set to increase marginally to 48% in FY2023 from 46% in FY2020, as the HA's asset wealth is forecast to grow in line with its debt accumulation. Bromford's gearing metric is in line the A2-rated peer median of 47% for FY2020.

Bromford's increased indebtedness will result in interest costs of £52 million in FY2021, from £47 million in FY2020, and interest costs are expected to grow in line with debt levels. The rise in financing costs will weaken the HA's interest cover ratios, with social housing letting interest coverage (SHLIC) at 1.4x and cash flow volatility interest cover (CVIC) at 2.3x in FY2020, from previously strong levels averaging 1.7x and 2.7x, respectively in FY2019. While SHLIC is expected to remain stable at 1.5x over the medium term, CVIC is expected to weaken further, dipping below 2.0x in FY2021 and FY2023, due to a forecast drop in cash flow from operations to £94 million in FY2021, from £125 million in FY2020, driven largely by a reduction in market sales income.

Bromford actively manages its risks related to its debt profile. In FY2020, it refinanced a £90 million legacy loan, which consequently generated £14 million of net present value savings, and substantially reduced the HA's refinancing risk, with 5% of drawn debt falling due in five years, down from 30% in FY2019. Bromford extended fixes on £110 million of drawn debt to reduce its exposure to variable rates. In FY2021, the HA sought deferred funding arrangements to secure low yields, with a £100 million deferred private placement, followed by a subsequent tap on its 2056 bond. Thanks to these deferred funding arrangements, Bromford has currently no funding requirement for the next two years. Bromford has also become a leader in ESG-linked lending as the first housing association to agree on an ESG-wrapped sustainability loan, linked to delivering on environmental objectives.

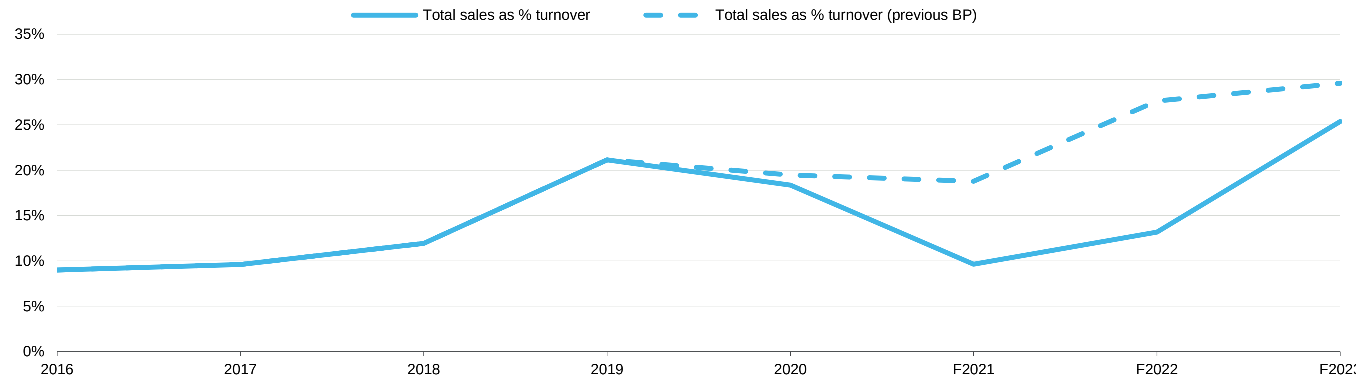
We consider interest rate risk to be low currently as a total of 3% of Bromford's drawn debt is subject to variable rates, and 100% of its swap portfolio (notional value of £86 million) is swapped to fixed rates. Bromford's management continue to take advantage of options to buy out of cancelable swaps, and maintain sufficient security to meet margin calls (£29 million security and £20 million unsecured thresholds charged against a negative mark-to-market position of £30 million as of 31st March 2020).

Ambitious development program, market sales exposure remains high beyond medium term adjustment

Bromford plans to deliver approximately an ambitious 7,000 units over the next five years, equating to 15% of its total stock, whereas the scale of planned development for other rated HAs tends to be around 10%. Of this five-year development plan, Bromford plans to deliver 1,400 affordable and intermediate homes by FY2024 in partnership with Homes England, through which it was able to secure £66 million in capital grant funding. The coronavirus outbreak has slowed capital spending for the HA in FY2020 and FY2021, but the group still expects to complete around 1,000 units in FY2021, compared to a pre-pandemic plan of 1,487 units.

Bromford's planned market sales exposure has reduced (Exhibit 3) compared to last year's business plan, with market sales income expected to generate 9% of turnover in FY2021. This largely reflects the HA's anticipation of a downturn in the UK housing market in the medium term. However, beyond FY2023, Bromford plans to grow market sales exposure to approximately 30% of turnover by FY2024. A high proportion of revenue from market sales introduces credit risk given the susceptibility related tenures have to market forces and the potential for volatility in cash flow.

Exhibit 3
Market sales exposure further lowered in updated business plan, but still remains high
Total sales as a proportion of turnover, previous and updated business plans



F: Forecast.
Source: Bromford, Moody's Investors Service

Extraordinary support considerations

The strong extraordinary support factored into the rating reflects the wide-ranging powers of redressal available to the regulator in the event of financial distress, with the possibility of a facilitated merger or a transfer of engagements. Recent history has shown that the UK government is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors in (1) the increasing exposure to non-core social housing activities in the sector, which adds complexity to HA operations, and (2) the weakening of the sovereign's financial resilience, making an extraordinary intervention slightly more difficult. In addition, our assessment that there is a very high default dependence between Bromford and the UK government reflects their strong financial and operational links.

ESG considerations

How environmental, social and governance risks inform our credit analysis of Bromford

Moody's takes account of the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of Bromford, the materiality of ESG to its credit profile is as follows:

Environmental considerations are not material to HAs' credit profiles. In line with the rest of the UK, the sector's main environmental risk exposures relate to water shortage and flood risk. Flood risk is managed by country and national authorities, and therefore the financial burden of adapting to increased flood risk will not fall on individual housing associations.

Social risks are material to HAs' credit profiles. In particular, the sector is exposed to risks stemming from socially-driven policy agendas affecting social rents, benefits and capital grants in addition to the impact of demographic trends on demand which are captured in our assessment of the operating environment. We view the coronavirus outbreak as a social risk under our ESG framework given its impact on health and safety. Overall, we expect the outbreak to cause ongoing operational disruption for HAs but do not expect a material credit impact as higher arrears and lower market sales receipts will be offset by cash savings from reduced capital spending on development and repairs. HAs are also impacted by customer relations and product quality. The Grenfell fire tragedy in June 2017 has encouraged higher health and safety standards with many HAs planning on increasing spending on the quality of their existing stock.

Governance considerations are also material to HAs' credit profiles and are captured in our assessment of governance and management. In general, housing association governance is strong with multi-year strategies supported by detailed forecasts, conservative liquidity policies, and robust risk management including stress testing.

Further details are provided in the "Baseline credit assessment" section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing ESG Risks.

Rating methodology and scorecard factors

The assigned BCA of a3 is aligned with the scorecard-suggested BCA.

The methodologies used in this rating are European Social Housing Providers, published April 2018 and Government Related Issuers, published in February 2020.

Exhibit 4
Bromford 2020 scorecard

Bromford Housing Group			
Baseline Credit Assessment	Sub-factor Weighting	Value	Score
Factor 1: Institutional Framework			
Operating Environment	10%	a	a
Regulatory Framework	10%	a	a
Factor 2: Market Position			
Units Under Management	10%	43,977	a
Factor 3: Financial Performance			
Operating Margin	5%	29.2%	a
Social Housing Letting Interest Coverage	10%	1.4x	baa
Cash-Flow Volatility Interest Coverage	10%	2.3x	a
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	4.6x	ba
Debt to Assets	10%	45.9%	ba
Liquidity Coverage	10%	1.8x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
Suggested BCA			**a3**

Source: Moody's Investors Service

Ratings

Exhibit 5

Category	Moody's Rating
BROMFORD HOUSING GROUP LIMITED	
Outlook	Stable
Issuer Rating -Dom Curr	A2

Source: Moody's Investors Service

REPORT NUMBER 1251482

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S
PUBLIC SECTOR EUROPE