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CREDIT OPINION
27 February 2019

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RATINGS

The Guinness Partnership Ltd.

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.

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The Guinness Partnership Ltd. (UK)

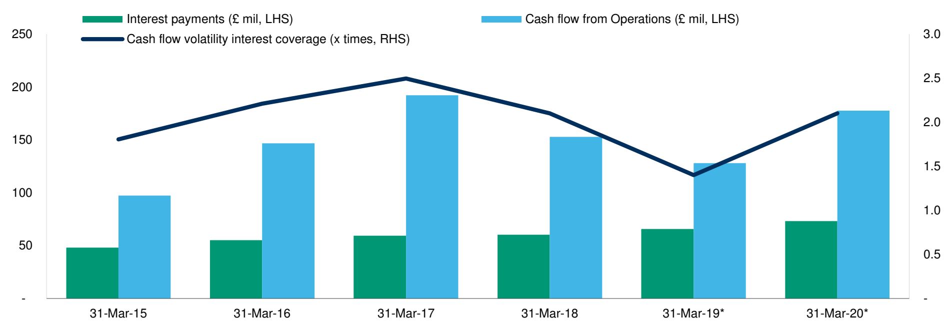
Update to credit analysis

Summary

The A2 issuer rating assigned to The Guinness Partnership (A2 stable) balances the housing association's robust social housing lettings interest cover, low debt burden, and adequate liquidity position, with risks stemming from a projected increase in market sales. Guinness' A2 rating also benefits from the strong regulatory framework governing English housing associations and our assessment that there is a strong likelihood that the UK government (Aa2 stable) would intervene in the event that Guinness faced acute liquidity stress.

Exhibit 1

Guinness' market sales strategy boosts cash flow, but renders it more volatile, weakening the cash flow volatility interest coverage metric



Source: Guinness Partnership and Moody's

Credit strengths

» Modest debt level and adequate liquidity

» Strong social housing letting interest coverage supported by improved operating margin

» Strong regulatory framework

Credit challenges

» Increasing exposure to market sales

» Operating environment remains challenging but policy is more stable

Rating outlook

The stable outlook on Guinness reflects the currently stable operating environment, which is unlikely to undergo further material change in the medium-term, and the stable outlook on the sovereign rating.

Factors that could lead to an upgrade

Positive pressure on the rating could result from strengthened Social Housing Letting Interest Cover (SHLIC) to a level structurally at or above 2.0x, operating margins which consistently exceed 30%, and/or reduced volatility in operating cash flow, supporting Cash Volatility Interest Cover (CVIC) remaining at or above 2.2x.

Factors that could lead to a downgrade

Given Guinness' increasing exposure to market sales, deteriorating house prices or falling demand resulting in underperformance would exert negative pressure on the rating. Negative pressure could also result from increased volatility in operating cash flow, leading to a weakening of the CVIC, SHLIC falling consistently below 1.5x, and/or liquidity coverage falling below 1.0x.

Key indicators

Exhibit 3

Guinness Partnership

	31-Mar-15	31-Mar-16	31-Mar-17	31-Mar-18	31-Mar-19*	31-Mar-20*
Units under management (no.)	60,216	60,671	65,363	65,538	64,631	65,291
Operating margin, before interest (%)	27.5	29.1	30.3	28.6	28.3	27.6
Net capital expenditure as % turnover	28.5	10.2	(11.7)	2.0	22.1	52.1
Social housing letting interest coverage (x times)	2.1	1.9	2.0	1.9	1.5	1.2
Cash flow volatility interest coverage (x times)	1.8	2.2	2.5	2.1	1.4	2.1
Debt to revenues (x times)	3.0	2.6	2.7	3.1	3.0	2.6
Debt to assets at cost (%)	37.8	37.5	36.6	35.8	34.5	38.8

*FY2019-FY2020 are forecasted figures
Source: Guinness Partnership, Moody's

Detailed credit considerations

Guinness' A2 rating combines (1) its baseline credit assessment (BCA) of a3 and (2) a strong likelihood of extraordinary support coming from the UK government in the event that the entity faces acute liquidity stress.

Baseline credit assessment

Modest debt level and adequate liquidity

As of the end of FY2018, Guinness' total debt stood at £1.15 billion, equivalent to 3.1x revenues, or 35.8% of assets-at-cost, one of the lowest debt burdens amongst Moody's rated housing associations. Despite modest growth in total debt over the last few years, Guinness' debt-to-revenues and debt-to-assets metrics remain a key credit strength, comparing favorably to the medians of A2 rated peers in FY2018, which stood at 3.7x and 40.5% for debt-to-revenues and debt-to-assets at cost, respectively. Refinancing risk is low, with around 84% of Guinness' outstanding debt maturing in five years or more. Likewise, interest rate risk is also relatively low, as 78% of Guinness' outstanding debt is fixed rate.

Over the next five years, Guinness plans to gradually take on approximately £600 million in additional debt which will push the debt-to-assets ratio to just under 40%. The debt-to-revenue ratio, however, will strengthen to 2.3x in the same time period, contingent upon the realization of a large outright sales programme. Planned borrowing is more than covered by currently available unencumbered assets of around £830 million.

Guinness' liquidity position remains adequate, supported by robust treasury policies which require available liquid funds to meet cash requirements for the next eighteen months. Furthermore, committed loan facilities must be in place for all contracted, approved, and pipeline commitments, in addition to a contingency of £25 million. As of September 2018, Guinness' immediately available liquidity consisted of £143.4 million in cash and £311.4 million of undrawn secured loan facilities, equating to a liquidity coverage of 1.3x.

Strong social housing letting interest coverage supported by stable interest costs

Although Guinness' Social Housing Letting Interest Cover (SHLIC) declined slightly in FY2018 at 1.9x from 2.0x in FY2017, this level of interest coverage remains strong, and well above the A2-peer median of 1.2x. The slight decline in the SHLIC was driven by a 5% drop in the social housing letting surplus, while Guinness' interest costs remained stable over the previous year at around £60 million. Social housing letting operating margin declined to 34%, from a very high 38% in FY2017, driven by higher management and planned maintenance costs. Overall, the housing association's operating margin dipped to 28.6% in FY2018, from 30% in FY2017, remaining below the 31% median of rated housing associations.

However, as the last years of the rent cut squeezes social housing letting margins and interest costs grow in line with the rising debt burden, Guinness' SHLIC will decline from its currently strong position, to an estimated 1.5x and 1.2x in FY2019 and FY2020, respectively. Looking further ahead, we expect interest costs to rise as Guinness takes on additional debt, and social housing letting revenues are not projected to keep pace, and the SHLIC will stabilize around 1.3x in FY2021 onwards.

Strong regulatory framework

The sector's credit quality will continue to benefit from the strong regulatory framework and oversight by the Regulator of Social Housing. The regulator maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and undertaking In-Depth Assessments of entities where deemed necessary. Additionally, the Regulator of Social Housing has powers to make board member and manager appointments where there has been a breach of Regulatory Standards. The regulator has charged fees for social housing regulation since October 2017 as a means of enhancing its independence and maintaining effectiveness.

Increasing development and market sales risk

Looking forward, Guinness' exposure to development risk will grow as the entity plans for net capex to rise from an average 12% of turnover over the last five years (FY2014-FY2018), to an average 25% of turnover in the next five years (FY2019-FY2023), with a peak at 52% in FY2020. Capital expenditure is driven by the housing association's intention to complete 10,000 units by FY2024, comprised of the aspirational "Guinness 2023" plan to deliver 7,500 units by FY2023, and the recently approved Homes England and GLA supported programme of an additional 2,500 units by FY2024. In total, grant funding secured will support 4,750 social units - the additional 2,500 units, as well as 2,250 units already included in the Guinness 2023 plan.

The development plan will include social rented units, shared ownership units and a material proportion of outright sales units. The units for outright sale would generate a subsidy for the social rented units, and have been front loaded into the currently identified development programme. Revenue from market sales, including the first tranche of shared ownership properties and outright sales, will comprise one third of Guinness' total revenue in FY2020, rising to and remaining around 45% of total revenue from FY2021-FY2023. The larger exposure to revenues from sales more closely links Guinness to the economic cycle, introducing additional risk to the housing association's credit profile.

Guinness' adequate liquidity coverage ratio - standing at 1.3x in FY2018 - somewhat mitigates the risk stemming from higher levels of capital expenditure. Guinness' performance on this metric, which measures forecast year-end liquidity against the following two years' net capex spend, is comfortable, and remains in line the A2 peer median of 1.3x. Looking forward, net capex will rise to 52% of turnover, but Guinness' liquidity coverage metric will remain stable at around 1.2x.

Operating environment remains challenging but policy is more stable

Moody's does not expect additional material adverse policy shifts for the sector and considers the operating environment to be stable in the medium term. Adverse policies announced in the last few years will continue to negatively impact revenues, especially the effects of the 1% annual decrease in social rents (until FY2020) and Universal Credit (a pillar of broader welfare reform measures). However, HAs have demonstrated resilience to adverse policies to date and been proactive to mitigate the impact. A reduction of capital grant for new social housing over the last five years has led to increased exposure to market sales activity, which has more than doubled since 2012 to reach 16% of turnover for Moody's rated HAs in FY2018. Credit risk association with exposure to market sales is incorporated in BCAs.

Extraordinary support considerations

The strong level of extraordinary support factored into the rating reflects the wide-ranging powers of redress available to the regulator in cases of financial distress, with the possibility of a facilitated merger or a transfer of engagements. Recent history has shown that the UK government (Aa2 stable) is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors increasing exposure to non-core social housing activities in the sector, that add complexity to HA operations, and the weakening of the sovereign's financial resilience, making an extraordinary intervention slightly more challenging. In addition, our assessment that there is a very high default dependence between Guinness Partnership and the UK government reflects their strong financial and operational linkages.

Rating Methodology and Scorecard Factors

The assigned BCA of a3 is the same as the scorecard suggested BCA.

The methodologies used in this rating were European Social Housing Providers, published in April 2018 and Government Related Issuers, published in June 2018.

Exhibit 4

Guinness Partnership

Baseline Credit Assessment	Sub-factor Weighting	Value	Score
Scorecard			
Factor 1: Institutional Framework			
Operating Environment	10%	a	a
Regulatory Framework	10%	a	a
Factor 2: Market Position			
Units Under Management	10%	65,538	aa
Factor 3: Financial Performance			
Operating Margin	5%	28.6%	a
Social Housing Letting Interest Coverage	10%	1.9x	a
Cash-Flow Volatility Interest Coverage	10%	2.1x	a
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.1x	baa
Debt to Assets	10%	35.8%	baa
Liquidity Coverage	10%	1.3x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
Suggested BCA			**a3**

Source: Guinness Partnership, Moody's

Ratings

Exhibit 5

Category	Moody's Rating
THE GUINNESS PARTNERSHIP LTD.	
Outlook	Stable
Issuer Rating -Dom Curr	A2
Senior Secured -Dom Curr	A2

Source: Moody's Investors Service

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