

Research Update:

U.K. Social Housing Provider The Guinness Partnership 'A-' Rating Affirmed; Outlook Stable

January 25, 2022

Overview

- We forecast that solid earnings from The Guinness Partnership's (Guinness) steadily growing asset base will mitigate the impact from higher spend on its existing homes, such that the group's S&P Global Ratings-adjusted EBITDA will exceed a modest 20% of adjusted revenue over the next two years.
- We consider that Guinness is likely to fund part of its capital expenditure (capex) program with the proceeds from asset sales and grant funding. In combination with a lower cost of debt, this would gradually strengthen the group's debt service metrics, in line with our previous assumptions.
- We affirmed our 'A-' long-term issuer credit rating on Guinness.
- The outlook is stable.

Rating Action

On Jan. 25, 2022, S&P Global Ratings affirmed its long-term issuer credit rating on The Guinness Partnership at 'A-'. The outlook is stable.

We also affirmed our 'A-' long-term issue rating on Guinness' senior secured debt of £400 million due 2055, £250 million due 2044, and £100 million due 2037.

Outlook

The stable outlook reflects our view that Guinness' adjusted EBITDA margins will exceed 20%, along with gradual strengthening of its adjusted EBITDA interest coverage, through our forecast period to the financial year ending March 31, 2024 (FY2024). We also consider that contained sales risk exposure and strong operational performance metrics mitigate the weaknesses on the financial side.

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Downside scenario

We could lower the rating if the group's costs increased above our expectations, such that financial performance came under pressure, which could also result in weaker debt service metrics and a deterioration of its liquidity position.

We could also lower the rating if we thought the likelihood of timely extraordinary support from the U.K. government to Guinness had decreased.

Upside scenario

We could consider an upgrade if Guinness' profitability improved on a sustained basis, supported by contained exposure to sales risk, resulting in a material strengthening of the group's debt service metrics.

Rationale

The affirmation reflects our view that Guinness benefits from generating most of its earnings in the predictable and countercyclical social-housing sector, supported by a solid market position together with a cautious approach to sales risk. We also consider that Guinness' steadily increasing revenue from its core rental business will mitigate the impact on the group's adjusted EBITDA from higher spend on its existing homes. We understand Guinness will fund part of its capex program with existing asset sales proceeds and grants, thereby containing an increase in debt, and we forecast that the group's interest coverage ratios will gradually strengthen through our forecast period to FY2024.

Like other English housing associations, we think there is a moderately high likelihood that Guinness would receive extraordinary support from the U.K. government in case of financial distress. This provides a one-notch uplift to the rating from the stand-alone credit profile. Guinness' primary purpose is to provide affordable homes, supporting important policy objectives of the U.K. government. We consider that the Regulator of Social Housing (RSH), a government agency, regulates Guinness to promote a viable, efficient, and well-governed social housing sector, and maintain lender confidence and low funding costs across the sector. It is therefore our view that the RSH would step in to prevent a default in the sector, based on its record of being willing and able to provide extraordinary support on a timely basis.

We assess the regulatory framework under which registered providers of social housing in England operate as strong, underpinned by their public policy mandate to provide affordable homes. We also consider that the sector benefits from solid ongoing oversight by the RSH. Offsetting these strengths, we consider that providers in England receive relatively low levels of grant funding for the development of affordable homes. We note that providers in England can develop homes for outright sale, using the proceeds as an alternative funding source; however, we think this exposes them to risks and potential volatility compared with providers in other regions. Providers in England are also subjected to negative intervention from the U.K. government in the form of rent-setting constraints or additional spending responsibilities, without adequate additional funding. This weighs on our view of the regulatory framework assessment.

Guinness owns and manages about 66,000 homes across England and continues to see strong demand for its properties, demonstrated by solid operational metrics. The group's average social and affordable rents are about 65% of the average market rent in England, and vacancy rates have been significantly lower than the sector at 0.7% on average over the past three years. That said,

we note that vacancy rates have increased this year, mainly due to pandemic-related issues. We also note positively that Guinness has been working to bring all its homes up to the Energy Performance Certificate (EPC) C level by 2030, with about 80% of its stock already at EPC C or above.

We assess the group's management and governance as solid and in line with peers in the sector, reflecting realistic and detailed strategic plans underpinned by adherence to risk management and financial policies. We understand Guinness has scaled back its development of new homes compared with our previous assumptions and view positively that the group has the flexibility to adjust its development program to reflect market conditions. At the same time, we note that the group is gradually increasing its exposure to sales risk, mainly through the development of shared ownership units. We forecast that revenue from homes sold on the open market, including the first tranche of shared ownership units, will reach 20% of adjusted revenue in FY2024 compared with less than 5% in FY2021.

We forecast increasing revenue stemming from a steadily increasing number of general needs units benefiting from the consumer price index +1% rent settlement applicable for five years from April 1, 2020. At the same time, we consider that Guinness will increase spend on existing homes to meet targets on energy efficiency, fire safety, and enhanced building standards. However, we anticipate that increasing earnings from Guinness' core rental business will mitigate the impact on the group's adjusted EBITDA margins, which we forecast will exceed a modest 20% through our forecast period to FY2024.

We understand Guinness will fund part of its capex program with the proceeds from asset sales and grant funding over the next two years, thereby containing a build-up of debt. We also factor in the group's lower interest costs following the repayment of a relatively expensive £110 million bond in March 2021. Although we forecast that the group's adjusted debt to non-sales EBITDA will remain just above 20x through FY2024, we expect the adjusted EBITDA interest coverage to gradually strengthen to 1.3x, from just below 1.2x forecasted for FY2022.

Liquidity

Guinness' liquidity position remains very strong, supported by our estimate that the group's sources of liquidity will cover its uses by 2.3x over the next 12 months. We view Guinness' access to the debt capital markets as satisfactory.

Sources of liquidity include:

- Cash and liquid investments exceeding £60 million;
- Cash flow from operations, adding back the non-cash cost of sales of close to £150 million;
- Undrawn committed credit facilities expiring beyond 12 months of £865 million; and
- Proceeds from fixed asset sales of close to £100 million.

Uses of liquidity include:

- Capex including spend on homes for sales of about £425 million; and
- Interest payment and debt maturities of about £95 million.

Key Statistics

Table 1

The Guinness Partnership--Key Statistics

Mil. £	--Year ended March 31--				
	2020a	2021a	2022e	2023bc	2024bc
Number of units owned or managed	64,039	64,236	64,767	65,785	66,997
Adjusted operating revenue	344.4	354.2	382.6	444.7	473.9
Adjusted EBITDA	64.7	88.4	75.9	90.5	100.8
Non-sales adjusted EBITDA	61.7	87.1	72.4	82.7	91.9
Capital expense	139.4	82.9	282.0	469.9	332.3
Debt	1,302.1	1,389.5	1,486.4	1,740.3	1,868.6
Interest expense	62.2	70.2	60.6	65.4	70.8
Adjusted EBITDA/Adjusted operating revenue (%)	18.8	25.0	19.8	20.4	21.3
Debt/Non-sales adjusted EBITDA (x)	21.1	16.0	20.5	21.0	20.3
Non-sales adjusted EBITDA/interest coverage(x)	1.0	1.2	1.2	1.3	1.3

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

Ratings Score Snapshot

Table 2

The Guinness Partnership--Ratings Score Snapshot

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

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.

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: 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

- 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
- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, Oct. 22, 2021
- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers, June 8, 2021
- Building Up Debt: U.K. Social Housing Sector Braces Itself For Borrowing, March 16, 2021

Ratings List

Ratings Affirmed

Guinness Partnership (The)

Issuer Credit Rating A-/Stable/--

Guinness Partnership (The)

Senior Secured A-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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