S&P Global
Ratings

RatingsDirect®

Notting Hill Genesis

Primary Credit Analyst:
Christopher Mathews, London + 44 20 7176 7115; christopher.mathews@spglobal.com

Secondary Contact:
Karin Erlander, London + 44 20 7176 3584; karin.erlander@spglobal.com

Research Contributor:
Mahek Bhojani, Mumbai; mahek.bhojani@spglobal.com

Table Of Contents

Notting Hill Genesis

Key Rating Factors

Issuer Credit Rating
A-/Stable/--

Enterprise profile

A large asset base puts Notting Hill Genesis (NHG) in a strong position to weather unexpected external shocks.

- Despite its large exposure to sales, we expect most of NHG's revenues to stem from social housing lettings, which is a low-risk industry.
- NHG's social rents are below 50% of market rents in London, which supports strong demand for its socially rented stock.
- Arrears have been increasing, a trend that could accelerate due to the pandemic. Voids were stable at 1.4% in the financial years (FY) ending March 31, 2019 and 2020.

Financial profile

NHG's nonsales EBITDA interest coverage remains weak, highlighting a reliance on its sales business for strong interest coverage at a group level.

- S&P Global Ratings-adjusted EBITDA margins will trend toward 30% as NHG executes its planned additions to its rental stock.
- That said, NHG's sales exposure--in particular, its stock of unsold homes--casts uncertainty on its operating performance.
- NHG retains a very strong liquidity position, which is supported by about £835 million of committed, undrawn facilities and a strong access to the capital markets.

Outlook

The stable outlook indicates that we expect NHG to manage the sale of unsold and new homes in a risk-appropriate manner, such that volatility from these sales does not impede improved financial performance.

Downside scenario

We could lower the ratings on NHG if its sales operations, particularly its handling of unsold stock, began to materially weaken its financial profile. Delays in sales of either unsold or new stock would subdue EBITDA growth, which could weigh on its debt servicing metrics.

We could also lower the rating should NHG not recover in line with our forecasts for the period after the pandemic, or if the consequences of Brexit weigh on NHG's operations--in particular its sales.

Furthermore, if we considered NHG had become less likely to receive extraordinary government support through the Regulator of Social Housing (RSH), we could also lower the rating.

Upside scenario

We could raise the ratings if we observed an improvement in financial performance, combined with contained exposure to sales activity. Under such a scenario, we would expect NHG to consistent display adjusted EBITDA margins above 30%, as performance at its traditional lettings business strengthened. This would help to significantly improve its EBITDA interest coverage and maintain its debt-to-adjusted EBITDA ratio well below 20x.

Rationale

NHG has navigated the COVID-19 pandemic well, supported largely by central government's response, including the Job Retention Scheme and the Covid Corporate Financing Facility (CCFF). The former has prevented large-scale unemployment and a subsequent spike in arrears for registered social landlords (RSLs) while the latter has helped support liquidity. As a result, RSLs such as NHG have remained fairly stable throughout FY2021.

Despite house prices remaining buoyant throughout 2020, lockdowns have obstructed the ability to sell homes. As of December 2020, NHG had a large stock of about 660 unsold homes. Our base-case assumes these will be sold in the years to FY2023, which would support an improvement in NHG's debt profile metrics.

NHG has taken steps to retain a very strong liquidity position during these uncertain times, demonstrated by its continued access to capital markets. NHG also utilized the CCFF. We do not include the short-term CCFF financing in our liquidity assessment.

As for other registered English social housing associations, we see a moderately high likelihood that NHG would receive extraordinary support in case of financial distress. This provides a one-notch uplift from the 'bbb+' stand-alone credit profile (SACP). NHG's primary purpose is to provide affordable homes, supporting important policy objectives of the U.K. government. The RSH, a government agency, regulates NHG to promote a viable, efficient, and well-governed social housing sector, and maintain lender confidence and low funding costs across the sector. In our view, the RSH would step in to prevent a default in the sector. It has a record of being willing and able to provide extraordinary support on a timely basis.

NHG's sales exposure remains high compared with peers, and we expect sales proceeds to account for around 27% on average for FY2021-FY2023. That said, NHG generates most of its revenue from its core social housing activities. Therefore, we consider that our rating on NHG benefits from the characteristics of this low-risk industry; namely, its anticyclicality and its high barriers to entry.

A strong presence in London supports demand for its operations, because, on average, NHG's social rents are below 50% of the market rents in the capital.

NHG's large asset base of around 65,000 units boosts its ability to withstand external shocks. As a result, its metrics have remained stable despite the current high number of unsold homes. The quality of its assets is high and voids remain flat at 1.4%, marginally higher than our rated average of 1.2%.

In October 2020, one of NHG's student accommodation and leasehold buildings needed evacuating after it was found to be unsafe with respect to fire safety regulations. Our base-case scenario includes the remedial costs required to retrospectively resolve this issue; we understand that capital expenditure will be required. Our base case assumes that NHG's student accommodation operations will generate no further revenue for some time. In our view, this will not alter NHG operations materially.

We expect NHG to expand its already large asset base, bolstering its adjusted EBITDA margins. We forecast that NHG will complete around 1,700 rented homes by FY2023, of which just over 60% will be for general needs. NHG's general needs and market rent operations return margins of about 25% and 50%, respectively. We therefore expect new completions to help margins improve to around 30% by FY2023.

NHG will largely debt-fund its development aspirations, but its planned private market and shared ownership sales should prevent a structural deterioration in its debt profile metrics. We forecast that NHG's debt will increase to £3.7 billion by FY2023 and that successful sales execution will cause debt to EBITDA to fall to about 17x in FY2023, from 20x in FY2021.

We assume new financing will be contracted at much more favorable rates that NHG's current cost of debt, helping to ease EBITDA interest cover. NHG contracted £250 million at 1.2% on a seven-year bond, the proceeds of which were used to repay revolving credit facilities. NHG's average cost of debt is 4.2% and we expect future debt issuances to be cheaper, given the U.K.'s low interest rates. We therefore forecast that EBITDA interest cover will rise to 1.5x by FY2023 from 1.2x in FY2021. EBITDA generated from lettings alone is likely to improve to 1.4x in FY2023 from 1.3x in FY2020. NHG's nonsales EBITDA coverage is supported by its general needs business and by its profitable market rent segment.

Liquidity

We regard NHG's liquidity position as very strong because of its large undrawn committed facilities and regular issuances in the debt capital markets. In our base case, we estimate sources of funds will cover uses by about 1.9x over the next 12 months.

Sources of liquidity will include:

- Adjusted EBITDA as a cash flow proxy (net of cost of sales relating to unsold homes) of close to £455 million;
- Cash and cash equivalents of £37 million;
- Proceeds from asset sales of around £47 million; and
- Available funds under undrawn committed facilities of close to £836 million.

Uses of liquidity will include:

- Capital expenditure of about £400 million;
- Interest and principal repayments of close to £290 million; and
- Grant repayment of around £19 million.

We view NHG's access to external liquidity as strong. Notting Hill Housing and Genesis Housing, which merged in 2018 to form NHG, demonstrated their ability to issue several bonds separately over the past few years. NHG itself issued its first £250 million 10-year maturity bond in January 2019.

Key Statistics

Table 1

Notting Hill Genesis Key Statistics					
	--Year ended March 31--				
(Mil. £)	**2019a**	**2020a**	**2021e**	**2022bc**	**2023bc**
Number of units owned or managed	63,475	64,847	65,630	66,040	66,563
Revenue§	659.4	721.2	759.3	841.6	740.8
Share of revenue from sales activities (%)	20.1	24.8	30.6	31.9	20.2
EBITDA§†	164.4	196.8	177.3	212.4	217.5
EBITDA/revenue §†(%)	24.9	27.3	23.4	25.2	29.4
Capital expense†	356.5	297.1	344.6	411.8	454.0
Debt	3,471.0	3,486.2	3,519.6	3,567.9	3,773.3
Debt/EBITDA §†(x)	21.1	17.7	19.8	16.8	17.3
Interest expense*	140.5	146.9	144.2	141.8	145.0
EBITDA/interest coverage§†* (x)	1.2	1.3	1.2	1.5	1.5
Cash and liquid assets	150.6	136.4	107.7	100.0	100.0

§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

Notting Hill Genesis Ratings Score Snapshot	
Industry Risk	2
Economic fundamentals and market dependencies	2
Strategy and management	3
Asset quality and operational performance	1
Enterprise profile	3
Financial performance	5
Debt profile	3
Liquidity	2
Financial policies	3
Financial profile	4

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: Group Rating Methodology, July 1, 2019
- 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, April 24, 2020
- U.K. Social Housing Providers Should Remain Largely Resilient To Short-Term Economic Difficulties From COVID-19, April 23, 2020
- COVID-19: Emerging Market Local Governments And Non-Profit Public-Sector Entities Face Rising Financial Strains, April 6, 2020
- U.K. Social Housing Ratings History: February 2020, March 3, 2020

Ratings Detail (As Of February 10, 2021)*	
Notting Hill Genesis	
Issuer Credit Rating	A-/Stable/--
Senior Secured	A-
Issuer Credit Ratings History	
05-Jun-2019	A-/Stable/--
27-Jul-2018	A/Negative/--
03-Apr-2018	A+/Negative/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.