FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Notting Hill Genesis at 'A'; Outlook Stable

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Fitch Ratings - London - 02 Nov 2021: Fitch Ratings has affirmed Notting Hill Genesis' (NHG) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) at 'A'. The Outlooks are Stable.

The ratings reflect continuing high demand for social housing (SH) in London and the south-east of England, NHGs' primary area of operation, and continuing cash flow from rented properties. They also factor in NHG's secured cash flow from public funds and the control and regulation provided through the Regulator of Social Housing (RSH). NHG's Standalone Credit Profile (SCP) is assessed at 'a-'.

KEY RATING DRIVERS

Status, Ownership and Control: 'Strong'

NHG is a private, not-for-profit, registered provider (RP) of SH in the UK, and as such it is not under the ownership of the UK government, due to its structure and status (in strict terms it has no legal owner). We view the regulatory framework for English SH as having a robust legal basis, and the RSH as maintaining sound control and tight monitoring of RPs. The regulator's history of oversight and (non-financial) intervention in (rare) cases of distress is a key factor behind the sector's solidity. In the event of financial distress, we expect a transfer of assets and liabilities to another RP within the sector under the direction of the RSH.

Support Track Record: 'Moderate'

NHG receives financial support through grants from Homes England (HE) and the Greater London Authority (GLA) at varying levels for social and affordable development. This is on an ongoing basis to support development, not to finance debt or prevent default. The regulator assesses governance and financial stability every 18-36 months, dependent on an RP's size, to assess need for intervention, and NHG's current regulatory judgement is G1/V2.

Socio-Political Implications of Default: 'Moderate'

In the unlikely event of financial default, other RPs can act as substitutes with only minor or temporary disruption to the service offered by NHG.

Financial Implications of Default: 'Weak'

Default would have a minimal impact on either the availability or cost of domestic financing of other RPs. Fitch believes that a default would be treated as an isolated case of mismanagement or viability issues and should therefore not affect the sector at large.

The following rating factors are reflected in NHG's 'a' SCP:

Revenue Defensibility: 'Stronger'

Fitch assesses revenue defensibility, which covers demand and pricing, as 'Stronger' overall. Demand for social housing remains strong and changes to rents are unlikely to materially affect demand. The supportive regulatory regime aims to maintain compensation for essential public services at sufficient levels to cover operating expenditure and debt servicing. RPs have limited revenue flexibility, as the UK government determines SH rent rises for core assets. Core social rents are currently able to increase CPI +1% per annum.

Operating Risk: 'Stronger'

Operating risk, which covers operating costs and resource management, is assessed as 'Stronger' overall. NHG has well-identified cost drivers and low potential volatility in major items. It has material capex in its development plans in the medium term but has flexibility to scale back committed schemes, defer uncommitted schemes and to rent out housing units if not sold, all of which to some extent have been utilised. Additionally, in the event of financial stress, NHG can cut back discretionary expenditure or non-essential major works.

NHG continues to face material fire-safety works costs, expected to be more than GBP100 million over the next five years. We also expect significant spending to meet environmental sustainability requirements in the medium- and long-term for NHG, which is factored into its long-term financial forecasts.

RPs in the UK have fared well throughout the pandemic as they had begun preparations ahead of uncertainty around Brexit, including putting additional liquidity facilities in place and reviewing supply lines. Brexit is having an impact on the availability and costs of resources and labour.

Financial Profile: 'Stronger'

NHG has demonstrated sound financial performance despite the challenges that have affected the sector over recent years. Continued high demand for social and affordable housing, cost-efficiency measures and increasing diversification into non-core business should allow NHG to maintain sufficient revenue to service debt and cross-subsidise its core business.

We expect NHG's sound financial performance to continue, as profits from the disposal of private-sale units will be re-invested to continue to build and provide affordable social units. The share of non-SH activity is expected to reduce but still remain a key feature of NHG. In the medium term, on average, 75% of the turnover will continue to be from SH-related activities (lettings and sales). NHG's board and management follow a prudent approach to risk and debt. Debt will continue to increase to fund capex as outlined under NHG's development plan.

NHG developed more than 1,342 units in FY21 (FY20: 1,960) and in its investment plan it aims to develop around 5,500 units over the next five years, split between 31% low-cost rental, 39% shared-ownership, 10% private rent and 20% private sale.

In its rating case, Fitch expects NHG's debt to increase to about GBP4.3 billion by FYE26, following investments (FYE21: GBP3.4 billion). NHG's net debt/ EBITDA is expected to remain at around 12x throughout the rating case (FYE21: 12.2x), despite lower revenue from sales and increased spending on fire-safety improvements in existing stock.

DERIVATION SUMMARY

The 'a-' SCP is driven by our assessment of 'Stronger' revenue defensibility, operating risk and financial profile and a comparison with peers in the sector.

Fitch views NHG as a government-related entity (GRE) in the UK, with a support score of 12.5 based on our above-mentioned assessments. This results in a bottom-up approach, with a one-notch uplift to the SCP to arrive at the Long-Term 'A' IDR, reflecting modest links with the government.

NHG's Short-Term 'F1+'IDR is the higher of two options mapping to a Long-Term 'A' IDR, reflecting the combination of a 'Stronger' revenue defensibility and a strong liquidity cushion and coverage ratio.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-Improvement of net adjusted debt/EBIDTA to below 10x on a sustained basis.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-Deterioration of net adjusted debt/ EBITDA to above 12x on a sustained basis, or an adverse change to our assessment of key rating factors.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

NHG has significant cash and un-drawn facility balances available of around GBP1 billion. It also has a substantial number of unencumbered assets should a need for financing arise, and its development and acquisition programme are expected to deliver an additional 5,500 units over the next five years that could be securitised. This is more than sufficient to cover the RP's forecast borrowing requirements. NHG issued a GBP250 million sustainable bond in FY22 rated by Fitch, providing funding capacity.

NHG's debt is similar to sector peers', spread across bonds, a revolving credit facility and term loans with limited near-term maturity.

ISSUER PROFILE

As of 1 April 2021, NHG owned or managed more than 66,500 housing units, ranking it among the largest RPs in England and a constituent member of the G15, the biggest RPs in London. NHG has strong growth aspirations and aims to provide as many affordable homes for residents as possible, with over 5,500 units planned for development or acquisition by 2026.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
GenFinance II PLC				
• senior secured	LT	A	Affirmed	A
Notting Hill Genesis	LT IDR	A Rating Outlook Stable	Affirmed	A Rating Outlook Stable
•	ST IDR	F1+	Affirmed	F1+

ENTITY/DEBT	RATING	PRIOR

VIEW ADDITIONAL RATING DETAILS

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PARTICIPATION STATUS

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APPLICABLE CRITERIA

Government-Related Entities Rating Criteria (pub. 30 Sep 2020)

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 01 Sep 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

GenFinance II PLC	UK Issued, EU Endorsed
Notting Hill Genesis	UK Issued, EU Endorsed

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