S&P Global Ratings

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Research Update:

U.K.-Based Social Housing Association bpha Ltd. Outlook Revised To Stable; 'A+' Rating Affirmed

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Overview

- bpha Ltd. (bpha) continues to focus its operations on affordable tenures in areas of high housing demand, on the back of a solid track record of managing a changing operating environment and risks associated with its investment needs.
- We expect revenue generated from new units delivered will support a gradual recovery in EBITDA, such that debt build-up will remain contained despite increasing investments in existing stock, and liquidity will remain very strong.
- We revised our outlook on bpha to stable from negative and affirmed our 'A+' long-term issuer credit rating.

Rating Action

On Oct. 22, 2021, S&P Global Ratings revised its outlook on bpha to stable from negative. At the same time, we affirmed the 'A+' long-term issuer credit rating on bpha.

We also affirmed our 'A+' issue rating on the £350 million senior secured bonds issued by bpha Finance PLC. bpha Finance PLC was set up for the sole purpose of issuing bonds and lending the proceeds to the group, and as such we view it as a core subsidiary of bpha.

Outlook

The stable outlook reflects our view that the gradual recovery in bpha's EBITDA offsets the risks associated with the group's increasing investments in existing assets and new development.

Downside scenario

We could lower the rating on bpha if the group materially expanded its development ambitions and risk appetite, such that its revenue relied more heavily on sales activities. This would likely to put pressure on the group's margins and debt metrics, due to higher capital expenditure (capex) resulting in faster debt build up.

Upside scenario

We could raise the rating on bpha if its exposure to market-related risks subsided and the company improved its EBITDA materially above our current projections.

Rationale

The outlook revision reflects our expectation that management will be able to maintain stable financial metrics in line with our current forecast, despite a weakening operating environment and rising risks associated with its investment needs. We expect bpha to continue generating most of its income from stable low-income social housing rental activities, generating about 20% of revenue from sales activities. The group has experienced some delays in delivering its development program, which we expect to pick back up through our forecast period (until March 2024). We expect lower margins on sales activities, combined with increasing investment in existing stock, will lead to lower S&P Global Ratings-adjusted EBITDA margins.

The ratings on bpha are supported by its continued focus on traditional social housing lettings activities, its dynamic area of operations, and a well-established track record of consistent strategy and prudent management. The group operates across the East of England, with core operating areas in Oxfordshire, Bedfordshire, and Cambridgeshire. This region remains one of the most dynamic in the country in economic terms, supported by investment in infrastructure--such as the East-West rail extension--which promotes job creation. We estimate that the group's social to market rent ratio stands at about 60% on average, which supports strong demand for its properties. This is also reflected in low voids, accounting for close to 1% of rent and service charges over the past two years.

Management has a strong focus on asset quality and environmental policy, having designated sustainability as one of the five key principles in its corporate strategy. The group's policies go beyond the government's Decent Homes Standards and look at carbon footprint, energy efficiency for tenants, construction best practices, and value for money. An integral part of bpha's asset strategy is its tower block project: It expects to refurbish 14 tower blocks over the next 10 years to meet higher environmental standards. The increased capital investment in existing stock will support the group's long-term asset quality but will also weigh on profitability over the forecast period.

We expect that through the financial year ending March 31, 2024 (FY2024), adjusted EBITDA margins will drop to below 40%, which we still consider strong compared with peers. This will mainly be the result of an expected increase in investments in existing assets and the addition of lower-margin outright sales into the tenure mix. Historically, the group has been engaged primarily in first-tranche sales in shared ownership units. We expect both outright and first-tranche sales tenures will carry lower margins than the group's traditional lettings tenure, for which operating margins stand at 35%-40%. In addition, the group may suffer some rent losses due to the government's job retention scheme coming to an end and more tenants applying for Universal Credit.

We expect bpha to develop slightly more than 1,300 units over FY2022-FY2024. We expect that about 60% of the development will be for affordable lettings, and the rest for shared ownership and private sales. We view bpha's management as having extensive experience in the social housing sector, with a development strategy aligned to its capabilities, and limited appetite for sales exposure.

Ongoing development efforts, combined with higher investment in existing assets, will increase the nominal debt burden. We expect debt to nonsales EBITDA to stand at about 18.4x on average over the forecast period, while interest coverage will average 1.3x over FY2022-FY2024.

We also think there is a moderately high likelihood that bpha would receive timely extraordinary government-related support in case of financial distress. This is now neutral to the rating because we have revised our stand-alone credit profile to 'a+'. Since one of the key goals of the Regulator for Social Housing (RSH) is to maintain lender confidence and low funding costs across the sector, we think it is likely that the RSH would step in to try and prevent a default in the sector. We base this view on previous records of the RSH mediating mergers or arranging liquidity support from other registered providers in cases of financial distress, and we think this would also apply to bpha.

Lastly, 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. These strengths are offset in our view by the relatively low levels of grant funding that the providers in England receive for the development of affordable homes. We consider that the providers in England have the ability to develop homes for outright sale, using the proceeds as an alternative funding source. However we think that 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 constraints of rent setting or additional spending responsibilities, without adequate additional funding. This weighs on our view of the regulatory framework assessment.

Liquidity

Liquidity remains a rating strength for bpha, underpinned by the group's financial policies. The group has established a target of maintaining funding facilities sufficient to cover two years of net development expenditure at all times. This is reflected in the high level of committed undrawn bank facilities, which together with the current cash and investments position, support our view of its very strong liquidity position. We estimate sources will cover uses by 3x over the next 12 months, although we expect that figure to be slightly lower thereafter. We also continue to view bpha's access to external liquidity as satisfactory.

We expect liquidity sources over the next 12 months will include:

- Cash flow generated from operating activities of about £74 million;
- Cash and liquid investments of £74 million;
- Proceeds from fixed asset sales of £15 million;
- Undrawn committed facilities maturing beyond 12 months and a portion of already secured retained bonds; amounting to about £280 million; and
- Grant receipt of about £5 million.

We expect liquidity uses over the same period will include:

- Capex of about £100 million; and
- Interest and principal repayment of about £50 million.

Key Statistics

Table 1

bpha Ltd.--Key Statistics

	--Year ended March 31--				
Mil. £	**2020a**	**2021a**	**2022bc**	**2023bc**	**2024bc**
Number of units owned or managed	19,235	19,464	19,753	20,118	20,441
Adjusted operating revenue	126.0	131.2	134.1	153.7	160.4
Adjusted EBITDA	56.7	59.1	49.3	55.9	56.6
Non-sales adjusted EBITDA	48.9	55.5	45.8	51.0	52.2
Capital expense	85.8	47.4	90.6	107.8	81.0
Debt	855.0	869.0	876.5	921.0	936.5
Interest expense	36.5	37.4	37.9	39.0	40.3
Adjusted EBITDA/adjusted operating revenue (%)	45.0	45.0	36.8	36.4	35.3
Debt/non-sales adjusted EBITDA (x)	17.5	15.6	19.1	18.0	17.9
Non-sales adjusted EBITDA/interest coverage(x)	1.3	1.5	1.2	1.3	1.3

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

Ratings Score Snapshot

Table 2

bpha Ltd.--Ratings Score Snapshot

	Assessment
Enterprise risk profile	2
Industry risk	2
Regulatory framework	3
Market dependencies	3
Management and Governance	2
Financial risk profile	3
Financial performance	3
Debt profile	4
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: Group Rating Methodology, July 1, 2019
- 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

- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers Published, June 8, 2021
- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, April 23, 2021
- Building Up Debt: U.K. Social Housing Sector Braces Itself For Borrowing, March 16, 2021
- Global Social Housing Ratings Score Snapshot: December 2020, Dec. 10, 2020
- Global Social Housing Ratings Risk Indicators: December 2020, Dec. 10, 2020
- Outlook 2021: Strong Liquidity Should Help Social Housing Providers Remain Resilient, Dec. 8, 2020
- ESG Industry Report Card: Public And Nonprofit Social Housing Providers Outside The U.S., Aug. 4, 2020

Ratings List

Ratings Affirmed; Outlook Action

	To	From
bpha Ltd.		
Issuer Credit Rating	A+/Stable/--	A+/Negative/--
Ratings Affirmed		
bpha Finance PLC		
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/sourceId/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.