

ClwydAlyn Housing Ltd.

August 2, 2023

This report does not constitute a rating action.

Credit Highlights

Overview

Enterprise profile

ClwydAlyn Housing Ltd. (ClwydAlyn)'s ongoing focus on traditional social housing activities and the supportive Welsh policy framework underpin its strong business profile.

--The primary focus on social and affordable tenures in North Wales is ClwydAlyn's credit strength, with sales exposure remaining nil.

--The demand for ClwydAlyn's social housing properties will remain strong, supported by its social and affordable rents at about 62% of the market rent in its areas of operations.

--We think management will carry out appropriate strategy and has sufficient expertise to manage the current cost pressures by reprofiling investment in existing stock if needed.

Financial profile

ClwydAlyn's expanding rental asset base, supported by the generous Welsh government's grant funding and annual rent uplift, will partly offset the effect of high investment needs in existing homes and inflationary pressure on the cost base.

--The expected narrowing of the gap between cost and rent increases will gradually help offset the rising cost of property maintenance.

--Favorable cost of debt and the government grants, combined with continued growth of the rental portfolio, will shore up interest coverage.

--Liquidity remains strong, backed by the government grants and available facilities.

Primary contact

Tim Chow, CFA

London
44-2071760684
tim.chow
@spglobal.com

Secondary contact

Karin Erlander

London
44-20-7176-3584
karin.erlander
@spglobal.com

Outlook

The stable outlook reflects our view that ClwydAlyn's solid and increasing rental revenue will mitigate the hit from the higher cost of maintaining its properties. We project that gradually

improving S&P Global Ratings-adjusted non-sales EBITDA and favorable cost of debt will support stable debt metrics, despite rising debt.

Downside scenario

We could lower our rating on ClwydAlyn if its financial performance deteriorates more than we currently expect, for example through higher inflation and investment in existing homes. Pressure on the rating could also arise from the group taking on more debt than we currently anticipate to fund its increasing development spend. In our view, these scenarios could weigh on the group's performance and sustainably weaken interest coverage toward 1x. We could also consider a negative rating action if we revised downward our view of the likelihood of the Welsh government providing extraordinary support in case of need.

Upside scenario

We could upgrade ClwydAlyn if its adjusted EBITDA improves materially, or its debt funding needs reduces, for example due to higher than expected grant funding for investment in existing or new homes. In our view, this could strengthen the group's debt profile and liquidity position.

Rationale

We expect ClwydAlyn to continue to receive solid grant funding from the Welsh government, which moderates the debt buildup for its development plan. Most of the total debt coming from the existing bond is at a favorable fixed rate, which will also limit its exposure to the high interest-rate environment. In our view, the group will continue to benefit from a predictable revenue stream from low-risk, countercyclical social housing rental activities, with no sales exposure. The supportive operating framework and expectation of rent increases will outpace the growth of cost inflation and increasing investment in existing homes.

Enterprise risk profile: Continued focus on the traditional social housing activities and balanced approach toward development of new homes

We estimate that the group's social and affordable rent is about 62% of the market rent, which bolsters solid demand for its properties, although we think that the housing market in North Wales is less sought after, with weaker economic fundamentals than in other U.K. regions. The fallout of the pandemic was still depressing the group's vacancy rates in care properties in the fiscal year ending March 31, 2023. Additionally, the group planned to sell one of its care properties, but the sale was delayed, thus failing to bring down the void losses. That said, we note that the group has ongoing plans to deal with these losses and expect its vacancy rates to decline. Overall, the group's average vacancy rate over the past three years was 2.9% of rent and service charge receivable; this rate is improving toward around 2%, which we estimate for the Welsh housing sector.

We consider that management has sufficient expertise to run the various segments of housing operations. In our view, the group will continue to focus on traditional social housing lettings in North Wales, mainly general needs and supported housing, with no exposures to sales. We expect the group to continue investing in its existing homes to comply with the required housing standards in areas, such as fire safety and decarbonization. We view positively that about 80% of the group's stock has attained an energy performance certificate rating of 'C' or above.

We assess the regulatory framework under which registered providers of social housing in the Wales operate as strong (for more information see "Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers," published June 8, 2021).

Financial risk profile: Increasing investment in existing and new homes strains the financial metrics but it is partly mitigated by the welsh government's strong grant funding support

We expect that the group will continue to demonstrate stable financial performance, with adjusted EBITDA margins hovering around 20%. We project that the increasing need to improve the existing housing stock, especially around sustainability, together with the inflationary pressure on the group's cost base, will constrain financial performance improvement. Nevertheless, we anticipate that the group will also receive government grants on its existing housing stock, which will partly offset these expenses, and the group has flexibility to reprofile the works if needed. In addition, we forecast the rent uplift in the following years will outpace cost inflation. We therefore project that ClwydAlyn's non-sales adjusted EBITDA will strengthen, hence alleviating the pressures on the debt metrics, which we predict will gradually recover toward fiscal 2026.

In our view, the government grant will help offset pressure on ClwydAlyn's debt metrics, although its debt levels are increasing. We expect the group will continue to enjoy the Welsh government's grant funding, which limits its future debt intake despite our forecast of increasing capital expenditure for new developments. We note that the group aims to complete a relatively large number of units in the coming one-to-two years following the pandemic and delays in planning and disruption. However, we anticipate that the grant will substantially cover about 50% of the development spend, which leads to a moderate buildup of the total debt in our forecast. We also project that the new developments will start to reduce after a spike in handovers by fiscal 2025, containing the future funding needs. Meanwhile, the group also benefits from the favorable cost of debt locked in by the existing bond, which makes up the majority of its total debt and hence supports the interest coverage.

Our strong view of ClwydAlyn's liquidity position is based on our forecast that over the next 12 months, sources of liquidity will cover uses approximately by 1.7x. We assess ClwydAlyn's access to external liquidity as satisfactory. This encompasses our forecast of liquidity sources of about £136 million--from cash, undrawn and available revolving credit facilities, deferred drawdown of the existing bond, asset sales, grant receipts, and cash from operations --which will cover liquidity uses of about £80 million (mainly capital expenditure and debt service payments). We continue to assess ClwydAlyn's access to external liquidity as satisfactory.

Government-related entity analysis

We think there is a high likelihood ClwydAlyn would receive extraordinary government-related support in case of financial distress. This leads us to apply a two-notch uplift to ClwydAlyn's stand-alone credit profile to derive the issuer credit rating. This is based on our opinion of the Welsh government's capacity to support public sector enterprises, and on our view that ClwydAlyn plays an important role for the Welsh government in social housing provision. We also consider that ClwydAlyn has a very strong link to the Welsh government because the government directly regulates the social housing sector, thus providing strong regulatory oversight.

Environmental, Social, And Governance

We think that U.K.-based social housing providers are exposed to elevated environmental and social risks that relate to affordability of services and increased investment in existing homes.

These include inflationary pressures, along with the need to enhance the quality of social housing stock, especially around fire and building safety, as well as the government's environmental agenda to achieve energy efficiency and net zero carbon.

We think these risks apply to ClwydAlyn, in line with the sector. However, we note that the group has limited exposure to fire safety spend and a relatively high proportion of assets close to the government's energy efficiency target.

Key Statistics

ClwydAlyn Housing Ltd.-- Key Statistics

	--Year ended March 31--				
Mil. £	2022a	2023e	2024bc	2025bc	2026bc
Number of units owned or managed	6,296	6,365	6,422	6,916	7,214
Adjusted operating revenue	47.3	50.7	53.4	59.1	63.7
Adjusted EBITDA	9.3	9.8	10.7	12.6	13.0
Nonsales adjusted EBITDA	9.3	9.8	10.7	12.6	13.0
Capital expense	52.3	48.7	73.3	56.2	33.9
Debt	234.3	234.9	272.3	275.6	291.0
Interest expense	7.9	8.1	8.8	9.4	9.8
Adjusted EBITDA/adjusted operating revenue (%)	19.7	19.4	20.1	21.3	20.5
Debt/nonsales adjusted EBITDA (x)	25.2	23.9	25.4	21.9	22.3
Nonsales adjusted EBITDA/interest coverage (x)	1.2	1.2	1.2	1.3	1.3

ClwydAlyn Housing Ltd.

a--Actual. e--Estimate. bc--Base case
reflects S&P Global Ratings'
expectations of the most likely
scenario. N.A.--Not available.

Rating Component Scores

ClwydAlyn Housing Ltd.-- Ratings Score Snapshot

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

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

ClwydAlyn Housing Ltd.

- 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

- United Kingdom Outlook Revised To Stable From Negative On Moderating Fiscal Risks; 'AA/A-1+' Ratings Affirmed, April 21, 2023
- U.K. Social Housing Borrowing 2023: On Pause, March 28, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings History: March 2023, March 27, 2023
- U.K. Social Housing Providers Set Their Sights On Cyber Risks, Dec. 16, 2022
- Non-U.S. Social Sector Outlook 2023: The Most Negative Bias Since 2018 Implies Significant Pressure On Ratings, Dec. 1, 2022
- Inflation To Erode The Performance Of U.K. Public Finance Sectors, Nov. 29, 2022
- Cap On Rent Increases Is Consistent With Our Base Case For English Social Housing Providers, Nov. 17, 2022
- The U.K. Social Housing Sector Now Displays A More Pronounced Negative Bias In Its Creditworthiness, Oct. 11, 2022
- Launch Of Rent Cap Consultation Adds Uncertainty To Creditworthiness Across English Housing Sector, Sept. 1, 2022
- Rated U.K. Social Housing Providers' Creditworthiness Could Suffer If The Gap Between Rent And Cost Increases Persists, Aug. 1, 2022
- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers, June 8, 2021

Ratings Detail (as of August 01, 2023)*

ClwydAlyn Housing Ltd

Ratings Detail (as of August 01, 2023)*

Issuer Credit Rating A/Stable/--

Issuer Credit Ratings History

24-May-2017 A/Stable/--

*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.

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