

CREDIT OPINION

26 October 2023

Update



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RATINGS

ClwydAlyn Housing Limited

Domicile	United Kingdom
Long Term Rating	A3
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Maylis Chapellier +44.20.7772.1429
 Analyst
maylis.chapellier@moodyys.com

Adam Chwojncki +44.20.7772.8778
 Ratings Associate
adam.chwojncki@moodyys.com

Sebastien Hay +34.91.768.8222
 Associate Managing Director
sebastien.hay@moodyys.com

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ClwydAlyn Housing Limited (UK)

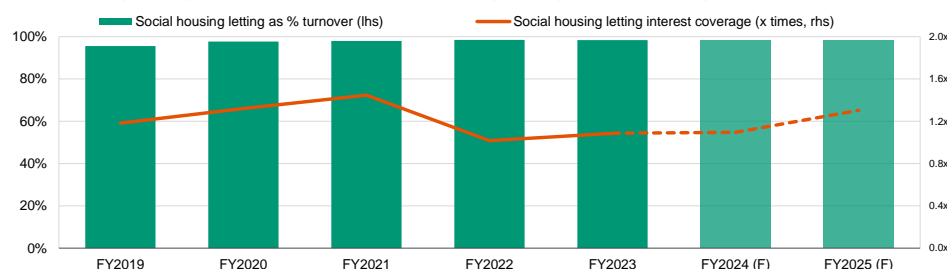
Update following outlook change to stable from negative

Summary

The credit profile of [ClwydAlyn Housing](#) (ClwydAlyn, A3 stable) reflects its high proportion of revenue derived from low-risk social housing lettings, which enhances revenue stability; its strong market position in North Wales; and its improved debt metrics. The rating also reflects its lower margins than peers, anchored by care and supporting housing activities, and decreased interest cover ratios. ClwydAlyn benefits from the strong regulatory framework governing Welsh housing associations (HAs) and our assessment that there is a strong likelihood that the government of the [United Kingdom](#) (UK, Aa3 stable) would intervene in the event that it faced acute liquidity stress.

Exhibit 1

ClwydAlyn continues to maintain a high proportion of social housing lettings
 Social housing letting as % turnover (lhs), social housing letting interest coverage (x times, rhs)



F: Forecast.

Source: ClwydAlyn and Moody's Investors Service

Credit strengths

- » Continued focus on low-risk social housing letting
- » Strengthened debt metrics thanks to added grants and stable debt
- » Supportive operating environment and regulatory framework

Credit challenges

- » Low operating margins
- » Slightly higher development ambitions than peers

Rating outlook

The stable outlook reflects the expected gradual reduction in inflation and associated cost pressures as well as the proactive actions taken by ClwydAlyn to mitigate the adverse effects of the weaker operating environment, thereby limiting development risk. It also reflects the support of the Welsh government and the additional grant funding to face heightened price inflation.

Factors that could lead to an upgrade

Upward pressure on the ratings could result from a significant improvement in operating performance or a material reduction in debt.

Factors that could lead to a downgrade

Downward pressure on the ratings could result from a prolonged weakening in operating performance, debt growing more quickly than forecasts, weaker liquidity or a failure to adapt strategies and risk appetite to mitigate against weaker economic conditions. Lower government support for the sector or a dilution of the regulatory framework could also lead to downward pressure on the ratings.

Key indicators

Exhibit 2

ClwydAlyn Housing Limited	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23	31-Mar-24 (F)	31-Mar-25 (F)
Units under management (no.)	5,998	6,048	6,240	6,296	6,390	6,451	7,072
Operating margin, before interest (%)	21.7	22.6	23.6	17.6	17.8	20.1	20.6
Net capital expenditure as % turnover	14.1	33.4	12.8	21.0	24.5	34.9	46.3
Social housing letting interest coverage (x times)	1.2	1.3	1.4	1.0	1.1	1.1	1.3
Cash flow volatility interest coverage (x times)	1.3	1.5	0.8	2.1	0.3	1.0	1.7
Debt to revenues (x times)	4.7	4.4	4.7	4.8	4.4	4.7	4.3
Debt to assets at cost (%)	45.6	45.8	44.5	42.2	40.5	40.5	41.0

F: Forecast.

Source: ClwydAlyn and Moody's Investors Service

Detailed credit considerations

On 25 October 2023, Moody's changed the outlook to stable from negative and affirmed ClwydAlyn's ratings. The change in outlook followed Moody's change in outlook of the Government of the United Kingdom's Aa3 rating to stable from negative on 20 October 2023.

ClwydAlyn's A3 rating combines (1) a baseline credit assessment (BCA) for the entity of baa1 and (2) a strong likelihood of extraordinary support coming from the national government in the event that the entity faced acute liquidity stress.

Baseline credit assessment

Continued focus on low-risk social housing letting

Low-risk social housing lettings, including supported and sheltered housing, contributed 98% of ClwydAlyn's turnover in FY2023, a level virtually unchanged since FY2014. This compares favourably with A3 rated peers, which derived a median of 75% of their revenue from social housing lettings in FY2023. We expect ClwydAlyn's proportion of turnover from social housing lettings to remain at 98% over the next five years.

More than half of the group's income is generated from housing benefits, care home fees funded by local authorities and government contracts to provide supporting living services - this backing of a significant proportion of revenue by government bodies is also credit positive as it reduces the risk of revenue losses.

ClwydAlyn does not build to sell (outright sales or shared ownership), which limits its exposure to volatile income sources, a credit positive.

ClwydAlyn is one of the largest housing associations in Wales with about 6,400 units under management and a turnover of £53 million in FY2023. It has the biggest market share in North Wales, a dispersed area with the second-biggest population concentration after the more urbanized south. ClwydAlyn's major operations are spread across seven local authorities in Wales.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Strengthened debt metrics thanks to added grants and stable debt

ClwydAlyn's debt levels are expected to increase to £290 million by FY2026, from £230 million at FY2023, to fund its development programme. Debt to revenue is expected to average of 4.4x over the next three years, higher than the A3 peer median of 4.2x over the same period, but in line with FY2023 level of 4.4x for ClwydAlyn. Gearing is expected to marginally increase, averaging 41% over the next three years from 40% in FY2023. This is much stronger than the expected A3 peer median of 53% over the same period, highlighting the more favorable Welsh grant regime, compared to the English one.

The HA was awarded £53 million of grants out of a total of about £300 million for the whole of Wales in FY2023, a positive. Whilst the majority was for development (£46 million), ClwydAlyn also benefitted from £1.8 million grants from Optimised Retrofit Programme to improve the energy efficiency of its housing stock and £4.7 million from Transitional Accommodation Capital Programme to fund refurbishment of void properties. Those grants will help ClwydAlyn reach the recently passed measure to improve the EPC ratings of Welsh social housing units to C by 2029.

ClwydAlyn's debt profile is low risk with 100% of its debt at fixed rates (including hedges) and low short-term refinancing risk, with 98% of debt due after more than five years as of FY2023. Its main refinancing risk lies with its £185 million bond (as of FY2023, or expected at £225 million as of FY2024), maturing in FY2052, but we note that the bond is repayable in several installments starting in 2038.

Supportive operating environment and regulatory framework

ClwydAlyn's credit quality will continue to benefit from the strong institutional framework governing Welsh HAs reflected in an Operating Environment score of a2 and a Regulatory Framework score of a1. These scores are assigned at a national level and reflect the following credit considerations:

The Housing Regulation Team (HRT), a departmental office sitting within the Welsh Government, regulates Welsh HAs. The HRT is responsible for protecting the public investment in social housing as well as ensuring that HAs are financially viable, well-governed and deliver high quality homes and services. The regulator monitors compliance with standards of performance through quarterly returns, long-term business plans, stress tests and regular interaction with senior management. In the latest regulatory assessment from March 2022, ClwydAlyn retained the highest scores (Green) for both Governance (including tenant services) and Financial Viability.

The operating environment for Welsh HAs remains supportive, with a very high demand for social housing. The Welsh government has committed to increased capital grants on more flexible terms for new social housing and introduced material cost increase grants to help HAs mitigate the impact of inflationary pressures on development.

The Welsh government is allowed to limit social rent increases when inflation is above 3% (the policy is to increase rents by CPI+1% otherwise). Due to high rates of inflation exceeding 3%, the Welsh government has set a 6.5% ceiling on social rent increases from April 2023 for one year and is likely to set another sub-inflationary ceiling from April 2024. The ceilings will likely result in an adverse differential between rental income and cost growth, driving lower margins and interest coverage. Nonetheless, we view the Welsh operating environment as more favourable than the English one as a result of a higher level of grants and less policy volatility.

Low operating margins

ClwydAlyn's operating margin will remain below peers, averaging 21% over the next 3 years, anchored by its supported housing and care activities and we assume a second below inflation rent cap. Supported housing and care activities have high cost structures compared to general needs units, and also suffered from higher voids than other tenures during the pandemic.

ClwydAlyn had an operating margin of 18% in FY2023, which is low compared to the A3 peer median of 22%. ClwydAlyn's 2023 margin was negatively impacted by increased utility bills and labour shortages as the HA had to hire subcontractors on top of inflation on maintenance and repairs costs. Like the rest of the sector, ClwydAlyn faced increased demand for repairs and maintenance, partially due to added vigilance on damp and mould, which further weighed on its performance. Besides, the HA was asked to retrofit 12 units to host refugees, to run a refugee center and to deliver a one-off bonus payment, those were all fully covered by grants or additional income, but lowered the margin.

Whilst Welsh housing associations have generally lower margins relative to their English peers, ClwydAlyn remains committed to delivering value for money efficiencies through improving voids, which increased due to the pandemic, consolidating its care activity and renegotiating fees with local authorities.

ClwydAlyn's social housing lettings interest coverage (SHLIC) of 1.1x in FY2023 is slightly higher than the A3 peer median of 1.0x. SHLIC is expected to slightly improve in FY2025, supported by growth in operating surplus from SHL and stable interest payments.

Cash flow volatility interest coverage (CVIC) decreased to 0.3x in FY2023 from 2.1x in FY2022, driven by the decrease in cash flows from operations. However, CVIC is expected to improve, averaging 1.3x over the next three years, despite rising interest costs thanks to improved operating surplus.

Slightly higher development ambitions than peers

ClwydAlyn plans to build 1,317 units over the next five years, or 21% of existing stock. The projected net capital spending over the next three years is ambitious, averaging 37% of turnover, compared to 24% in FY2023. It is also slightly higher than A3 rated peers, averaging at 36%. We note the HA revised down its development targets, a credit positive.

Although this is high, ClwydAlyn benefits from high grants from the Welsh Government as this is in line with its ambitions to build 20,000 low-carbon homes across Wales by 2026. Besides, ClwydAlyn also benefitted from £3.7 million Material Cost Increase grant from the Welsh Government for development schemes that are significantly impacted by inflationary pressures.

91% of the units built are planned to be general needs units, 100 affordable housing units and 23 supported housing over the next five years. This is credit positive as ClwydAlyn will benefit from very strong demand on general needs units, characterised stable cash flows.

ClwydAlyn's liquidity coverage is adequate at 1.0x in FY2023, although lower than peers (median of 1.2x). ClwydAlyn's unencumbered assets allow for a borrowing capacity of £108 million, which compares well with its funding needs, £95 million for its 5-year development programme.

Extraordinary support considerations

The strong level of extraordinary support factored into the rating reflects the wide-ranging powers available to the regulator in cases of financial distress, with the possibility of a facilitated merger or a transfer of engagements. However, the process can be protracted and is reliant on HAs agreeing to merge, which could be more challenging in a weakening operating environment. Recent history has shown that the UK government is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors increasing exposure to non-core social housing activities in the sector, that add complexity to HA operations, and the weakening of the sovereign's financial resilience, making an extraordinary intervention slightly more challenging. In addition, our assessment that there is a very high default dependence between ClwydAlyn and the UK government reflects their strong financial and operational linkages.

ESG considerations

ClwydAlyn Housing Limited's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 3

ESG Credit Impact Score

CIS-2

Neutral-to-Low

For an issuer scored CIS-2 (Neutral-to-Low), its ESG attributes are overall considered as having a neutral-to-low impact on the current rating; i.e., the overall influence of these attributes on the rating is non-material.

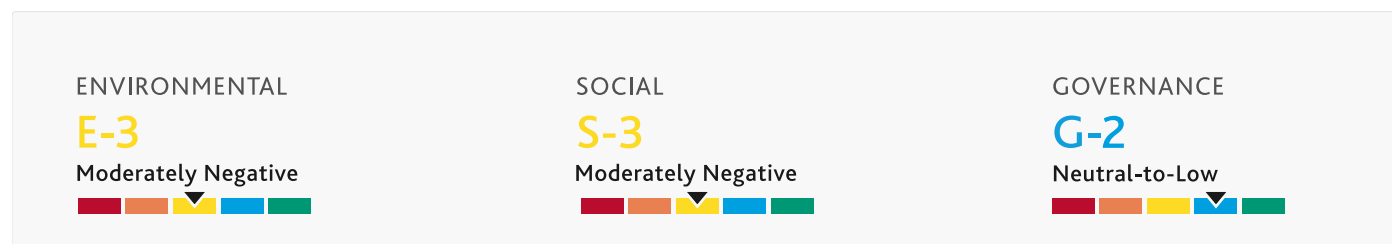


Source: Moody's Investors Service

ClwydAlyn's **CIS-2** indicates that ESG risks have a limited impact on its rating. Although carbon transition risks and social risks are prevalent we consider that ClwydAlyn has the ability to effectively mitigate them through its strong governance and management practices, as well as additional support from the Welsh government. We also consider that the supportive regulatory framework for the sector offsets some ESG risks.

Exhibit 4

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

ClwydAlyn has a material exposure to environmental risks (**E-3**) relating to a significant proportion of its stock requiring retrofit to meet energy efficiency standards by 2029 (carbon transition risks), leading to increased expenditure.

Social

ClwydAlyn has a material exposure to social risks (**S-3**) through sector-wide legislative requirements to improve the safety of existing housing stock (responsible production risks) which weighs on expenditure and operating margins, and the impacts of cost of living or affordability pressures on social tenants (demographic and societal trends) which led to the Welsh government capping social rent increases below inflation in fiscal 2024 in Wales, which will also have a negative impact on margins.

Governance

ClwydAlyn has limited governance risks (**G-2**). Its governance is fit for purpose, with strong financial management policies and processes, detailed reporting and a simple organisational structure. The regulatory framework also supports good governance in the sector.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The assigned BCA of baa1 is one notch above the scorecard-indicated BCA of baa2.

The methodologies used in this rating were [European Social Housing Providers](#), published in April 2018, and [Government Related Issuers](#), published in February 2020.

Exhibit 5

31 March 2023

ClwydAlyn Housing Limited

Baseline Credit Assessment	Sub-factor Weighting	Value	Score
Factor 1: Institutional Framework			
Operating Environment	10%	a	a
Regulatory Framework	10%	a	a
Factor 2: Market Position			
Units Under Management	10%	6,390	baa
Factor 3: Financial Performance			
Operating Margin	5%	17.8%	baa
Social Housing Letting Interest Coverage	10%	1.1x	baa
Cash-Flow Volatility Interest Coverage	10%	0.3x	b
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	4.4x	ba
Debt to Assets	10%	40.5%	ba
Liquidity Coverage	10%	1.0x	baa
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
Scorecard - Indicated BCA Outcome			baa2
Assigned BCA			baa1

Source: ClwydAlyn and Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
CLWYDALYN HOUSING LIMITED	
Outlook	Stable
Baseline Credit Assessment	baa1
Issuer Rating -Dom Curr	A3
PENARIAN HOUSING FINANCE PLC	
Outlook	Stable
Senior Secured -Dom Curr	A3

Source: Moody's Investors Service

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