FitchRatings

RATING ACTION COMMENTARY

Fitch Rates Metropolitan Thames Valley Housing Group 'A': Outlook Stable

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Feedback

Fitch Ratings - London - 19 Jul 2021: Fitch Ratings has assigned Metropolitan Thames Valley Housing Group (MTVH) a Long-Term Issuer Default Rating (IDR) of 'A' and their GBP2 billion EMTN programme long-term senior secured and unsecured ratings of 'A(EXP)'.

The Outlook on the Long-Term IDR is Stable.

The notes under the programme are expected to constitute unconditional, secured or unsecured and unsubordinated liabilities of MTVH. As such they will rank equal with all other direct obligations and are therefore linked to its Long-Term IDR.

The assignment of final rating is contingent on the receipt of final documents conforming to information already received.

KEY RATING DRIVERS

Status, Ownership and Control: 'Strong'

MTVH is a private, not-for-profit, registered provider (RP) of social housing (SH) in the UK, as such it is not under the ownership of the UK government due to its structure and status (in strict terms there is no legal owner). We view the regulatory framework for English SH as having a robust legal basis, and the Regulator of Social Housing (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'

MTVH receives financial support through grants from Homes England and the Greater London Authority (GLA) at varying levels to generate 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. MTVH is a strategic partner of the GLA and has continuous market engagement with Homes England.

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 MTVH, not materially affecting the provision of service.

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.

Standalone Credit Profile (SCP)

MTVH's SCP is assessed at 'a-', driven by a 'Stronger' assessment for revenue defensibility, operating risk assessment and financial profile.

Revenue Defensibility: 'Stronger'

MTVH relies on affordable and social rent and care income for revenue, with a shared-ownership (SO) sale portfolio in a large and profitable market. The affordable and social revenue stream is highly regulated, with rents in SH reducing by 1% per annum between

2016 and 2020. From 1 April 2020, increases to social rent of CPI +1% were put in place for the next five years.

MTVH operates primarily in the south of the UK, and the midlands near to major cities, both deemed as economically prosperous areas. However, low-cost accommodation, which generates significant demand for SH properties, tends to be limited with a waiting list of over 80,000 people in the top 10 local council areas MTVH operates in. The differential between market and affordable rents is significant in these areas, which exacerbates demand for low-cost rental or ownership housing.

MTVH has diverse revenue streams with a strong core revenue base, with around 65%-70% generated by SH lettings, the remainder through development for sale, private-rental schemes, first-tranche sales and care activity. MTVH has an active stock-rationalisation plan in place, under which it expects to dispose of around 1,400 units over the next five years.

Around 50% of MTVH's tenants are in receipt of housing benefit (HB) or universal credit (UC); these benefits have remained broadly unchanged in recent years and represent about one-third of the RP's annual revenue, with a slight 2% increase last year due to Covid-19, demonstrating consistent cashflows supported by government funding.

Operating Risk: 'Stronger'

MTVH has new stock in comparison with others in the sector, with 72% at less than 40 years old, and almost 50% less than 20 years old. Newer stock limits the costs of maintenance required to meet their duty to provide quality housing for their tenants. MTVH also holds significant SO properties (around 15%) where repairs and maintenance are often the responsibility of the tenant. To realise the greatest value for maintenance costs MTVH has set up an internal maintenance provider (Metworks) to undertake all routine repairs and maintenance across their portfolio. Staff costs, the largest rigid cost across the sector, accounts for only 25% of operating expenditure, which is in line with that of some strongest peers at the lower end of the cost scale.

The SH sector faces significant costs relating to fire safety, for which MTVH has already planned remediation costs. It has 73 blocks over 18m high, which are estimated to cost GBP108 million to remediate, and 246 blocks 11m-18m high, which are expected to cost GBP50 million to meet the highest safety standards.

Over the next 10 years MTVH expects to develop 13,700 homes costing GBP4.7 billion, of which 78% will be affordable. This has been factored into all business plans and funding expectations.

Financial Profile: 'Stronger'

The 'Stronger' financial profile reflects our expectations of net debt/EBITDA remaining around or below 12x throughout our rating case. MTVH has consistent, reliable cashflows from rental income and full ability to flexibly adjust their non-regulated activities to cross-subsidise their core mission of providing SH.

EBITDA is expected to average around GBP170 million across the next five years, with slight fluctuations year-on-year as a result of development-completion timing. With considerable revenue from UC and HB, cashflows are expected to be maintained.

MTVH is expected to continue to generate revenue of around GBP480 million in the medium term, all of which is available for debt-service. Net debt in financial year to 31 March 2020 was GBP1.8 billion, and is expected to steadily increase to around GBP2.3 billion by FY25.

DERIVATION SUMMARY

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

Fitch views MTVH as a government-related entity (GRE) of the UK government. 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. MTVH has a key public-policy mission to provide affordable homes to those in need across England.

MTVH's Short-Term 'F1+'IDR is the higher of two options mapping to a Long-Term 'A' IDR as the RP meets all relevant liquidity criteria (cushion and coverage).

RATING SENSITIVITIES

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

A sustained improvement in net debt/ EBITDA towards 10x in the medium term or a favourable change to the assessment of key rating factors.

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

A multi-notch downgrade to the sovereign, deterioration in net debt/ EBITDA above 12x on a sustained basis or an adverse change to the 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.

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LIQUIDITY AND DEBT STRUCTURE

MTVH currently has GBP1.3 billion in unencumbered assets ready to be secured. Its development programme delivers a net additional 7,600 social units over 10 years. Based on current market values this enables a further GBP0.75 billion in security by 2031, allowing for a total of around GBP2.1 billion in security. This is sufficient to cover the RP's forecast borrowing requirements, including the GBP2 billion EMTN programme.

ISSUER PROFILE

MTVH is an SH RP based primarily out of London and the South-east, providing around 57,000 affordable homes. MTVH is one of the largest RPs in the UK and a constituent member of the G15, the biggest RP in London.

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

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.

RATING ACTIONS

ENTITY/DEBT	RATING		
Metropolitan Thames Valley Housing Group	LT IDR	A Rating Outlook Stable	New Rating
•	ST IDR	F1+	New Rating
•	LC LT IDR	A Rating Outlook Stable	New Rating
•	LC ST IDR	F1+	New Rating
• senior	LT	A(EXP)	Expected Rating

VIEW ADDITIONAL RATING DETAILS

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Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

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

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 23 Feb 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

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Endorsement Policy

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Metropolitan Thames Valley Housing Group -

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