

Research Update:

# U.K.-Based Metropolitan Thames Valley Housing Outlook Revised To Stable; 'A-' Ratings Affirmed

December 19, 2023

## Overview

- We project that Metropolitan Thames Valley Housing (MTVH) will ramp up investments in existing homes, mainly to address fire and building safety issues and enhance the energy efficiency performance.
- At the same time, we acknowledge management's efforts to contain costs, including securing external funding for these investments.
- We expect rents will increase faster than cost inflation in the coming two to three years, supporting our forecast that the group's financial metrics should stabilize in line with our base case.
- We therefore revised our outlook on MTVH to stable from negative. At the same time, we affirmed our 'A-' long-term issuer credit rating on MTVH.

## Rating Action

On Dec. 19, 2023, S&P Global Ratings revised its outlook on MTVH to stable from negative. At the same time, we affirmed our 'A-' long-term issuer credit rating on MTVH.

We also revised our outlook on Metropolitan Housing Trust Ltd. (MHT) to stable from negative, and affirmed our 'A-' long-term issuer credit rating. We consider MHT a core subsidiary of MTVH, since it owns and manages most of the group's rental units and shared ownership sales. We also affirmed our 'A-' rating on MHT's £2 billion senior secured and unsecured medium-term notes program and the £250 million senior secured bond.

At the same time, we affirmed our issue rating on Metropolitan Funding PLC's £250 million senior secured bond at 'A-'. Metropolitan Funding PLC was set up for the sole purpose of issuing bonds and lending the proceeds to the group, and we view it as a core subsidiary of MTVH.

### PRIMARY CREDIT ANALYST

**Noa Fux**  
London  
+ 44 20 7176 0730  
noa.fux  
@spglobal.com

### SECONDARY CONTACTS

**Karin Erlander**  
London  
+ 44 20 7176 3584  
karin.erlander  
@spglobal.com

**Felix Ejgel**  
London  
+ 44 20 7176 6780  
felix.ejgel  
@spglobal.com

### ADDITIONAL CONTACT

**Sovereign and IPF EMEA**  
SOVIPF  
@spglobal.com

## Outlook

The stable outlook reflects our view that MTVH will be able to manage risks associated with its large program of investments in existing stock through effective grants negotiation and cost management, while keeping its development program contained.

## Downside scenario

We could lower the rating if investments in existing stock increase beyond our expectations, or if the group increases its debt-funded development on new homes. We think this would weaken the group's financial metrics.

We could also lower the rating if we were to revise downward our view of the likelihood of extraordinary support to MTVH from the U.K. government in the event of financial distress.

## Upside scenario

We would consider an upgrade if management's actions and improvements in the operating environment led to substantially better credit metrics than our current expectations, on a sustained basis.

## Rationale

The outlook revision reflects our view that MTVH's credit metrics are expected to stabilize, despite the group's large program of investments in existing homes. Our projections are underpinned by our view that management has a more accurate estimate of the scope of necessary works, and has taken steps to secure external funding for them. These actions help to limit the financial impact of the expenditure associated with fire and building safety, as well as energy efficiency of the social housing stock. We also project that rents will grow faster than cost inflation over our three-year forecast horizon, further supporting MTVH's financial performance. In addition, in recent years MTVH has scaled down its development aspirations, reducing debt accumulation.

## Enterprise profile: Large asset base, affordability levels, and contained sales risk support the enterprise risk profile

MTVH's affordability levels in its main areas of operations and large stock support our view of its creditworthiness. The group owns and manages about 57,000 units, and we consider that its substantial size and geographic footprint in the U.K. allow it to build up economies of scale in its operations. MTVH's stock is mainly in and around London, which benefits from higher demand and market rent than the national average. On average, we assume the group's social and affordable rent levels are at about half of the prevailing market rents. We consider that despite being higher than historical levels, the group's vacancy rates over the past three years--of 1.6% of rent receivable and service charges--remain broadly in line with the sector average of 1.7%.

We think that MTVH's management is making strategic decisions and taking proactive measures to limit the impact from macroeconomic pressures and internal factors on financials. These actions include securing grants and external funding for investments in existing homes and a refreshed approach on asset disposals. For example, we understand MTVH has successfully

negotiated with developers to contribute toward fire and building safety remediation in its properties. Nonetheless, we think that the group is still exposed to risks associated with the existing stock works, and that flexibility is constrained because of fairly modest financial metrics and the need to deliver on their partnerships-led development program.

Furthermore, we consider positively that the group has set stricter limits on its sales exposure and overall scaled back its development aspirations over the past couple of years. We expect the group's sales exposure will be mainly contained to first-tranche sales of shared ownership units, while open market sales will be largely delivered through joint ventures (JVs). We project the group's revenues from sales activities, including those from JVs, will be contained below one-third of its total S&P Global Ratings-adjusted operating revenue over the coming years.

We assess the regulatory framework under which registered providers of social housing in England operate as strong (see "Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks," published Oct. 23, 2023, on RatingsDirect).

### **Financial profile: Modest yet stable financial metrics underpin the financial risk profile**

We anticipate adjusted EBITDA margins will remain slightly above 20% in the coming three years, similar to our previous performance and the group's historical performance indicator. Unlike many peers, MTVH's performance remained relatively stable in fiscal year ending March 31, 2023, despite the increased demand for services. This was supported by a capital contribution to investments in existing stock, which we think will continue at a lower amount in fiscal 2024.

We expect additional external funding for investments in existing homes will be available for the group in the coming years. This includes grants from the social housing decarbonization fund and building safety fund, as well as developers' participation in fire and safety-related remediation. Nonetheless, the size of the fire and safety program remains significant, and it is likely to hinder improvement in the group's adjusted EBITDA margins, in our view.

We project that the group's debt metrics will remain weak, at a similar level to our previous forecast. Despite grant funding from the group's partnerships with Homes England and the Greater London Authority, as well as proceeds from the sale of fixed assets, we expect MTVH will still require new borrowing to fund its development program. That said, we expect debt build up to moderate compared with our previous expectations. MTVH's debt profile benefits from a relatively low share of variable rates debt, estimated to be less than 15% currently. With modest refinancing needs and slightly improving nonsales EBITDA, we think that MTVH's interest risk exposure is contained despite the generally higher interest rate environment.

We view MTVH's liquidity as very strong. This is based on our expectation that the group's sources of liquidity will exceed uses by about 2x over the next 12 months, and our view that it has satisfactory access to external liquidity. We forecast liquidity sources of about £980 million--mainly via cash from operations after adding back the noncash cost of sales, cash, and undrawn available facilities; grant receipts; and sales proceeds from fixed asset sales. This compares with liquidity uses of about £480 million--primarily capital expenditure, interest, and principal repayments.

### **Government-related entity analysis**

We think there is a moderately high likelihood that MTVH would receive timely extraordinary government-related support in case of financial distress. This provides two notches of uplift from

the stand-alone credit profile (SACP). Because one of the key goals of the Regulator of 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 to 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 think this would also apply to MTVH.

Table 1

**Thames Valley Housing Association--Key statistics**

| Mil. £   | --Year ended March 31-- |         |         |         |         |
|--|-------------------------|---------|---------|---------|---------|
|  | 2022a                   | 2023a   | 2024bc  | 2025bc  | 2026bc  |
| Number of units owned or managed               | 57,184                  | 56,947  | 56,885  | 56,668  | 57,198  |
| Adjusted operating revenue                     | 408.1                   | 383.0   | 404.8   | 440.1   | 449.8   |
| Adjusted EBITDA                                | 81.2                    | 84.3    | 89.9    | 89.3    | 95.2    |
| Nonsales adjusted EBITDA                       | 71.9                    | 81.0    | 86.1    | 83.8    | 90.2    |
| Capital expense                                | 158.0                   | 188.4   | 356.7   | 295.8   | 354.3   |
| Debt   | 1,915.5                 | 1,947.1 | 1,972.1 | 2,073.1 | 2,237.1 |
| Interest expense                               | 76.6                    | 84.9    | 93.1    | 96.0    | 100.9   |
| Adjusted EBITDA/Adjusted operating revenue (%) | 19.9                    | 22.0    | 22.2    | 20.3    | 21.2    |
| Debt/Nonsales adjusted EBITDA (x)              | 26.6                    | 24.0    | 22.9    | 24.7    | 24.8    |
| Nonsales adjusted EBITDA/interest coverage(x)  | 0.9                     | 1.0     | 0.9     | 0.9     | 0.9     |

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

**Ratings Score Snapshot**

Table 2

**Metropolitan Thames Valley Housing--Ratings Score Snapshot**

|                            | Assessment |
|----------------------------|------------|
| Enterprise risk profile    | 3          |
| Industry risk              | 2          |
| Regulatory framework       | 3          |
| Market dependencies        | 2          |
| Management and governance  | 3          |
| Financial risk profile     | 4          |
| Financial performance      | 4          |
| Debt profile               | 6          |
| Liquidity                  | 2          |
| Stand-alone credit profile | bbb        |
| Issuer credit rating       | A-         |

S&P Global Ratings bases its ratings on nonprofit social housing providers on the seven main rating factors listed in the table above. Our "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

## Related Research

- Non-U.S. Social Housing Sector Outlook 2024: At A Turning Point?, Nov. 29, 2023
- Non-U.S. Social Housing Providers Ratings Risk Indicators November 2023, Nov. 15, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot November 2023, Nov. 15, 2023
- Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks, Oct. 23, 2023
- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, Oct. 20, 2023
- U.K. Social Housing Providers' Credit Headroom Could Tighten If The Operating Environment Deteriorates, Oct. 4, 2023
- European Housing Markets: Sustained Correction Ahead, July 20, 2023
- U.K. Social Housing Borrowing 2023: On Pause, March 28, 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

## Ratings List

### Ratings Affirmed

#### Metropolitan Funding PLC

|                |    |
|----------------|----|
| Senior Secured | A- |
|----------------|----|

#### Metropolitan Housing Trust Ltd.

|                |    |
|----------------|----|
| Senior Secured | A- |
|----------------|----|

### Ratings Affirmed; Outlook Action

|  | To | From |
|--|----|------|
|--|----|------|

#### Metropolitan Thames Valley

#### Metropolitan Housing Trust Ltd.

|                      |              |                |
|----------------------|--------------|----------------|
| Issuer Credit Rating | A-/Stable/-- | A-/Negative/-- |
|----------------------|--------------|----------------|

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.spglobal.com/ratings](http://www.spglobal.com/ratings) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceid/504352>. Complete ratings information is available to RatingsDirect subscribers at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.spglobal.com/ratings](http://www.spglobal.com/ratings). Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.

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