S&P Global
Ratings

RatingsDirect®

## Research Update:

# U.K.-Based Metropolitan Housing Trust 'A+' Long-Term Rating Affirmed; Outlook Stable

**Primary Credit Analyst:**
Jean-Baptiste Legrand, London (44) 20-7176-3609; jb.legrand@spglobal.com

**Secondary Contact:**
Ratul Sood, London +44 (0) 20 7176 6536; ratul.sood@spglobal.com

## Table Of Contents

Research Update:

# U.K.-Based Metropolitan Housing Trust 'A+' Long-Term Rating Affirmed; Outlook Stable

## Overview

- We are affirming our 'A+' long-term issuer credit ratings on Metropolitan Housing Trust (Metropolitan), a U.K.-registered provider of social housing.
- Our assessment of Metropolitan Housing Trust benefiting from a moderately high likelihood of receiving extraordinary support from the U.K. government, working through the Homes and Communities Agency, has a neutral impact on the rating.
- The stable outlook reflects our base-case expectation that Metropolitan will continue to show a very strong enterprise profile and a strong financial profile over the next two years, with continued government support.

## Rating Action

On July 22, 2016, S&P Global Ratings affirmed its 'A+' long-term credit rating on U.K. social housing provider Metropolitan Housing Trust (Metropolitan). The outlook remains stable.

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

## Rationale

The 'A+' rating on Metropolitan is based on its stand-alone credit profile (SACP), which we assess at 'a+'. Our assessment of Metropolitan benefiting from a moderately high likelihood of extraordinary support from the U.K. government (AA/Negative/A-1+), working through the Homes and Communities Agency (HCA), in the event of financial distress, has a neutral impact on the rating.

In accordance with our criteria for government-related entities (GREs), our view of a moderately high likelihood of extraordinary government support is based on our assessment of Metropolitan’s important role for the U.K. government and its public policy mandate; and its strong link with the U.K. government, demonstrated by the government's track record of providing strong credit support in certain circumstances.

The rating is supported by the group's very strong enterprise profile, bouyed by strong economic fundamentals as well as sound asset quality and operational performance with low voids of 2.5% on average over the past three years (2014-2016) and falling arrears, from 6.2% in FY2014 to 4.7% in FY2016. Metropolitan benefits from its exposure to geographical areas of operation characterized by high demand, with 60% of its housing stock located in London. The rating also takes into account



1679595 | 302011598

Metropolitan's strong financial profile, supported by adequate overall financial performance, and a very strong liquidity and debt profile.

Thanks to a turnaround plan implemented by a refreshed and experienced executive team, Metropolitan has significantly improved its financial performance over the last few years, improving its adjusted EBITDA margins to 35% per year in 2014-2016 from 17% in 2010-2013. We forecast adjusted EBITDA margins to remain sound at 32% of total revenues over our 2017-2019 base-case scenario, supported by an increase in first tranche sales from shared ownership and open market sales. Metropolitan is also committed to tackling the challenge presented by the decrease in social rents from 2016, by delivering operating savings in routine and planned maintenance, through the in-house contractor initiative Metworks.

Based on its updated development program, we understand Metropolitan is willing to deliver about 2,600 new units in our 2017-2019 forecast period, of which only 28% are committed units as of July 2106 (excluding JVs). The majority (55%) of it remains focused in London, which in our view is supportive of its very strong enterprise profile. Despite the downward revision of the stock development for private sale, which will only account for 12% of the development plan in our 2017-2019 base-case scenario (excluding shared ownership), we forecast market sales to account for 32% of revenues on average in our 2017-2019 base-case scenario (including revenue from shared-ownership), up from less than 6% over 2015-2016. This could subject Metropolitan's margins to more volatility. As a result, Metropolitan's non-traditional activities' revenues (including care, support and non-social lettings in addition of development for sale) are set to rise close to 50% of revenues in FY2019, from about 19% in FY2016.

Overall, we assess Metropolitan's debt profile as very strong. As a result of the £250 million bond issuance in 2015, debt stock increased by 8% in 2015/16, rising to about 14.9x adjusted EBITDA. Thanks to gradual improvement of adjusted EBITDA, we expect a decrease in debt to adjusted EBITDA at 9.6x in FY2019. We also foresee substantial increase in interest coverage standing at 2.4x in FY2019 from 1.3x in FY2016 and we continue to positively factor in Metropolitan's large unencumbered asset base of £1.1 billion at market value at the end of FY2016 (105% of debt stock).

### Liquidity

We continue to see Metropolitan's liquidity position as very strong. As of July 2016, we estimate that Metropolitan's sources of funding will cover its uses of funding by about 1.9x over the next 12 months, notably supported by £230 million of committed undrawn bank facilities, £100 million of retained bond proceeds, and £35 million of cash. We also believe that Metropolitan continues to benefit from satisfactory access to external liquidity, marked by its 2015 £250 million bond issuance and its continued access to a diversified pool of banks.

## Outlook

The stable outlook reflects our view that Metropolitan will maintain its very strong enterprise profile over the next 24 months, with sound operational performance, while being able to contain the negative effect of social rent decrease and maintain its adjusted EBITDA margins above 30%.

We could lower the rating on Metropolitan if we observed deterioration in the financial performance, with adjusted EBITDA margins falling below 30% owing to weakening cost control or inability to meet revenue target from shared ownership and open market sales. Under such a scenario, we would likely observe a worsening of the liquidity position and rising debt levels, which would prompt us to revise downward our assessment of Metropolitan’s financial profile.

Alternatively, we could raise the rating on Metropolitan over the next 24 months if we observed a substantial improvement in the financial performance, with adjusted EBITDA moving rather permanently within the 40%-50% range of turnover. Under such a scenario, we would likely observe additional cash generated used to pay down debt, thereby reducing debt to adjusted EBITDA below 10x on average.

However, we view both our upside and downside scenarios as unlikely at this stage.

## Social Housing Publication Table

| | --Fiscal year ended March 31st-- | | | | |
|---|---|---|---|---|---|
| **('000. £)** | **2015a** | **2016e** | **2017bc** | **2018bc** | **2019bc** |
| Number of units | 38,415 | 37,831 | 40,495 | 40,980 | 41,338 |
| Vacancy rates (% of net rental income) | 3.1 | 2.2 | 2.5 | 2.5 | 2.5 |
| Arrears (% of net rental income)* | 5.2 | 4.7 | 5.0 | 5.0 | 5.0 |
| Revenue | 230,365 | 234,897 | 259,300 | 332,700 | 412,500 |
| Share of revenue from non-traditional activities (%) | 20.9 | 19.2 | 25.0 | 40.5 | 50.8 |
| Operating expense | 145,415 | 154,228 | 169,500 | 219,800 | 283,300 |
| EBITDA§ | 92,603 | 73,577 | 81,400 | 109,400 | 126,800 |
| EBITDA/revenue (%) | 40.0 | 31.0 | 31.4 | 32.9 | 30.7 |
| Interest expense | 54,576 | 57,182 | 52,000 | 48,900 | 51,900 |
| Debt/EBITDA (x) | 10.6 | 14.9 | 13.0 | 10.2 | 9.6 |
| EBITDA/interest coverage (x)† | 1.7 | 1.3 | 1.6 | 2.2 | 2.4 |
| Capital expense | 121,162 | 112,441 | 191,900 | 238,500 | 290,600 |
| Debt | 979,982 | 1,094,785 | 1,054,700 | 1,111,300 | 1,217,800 |
| Housing properties (according to balance-sheet valuation) | 2,705,164 | 2,729,221 | 2,875,100 | 3,016,700 | 3,195,700 |
| Loan to value of properties (%) | 36.2 | 40.1 | 36.7 | 36.8 | 38.1 |
| Cash and liquid assets | 121,072 | 182,283 | 34,700 | 1,400 | 55,500 |

*Current arrears §Adjusted for capitalized repairs. †Including capitalized interest. a--Actual e--Estimate bc--Base case reflects Standard & Poor's expectations of the most likely scenario

## Related Criteria And Research

### Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions - March 25, 2015
- Criteria - Governments - General: Methodology For Rating Public And Nonprofit Social Housing Providers - December 17, 2014
- General Criteria: Group Rating Methodology - November 19, 2013
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating - October 01, 2010
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

### Related Research

- Ratings On The United Kingdom Lowered To 'AA' On Brexit Vote; Outlook Remains Negative On Continued Uncertainty - June 27 2016
- Metropolitan Housing Trust Long-Term Rating Lowered To 'A+' Following Downgrade Of The United Kingdom; Outlook Stable - July 4, 2016

## Ratings List

| | Rating | |
|---|---|---|
| | To | From |
| Metropolitan Housing Trust Ltd. | | |
| Issuer Credit Rating | | |
| Foreign and Local Currency | A+/Stable/-- | A+/Stable/-- |
| Senior Secured | | |
| Local Currency | A+ | A+ |
| Metropolitan Funding PLC | | |
| Senior Secured | | |
| Local Currency | A+ | 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. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public Web site 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.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.