

Research Update:

# U.K.-Based Housing Association Peabody Trust 'A-' Rating Affirmed; Outlook Stable

July 7, 2022

## Overview

- We anticipate that the merger of U.K. social housing provider Peabody Trust with Catalyst Housing, and refinancing at lower interest rates, will marginally strengthen Peabody's credit metrics compared with our previous forecast.
- In our view, Peabody Trust will likely develop fewer debt-funded new homes than we previously forecast while it invests in its existing homes, thereby mitigating the effect on the group's debt and interest coverage ratios.
- We project that increasing investment in the group's existing homes and rising inflationary pressure will continue to weigh on its financial performance.
- We affirmed our 'A-' long-term issuer credit rating on Peabody Trust. The outlook is stable.

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## Rating Action

On July 7, 2022, S&P Global Ratings affirmed its 'A-' long-term issuer credit rating on Peabody Trust. The outlook is stable.

At the same time, we affirmed our 'A-' long-term issuer credit ratings on Town & Country Housing Group and Catalyst Housing, because we consider them to be core subsidiaries of Peabody. We also affirmed the 'A-' issue ratings on the senior secured debt issued by Catalyst, TCHG Capital PLC, and Peabody Capital No 2 PLC, because we consider these two finance vehicles to be core subsidiaries of Peabody.

## Outlook

The stable outlook reflects our view that Peabody's rising investment in its existing homes will be mitigated by the steps it is taking to contain debt buildup and reduce the average cost of debt. We project that these steps would lead to a marginal strengthening of the group's credit metrics through to the financial year ending March 2025.

## **Downside scenario**

We could consider lowering the ratings on Peabody if inflationary cost pressures and higher-than-anticipated investments in the existing asset base reduced the group's adjusted EBITDA, which would bring down interest coverage ratios such that the adjusted non-sales EBITDA interest coverage remained below 1x. A downgrade could also follow if Peabody develops more debt-funded new homes than we currently assume, which could weaken the debt profile further. We could also lower the ratings if we assessed that the likelihood of support from the government had lessened.

## **Upside scenario**

We could upgrade Peabody if the group sustainably strengthens its credit metrics through solid cost management while containing the debt funding of new developments. An upgrade would depend on the group's adjusted EBITDA margins sustainably strengthening to more than 20%, the non-sales EBITDA interest coverage staying above 1.25x, and a material reduction of the debt/non-sales EBITDA ratio, all else being equal.

## **Rationale**

The affirmation reflects our view that Peabody benefits from operating in the predictable and countercyclical social housing sector. The group has a strong market position in its main areas of London and the Southeast of England, supported by general needs rents that are less than 50% of the prevailing market rent. It also benefits from low vacancy rates that--at 1.3%, on average, over the past three years--are somewhat lower than the English social housing sector average. We consider that as a large provider of social housing, with more than 104,000 units, Peabody could withstand external shocks better than a smaller entity.

We project increasing investment in the group's existing homes and rising inflationary pressures would keep the group's financial performance weaker than many peers, partly due to its policy to maintain low rents for its tenants. We understand that Peabody is focusing on fire and building safety in the near term, as well as making its homes more energy efficient. Furthermore, we think that cost inflation could exceed rent increases, which will continue to pressure the group's S&P Global Ratings-adjusted EBITDA margins, which are likely to remain below 20% through our forecast period to the financial year ending March 31, 2025.

We consider that despite continued pressure on Peabody's adjusted EBITDA, steps taken by management over the past year as part of the merger with Catalyst--which completed on April 1, 2022--will strengthen the group's credits metrics. Over the past year, the group has repaid high-coupon debt while issuing a £350 million bond with a 2.75% coupon, thereby lowering its average interest costs. We also understand that Peabody is developing fewer new homes than we had expected while focusing on investing in its existing homes, and therefore forecast that debt buildup will be more contained than we previously assumed. We forecast that Peabody's adjusted non-sales EBITDA interest coverage would increase toward 1x and the adjusted debt/non-sales EBITDA ratio reduce to less than 30x by the financial year ending March 31, 2025.

We think that Peabody's reduction of its development plan implies that the group is mindful of its overall capacity during a period of increasing inflation and higher investment in the existing homes. We understand that Peabody's strategy to focus on strengthening the quality of the asset base in line with new standards on fire and building safety, while making the homes more energy

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efficient. More than 75% of the stock already meets Energy Performance Certificate C standards, with Peabody aiming to meet 100% by 2030. We view positively that Peabody continues to contain the group exposure to sales risk to less than 25% of the adjusted operating revenues.

We believe there is a moderately high likelihood that Peabody would receive timely extraordinary government support in the case of financial distress. This provides two notches of uplift from the stand-alone credit profile. As one of the Regulator of Social Housing's (RSH's) key goals is to maintain lender confidence and low funding costs across the sector, we believe it is likely that the RSH would step in to try and 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 Peabody.

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

### Liquidity

Peabody's liquidity position is very strong, with sources covering uses by 2.1x in the next 12 months. We also consider that Peabody has strong access to external funding when needed.

Liquidity sources include:

- Cash and cash equivalents of £110 million;
- Our forecast of cash from operations of close to £320 million, adding back the noncash cost of sales;
- Proceeds from asset sales of more than £220 million;
- Available facilities maturing beyond the next 12 months of close to £1,400 million; and
- Grant funding and other inflows exceeding £95 million.

Liquidity uses include:

- Capital expenditures, including spending on units for sale, exceeding £800 million; and
- Interest and principal repayments of more than £180 million.

### Key Statistics

Table 1

#### Peabody Trust--Key Statistics

Mil. £	--Year ended March 31--				
	2021a	2022e	2023bc	2024bc	2025bc
Number of units owned or managed	101,061	104,596	106,454	107,541	109,210
Adjusted operating revenue	911.2	939.4	1035.7	1026.3	1153.3
Adjusted EBITDA	213.1	152.2	162.4	165.8	227.8
Non-sales adjusted EBITDA	190.1	125.5	137.6	154.2	187.0
Capital expense	467.0	613.0	820.9	756.4	815.5
Debt	4160.0	4398.4	4627.6	4879.7	5157.5

Table 1

**Peabody Trust--Key Statistics (cont.)**

Mil. £	--Year ended March 31--				
	2021a	2022e	2023bc	2024bc	2025bc
Interest expense	149.9	151.0	163.6	170.3	178.0
Adjusted EBITDA/Adjusted operating revenue (%)	23.4	16.2	15.7	16.2	19.8
Debt/Non-sales adjusted EBITDA (x)	21.9	35.0	33.6	31.6	27.6
Non-sales adjusted EBITDA/interest coverage(x)	1.3	0.8	0.8	0.9	1.1

a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

**Ratings Score Snapshot**

Table 2

**Peabody Trust--Ratings Score Snapshot**

	Assessment
Enterprise risk profile	3
Industry risk	2
Regulatory framework	3
Market dependencies	1
Management and Governance	4
Financial risk profile	4
Financial performance	5
Debt profile	6
Liquidity	2

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**

- 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 'AA/A-1+' Ratings Affirmed; Outlook Stable, April 22, 2022
- U.K. Social Housing Sector Borrowing Needs To Rise To Fund Investment In New Homes, March 31, 2022
- Social Housing Outlook 2022: Green Agenda Takes Root In Investment Plans, Nov. 23, 2021
- How U.K. Public Finance Sectors Fare Under Latest Spending Review, Nov. 11, 2021
- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers, June 8, 2021

## Ratings List

### Ratings Affirmed

#### Peabody Trust

#### Town & Country Housing Group

#### Catalyst Housing Ltd.

Issuer Credit Rating	A-/Stable/--
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#### Catalyst Housing Ltd.

Senior Secured	A-
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#### Peabody Capital No 2 PLC

Senior Secured  U^	A-
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#### TCHG Capital PLC

Senior Secured	A-
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|U^ Unsolicited ratings with issuer participation, access to internal documents and access to management.

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](http://www.standardandpoors.com) for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at [https://www.standardandpoors.com/en\\_US/web/guest/article/-/view/sourceId/504352](https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352) Complete ratings information is available to subscribers of RatingsDirect 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.standardandpoors.com](http://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; or Stockholm (46) 8-440-5914

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