FitchRatings

Fitch Affirms Places for People Group at 'A'; Outlook Stable

Fitch Ratings - London - 16 December 2019:

Fitch Ratings has affirmed Places for People Group Limited's (PfPG) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) at 'A'. The Outlooks are Stable. Simultaneously Fitch has affirmed the 'A' long-term ratings on the senior secured and unsecured bonds issued by PfPG's subsidiaries Places for People Treasury plc, Places for People Homes Limited, Places for People Capital Markets plc and Places for People Finance plc.

Key Rating Drivers

PfPG is a social housing registered provider (RP). Fitch rates RPs in England under its Revenue Supported Rating Criteria, and takes into account such factors as revenue defensibility, operating risk and the RP's financial profile assessment. We incorporate public support factors, notably the strong predictability of the RP's cash flow through direct and indirect government funding. Fitch also applies its Government-Related Entities (GRE) Criteria, whereby we assess RPs in England as non-credit-linked entities and apply a one-notch uplift to the standalone ratings. This reflects the assessment of strength of linkage and incentive to support factors. As a consequence, RPs' ratings do not automatically move in line with those of the UK sovereign.

PfPG's standalone 'A-' rating reflects the following rating factors:

Revenue Defensibility: Strong

Fitch assesses Revenue Defensibility, which covers demand and pricing, overall as strong. Demand for social housing remains strong, and any change in the rents that RPs are allowed to charge would be unlikely to materially affect demand. The regulatory regime aims to maintain compensation for services at a level consistently supporting solvency for not-for-profit RPs, considered an essential public service. On the core business aspect of operations, RPs have limited revenue flexibility, as the UK government determines social housing rent rises. Since April 2016, rents have been reduced by 1% per year. On 4 October 2017, it was announced that rents would return to the consumer price index (CPI) plus 1% for the five years from 1 April 2020. However, due to the increasing share of revenue from non-social housing activity, RPs have been gaining more flexibility to collect enough revenue to cover all costs.

Operating Risk: Strong

Operating Risk covers operating costs and resource management. Overall Fitch assesses this factor as strong for PfPG. PfPG has well-identified and consistent cost drivers, and low potential volatility in major expenses. PfPG has material capex in its development plans in the medium term, but has opportunities to slow down committed schemes, defer uncommitted schemes or switch tenure from sale to market rent, or vice-versa. Additionally, in the event of financial stress, PfPG can curtail some discretionary expenditure, or spending on non-essential major works and improvements, or sell some of its commercial assets.

Regarding resource management risk, due to its size and geography of operations Fitch believes that PfPG is capable of mitigating supply constraints for labour or resources. The main implications of Brexit for the sector will be continued uncertainty, and short- to medium-term turbulence in the financial and housing markets. This may lead RPs to delay any planned bond issuances, and put pressure on refinancing. The depth of the impact of Brexit on RPs' business plans will depend on its ultimate nature and timing. However, PfPG has undertaken significant work to assess Brexit's potential impact on the UK economy, public finances, political continuity and its supply chain and factored this into its stress testing.

PfPG has stress-tested and run multi-variable scenarios for its business plan. In general, throughout the stress tested business plan interest cover and gearing covenants are met, albeit with decreased headroom. In some scenarios, where multiple risks materialise at once, interest cover could be breached, but only when no corrective measures are taken, which is unlikely. Fitch will continue to monitor PfPG's resilience and assess its ability to overcome possible further turmoil. We will also closely review the robustness of the stress testing relative to its ratings, including the impact of the Brexit on its business plan, and assess PfPG's flexibility to adapt to market conditions.

Financial Profile: Strong

Fitch believes PfPG is showing good performance, despite the challenges that have affected the sector over recent years. Continued high demand for social and affordable housing, cost-efficiency measures and increased diversification into non-core business should allow PfPG to maintain sufficient revenue to service debts and cross-subsidise its core business.

Derivation Summary

PfPG's ratings reflect continuing high demand for social housing in the UK and continued cash flow from rented properties. They also factor in PfPG's secured cash flow from public funds and the control and regulation provided through the Regulator of Social Housing (RSH). At 31 March 2019, PfPG owned or managed more than 197,700 housing units (including 66,000 social and affordable), which ranks PfPG among the largest RPs in England.

The ratings also reflect PfPG's moderate debt level, with stable debt metrics and strong liquidity, which we expect to remain stable, despite the sizable development plan to deliver around 8,500 units within the next three years. The ratings also reflect the one-notch uplift that we apply to PfPG's standalone ratings, driven by the application of the GRE Criteria and Fitch's assessment of four factors under the strength of linkage and incentive to support.

The Stable Outlook reflects Fitch's view that PfPG will continue to show satisfactory performance, despite the weakened operating environment and increased challenges faced by RPs in England. The impact of Brexit on the sector, although still uncertain, appears less significant than on other public finance sectors, although the possible consequences have been factored into PfPG's stress tests. The RSH continues to provide strong oversight.

Key Assumptions

We expect PfPG's satisfactory performance to continue, aided by the economics of scale due to its size and area of operations, supported by the recent mergers. Profits from the market sale units will be re-invested in the RP to continue to build and provide affordable social units. Although the share of non-social housing activity is expected to peak in FYE20-FYE21 at 66% from 57% in FYE19 of total turnover, in the medium term around 40% of the turnover will continue to come from social housing lettings and sales.

PfPG developed or acquired more than 1,870 units in FYE19 (FYE18: 2,090) and it aims to develop around 8,500 units over the next three years. This will comprise different tenures, across the UK, many of which will be developed in partnerships with others, allowing PfPG to share exposure to development risk with other entities.

In its rating case scenario, Fitch expects PfPG's turnover to increase to about GBP900 million in FY20-24, with the operating surplus averaging a high of GBP200 million-GBP250 million a year. Direct risk (debt and financial leases) is expected to increase to about GBP3.5 billion by FYE24 following investments. However, net direct risk to Fitch-calculated EBIDTA is likely to remain below 12x (FYE19: 10.4x) and in line with the lower end of 'A' category peers. In FYE19, PfPG reported GBP827 million of turnover (FYE18: GBP754 million) and an operating surplus of GBP201 million. Direct risk at FYE19 was GBP3.0 billion (FYE18: GBP2.9 billion).

Under Fitch's GRE criteria, we assess status, ownership and control as Strong, support track record and expectations as Moderate and the socio-political implications of default as Moderate and the financial implications of default as Weak. This gives a total score of 12.5, leading to a bottom up + 1 under the Notching Guideline Table.

RATING SENSITIVITIES

The standalone ratings could be downgraded if there is further pressure on the sector, or on PfPG as a result of the negative operating environment in the UK

The ratings could also be downgraded in the event of:

- Greater pressure on headroom on existing interest cover and gearing covenants.

- Increased volatility in operating revenue as a result of higher exposure to development activities and a significant increase in gearing and net direct risk/Fitch calculated EBITDA ratios, of above 12x.

Conversely, the IDRs could be upgraded if the net adjusted debt to Fitch-calculated EBIDTA declines towards 10x, on a sustained basis.

The UK sovereign is on Rating Watch Negative, and in the event of a further downgrade Fitch may re-assess the impact that the sovereign credit metrics weakening would have on the RP's standalone credit profiles, notching uplift and ratings relativity.

Liquidity and Debt Structure

PfPG's board and management follow a prudent approach to risk and debt. The debt repayment profile is overall very long-term and smooth, which mitigates repayment pressure. There is a peak refinancing need in FYE26 as around 16% of debt stock outstanding at FYE19 will mature. However, we do not expect PfPG to have problems refinancing the maturing debt, given that it has the capacity to generate surpluses, as well as good access to the capital markets, with high value assets on its balance sheet. PfPG's Treasury Policy was amended in 2017 and is reviewed annually, and requires cover for 12 months approved cash flow plus 25% sales contingency. However, on average the issuer maintains up to 18 months of committed liabilities cover.

Fitch expects that PfPG's debt will continue to increase to fund capital expenditure on development programmes. However, Fitch believes that PfPG's recourse to debt will not be significant, as the majority of capital expenditure is likely to be financed with own sources, mainly proceeds from sale of units, supported by profits from property management services. PfPG became a strategic partner of Homes England (HE) in July 2018, releasing grant funding of over GBP70million to develop affordable 2,600 homes.

ESG Considerations

The ESG credit relevance score is '3', meaning that ESG issues are credit neutral. The issuer's mission and institutional framework mean that these issues are minimally relevant to the rating.

RATING ACTIONS

ENTITY/DEBT	RATING		PRIOR
Places for People Capital Markets plc			
senior unsecured	LT A Affirmed		A
Places for People Group Limited	LT IDR A ⭘ Affirmed		A ⭘
	ST IDR F1+ Affirmed		F1+
	LC LT IDR A ⭘ Affirmed		A ⭘
	LC ST IDR F1+ Affirmed		F1+
Places for People Finance plc			
senior unsecured	LT A Affirmed		A
Places for People Homes Limited			
senior unsecured	LT A Affirmed		A
senior secured	LT A Affirmed		A
Places for People Treasury plc			
senior unsecured	LT A Affirmed		A

Additional information is available on www.fitchratings.com

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Applicable Criteria

Short-Term Ratings Criteria (pub. 02 May 2019)
Government-Related Entities Rating Criteria (pub. 13 Nov 2019)
Public Sector, Revenue-Supported Entities Rating Criteria (pub. 07 Nov 2019)

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