MOODY'S
PUBLIC SECTOR EUROPE

CREDIT OPINION
11 December 2017

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RATINGS

Moat Homes

Domicile	United Kingdom
Long Term Rating	A2
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Moat Homes

Update to credit analysis

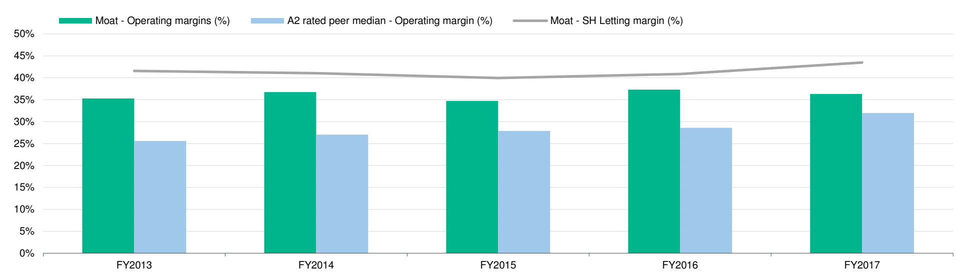
Summary

The credit profile of Moat Homes (A2 stable) reflects its healthy margins, ample social housing interest coverage and modest levels of debt. The rating also takes into account Moat's forecast increase to market sales exposure and anticipated rise in debt to fund its development programme. In addition, Moat's A2 rating benefits from the strong regulatory framework governing English housing associations and our assessment that there is a strong likelihood that the UK government (Aa2 stable) would intervene in the event that Moat faced acute liquidity stress. Moat is rated at the upper end of Moody's-rated English housing associations, whose ratings span from A1 to Baa2.

Exhibit 1

Moat has benefited from a consistently stronger operating margin over its peers, driven by a strong margin on their core social housing business.

Operating margin (%) and social housing letting margin (%)



Note: FY2015 and FY2016 have been restated in FRS102 format.
Source: Moat and Moody's

Credit Strengths

» Strong margins and Social Housing Letting Interest Coverage (SHLIC) metrics

» Medium-sized association with a straightforward structure

» Strong regulatory framework

Credit Challenges

» Projected increase in exposure to riskier market sale activity

» Debt levels expected to rise from relatively low base

» Operating environment remains challenging but policy is more stable

Rating Outlook

The stable outlook on Moat reflects the currently stable operating environment, which is unlikely to undergo further material change in the medium-term, and the stable outlook on the sovereign rating.

Factors that Could Lead to an Upgrade

Positive pressure on the rating could result from one or a combination of the following; reduced exposure to market sale activities, maintenance of a healthy operating margin and Social Housing Letting Interest Coverage (SHLIC) rising to, and remaining at or above, 1.9x

Factors that Could Lead to a Downgrade

Downward ratings pressure would be prompted by further deterioration of the UK sovereigns' creditworthiness. Additionally, any sector or issuer-specific risks emerging in this context would exacerbate downward ratings pressures. Negative pressure could be exerted on the rating by one or a combination of following; a deterioration of Social Housing Letting Interest Coverage (SHLIC) ratio in relation to peers, persistent weakness in the Cash Flow Volatility Interest Coverage (CVIC) ratio, weakening of the liquidity position, and increased reliance on shared ownership and outright sales above current levels. In addition, a weaker regulatory framework, a dilution of the overall level of support from the UK government or a downgrade of the UK sovereign rating would also exert downward pressure on the rating.

Key Indicators

Moat Homes

	31-Mar-13	31-Mar-14	31-Mar-15	31-Mar-16	31-Mar-17	31-Mar-18*	31-Mar-19*
Units under management (no.)	20,951	20,922	21,115	21,321	21,107	21,374	21,749
Operating margin, before interest (%)	35.3	36.7	34.7	37.3	36.3	30.0	27.3
Net capital expenditure as % turnover	39.9	53.4	55.1	36.9	49.1	89.4	81.1
Social housing letting interest coverage (x times)	1.8	1.6	1.5	1.7	1.8	1.9	1.6
Cash flow volatility interest coverage (x times)	2.1	2.3	1.7	2.6	2.4	1.7	1.6
Debt to revenues (x times)	3.7	3.9	3.7	3.6	3.5	4.6	4.4
Debt to assets at cost (%)	30.8	31.6	32.1	32.6	31.2	38.1	42.4

*FY2018 and FY2019 are forecasted figures.
Note that FY2015 and onwards are prepared in FRS102 format while prior years were prepared using the old UK GAAP.
Source: Moat and Moody's

Detailed Rating Considerations

The credit profile of Moat, as expressed in an A2 stable rating, combines (1) a baseline credit assessment (BCA) of a3, and (2) a strong likelihood of extraordinary support coming from the national government in the event that the entity faced acute liquidity stress.

Baseline credit assessment

SOLID SOCIAL HOUSING LETTING INTEREST COVERAGE AND STRONG MARGINS

Moat benefits from continued strong interest coverage metrics with social housing letting interest coverage (SHLIC) at 1.8x in FY2017, in-line with the A2 peer median. Moat's cash interest coverage reached 2.9x this year, above A1 peer median of 2.7x, and has remained consistently above 2.0x since FY2012. Moat's Cash Flow Volatility Interest Coverage (CVIC) ratio was 2.4x in FY2017, and is forecast to decrease to 1.7x in FY2018, falling below Moody's-rated peer median (in FY2017) of 2.2x. This is driven by an upswing in development for sale leading to volatility in operating cash flow (CFO). Current business plan forecasts show Moat's CVIC returning to 1.7x in FY2018 and remaining at this level up to 2020. A key credit driver will be how effectively Moat can achieve CVIC levels closer in-line with peers throughout their proposed development programme.

Moat's total revenue stayed at £121 million in FY2017 (2016: £121 million), while operating margins declined slightly to 36%. Despite this decline, Moat's operating margins remain amongst the highest of Moody's rated peers, comparing favourably to an A2-rated peer median of 32%, because they are supported by Moat's core social housing letting business, which recorded margins of 43% this year (Exhibit 1). Total operating margins are forecast to continue a downward trend to reach 30% in FY2018, driven by losses of 12% from other social housing activity. Moat's business plan for FY2018-22 projects operating margins will fall closer to the peer median in FY2018 and FY2019, as interest expenses increase to service rising debt.

MEDIUM-SIZED ASSOCIATION WITH A STRAIGHTFORWARD GOVERNANCE STRUCTURE

Moat is a medium-sized provider of social housing in England, with around 21,000 units under management. Located in the south east of England, Moat operates in areas where demand for social housing is high, supporting social housing letting turnover stability. Moat has achieved an asset management plan target to further consolidate operations to 30 key local authority areas, identified as "growth areas", as Moat works to achieve operational efficiencies.

Moat Homes Limited is a charitable registered provider and the asset holding parent of the group. While there are currently six subsidiaries, two of these are dormant and one has been discontinued. The remaining three include Moat Foundation, a charitable arm that focuses on supporting community development activities, Moat Housing Group Limited (MHG), a non-charitable registered provider set up for the development of homes for market sale, and the group's financing vehicle named Moat Homes Finance PLC. The parent effectively retains control and oversight over the group.

Social housing letting as a percentage of Moat's turnover grew slightly from last year to 79% (FY2016: 77%), and is in line with Moody's A2 rated peers (78% in FY2017). Moat's business plan forecasts social housing letting will deliver 81% of turnover in FY2018, before dropping to 71% in the subsequent year. As Moat plans to increase development with an element of sale, including first-tranche shared ownership and outright sale, turnover from social housing letting is expected to fall to 50% of total turnover in FY2020.

PROJECTED INCREASE IN EXPOSURE TO RISKIER MARKET SALE

With sales revenues at 19% of turnover in FY2017 (currently consisting only of first tranche shared ownership (FTSO) sales), we consider Moat's exposure to the cyclical property market as high relative to peers. Although this is set to reduce to 16% in FY2018 during a period of construction, the business plan forecasts that sales revenue as a proportion of turnover would grow to 28% in FY2019 and 48% in FY2020. Moat has delivered shared ownership development for several years, considering itself to be a sector specialist, and the receipts from the FTSO sales are set to make up the largest proportion of sales revenues up to FY2019. Moat had no outright market sales this year and are not forecasting any in FY2018. However, the development programme aims to deliver five units for market sale in FY2019, and 120 units in the subsequent year, contributing 5% and 35% to total turnover, respectively, and surpassing the contribution to revenue made by FTSO sales in FY2020. The increasing trend in market sales (FTSO and outright sale combined) as a proportion of revenue is a continuation from last year's business plan, which aimed to have 30% of revenue sourced from market sales by FY2020. Given that social housing lettings receipts are far more predictable than those generated from market sales, this exposure will be a key credit challenge for Moat.

Moat's experience in the shared ownership market is demonstrated by both the proportion of turnover from FTSO sales (19% in FY2017) as well as the 31% margin on these sales. However it is noted that operating margins on FTSO sales decreased from FY2016 levels of 41%, and are forecast to decrease further in FY2018 to 20%. Moat's FY2018-FY2022 development pipeline plans for approximately 2,780 units, of which shared ownership would make up 54% of the tenure mix, 27% allocated as sub-market affordable rent, 6% as market rent and 13% as outright sales. The strength of Moat's core social housing business will partially mitigate some of the risks associated with market sales activity. Historically, Moat have used conservative assumptions in long term business planning, which incorporated layers of contingency and helped mitigate market sales risk further. The current Long Term Plan (LTP) states that contingency areas have been minimised as to properly assess development capacity and forecast performance, while still retaining a prudent approach to assumptions. Currently, Moat's business plan assumptions can be considered overall realistic, such as CPI at 2.8% in FY2018 and a return to social rent growth in FY2020, however Moat's assumption on house price inflation at 3.5% in FY2018 are currently over national and regional (South-East) forecasts.

Net capital expenditure (capex) as a percentage of turnover was 49% in FY2017 and is forecast to rise to 89% in FY2018, driven by planned development and a significant regeneration project. Moat's liquidity is sufficient to cover this rise in expenditure, however, as measured by Moody's liquidity metric, Moat's position in FY2017 was somewhat weaker than peers. Moody's liquidity coverage metric measures the ability of available liquidity to cover the following two years of net capex. Due to the anticipated rise in net capex in FY2018 and FY2019, Moat's liquidity coverage ratio as of March 2017 was 0.75x. However, net capex is projected to decrease in FY2020, contingent on sales revenues materialising as expected and an uplift to cash flows. The reduction in net capex combined with the availability of facilities leads to an expected improvement in the liquidity coverage metric to 1.04x in FY2018 and 1.20x in FY2019.

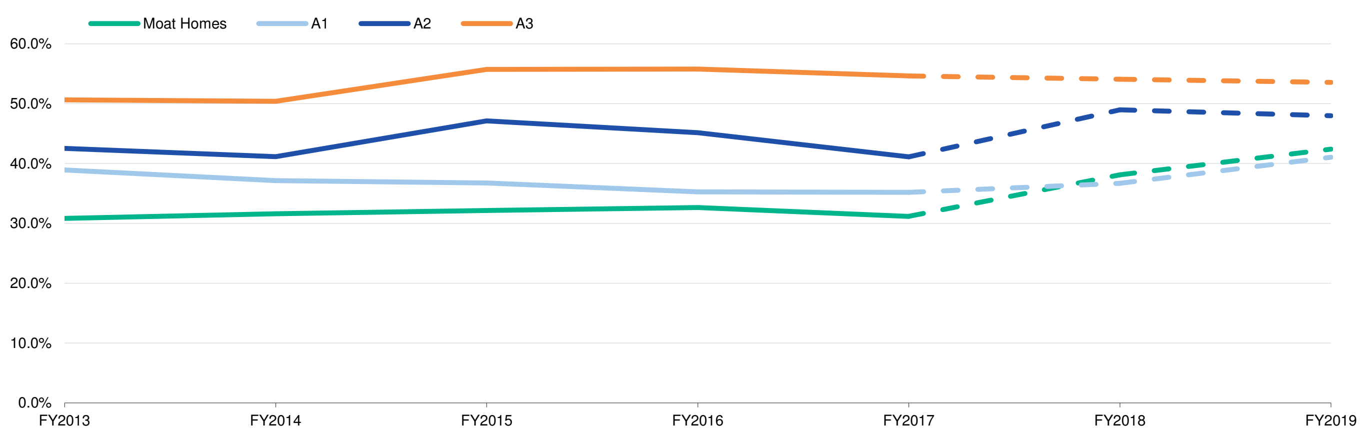
Moat Homes Group Limited (MHG) will act as the group's commercial subsidiary overseeing outright sales activity. The subsidiary has four non-executive board members with expertise in property development that monitor activity on a scheme by scheme basis. In FY2017 MHG made a loss of £108,000, as there were no outright sales made. Moat is currently assessing the option of building reserves in MHG through its future operations, instead of the subsidiary gift aiding profits to the parent (MHL).

DEBT RISING, BUT FROM A RELATIVELY LOW BASE

At FY2017, Moat's debt was £428 million, equivalent to 3.5x revenues or 31% of assets at cost, which is in line with their debt position in the previous year. The business plan anticipates that debt will grow by 25% or approximately £110 million in FY2018, which would be equivalent to 4.6x forecast FY2018 revenues or 38% of assets at cost. Moat has historically performed better on debt metrics than A2 rated peers, a credit strength (Exhibit 3), but are forecast to deteriorate going forward, weakening from a strong position. While we expect Moat to take on additional debt over the next five years, with debt-to-assets reaching 44% by FY2020, the organisation will retain sufficient headroom against covenants.

Moat's treasury policy allows for 60-90% debt to be at a fixed rate, and as of end of February 2017 Moat held approximately 80% of its debt at fixed rates. Included in the fixed rate debt is a portfolio of stand-alone swaps with a notional value of £143 million, and a mark-to-market valuation of £75.4 million as of 8th March 2017, which is covered by a combination of security and cash. We consider this as moderately high exposure to interest rate risk, mitigated however by estimated liquidity of close to 140% of projected FY2018 revenues, well above the 97% average of Moody's rated portfolio. Furthermore, total unencumbered assets would allow for more than £410 million of additional borrowing.

Exhibit 3
Moat's debt metrics are forecast to weaken from a historically strong position
Debt-to-assets (%)



* FY2018 and FY2019 are forecasted figures.
Note that FY2015 and onwards are prepared in FRS102 format while prior years were prepared using the old UK GAAP.
Source: Moat and Moody's

STRONG REGULATORY FRAMEWORK

The sector's credit quality will continue to benefit from the strong regulatory framework and oversight by the Homes and Communities Agency (HCA). The HCA maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and undertaking In-Depth Assessments of entities where deemed necessary. Additionally, the HCA has powers to make board member and manager appointments where there has been a breach of Regulatory Standards. From October 2017, the HCA will charge fees for social housing regulation, as a means of enhancing the independence and maintaining the effectiveness of the regulator.

OPERATING ENVIRONMENT REMAINS CHALLENGING BUT POLICY IS MORE STABLE

Moody's does not expect additional material adverse policy shifts for the sector and considers the operating environment to be stable in the medium term. Adverse policies announced in the last few years will continue to negatively impact revenues, especially the effects of the 1% annual decrease in social rents (until FY2020) and Universal Credit (a pillar of broader welfare reform measures). However, HAs have demonstrated resilience to adverse policies to date and been proactive to mitigate the impact. A reduction of capital grant for new social housing over the last five years has led to increased exposure to market sales activity, which has more than doubled since 2012 to reach 17% of turnover for Moody's rated HAs in FY2016. Credit risk association with exposure to market sales is incorporated in BCAs.

Extraordinary Support Considerations

The strong level of extraordinary support factored into the rating reflects the wide-ranging powers of redress available to the regulator in cases of financial distress, with the possibility of a facilitated merger or a transfer of engagements. Recent history has shown that the UK government (Aa2 stable) is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors increasing exposure to non-core social housing activities in the sector, that add complexity to HA operations, and the weakening of the sovereign's financial resilience, making an extraordinary intervention slightly more challenging. In addition, our assessment that there is a very high default dependence between (HA) and the UK government reflects their strong financial and operational linkages.

Rating Methodology and Scorecard Factors

European Social Housing Providers, July 2016 (190944)

Government Related Issuers, August 2017 (1047378)

Ratings

Exhibit 4

Category	Moody's Rating
MOAT HOMES	
Outlook	Stable
Issuer Rating -Dom Curr	A2
MOAT HOMES FINANCE PLC	
Outlook	Stable
Senior Secured -Dom Curr	A2

Source: Moody's Investors Service

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CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

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