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CREDIT OPINION
30 October 2023

Update

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RATINGS

Moat Homes

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

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 (United Kingdom)

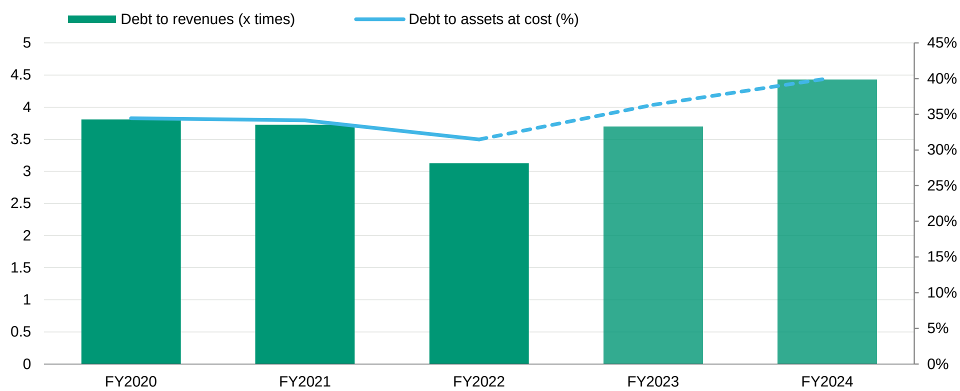
Update following affirmation of A2 negative

Summary

The credit profile of Moat Homes (Moat, A2 negative) reflects its good financial performance, strong liquidity and a straightforward organisational structure. The rating also takes into account Moat's increase in debt levels and weakening interest coverage metrics. Moat's A2 rating benefits from the supportive institutional framework for English housing associations (HAs) and our assessment that there is a strong likelihood that the government of the United Kingdom (UK, Aa3 stable) would intervene in the event that Moat faced acute liquidity stress.

Exhibit 1

Debt to revenue and gearing (debt to assets) are expected to weaken sharply due to rising development and asset management expenditure



Fiscal years ended March 2023 and 2024 (FY2023 and FY2024) are forecasted figures.
Source: Moat and Moody's Investors Service

Credit Strengths

» Decent track record of financial performance and reducing exposure to market sales

» Simple governance structure which supports effective risk management

» Supportive institutional framework in England

Credit Challenges

» Increasing debt levels and weakening debt metrics

» Weakening interest coverage metrics

Rating Outlook

The negative outlook reflects Moat's high capital expenditure and projected deterioration of debt metrics, which may weaken its financial performance considering elevated inflation and high interest rates.

Factors that Could Lead to an Upgrade

Rating upgrade is unlikely given the negative outlook. The negative outlook could be changed to stable if Moat is able to maintain relatively stable debt metrics over the medium term.

Factors that Could Lead to a Downgrade

Downward pressure on the rating could result from a significant sustained weakening in operating margins and interest coverage ratios, material increases in debt levels beyond that currently anticipated, a significant deterioration in liquidity or a significant scaling up in market sales exposure beyond what is planned. A weakening of the regulatory framework or dilution of the overall level of support from the UK government could also lead to downward pressure on the ratings.

Key Indicators

Exhibit 2

Moat Homes

	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23 (F)	31-Mar-24 (F)
Units under management (no.)	20,258	20,472	20,803	21,097	21,433	21,553	22,260
Operating margin, before interest (%)	34.1	28.9	27.0	30.6	27.3	26.9	28.9
Net capital expenditure as % turnover	69.9	80.2	59.5	26.4	11.6	44.4	73.5
Social housing letting interest coverage (x times)	2.1	1.8	1.7	1.9	1.6	1.7	1.4
Cash flow volatility interest coverage (x times)	0.7	0.6	1.5	2.4	2.5	2.4	1.2
Debt to revenues (x times)	3.7	3.9	3.8	3.7	3.1	3.7	4.4
Debt to assets at cost (%)	31.0	33.8	34.4	34.2	31.5	36.3	40.0

Fiscal year ended March 2023 and 2024 (FY2023 and FY2024) are forecast figures.
Source: Moat and Moody's Investors Service

Detailed Rating Considerations

On 25 October 2023, Moody's affirmed Moat's ratings and maintained its negative outlook. The affirmation followed Moody's change in outlook of the Government of the United Kingdom's Aa3 rating to stable from negative on 20 October 2023.

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

Baseline credit assessment

Decent track record of financial performance and reducing exposure to market tenures

Moat has a history of achieving good operating margins, with an average of 28% over fiscal 2020 to 2022, compared with an A2 peer median of 24%. This is mainly due to very strong margins on social housing lettings of 40% over the same period, as margins on market sales (including first tranche shared ownership) have been weaker - at an average of 14%. Moat projects strengthening operating margins over the next few years, however we consider this will be challenging to achieve considering Moat's still substantial expenditure remaining on building safety (although around half of this expenditure will be capitalised) in addition to a capped social rent increase at 7% in fiscal 2023 and a housing market downturn. Moat's reliance on revenues from market tenures will decrease substantially however - reducing from 35% of turnover in fiscal 2022 to 10% in fiscal 2024 - reducing its exposure to volatile returns. The market sales exposure over the next three years is mainly driven by shared ownership, with the sales margin (incorporating both shared ownership and outright sales) expected to be at an average of 12%, relative to the previous three-year average of 14%, driven by a reduction in expected margins on shared ownership, as a result of higher competition and costs for securing land, particularly as Moat is shifting more towards land-led development.

Simple governance structure which supports effective risk management

Moat is a medium-sized provider of social housing in the south east of England, with just over 21,000 units under management. Moat has a very straightforward organisational structure. Moat Homes Limited is a charitable registered provider and the asset holding parent of the group, with two active subsidiaries: 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 - Moat Homes Finance PLC. The parent retains control and oversight over the group. There is one group board which determines the risk appetite of the group on an annual basis and controls risk management.

Supportive institutional framework in England

The sector's credit quality will continue to benefit from the strong institutional framework governing English housing associations (HAs) reflected in an Operating Environment score of a3 and a Regulatory Framework score of a1. These scores are assigned at a national level and reflect the following credit considerations:

The regulator maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and by undertaking biennial In-Depth Assessments (IDAs) for large and complex HAs. The regulator has a strong track record of intervention in cases of mismanagement or financial stress with powers to provide financial assistance and/or make manager appointments where there has been a breach of regulatory standards.

The operating environment for English HAs remains supportive. Demand for social housing remains very high and the government has committed to increased capital grant on more flexible terms for new social housing. English HAs retain some expenditure flexibility and have a track record of reducing costs to mitigate lower income.

However, due to presently very high rates of inflation, the government has intervened on social rent policy with a 7% ceiling on social rent increases to be implemented from April 2023 for one year. The ceiling of 7% will likely result in an adverse differential between rental income and cost growth, driving lower margins and interest coverage. The intervention introduces policy volatility to the sector as the ceiling will supersede the allowable increase of consumer price inflation (CPI) plus 1% under the current rent standard, which is in place until March 2025.

Increasing debt levels and weakening debt metrics, driven by capex requirements on development and asset management

Moat's total debt levels are expected to increase to fund its asset management and development commitments. Although it has now reduced its development ambitions over the longer term, with development planned to reduce to 450 units from fiscal 2025, over the next two years it still plans to develop around 650 units per year, up from 550 in its previous business plan. In its most recent business plan debt is projected to increase from £567 million as of fiscal year end 2022, to £802 million by fiscal year end 2025 - an increase of 44%. This would result in weakening debt metrics with debt to assets increasing to 42% by fiscal 2025 from 31% in fiscal 2022, and debt to revenues to 4.8x in fiscal 2025 from 3.1x in fiscal 2022. However, we consider that Moat's debt projections are generally very conservative and this pace and extent of debt growth is unlikely - over the past few years actual debt growth has been well below projected levels. For example, its 2020 business plan it projected total debt to be £661 million by fiscal 2022, whereas the actual figure was nearly £100 million less at £567 million. In addition, Moat - to be prudent - has assumed that it needs to repay capital grants on shared ownership staircasing, requiring financing, however to date it has always signed agreements with Homes England to enable them to recycle this grant into new schemes.

In addition to development, Moat also has large capital expenditure requirements on fire and building safety, building quality and decarbonisation. Fire safety costs are expected to be around £45 million over the next ten years - however, this estimate may also be conservative as more intrusive surveys are demonstrating that less work needs to be undertaken. Decarbonisation needs are estimated at around £175 million to 2030, although these estimates are relatively uncertain being at an early stage of preparation. Approximately 70% of its housing stock is at EPC-C or above, which is in line with the majority of the rated sector.

With regards to Moat's debt structure, its treasury policy allows for 60-90% of debt to be at a fixed rate and as at March 2022, Moat held 71% of its debt at fixed rates, before hedging. Moat has maintained the notional value of £143 million of its stand-alone swap portfolio, which had a mark-to-market valuation of approximately £6 million as of March 2022, with all of the swaps covered by property and cash. Moat's unencumbered assets position is strong, and would allow for approximately £440 million of additional borrowing as of March 2022, which equates to around 79% of Moat's total debt in fiscal 2022.

Available liquidity, represented by cash and cash equivalents alongside undrawn secured facilities stood at approximately £308 million as of December 2022, representing around 1.1x of the following two years' net capex. Moat's liquidity position is underpinned by a strong treasury policy, which stipulates that the committed development programme should be fully funded for 36 months and assumes all asset sales are delayed for 12 months. Refinancing risk is minimal - two RCFs maturing in 2023 have already been renegotiated and extended, which will improve Moat's liquidity further. The remainder of Moat's debt portfolio is long-tenored.

Weakening interest coverage

Moat's social housing lettings interest coverage (SHLIC) decreased to 1.6x in fiscal 2022 from 1.9x in the prior year, in line with a reduction in the margin achieved on social housing lettings which reduced from 41% to 38% over the same period. We expect its SHLIC to decrease further over the next three years due to rising maintenance costs on existing housing stock, the adverse differential between cost inflation and rent increases imposed by the rent cap in fiscal 2024, rising debt levels, as well as increasing financing costs although Moat's high levels of liquidity, low refinancing risk and high proportion of fixed rate debt will limit their exposure to this trend over the medium term. SHLIC is expected to decrease to around 1.4x over fiscal 2024 to fiscal 2026, compared with an expected A2 peer median of 1.7x over the same period.

Extraordinary Support Considerations

The strong level of extraordinary support factored into the rating reflects the wide-ranging powers available to the regulator in cases of financial distress, with the possibility of a facilitated merger or a transfer of engagements. However, the process can be protracted and is reliant on HAs agreeing to merge, which could be more challenging in a weakening operating environment. Recent history has shown that the UK government 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 Moat and the UK government reflects their strong financial and operational linkages.

ESG considerations

Moat Homes' ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 3
ESG Credit Impact Score

CIS-3
Moderately Negative

For an issuer scored CIS-3 (Moderately Negative), its ESG attributes are overall considered as having a limited impact on the current rating, with greater potential for future negative impact over time. The negative influence of the overall ESG attributes on the rating is more pronounced compared to an issuer scored CIS-2.

Source: Moody's Investors Service

Moat's **CIS-3** reflects our view that ESG risks have a materially negative impact on its rating. In particular, expenditure requirements related to the carbon transition and building safety will weaken margins and increase financing needs, as well as affordability constraints for low-income social tenants which have led to government-imposed sub-inflationary rent caps in the sector.

Exhibit 4
ESG Issuer Profile Scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-3	S-4	G-2
Moderately Negative	Highly Negative	Neutral-to-Low

Source: Moody's Investors Service

Environmental

Moat has material exposure to environmental risks (**E-3**) relating to a significant proportion of its stock requiring retrofit to meet energy efficiency standards by 2035 (carbon transition risks), leading to increased expenditure.

Social

Moat is highly exposed to social risks (**S-4**) through sector-wide legislative requirements to improve the safety of existing housing stock (responsible production risks) for which Moat has considerable expenditure requirements which will weigh on its margins and interest coverage over the medium term. Moat is also affected by cost of living or affordability pressures on social tenants (demographic and societal trends) which led to the UK government capping social rent increases below inflation in fiscal 2024 in England, which will also have a negative impact on margins.

Governance

Moat has limited governance risks (**G-2**). Its governance is fit for purpose, with strong financial management policies and processes, detailed reporting and a simple organisational structure. The regulatory framework also supports good governance in the sector.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating Methodology and Scorecard Factors

The assigned BCA of a3 is the same as the scorecard-indicated BCA outcome.

The methodologies used in this rating were European Social Housing Providers, published in April 2018 and Government Related Issuers, published in February 2020.

Scorecard
31 March 2022

Moat Homes			
Baseline Credit Assessment	**Sub-factor Weighting**	**Value**	**Score**
Factor 1: Institutional Framework			
Operating Environment	10%	a	a
Regulatory Framework	10%	a	a
Factor 2: Market Position			
Units Under Management	10%	21,433	a
Factor 3: Financial Performance			
Operating Margin	5%	27.3%	a
Social Housing Letting Interest Coverage	10%	1.6x	a
Cash-Flow Volatility Interest Coverage	10%	2.5x	a
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.1x	baa
Debt to Assets	10%	31.5%	baa
Liquidity Coverage	10%	1.6x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
Scorecard - Indicated BCA Outcome			**a3**
Assigned BCA			**a3**

Source: Moat Homes, Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
MOAT HOMES	
Outlook	Negative
Baseline Credit Assessment	a3
Issuer Rating -Dom Curr	A2
MOAT HOMES FINANCE PLC	
Outlook	Negative
Senior Secured -Dom Curr	A2

Source: Moody's Investors Service

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