

Research Update:

# U.K.-Based Paradigm Housing Group Ltd. Affirmed At 'A+'; Outlook Stable

May 11, 2022

## Overview

- We expect Paradigm Housing Group Ltd. (Paradigm) to prudently manage increasing costs and maintain a conservative strategy that largely focuses on its core social housing rental business.
- We forecast interest cover will strengthen across our forecast, despite the group predominantly funding its development program with debt.
- We affirmed our 'A+' long-term issuer credit rating on Paradigm. The outlook is stable.

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## Rating Action

On May 11, 2022, S&P Global Ratings affirmed its 'A+' long-term issuer credit rating on Paradigm Housing Group Ltd. The outlook is stable.

We also affirmed our 'A+' issue rating on the £350 million bond issuance, due on May 2051 and issued by Paradigm Homes Charitable Housing Association Ltd., which we consider a core subsidiary of the group.

## Outlook

The stable outlook reflects balanced risks to Paradigm's creditworthiness over the next 24 months. We expect management will contain pressures on its cost base while achieving its investment targets, with limited exposure to sales.

## Downside scenario

We could lower the rating on Paradigm if the group's S&P Global Ratings-adjusted EBITDA reduced due to higher costs than we currently forecast, which could put pressure on margins and debt metrics. We could also lower the rating if Paradigm materially increased its exposure to sales risk, such that revenue from these activities represented more than one third of the group's adjusted revenue. We would reassess management and strategy in these scenarios.

## **Upside scenario**

We could raise the rating if Paradigm managed to consistently achieve stronger financial metrics, such as adjusted EBITDA margins above 40% and debt to non-sales EBITDA below 15x.

## **Rationale**

The affirmation of the rating reflects our view of Paradigm's conservative and consistent strategy and experienced management, which we expect will continue to deliver strong operating and financial performance. We expect the group's costs to be contained despite inflationary pressures, still providing headroom for the group's increasing investments in new and existing homes. We forecast that interest cover will strengthen despite its debt increasing to fund its development of new homes.

Paradigm manages more than 16,000 homes in the southeast of England, with a focus on social and affordable rental accommodation. To gain operational efficiencies, the group continues consolidating its operations in its core geographic areas, which have a high demand for social housing and affordable home ownership products, in our view. This is demonstrated by the group's vacancy rates, which have averaged 0.8% over the past three years, significantly lower than the sector average. This strong demand is supported by Paradigm's average social and affordable rent, which is only about 60% of the market rent on the areas where it operates.

As part of its 2021-2026 development strategy, the group aims to complete 2,250 new homes. Although we expect units developed for shared ownership will increase through our forecast, the plan remains predominantly focused on the development of affordable rental units. This further supports our expectation that revenue from sales related activities will be limited.

In our view, Paradigm's management has extensive expertise in the sector and maintains conservative risk management standards. We view positively that after achieving savings on its business plan, the group has accommodated investments to bring forward its target to reach energy efficiency of above EPC C on all its stock to 2030 from 2035. We think the group has scope to adjust this plan should financial developments require it.

We expect adjusted EBITDA margins to weaken as the group frontloads investments on its existing stock. We also expect debt will increase through our forecast as Paradigm funds its development with additional borrowing. However, we estimate that non-sales EBITDA interest cover will strengthen on the back of the meaningful average cost of debt reduction that the group achieved last year after refinancing part of its high-interest-rate debt with a bond issuance.

We assess the regulatory framework under which registered providers of social housing in England operate as strong, underpinned by the public policy mandate to provide affordable homes. We also consider that the sector benefits from solid ongoing oversight by the Regulator of Social Housing (RSH). These strengths are offset, in our view, by the relatively low levels of grant funding that housing providers in England receive for the development of affordable homes. We consider that the providers in England have the ability to develop homes for outright sale, using the proceeds as an alternative funding source; however, we think that this exposes them to risks and potential volatility compared with providers in other regions. Providers in England are also subject to negative intervention from the U.K. government, in the form of constraints on rent setting or the imposition of additional spending responsibilities, without adequate additional funding. This weighs on our view of the regulatory framework assessment.

We think there is a moderately high likelihood that Paradigm would receive timely extraordinary

government related support in case of financial distress. This is neutral to the rating on Paradigm. Since one of the key goals of the RSH is to maintain lender confidence and low funding costs across the sector, we think 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 we think this would also apply to Paradigm.

## Liquidity

We expect Paradigm will maintain a very strong liquidity position over the next 12 months, with the estimated sources-to-uses liquidity ratio at 2.4x.

The group's very strong liquidity is supported by its high level of undrawn bank facilities, the £100 million secured and available deferred drawdown from its bond issuance, and its ability to generate cash consistently through our base case. We view Paradigm's access to external liquidity as satisfactory.

Liquidity sources include:

- Adjusted internal cash flow generation for the next 12 months, adding back the noncash cost of sales, of close to of £58 million;
- Cash and liquid investments of £35 million;

Proceeds from asset sales of £10 million;

- The undrawn part of its contracted and secured bank facilities maturing beyond 12 months and the secured and available deferred bond, amounting to £250 million; and
- Government grants of about £3 million.

Liquidity uses include:

- Expected capital expenditure, adjusted for cost of sales and capitalized repairs, amounting to £115 million; and
- Interest and principal repayment of £33 million.

## Key Statistics

Table 1

### Paradigm Housing Group --Key Statistics

Mil. £	--Year ended March 31--				
	2021a	2022e	2023bc	2024bc	2025bc
Number of units owned or managed	15,650	16,051	16,084	16,639	16,844
Adjusted operating revenue	153.1	116.8	119.9	135.3	140.7
Adjusted EBITDA	49.6	46.9	48.7	52.1	55.0
Non-sales adjusted EBITDA	45.7	43.0	46.7	49.4	52.4
Capital expense	48.9	107.7	114.6	118.8	117.5
Debt	713.9	788.8	836.2	901.3	957.3

Table 1

**Paradigm Housing Group --Key Statistics (cont.)**

Mil. £	--Year ended March 31--				
	2021a	2022e	2023bc	2024bc	2025bc
Interest expense	32.7	29.7	29.1	30.7	32.2
Adjusted EBITDA/Adjusted operating revenue (%)	32.4	40.1	40.6	38.5	39.1
Debt/Non-sales adjusted EBITDA (x)	15.6	18.3	17.9	18.3	18.3
Non-sales adjusted EBITDA/interest coverage(x)	1.4	1.4	1.6	1.6	1.6

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

**Ratings Score Snapshot**

Table 2

**Paradigm Housing Group--Ratings Score Snapshot**

	Assessment
Enterprise risk profile	2
Industry risk	2
Regulatory framework	3
Market dependencies	2
Management and Governance	2
Financial risk profile	3
Financial performance	3
Debt profile	4
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, Apr 22, 2022
- U.K. Social Housing Sector Borrowing Needs To Rise To Fund Investment In New Homes, Mar 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

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**Paradigm Housing Group Ltd.**

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Issuer Credit Rating A+/Stable/--

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**Paradigm Homes Charitable Housing Association Ltd.**

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Senior Secured A+

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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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