

Research Update:

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

May 22, 2023

Overview

- We forecast that increasing operating costs alongside high investments on existing stock will reduce Paradigm Housing Group's S&P Global Ratings-adjusted EBITDA through March 31, 2026.
- Although we expect debt to modestly increase to finance development of new homes, we estimate that lower-than-previously expected non-sales adjusted EBITDA will weaken Paradigm's debt metrics.
- However, mitigating these pressures is our view of Paradigm's very strong management and significant flexibility to adapt its strategy, such that financial performance and liquidity remain very solid.
- We therefore affirmed our 'A+' long-term issuer credit rating on Paradigm and maintained the stable outlook.

Rating Action

On May 22, 2023, 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 in 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 our view that Paradigm will manage adequately its financial headroom and flexibility to balance the pressure of lower adjusted EBITDA.

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Downside scenario

We could lower the rating if Paradigm's strategy becomes more aggressive, for instance by increasing debt-funded development, making higher investments on existing stock above our current expectations, or by increasing materially the group's exposure to sales risk--all of which could negatively affect our view on the group's management.

Upside scenario

An upgrade would depend on Paradigm materially strengthening its financial performance, which would support a significant improvement of its debt metrics, all else remaining equal.

Rationale

The affirmation reflects our expectation that Paradigm's management will prudently execute its business plan while keeping enough headroom to mitigate any undue pressure on its financial indicators. Although we forecast a weakening compared with our previous expectations, we expect the group's financial indicators will remain commensurate with the current rating level.

Given the current pressures around high inflation, rising investments on existing stock, and high interest rates, Paradigm's management has prudently scaled back its new homes development targets and has kept ample flexibility to mitigate unexpected risks. However, because we expect that these pressures will result in lower non-sales adjusted EBITDA, we estimate that Paradigm's debt metrics will weaken from our previous expectations.

Enterprise profile: Experienced management with significant flexibility to adapt its strategy while operating in an affluent area in the southeast of England

Paradigm manages more than 16,000 homes in the southeast of England, with a focus on social and affordable housing. To achieve operational efficiencies, the group continues consolidating its operations in its core geographic areas of Buckinghamshire, Bedfordshire, and Hertfordshire, and reducing its stock in London.

Demand for Paradigm's properties is strong, in our view, supported by Paradigm's average social and affordable rent, which is only about 60% of the market rent. This is further demonstrated by the group's vacancy rates, which, at 0.8% over the past three years, remain significantly lower than the sector's average.

In our view, Paradigm's management is experienced and has extensive expertise in the sector. It has proactively adapted its business plan to the sector's challenges and scaled down development of new homes while keeping its targeted investments on existing properties. In addition, the group's capital expenditure program is flexible, underpinned by a large proportion of expenditure being uncommitted.

As part of its strategy, to limit direct exposure to outright sales, Paradigm has entered into a joint venture agreement. We estimate that exposure to sales will remain below 25% of total operating revenue after considering the group's exposure through the joint venture.

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 June 8, 2021, on RatingsDirect.

Financial profile: Lower adjusted EBITDA will weaken Paradigm's debt metrics from previous expectations, however, the group's liquidity position will remain solid.

We estimate that the impact of high inflation on Paradigm's cost base will not be fully balanced by additional rental revenue from recent acquisitions and organic growth. We therefore expect that through our forecast horizon through 2026, the group's adjusted EBITDA margins will reduce from our previous expectations but remain above 30%. This as we anticipate that the group will continue prioritizing investments in its existing stock to achieve energy performance certificate levels above EPC C on all its stock by 2030.

While the scaling down of the development program has reduced slightly the previously expected debt funding need, we anticipate that lower non-sales adjusted EBITDA will result in a debt burden that will steadily exceed 20x through our forecast period. However, we expect that, despite reducing, non-sales EBITDA interest coverage will remain robust at close to 1.3x, thanks to the group's lower cost of debt achieved through the last refinancing exercise in 2021.

We assess Paradigm's liquidity position as very strong, with sources covering uses by 1.9x in the next 12 months. This is based on our forecast of liquidity sources of about £340 million from cash, undrawn and available revolving credit facilities, secured and available deferred bond receipts, grant funding and cash from operations (adding back the noncash cost of sales) that will cover liquidity uses of about £175 million (mainly capital expenditure, and debt service payments).

In our analysis, we also consider that Paradigm has satisfactory access to external funding when needed.

Government-related entity analysis

We believe there is a moderately high likelihood that Paradigm would receive timely extraordinary support from the government in case of financial distress. This is neutral to the rating on Paradigm. Since one of the key goals of the Regulator of Social Housing (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.

Selected Indicators

Table 1

Paradigm Housing Group --Key Statistics

Mil. £	--Year ended March 31--				
	2022a	2023e	2024bc	2025bc	2026bc
Number of units owned or managed	16,022	16,259	16,518	16,794	17,031
Adjusted operating revenue	116.6	126.7	138.7	138.1	151.2
Adjusted EBITDA	43.9	45.1	43.9	46.8	49.9

Table 1

Paradigm Housing Group --Key Statistics (cont.)

Mil. £	--Year ended March 31--				
	2022a	2023e	2024bc	2025bc	2026bc
Non-sales adjusted EBITDA	40.2	42.2	38.8	43.3	44.4
Capital expense	90.7	142.3	126.6	90.0	86.0
Debt	784.7	859.5	909.2	954.1	974.1
Interest expense	30.2	31.1	32.2	33.1	33.3
Adjusted EBITDA/Adjusted operating revenue (%)	37.7	37.6	31.6	33.9	33.0
Debt/Non-sales adjusted EBITDA (x)	19.5	20.4	23.4	22.0	21.9
Non-sales adjusted EBITDA/interest coverage(x)	1.3	1.4	1.2	1.3	1.3

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	5
Liquidity	2

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 Outlook Revised To Stable From Negative On Moderating Fiscal Risks; 'AA/A-1+' Ratings Affirmed, April 21, 2023
- U.K. Social Housing Borrowing 2023: On Pause, March 28, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings History: March 2023, March 27, 2023
- U.K. Social Housing Providers Set Their Sights On Cyber Risks, Dec. 16, 2022
- Non-U.S. Social Housing Sector Outlook 2023: The Most Negative Bias Since 2018 Implies Significant Pressure On Ratings, Dec. 1, 2022
- Inflation To Erode The Performance Of U.K. Public Finance Sectors, Nov. 29, 2022
- Bulletin: Cap On Rent Increases Is Consistent With Our Base Case For English Social Housing Providers, Nov. 17, 2022
- The U.K. Social Housing Sector Now Displays A More Pronounced Negative Bias In Its Creditworthiness, Oct. 11, 2022
- Bulletin: Launch Of Rent Cap Consultation Adds Uncertainty To Creditworthiness Across English Housing Sector, Sept. 1, 2022
- Rated U.K. Social Housing Providers' Creditworthiness Could Suffer If The Gap Between Rent And Cost Increases Persists, Aug. 1, 2022
- Global Regulatory Framework Report Card For Public And Nonprofit Social Housing Providers Published, June 8, 2021

Ratings List

Ratings Affirmed

Paradigm Housing Group Ltd.

Issuer Credit Rating A+/Stable/--

Paradigm Homes Charitable Housing Association Ltd.

Senior Secured A+

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 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/sourceld/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at 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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