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CREDIT OPINION
24 January 2024

Update

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RATINGS

Alliance Homes Group

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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Alliance Homes Group (United Kingdom)

Update to credit analysis

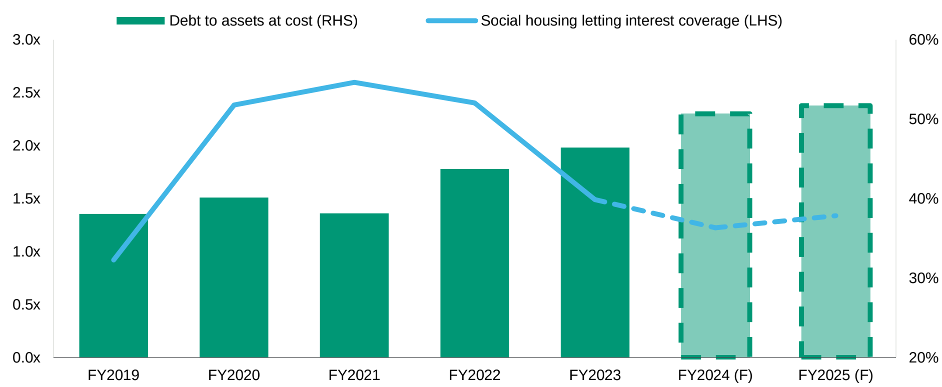
Summary

The credit profile of Alliance Homes Group (Alliance, A2 stable) reflects its focus on social housing lettings, low debt to revenue and robust debt management practices. It also incorporates rising debt to support its development programme and a weakened operating performance. Alliance benefits from the strong regulatory framework governing the English housing association sector and our assessment that there is a strong likelihood the government of the United Kingdom (Aa3 stable) would intervene in the event it faced acute liquidity distress.

Exhibit 1

Debt and interest coverage metrics will weaken due to a large capital expenditure programme

Debt to assets at cost and social housing letting interest coverage, fiscals 2019-2025



Fiscals 2024 and 2025 are forecasts based on Alliance's 2023 Business Plan.
Source: Alliance, Moody's Investors Service

Credit strengths

- Clear strategy focused on social housing lettings, with no outright sales exposure
- Low debt to revenue and strong debt management practices
- Supportive institutional framework in England

Credit challenges

- Increasing debt to support an ambitious development strategy
- Weak operating performance

Rating outlook
The stable outlook reflects the expected gradual reduction in inflation and associated cost pressures, which will support Alliance's credit profile.

Factors that could lead to an upgrade
Upward pressure on Alliance's rating could result from a significant improvement in operating performance, a material reduction in debt or a significant increase in government support for the sector, especially significantly higher levels of capital grants.

Factors that could lead to a downgrade
Downward pressure on Alliance's rating could result from a prolonged weakening in operating performance, debt growing more quickly than forecasts, weaker liquidity or a failure to adapt strategies and risk appetite to mitigate weaker economic conditions. Lower government support for the sector or a dilution of the regulatory framework could also lead to downward pressure on Alliance's rating.

Key indicators

Exhibit 2

Alliance Homes Group

	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23	31-Mar-24 (F)	31-Mar-25 (F)
Units under management (no.)	6,610	6,662	6,689	6,915	7,065	7,246	7,456
Operating margin, before interest (%)	25.3	21.5	23.0	21.9	17.6	22.0	22.8
Net capital expenditure as % turnover	23.5	23.6	-2.7	64.5	53.7	66.1	33.0
Social housing letting interest coverage (x times)	0.9	2.4	2.6	2.4	1.5	1.2	1.3
Cash flow volatility interest coverage (x times)	1.6	4.6	5.1	3.6	3.7	1.6	2.6
Debt to revenue (x times)	2.0	2.1	2.1	2.2	2.4	2.9	3.0
Debt to assets at cost (%)	38.1	40.1	38.2	43.7	46.4	50.7	51.7

Source: Alliance, Moody's Investors Service

Detailed credit considerations
Alliance's 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 Alliance faced acute liquidity stress.

Clear strategy focused on social housing lettings, with no outright sales exposure
Alliance is a small social housing provider, managing approximately 7,000 units in the West of England. The group has a simple structure comprising the parent entity, Alliance Homes Limited, a subsidiary providing repairs and maintenance services and another subsidiary managing a photovoltaic panels business.

Alliance benefits from revenue stability, primarily due to its well-defined strategy focused on social housing lettings. In fiscal 2023, social housing lettings made up 72% of the group's turnover, while the remaining turnover was mainly derived from first tranche shared ownership sales (14%).

The group's development plan and strategy continue to prioritise social housing lettings and shared ownership sales. We expect that social housing lettings will account for 77% of turnover over the next five years, with shared ownership sales contributing 12%. The group has no plans to develop properties for outright sale, a credit positive as it minimises exposure to the housing market downturn.

Low debt to revenue and strong debt management practices
Alliance's debt to revenue is expected to remain relatively low despite the anticipated increase in debt to finance the development programme. Debt to revenue increased to 2.4x in fiscal 2023, from 2.2x in fiscal 2022, due to a £24 million (24%) rise in debt within the year. Over the next three years, we anticipate a further increase to an average of 3.1x. However, this remains below the A2-rated peer median of 3.5x over the same period, supported by robust turnover growth resulting from the resumption of consumer price inflation (CPI)-linked rent increases from fiscal 2025 and the delivery of new social rent units.

Alliance demonstrates robust debt management practices, underlined by its straightforward debt profile consisting of one bank loan and two private placements. The group effectively decreased its exposure to variable rate debt to 13% in December 2023, from 26% in January 2023, and has no debt maturities until 2038 (excluding scheduled amortisation payments). Alliance arranged a deferred drawdown on its private placement, with the final tranche of £40 million due in July 2024, securing access to competitively priced funding in the current high-interest-rate environment.

Alliance also benefits from strong liquidity with a substantial unencumbered asset base. It maintains significant headroom above its liquidity golden rule of having at least 18 months of forecast liquidity requirement. The liquidity coverage ratio stood at 1.5x the forward-looking two-year cash needs as of September 2023, supported by £15 million of cash and cash equivalents and a £75 million undrawn revolving credit facility. As of September 2023, unencumbered assets provided an additional borrowing capacity of approximately £174 million, comfortably covering the net funding needs of around £135 million for the next five years.

Supportive institutional framework in England

The sector's credit quality will continue to benefit from the strong institutional framework governing English housing associations 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 and annual reviews and by undertaking biennial In-Depth Assessments (IDAs) for large and complex housing associations. 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 housing associations 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 housing associations retain some expenditure flexibility and have a track record of reducing costs to mitigate lower income.

However, due to high rates of inflation in 2022, with CPI at 10.1% as of September 2022 on a year-on-year basis, the government implemented a 7% ceiling on social rent increases from April 2023 for one year. The ceiling of 7% results in an adverse differential between rental income and cost growth, which we expect will drive lower margins and interest coverage across the sector in fiscal 2024. The UK government has confirmed that the English sector will return to rent increases of September CPI plus 1% in fiscal 2025 (7.7%), which will be favourable considering that CPI stood at 4.0% in December 2023.

Increasing debt to support an ambitious development strategy

Alliance plans to develop close to 1,000 new social homes over the next five years. The mix will consist of 46% general needs, 23% affordable housing and 31% shared ownership properties. Alliance has already accelerated its development since fiscal 2022, with net capital expenditure to revenues averaging 59% over the past two years, a significant increase from the average of 15% between fiscals 2019 and 2021. Over the next three years, net capital expenditure is projected to remain at high levels, averaging 49% of turnover.

Alliance will increase borrowing to fund its development programme, leading to a deterioration in debt metrics. The group's debt is expected to more double over the next five years, reaching £263 million in fiscal 2028 from £125 million in fiscal 2023. Consequently, gearing will rise by 10 percentage points during the period, reaching 56% by fiscal 2028. This will be significantly higher than the A2-rated peer median of 48% for that year.

Weak operating performance

Alliance's operating margin is weak relative to peers. The margin on social housing lettings declined to 16% in fiscal 2023 from 21% in the previous year due to increased maintenance and management costs. The group expects a recovery of the margin to an average of 21% over the next three years, driven by a return to CPI-linked rent increases from fiscal 2025. However, this remains lower than the A2-rated peer median of 29% over the same period.

Alliance's social housing letting interest coverage (SHLIC) stood at 1.5x in fiscal 2023, a decline from 2.4x in fiscal 2022. This decrease was a result of the significant drop in the margin on social housing lettings combined with increased interest expenses due to higher debt. While this still compares favourably to the A2-rated peer median of 1.4x in fiscal 2023, SHLIC is expected to further deteriorate to 1.2x in fiscal 2024 and 1.3x in fiscal 2025 as debt continues to increase. However, Alliance intends on increasing rents in line with the allowable increase of 7.7% for fiscal 2025; as a result, there is potential for improvement in these forecasts as they assume a rent increase of 5% in fiscal 2025.

Alliance has tight headroom on one of its interest coverage covenants due to its weakened operating performance. However, discussions are currently underway to renegotiate the covenant to EBITDA only from EBITDA MRI, which should provide adequate covenant headroom once implemented.

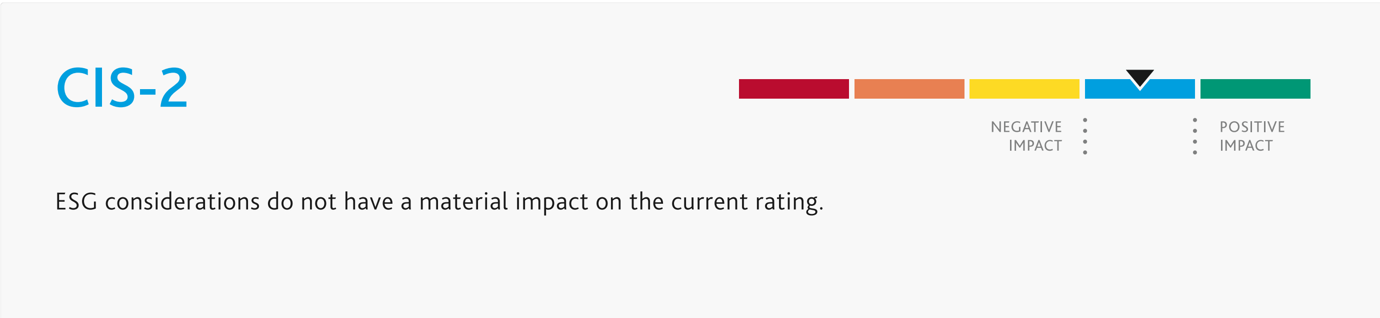
Extraordinary Support Considerations

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 housing associations 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 in increasing exposure to non-core social housing activities in the sector, that add complexity to housing association operations. In addition, our assessment that there is a very high default dependence between Alliance and the UK government reflects their strong financial and operational linkages.

ESG considerations

Alliance Homes Group's ESG credit impact score is CIS-2

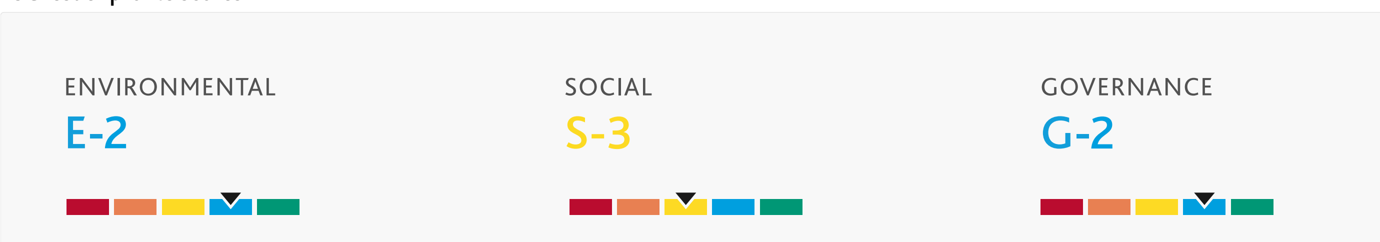
Exhibit 3
ESG credit impact score



Source: Moody's Investors Service

Alliance's **CIS-2** indicates that ESG risks have a limited impact on its rating. Alliance has limited exposure to carbon transition risks as the majority of its stock already meets energy efficiency requirements, and although social risks are prevalent we consider that Alliance has the ability to effectively mitigate them through its strong governance and management practices. We also consider that the supportive regulatory framework for the sector offsets some ESG risks.

Exhibit 4
ESG issuer profile scores



Source: Moody's Investors Service

Environmental

Alliance has limited exposure to environmental risks (**E-2**). English housing associations have the legislative requirement to improve the energy efficiency of their existing housing stock by 2035 (carbon transition risks), leading to increased expenditure. However, we assess that Alliance has a low exposure to this risk as the vast majority of its housing stock already meets the required efficiency standards.

Social

Alliance has a material exposure to social risks (**S-3**) through sector-wide legislative requirements to improve the safety of existing housing stock (responsible production risks), which weighs on expenditure and operating margins, and the impacts of 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

Alliance 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 in line with the scorecard-indicated BCA outcome for fiscal 2023.

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

Exhibit 5

2023 Scorecard

Alliance Homes Group			
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%	7,065	baa
Factor 3: Financial Performance			
Operating Margin	5%	17.6%	baa
Social Housing Letting Interest Coverage	10%	1.5x	baa
Cash-Flow Volatility Interest Coverage	10%	3.7x	aaa
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	2.4x	a
Debt to Assets	10%	46.4%	ba
Liquidity Coverage	10%	1.5x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	a	a
Scorecard - Indicated BCA Outcome			**a3**
Assigned BCA			**a3**

Source: Alliance, Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
ALLIANCE HOMES GROUP	
Outlook	Stable
Baseline Credit Assessment	a3
Issuer Rating -Dom Curr	A2

Source: Moody's Investors Service

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