MOODY'S
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CREDIT OPINION
7 December 2020

Update

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RATINGS

ClwydAlyn Housing Limited

Domicile	United Kingdom
Long Term Rating	Baa1
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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ClwydAlyn Housing Limited (UK)

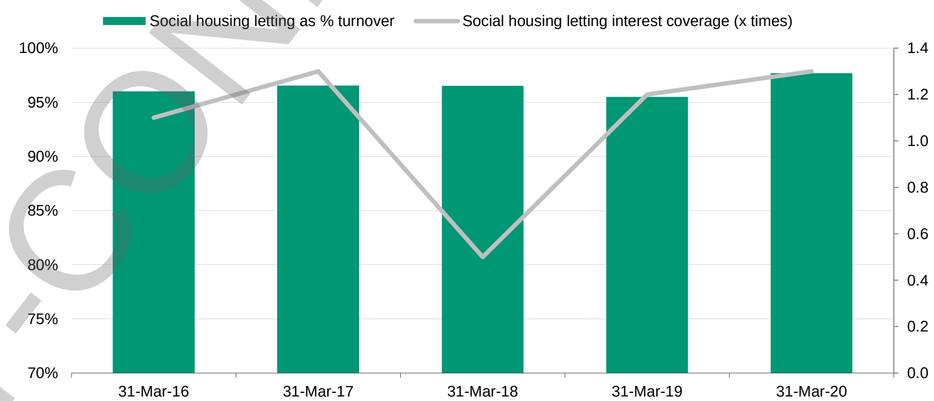
Update following upgrade to A3 stable

Summary

The credit profile of ClwydAlyn Housing (ClwydAlyn, A3 stable) reflects its high proportion of revenue derived from low-risk social housing lettings, which enhances revenue stability; its strong market position in North Wales; and its good financial management and governance. In addition, ClwydAlyn benefits from the strong regulatory framework governing Welsh housing associations 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 it faced acute liquidity stress.

Exhibit 1

ClwydAlyn continues to maintain a high proportion of social housing lettings



In FY2018, ClwydAlyn's SHLIC reduced due to one-off breakage costs of debt refinancing
Source: Moody's Investors Service, ClwydAlyn

Credit strengths

» Continued focus on low-risk social housing letting supporting cash flow stability

» Strong management and governance

» Supportive operating environment and regulatory framework, which supports revenue stability

Credit challenges

» Debt to revenues metric is higher than peer median, but stable

» Low operating margins but on an improving trend

Rating outlook

The stable outlook reflects our expectation that ClwydAlyn's financial performance will remain in line with A3 peers.

Factors that could lead to an upgrade

An upgrade of the ratings could result from sustained improvement in financial performance, including social housing lettings interest coverage and cash flow volatility interest coverage above 2.0x and an operating margin above 30%.

Factors that could lead to a downgrade

A downgrade of the ratings could result from the operating margin falling below 20% on a sustained basis, with social housing lettings interest coverage and cash flow volatility interest coverage below 1.0x and debt to revenues metric increasing above 6.0x. In addition, any weakening of the regulatory framework or dilution of the overall level of support from the UK government could also exert downward pressure on the rating.

Key indicators

Exhibit 2

ClwydAlyn

	31-Mar-16	31-Mar-17	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21 (F)	31-Mar-22 (F)
Units under management (no.)	5,678	5,706	5,794	5,998	6,048	7,020	7,327
Operating margin, before interest (%)	20.0	26.0	27.0	22.0	23.0	25.0	25.0
Net capital expenditure as % turnover	9.9	14.3	73.3	14.1	33.4	86.2	24.7
Social housing letting interest coverage (x times)	1.1	1.3	0.5	1.2	1.3	1.4	1.5
Cash flow volatility interest coverage (x times)	1.6	1.7	0.5	1.3	1.5	1.6	1.6
Debt to revenues (x times)	4.0	4.6	5.1	4.7	4.4	5.1	4.9
Debt to assets at cost (%)	41.0	41.0	46.0	46.0	46.0	47.0	45.0

In FY2018, the metrics were negatively affected by £15.9 million breakage costs.
Source: Moody's Investors Service, ClwydAlyn

Detailed credit considerations

On 7 December 2020, Moody's upgraded ClwydAlyn's ratings to A3 from Baa1. The upgrade reflected its strengthened financial management and governance.

ClwydAlyn's rating combines (1) its Baseline Credit Assessment (BCA) of baa1, and (2) a strong likelihood of extraordinary support coming from the UK government in the event that the organisation faced acute liquidity stress.

Baseline credit assessment

Continued focus on low-risk social housing letting supports cash flow stability

ClwydAlyn's total turnover has grown steadily over the last five years, reaching £46.1 million in FY2020 from £35.9 million in FY2016, due to its steady growth of assets through its development programme. ClwydAlyn's total units under management were 6,048 in FY2020, growing from 5,678 in FY2016. Low-risk social housing lettings, including supported and sheltered housing, contributed 98% of the organisation's turnover in FY2020, a level virtually unchanged since FY2014. This compares favourably with our rated portfolio of housing associations in the UK, which, as a whole, derived 74% of their revenue from social housing lettings in FY2020. We do expect ClwydAlyn's proportion of turnover from social housing lettings to reduce marginally to an average of 92% over the next three years due to a small amount of rent to own properties being developed over this period, however the vast majority of its development programme is for social rented properties. Its development programme includes 1,125 units over FY2021 to FY2023, with 60 of these being rent to own and the remainder general needs or supported housing. In addition, over half of the group's income is generated from housing benefits, care home fees funded by local authorities and government contracts to provide supporting living services - this backing of a significant proportion of revenue by government bodies is also credit positive as it reduces the risk of revenue losses.

ClwydAlyn is one of the largest housing associations in Wales and has the biggest market share in North Wales, a dispersed area with the second-biggest population concentration after the more urbanized south (where cities like Cardiff and Swansea are located). ClwydAlyn's major operations are spread across six local authorities in Wales.

Strong management and governance

ClwydAlyn has made significant improvements in its management and governance over the last 1-2 years. This includes implementing golden rules to monitor its financial performance, detailed scenario analysis and stress testing, renewal of its Executive Team and Board and improving its liquidity management, including strengthening its liquidity policy. Its liquidity policy is now in line with others in the sector with 12 months of forecast cash outflows helds as cash and immediately accessible funding and 24 months of forecast cash outflows held as cash, immediately accessible funding and committed, but uncharged, loan facilities. In 2020, the Executive Team implemented a new resilience plan to respond to the coronavirus pandemic, which included furloughing staff, reducing spend on materials and its development programme and undertaking a range of scenario analysis to model financial impacts on its golden rules and covenants.

Supportive operating environment and regulatory framework, which provides revenue stability

Welsh housing associations operate under a co-regulated environment with engaged oversight exercised by the sector's regulator, the Housing Regulation Team (HRT). The HRT is a departmental office sitting within the Welsh government and reports to the Welsh Government Housing Division. The sector's regulator is responsible for protecting the public investment in social housing as well as building confidence to support the reputation and financial viability of the sector. The regulator monitors compliance with standards of performance through quarterly returns, long-term business plans, stress tests and regular interaction with senior management, and focuses on governance, financial viability, value for money and rents.

At least annually, the Welsh ministers publish a regulatory judgement for each housing association in Wales. In the latest assessment from September 2019, ClwydAlyn achieved the highest score for both Governance and Service Delivery and for Financial Management.

Social housing rents, which represent the bulk of the revenue for most housing associations, are stable and predictable, but their level is set by the National Assembly for Wales, which overruled the rent reduction policy imposed on English housing associations. As of FY2021, the Welsh Governments rent settlement is for CPI+1%, in line with English housing associations.

Debt to revenues metric is higher than the peer median, but stable

ClwydAlyn's debt levels are expected to increase to £250 million by FY2024, from £205 million at FYE2020, an increase of £45 million. However debt metrics are not expected to change materially due to new assets and revenues being delivered by the development programme. Debt to revenues are expected to be an average of 4.9x over the next three years, higher than the A3 peer median of 4.3x over the same period. However, despite being higher than the peer median, this level is relatively stable, as the average for this metric as also 4.9x over the previous three years. Its debt to assets metric is expected to be an average of 45% over the next three years, stronger than the expected A3 peer median of 54% over the same period. Its debt growth is relatively modest, which reflects the high levels of grant that Welsh housing associations receive to deliver new social housing, in contrast to much lower levels in England.

ClwydAlyn's liquidity coverage is 1.1x in FY2021. This includes £16 million of cash and £35 million of immediately accessible facilities through its revolving credit facility. ClwydAlyn has access to another £88 million of borrowing capacity through its unencumbered assets portfolio, a decent level. As its peak debt level is already secured we do not expect ClwydAlyn to use a significant amount of its additional borrowing capacity.

Low operating margins but on an improving trend

ClwydAlyn had an operating margin of 23% in FY2020, which is relatively low compared to the A3 peer median of 29%. Margins in the Welsh Housing Association sector have generally been low relative to the English sector, in addition ClwydAlyn undertaken some supported housing and care activities which typically have low margins. ClwydAlyn plans to improve its margin to 27.5% by FY2024, with a particular emphasis on delivering value for money efficiencies through improved procurement, sharing maintenance activities with other HAs to achieve economies of scale and delivering a new housing management system.

ClwydAlyn's social housing lettings interest coverage (SHLIC) of 1.3x in FY2020 is the same as the A3 peer median and has improved over recent years. This is also expected to continue to improve, in line with its operating margin.

Extraordinary support considerations

The strong level of extraordinary support 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 is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors in the increasing exposure to non-core social housing activities in the sector, which 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 ClwydAlyn and the UK government reflects their strong financial and operational links.

ESG Considerations

How environmental, social and governance risks inform our credit analysis of ClwydAlyn Housing

Moody's takes account of the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of ClwydAlyn, the materiality of ESG to its credit profile is as follows:

Environmental considerations are not material to HAs' credit profiles. In line with the rest of the UK, the sector's main environmental risk exposures relate to water shortage and flood risk. Flood risk is managed by country and national authorities, and therefore the financial burden of adapting to increased flood risk will not fall on individual housing associations.

Social risks are material to HAs' credit profiles. In particular, the sector is exposed to risks stemming from socially-driven policy agendas affecting social rents, benefits and capital grants in addition to the impact of demographic trends on demand which are captured in our assessment of the operating environment. We view the coronavirus outbreak as a social risk under our ESG framework given its impact on health and safety. Overall, we expect the outbreak to cause ongoing operational disruption for HAs but do not expect a material credit impact as higher arrears and lower market sales receipts will be offset by cash savings from reduced capital spending on development and repairs. HAs are also impacted by customer relations and product quality. The Grenfell fire tragedy in June 2017 has encouraged higher health and safety standards with many HAs planning on increasing spending on the quality of their existing stock.

Governance considerations are also material to HAs' credit profiles and are captured in our assessment of governance and management. In general, housing association governance is strong with multi-year strategies supported by detailed forecasts, conservative liquidity policies, and robust risk management including stress testing.

Further details are provided in the "Baseline credit assessment" section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing ESG Risks.

Rating methodology and scorecard factors

The assigned BCA of baa1 is the same as the scorecard-indicated BCA.

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

Exhibit 3

31 March 2020

ClwydAlyn			
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%	6,048	baa
Factor 3: Financial Performance			
Operating Margin	5%	22.6%	baa
Social Housing Letting Interest Coverage	10%	1.3x	baa
Cash-Flow Volatility Interest Coverage	10%	1.5x	baa
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	4.4x	ba
Debt to Assets	10%	45.8%	ba
Liquidity Coverage	10%	1.2x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
Suggested BCA			**baa1**

Source: Moody's Investors Service, ClwydAlyn

Ratings

Exhibit 4

Category	Moody's Rating
CLWYDALYN HOUSING LIMITED	
Outlook	Stable
Issuer Rating -Dom Curr	Baa1
PENARIAN HOUSING FINANCE PLC	
Outlook	Stable
Senior Secured -Dom Curr	Baa1

Source: Moody's Investors Service

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