

Research Update:

Scotland-Based Registered Social Landlord Wheatley Housing Group 'A+' Rating Affirmed; Outlook Stable

May 20, 2024

Overview

- In our view, Wheatley Housing Group Ltd.'s focus on traditional social housing activities, solid management expertise, and flexibility in plans will help strengthen the group's financial metrics.
- We forecast the increase in Wheatley's rental income to offset the pressures from rising investments in existing stock, thereby supporting the recovery in S&P Global Ratings-adjusted EBITDA.
- This, alongside a modest rise in debt, leads us to expect improvements in Wheatley's interest coverage through to the fiscal year ending March 31, 2027.
- We therefore affirmed our 'A+' long-term issuer credit rating on Wheatley. The outlook remains stable.

Rating Action

On May 20, 2024, S&P Global Ratings affirmed its 'A+' long-term issuer credit ratings on Wheatley Housing Group Ltd. (Wheatley) and core group entity Wheatley Homes Glasgow. The outlooks are stable.

We also affirmed our 'A+' issue rating on the £300 million bond issued by Wheatley Group Capital PLC, which we consider a core subsidiary of the group.

In addition, we affirmed our 'A' long-term issuer credit rating on Lowther Homes, Wheatley's commercial arm that provides mid-market homes and property management services. The rating on Lowther is one notch lower than that on Wheatley, reflecting Lowther's status as a highly strategic entity within the group. The outlook is also stable.

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Outlook

The stable outlook reflects our view that Wheatley's management will prudently execute its business plan while keeping enough financial headroom to mitigate cost and investment pressures.

Downside scenario

We could lower the rating if we see a material weakening of the group's credit metrics. This could happen if management is unable to control costs, such that they significantly surpass our current projections, or if debt-funded spending on development increases materially beyond our projections, which would also weaken liquidity.

Upside scenario

We could raise the rating on Wheatley if cost-control efforts or additional income from rents or grants secured for investments in existing stock result in EBITDA margins improving materially above our current projections, helping to strengthen the group's debt metrics, all else equal.

We could also raise the rating if we think Wheatley's role for, and link with, the Scottish government have strengthened, implying a higher likelihood of extraordinary support.

Rationale

The rating affirmation reflects our view that strong demand for Wheatley's properties and management's sound practices will help offset the pressure from increasing investment in existing and new homes. We expect an uptick in rental revenues, on the back of the group's expanding asset base and planned rent increases, alongside the group's ability to secure grants for investments in existing stock, to gradually strengthen Wheatley's financial performance. Furthermore, with the considerable grant support from the Scottish government to fund development and the flexibility in the group's plan to reprofile its development program, we anticipate that debt will increase at a modest pace, supporting the improvement of Wheatley's interest coverage.

Enterprise profile: Robust management strategies, no exposure to riskier market sale activities, and a strong market position

We view Wheatley as a traditional social housing provider that enjoys strong demand for its properties. It is the largest housing association in Scotland, with an asset base of about 65,000 units, of which over 90% are for general needs rent. The group's geographical footprint stretches from the central belt of Scotland between Glasgow and Edinburgh to the southwest of Scotland, down to the English border. We think that Wheatley's relatively low general needs rent, which we estimate close to 60% of Scotland's average market rent, reflects strong affordability levels and supports high demand for Wheatley's properties. This also becomes apparent in the average vacancy rates of about 1.1% over the past three years, which we estimate to be slightly below the sector average.

In our opinion, Wheatley's management has extensive experience in the social housing sector and

a good understanding of its business opportunities and challenges. The group's strategy remains prudent, and it continues to focus on organic expansion, with all development planned to include only affordable and mid-market rental homes. Although not classified as social tenure in Scotland, mid-market rental homes are a form of subsidized housing with below-market rents.

We favorably view the flexibility in Wheatley's plans with respect to investments in new and existing homes. We understand that the group is actively working on plans to deliver cost efficiencies. This, teamed with the solid quality of the group's existing assets and that discretionary spending has been included in the investment program, should provide the group some headroom to adjust costs. About 92% of its stock already meets Energy Performance Certificate (EPC) C standards (or higher); we view this as more favorable than sector peers. In terms of new development, we understand that a material part of the group's development program--more than 50% on average over our forecast horizon comprising the fiscal years 2025 to 2027--remains uncommitted, allowing the group to scale back spending if needed.

We assess the regulatory framework under which registered providers of social housing in Scotland operate as very strong (see "Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks," published Oct. 23, 2023, on RatingsDirect).

Financial profile: An anticipated solid recovery in S&P Global Ratings-adjusted EBITDA and interest coverage

We expect Wheatley's margins to recover to about 27% by the end of March 31, 2027 (fiscal 2027), from about 21% estimated for fiscal 2024. In our view, the group's ability to raise rents, its expanding asset base, and the grants secured for investments in existing stock will gradually offset the cost pressures from the increasing investments in existing stock. Over our forecast horizon, we anticipate that the group will raise rents more than it has historically, bringing its rent increases to more in line with the average across the Scottish housing sector. We expect the resulting increase in rental income to create additional headroom for expanding investments in existing homes, thereby underpinning the projected recovery in financial performance.

We anticipate the group's debt metrics will improve to relatively modest levels over our forecast horizon compared with that of peers across the U.K., supported by the recovery in non-sales EBITDA, as adjusted by S&P Global Ratings. Wheatley's development program remains financed via a roughly equal mix of grant income and debt funding, reducing its reliance on capital markets compared with English peers'. Moreover, Wheatley has access to the Scottish government's charitable bond program, administered by Allia, on which interest is to be repaid only on maturity. This reduces medium-term cash interest strain for the group.

We view Wheatley's liquidity as very strong. Sources of liquidity are estimated to cover uses by about 1.5x over the next 12 months. This is based on our forecast of liquidity sources of close to £500 million (mainly comprising cash and undrawn available facilities, fixed asset sales proceeds, grant receipts, and cash from operations) compared with liquidity uses of just under £340 million (primarily capital expenditure, interest, and principal repayments). Although we anticipate a slight deterioration in the liquidity coverage ratio, we assume the group's plans to secure additional funding over the next few months suggests the weakening is only temporary. Over the past 12-18 months, amid unfavorable interest rate conditions, the group has heavily relied on its committed facilities to fund capital investments. While this has led to a temporary shrinkage of the group's liquidity buffers, we expect reserves to be replenished over the next few months.

We continue to consider that Wheatley has satisfactory access to external funding if needed.

Government-related entity analysis

We think there is a high likelihood that the Scottish government would provide timely and sufficient extraordinary support to Wheatley, through the Scottish Housing Regulator, in the event of financial distress. We base our opinion on our assessment of the group's very important role for the Scottish government and its public policy mandate, as well as its strong link with the Scottish government. This is demonstrated by the government's track record of providing strong credit support to the sector in certain circumstances. The regulator continues to view Wheatley as a systemically important registered social landlord. This, in our view, indicates that financial distress at Wheatley could make it difficult for the regulator to fulfill its statutory objective of protecting tenants, since Wheatley remains a key delivery partner of the Scottish government's affordable housing program. We note that Wheatley lies in the regulator's high category of engagement, based on its large asset base, turnover, debt levels, and significance in its areas of operation.

Selected Indicators

Table 1

Wheatley Housing Group Ltd.--Key statistics

Mil. £	--Fiscal year ends March 31--				
	2023a	2024e	2025bc	2026bc	2027bc
Number of units owned or managed	64,977	64,701	65,253	66,086	66,881
Adjusted operating revenue	364.7	381.8	399.0	410.8	433.5
Adjusted EBITDA	85.4	80.8	97.2	107.6	116.2
Non-sales adjusted EBITDA	85.4	80.8	97.2	107.6	116.2
Capital expense	137.6	167.5	234.7	282.0	272.5
Debt	1546.0	1616.7	1715.4	1801.9	1900.8
Interest expense	63.3	65.3	66.3	69.5	74.5
Adjusted EBITDA/Adjusted operating revenue (%)	23.4	21.2	24.3	26.2	26.8
Debt/Non-sales adjusted EBITDA (x)	18.1	20.0	17.7	16.8	16.4
Non-sales adjusted EBITDA/interest coverage(x)	1.3	1.2	1.5	1.5	1.6

a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N.A.--Not available.

Ratings Score Snapshot

Table 2

Wheatley Housing Group Ltd.--Ratings score snapshot

	Assessment
Enterprise risk profile	2
Industry risk	2
Regulatory framework	2

Table 2

Wheatley Housing Group Ltd.--Ratings score snapshot (cont.)

	Assessment
Market dependencies	2
Management and governance	2
Financial risk profile	3
Financial performance	4
Debt profile	4
Liquidity	2
Stand-alone credit profile	a+
Issuer credit rating	A+

S&P Global Ratings bases its ratings on nonprofit social housing providers on the seven main rating factors listed in the table above. Our "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

Related Research

- Full Analysis: United Kingdom, April 22, 2024
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2024, March 11, 2024
- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2024, March 11, 2024
- U.K. Social Housing Borrowing 2024: Borrowing capacity remains constrained, March 6, 2024
- European Housing Markets: Forecast Brightens Amid Ongoing Correction, Jan. 25, 2024
- Non-U.S. Social Housing Sector Outlook 2024: At A Turning Point?, Nov. 29 2023
- Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks, Oct. 23, 2023
- U.K. Social Housing Providers' Credit Headroom Could Tighten If The Operating Environment Deteriorates, Oct. 4, 2023

Ratings List

Ratings Affirmed

Wheatley Housing Group Ltd.

Wheatley Homes Glasgow Ltd.

Issuer Credit Rating A+/Stable/--

Lowther Homes Limited

Issuer Credit Rating A/Stable/--

Wheatley Group Capital PLC

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.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceid/504352>. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.

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