Research Update:

U.K.-Based Housing Association Anchor Hanover Group Assigned 'A+' Rating; Outlook Stable

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Overview

- Anchor Hanover Group benefits from strong demand for its services. It operates a high-quality asset base in the English retirement housing market, where we expect strong demographic growth over the next decade.
- Anchor Hanover aims to maintain very strong liquidity, moderate leverage, and solid interest cover. This is because management is mindful of the group's modest financial profitability from its core activity, the impact of the COVID-19 pandemic, and continued investment in its existing properties.
- We are assigning our 'A+' long-term issuer credit rating to Anchor Hanover.
- The stable outlook reflects our view that management will successfully deliver its refinancing plan and contain its exposure to developments for sale.

Rating Action

On March 23, 2021, S&P Global Ratings assigned its 'A+' long-term issuer credit rating to Anchor Hanover Group. The outlook is stable.

Rationale

The rating on Anchor Hanover is underpinned by the group's focus on traditional activities, strong demand for its units, and its excellent asset quality demonstrated by very strong operational metrics. Anchor Hanover was formed in 2018 following the merger of Anchor Trust and Hanover Housing Association. It has about 54,000 properties under management across England, operating in more than 85% of local authorities. The group focuses on social and affordable rent accommodation, mainly retirement housing, independent living schemes, and care homes. The group also offers its tenants some home-ownership alternatives, both shared ownership and outright sales. In our view, the retirement housing and care segments carry low industry risk globally given their low cyclicality, high demand, and ongoing regulatory oversight.

The group mainly operates in a stable and predictable segment of social housing. We think its exposure to higher-risk developments for sale activities will remain very contained, averaging less than 10% of total revenue in the fiscal year ending March 31, 2021 (FY2021) to FY2023. Following completion of the group's refinancing and corporate restructure, expected in FY2022, we understand the group will take advantage of its new headroom to increase development, delivering 5,700 units over 10 years. We expect the plan will be split evenly between socially rented tenures, shared ownership units, and outright sales. Overall, we think Anchor Hanover's strategy aligns with the market conditions and that management and the board have extensive experience in the business segment in which they operate.

Strong demand for Anchor Hanover's units stems from the high standard of its assets and the population segment that it targets--that is, tenants aged 60 years and above. England has an increasing aging population, with the Office for National Statistics forecasting the number of people over 60 years old to increase by 2% each year until 2030. The strong growth of Anchor Hanover's target customer base is also reflected in its waiting list, which increased to 30,000 individuals in March 2020 from 19,000 in March 2019. The group's nationwide presence in more than 85% of local authorities allows it more flexibility to develop and grow in those areas where demographic demand increases at a faster pace. Anchor Hanover demonstrates very strong operational metrics compared with peers thanks to these demographic trends and management's focus on operations. We also note that the rollout of new welfare reforms in England did not affect the group's operational metrics. Over the past two years, voids have remained very low, at about 0.5% of rent and service charge income in vacant properties, and gross arrears have remained below 3% of rent and service charge income.

However, Anchor Hanover's exposure to care leads to structurally low margins, which have further diminished due to the pandemic and the group's increasing investment in its existing stock. These factors will keep the group's profitability subdued over the forecast period of FY2021-FY2023, with S&P Global Ratings-adjusted EBITDA margins expected to average 12%. Despite high demand for its units, we expect the group will have lower income than budgeted in both FY2021 and FY2022 as a result of pandemic-related reduced occupancy and longer re-let times for its properties. The group has also rephased its repairs program because it was unable to deliver a significant part of its planned expenditure on existing assets in FY2021, and these have now been deferred onto the next two years. This stemmed from both the pandemic and the vulnerable nature of the group's tenants. Anchor Hanover's increasing investments in its existing assets help it to preserve the high quality of its rental units, with more than 70% of its units standing at EPC level C or above. The already high standard of the group's assets enables management to have more flexibility regarding the timing of repairs and maintenance.

Anchor Hanover's debt profile is a rating strength, with modest indebtedness and strong interest coverage. We expect nominal debt will not materially increase over the next two to three years since management will continue to prioritize investments in existing stock and remain cautious regarding leverage, in our view. We expect the group's debt to stay at about 10x EBITDA on average over FY2021-FY2023 in our base case. This is lower than for other rated peers operating in the care sector, for which we see this metric trending toward 18x. We expect interest coverage will remain very solid, averaging 2.5x over FY2021-FY2023. The coverage will further strengthen following the debt refinancing, since Anchor Hanover plans to issue a benchmark bond issuance in mid-2021 as part of a broader refinancing of its existing facilities.

As for other English housing associations, we think there is a moderately high likelihood that Anchor Hanover would receive extraordinary support in case of financial distress. This provides no uplift from the stand-alone credit profile. Anchor Hanover's primary purpose is to provide affordable homes, supporting important policy objectives of the U.K. government. We consider that the Regulator of Social Housing (RSH), a government agency, regulates Anchor Hanover to promote a viable, efficient, and well-governed social housing sector, and maintain lender confidence and low funding costs across the sector. It is therefore our view that the RSH would step in to prevent a default in the sector, based on its record of being willing and able to provide extraordinary support on a timely basis.

Liquidity

We view Anchor Hanover's liquidity position as very strong, and think it could strengthen further following the debt refinancing program. We expect the group to refinance its banking facilities and its outstanding facility with the Bank of England under the Covid Corporate Financing Facility (CCFF) program over the coming months, replacing these facilities with a capital markets bond issuance. We assess the sources-to-uses liquidity ratio at 2.2x, but we expect that following the refinancing, the group's liquidity ratio will strengthen toward 3.0x. The group's very strong liquidity is supported by its high level of undrawn bank facilities and its ability to generate cash consistently in our base case. We view Anchor Hanover's access to external liquidity as satisfactory.

Current sources of liquidity include:

- Our forecast of cash generated from continuing operations of close to £110 million;
- Cash and liquid investments of more than £107 million;
- Proceeds from asset sales of about £10 million; and
- The undrawn, available portion of committed bank facilities or bank lines maturing beyond the next 12 months, and which can be drawn, totaling £245 million.

Current uses of liquidity include:

- Expected capital expenditure of about £58 million;
- Expected repayment of the Bank of England CCFF of £140 million; and
- Interest payable on short- and long-term debt obligations coming due of £25 million.

Outlook

The stable outlook on Anchor Hanover reflects our view that management will successfully deliver its refinancing plan. It also indicates that we expect management to contain the group's exposure to development for sale activities.

Downside scenario

We could lower the rating on Anchor Hanover should its strategy deviate to incorporate higher exposure to more risky activities, especially developments for sale. We could also lower the rating should the financial impact of the pandemic weaken margins more than we expect, putting greater pressure on financial performance and on the group's interest coverage than we currently forecast.

Upside scenario

We could raise the rating if management consistently outperforms its business plan's targets and builds a track record of strong alignment to its strategy, combined with a strengthening in margins.

Key Statistics

Table 1

Anchor Hanover Group -- Key Statistics

	--Year ended March 31--				
(Mil. £)	**2018a**	**2019a**	**2020e**	**2021bc**	**2022bc**
Number of units owned or managed	53,441	53,908	54,044	54,182	54,334
Revenue*	511.1	507.4	509.2	541.5	557.3
Share of revenue from sales activities (%)	10.7	8.7	9.0	10.4	9.2
EBITDA*§	76.7	49.3	52.4	64.5	72.4
EBITDA/revenue*§(%)	15.0	9.7	10.3	11.9	13.0
Capital expense§	14.3	23.8	44.7	45.9	95.0
Debt	542.6	604.8	658.7	648.2	700.1
Debt/EBITDA*§(x)	7.1	12.3	12.6	10.0	9.7
Interest expense†	22.0	21.7	26.0	24.2	24.7
EBITDA/interest coverage*§† (x)	3.5	2.3	2.0	2.7	2.9
Cash and liquid assets	152.9	130.2	139.1	131.9	137.7

*Adjusted for grant amortization. §Adjusted for capitalized repairs. †Including capitalized interest. a--Actual. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. e--Estimate. N.A.--Not available.

Ratings Score Snapshot

Table 2

Anchor Hanover Group -- Ratings Score Snapshot

Industry Risk	2
Economic fundamentals and market dependencies	2
Strategy and management	3
Asset quality and operational performance	1
Enterprise profile	2
Financial performance	5
Debt profile	2
Liquidity	2
Financial policies	3
Financial profile	3

Table 2

Anchor Hanover Group -- Ratings Score Snapshot (cont.)

S&P Global Ratings bases its ratings on non-profit social housing providers on the eight main rating factors listed in the table above. S&P Global Ratings' "Methodology For Rating Public And Nonprofit Social Housing Providers," published on Dec. 17, 2014, summarizes how the eight factors are combined to derive each social housing provider's stand-alone credit profile and issuer credit rating. For social housing providers generating more than a third of its consolidated revenues from open market sales, we also refer to the "Key Credit Factors For The Homebuilder And Real Estate Developer Industry."

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, Dec. 17, 2014
- 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

- Global Social Housing Ratings Score Snapshot: December 2020, Dec. 10, 2020
- Global Social Housing Ratings Risk Indicators: December 2020, Dec. 10, 2020
- Outlook 2021: Strong Liquidity Should Help Social Housing Providers Remain Resilient, Dec. 8, 2020
- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, Oct. 23, 2020
- ESG Industry Report Card: Public And Nonprofit Social Housing Providers Outside The U.S., Aug. 4, 2020
- U.K. Social Housing Providers Should Remain Largely Resilient To Short-Term Economic Difficulties From COVID-19, April 23, 2020
- U.K. Social Housing Ratings History: February 2020, March 3, 2020
- Why Most Rated U.K. Social Housing Providers Are At Home In The 'A' Category, Dec. 3, 2019

Ratings List

New Rating; CreditWatch/Outlook Action	
Anchor Hanover Group	
Issuer Credit Rating	A+/Stable/--

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; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.