Research Update:

U.K.-Based Lincolnshire Housing Partnership 'A+' Rating Affirmed; Outlook Negative

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Overview

- We expect Lincolnshire Housing Partnership (Lincolnshire) to continue with the asset rationalization that identified during its preparations for the merger of Shoreline and Boston Mayflower.
- In the short term, Lincolnshire is concentrating on traditional social housing, which generates predictable income streams, to ensure management remains focused on establishing a strong operational basis while the new organization settles in.
- We are therefore affirming our 'A+' long-term issuer credit rating on Lincolnshire.
- The negative outlook reflects the outlook on the U.K. This is because if we were to lower our U.K. sovereign rating, we would no longer factor one notch of uplift for government support into our rating on Lincolnshire.

Rating Action

On April 29, 2019, S&P Global Ratings affirmed its 'A+' long-term issuer credit rating on U.K. social housing provider Lincolnshire Housing Partnership (Lincolnshire). The outlook is negative.

At the same time, we affirmed our 'A+' rating on the £150 million bond issued in September 2014 by Boston Mayflower Finance PLC, Lincolnshire's funding vehicle. Boston Mayflower Finance was set up for the sole purpose of issuing bonds and lending the proceeds to Boston (now Lincolnshire). We view Boston Mayflower Finance as a core subsidiary of the Lincolnshire group.

Rationale

The affirmation is based on our assessment of Lincolnshire's stand-alone credit profile (SACP), which we continue to assess at 'a'. The 'A+' rating incorporates one notch of uplift from its SACP due to our opinion that there is a moderately high likelihood of extraordinary support from the U.K. government, if needed. The rating also reflects our view of the low industry risk under which Lincolnshire operates.

Lincolnshire's area of operation is now spread over a larger geographic area in East England with access to a larger demographic and economic mix, which we view as positive. We think management is adequately operating the merger program; the risks associated with Brexit, such as a strain on the housing market and increasing development build costs; and the rollout of Universal Credit. Financial management is adequate with a focus on protecting financial covenants.

We assess Lincolnshire's economic profile as strong. East England shows slow but steady population growth. The number of households on the local authority's housing waiting list crept over 3,630 in 2018, with 1.1% year-on-year growth since 2016. The area also benefits from lower social rents than market rents. This results in good levels of affordability and a steady demand for social housing, in our view. Lincolnshire continues to concentrate on developing traditional social rent units, which carry lower market risk and have predictable income streams. A small number of low cost home ownership (Shared Ownership) developments supports the local area's housing needs. These units are only built in the areas where a need arises and therefore are not speculative.

Lincolnshire's management adopted a risk-averse business strategy in the post-merger period as demonstrated by the new build development concentrated on traditional social housing activities. A detailed risk strategy and scenario analysis accompany the long-term financial model. The long-term financial model is in line with Lincolnshire's overall strategy. We also view the board and the executive management as well established and experienced to guide the organization through the post-merger period.

We assess Lincolnshire's financial profile as strong. The group has actively managed the roll out of Universal Credit and current rental arrears appear to be falling. Management is engaging with tenants to ensure early detection of potential arrears and working closely with tenants to minimize cases. However, Lincolnshire carries high gross rental arrears, at 6.2%, which is higher than its peers and above the average among the social housing providers that we rate (as of March 2018). The increase in arrears is linked to Shoreline's high gross arrears before the merger.

The annual rent cuts combined with increased capital expenditure on existing (Shoreline) stock after the merger has pressured EBITDA. Some of Shoreline's stock was below the Decent Homes Standard. Lincolnshire has now addressed this, achieving full compliance with the standard in March 2019. The group maintained 22% adjusted EBITDA throughout our base-case period, improving to 24% in 2022 supported by new social units. Lincolnshire has adequate financial policies in place to support the modest development of 435 new units. Development strategy remains prudent, with 75% of new units being social and affordable rent products. The remainder comprises non-traditional low cost home ownership units. There is no open market sales activity in the program. Less than 20% of the development program is committed (as of March 2019), which gives Lincolnshire some flexibility. Under our base case, we forecast an increase in capital expenditure in 2019 reflecting the investment in existing stock to bring it up to the Decent Homes Standard as well as the capital spend on the modest development program. The capital investment program is funded by the existing £29.2 million revolving credit facility (RCF) as well as the issuance of the deferred bond finance. We therefore forecast an increase in long-term debt from £160.7 million in 2019 to £188.9 million in 2022, with the debt-to-adjusted EBITDA ratio rising to 14.8x from 14.3x over the same period. We forecast the relatively high margins from traditional activities to maintain a stable EBITDA interest coverage ratio of 1.5x, on average, over the financial years 2020-2022. Based on the latest valuation of Lincolnshire's stock, our loan-to-value ratio is 59.8% (as of March 2018), reflecting Lincolnshire's higher fixed-to-variable debt ratio.

Liquidity

We view Lincolnshire's external liquidity positon as very strong with adequate access to bank funding and capital markets. This is shown by the fixed term and RCF bank funding, £150 million own name bond issuance, and £15 million private placement in 2014. Of the bond, £75 million is deferred until needed and £29.2 million of the RCF is currently undrawn. As of March 31, 2019, expected sources of liquidity of £49.2 million will cover uses by 1.8x over the following 12 months. Our forecast sources of liquidity excludes the deferred bond. The liquidity uses of £27.7 million includes the forecast capital expenditure on the new build development program and servicing of debt.

Outlook

The negative outlook reflects the outlook on the U.K. sovereign. We could lower the rating on Lincolnshire if we lowered the sovereign credit rating or if we revised downward our view of the likelihood of U.K. government support for the social housing sector. In such circumstances, the positive one-notch uplift to Lincolnshire's SACP would no longer apply.

We could revise the outlook to stable if in the next 12 months we revise the outlook on the U.K. sovereign to stable.

Key Statistics

Lincolnshire Housing Partnership Selected Financial Indicators

	--Year ended March 31--					
(Mil. £)	**2017a**	**2018a**	**2019e**	**2020bc**	**2021bc**	**2022bc**
Number of unites owned or managed	14,065	13,129	13,301	13,433	13,500	13,564
Vacancy rates (%)*	2.2	1.8	N.A.	N.A.	N.A.	N.A.
Arrears (%)*	6.5	6.2	N.A.	N.A.	N.A.	N.A.
Revenue§	51.7	50.5	52.5	51.9	51.9	54.3
Share of revenue from nontraditional activities (%)	1.5	2.8	6.9	6.0	2.9	3.3
EBITDA†	14.3	11.4	11.3	11.7	12.0	12.8
EBITDA/revenue (%)	27.6	22.5	21.5	22.6	23.0	23.5
Interest expense	7.2	7.3	7.3	7.5	7.9	8.4
Debt/EBITDA (x)	10.5	13.1	13.5	13.1	12.8	12.0
EBITDA/interest coverage** (x)	2.0	1.6	1.5	1.6	1.5	1.5
Capital expense†	4.8	16.3	25.9	20.2	19.5	19.7
Debt	158.6	160.7	160.7	167.8	179.8	188.9
Housing properties (according to balance sheet valuation)	251.8	268.9	N.A.	N.A.	N.A.	N.A.
Loan to value of properties (%)	63.0	59.8	N.A.	N.A.	N.A.	N.A.

Lincolnshire Housing Partnership Selected Financial Indicators (cont.)

	--Year ended March 31--					
(Mil. £)	2017a	2018a	2019e	2020bc	2021bc	2022bc
Cash and liquid assets	39.1	30.8	7.1	0.0	0.0	0.0

*Rent and service charge. §Adjusted for grant amortization. †Adjusted for capitalized repairs. **Including capitalized interest. 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

Lincolnshire Housing Partnership Ratings Score Snapshot

Industry Risk	2
Economic fundamentals and market dependencies	2
Strategy and management	3
Asset quality and operational performance	3
Enterprise profile	3
Financial performance	4
Debt profile	3
Liquidity	2
Financial policies	2
Financial profile	3

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: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

Lincolnshire Housing Partnership Ltd.	
Issuer Credit Rating	A+/Negative/--
Lincolnshire Housing Partnership Ltd.	
Senior Secured	A+
Boston Mayflower Finance PLC	
Senior Secured	A+