MOODY'S
PUBLIC SECTOR EUROPE

CREDIT OPINION
3 March 2022

RATINGS

Alliance Homes Group

Domicile	United Kingdom
Long Term Rating	A1
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.

Contacts

Jeanne Harrison +44.20.7772.1751
Vice President - Senior Credit Officer
jeanne.harrison@moodys.com

Gleb Pilipenko +44.20.7772.1234
Associate Analyst
gleb.pilipenko@moodys.com

Sebastien Hay +34.91.768.8222
Senior Vice President/Manager
sebastien.hay@moodys.com

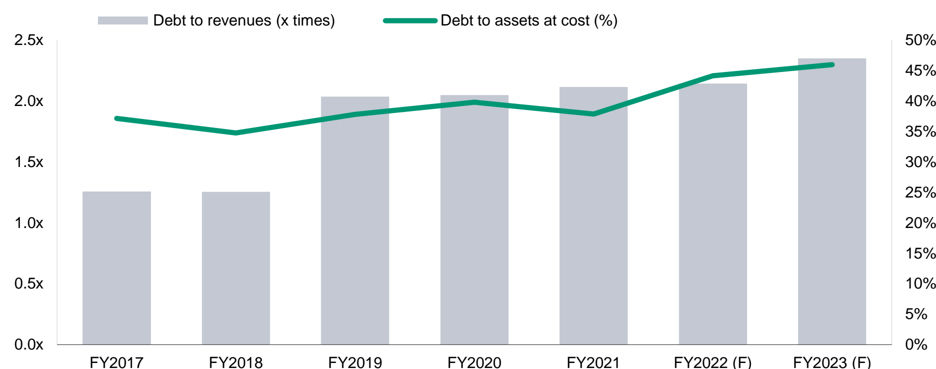
Alliance Homes Group (UK)

Update to credit analysis

Summary

The credit profile of Alliance Homes Group (Alliance, A1 stable) reflects its strong interest cover ratios, low debt to revenues, straightforward debt profile, and growing risk appetite which will result in increased debt and development risk. Alliance also 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
Gearing will increase to support the group's development programme
Debt to revenues (x times) and gearing (debt to assets at cost, %) FY2017-FY2023



Fiscal years ended March 2022 and 2023 (FY2022 and FY2023) are forecasted figures.
Source: Alliance Financial Statements, Moody's forecasts, F=Forecast

Credit strengths

» Very strong interest cover ratios

» Low debt to revenues, simple debt profile and strong unencumbered assets position

» Strong governance and management with clear strategy

» Supportive institutional framework in England

Credit challenges

» Weak profitability

» Increased debt to support new strategy, higher development risk

Rating outlook
The stable outlook on Alliance reflects our expectation that strategy will remain stable, focused on social housing and communities, with limited diversification. The stable outlook also reflects the stable operating and policy environment for English housing associations.

Factors that could lead to an upgrade
Upwards pressure on Alliance's rating would result from a combination of the following key factors: 1) improved operating margin sustained above 35%, 2) reduced gearing (debt to assets at cost) sustained below 40%, 3) market sales exposure sustained at low levels (<5% of turnover), and/or 4) stronger than projected liquidity, with liquidity coverage remaining above 1.5x.

Factors that could lead to a downgrade
One or a combination of the following key factors would result in downward pressure on Alliance's rating: 1) a deterioration in liquidity beyond levels expected in the business plan, 2) a material increase in borrowing pushing gearing above 50%, 3) increased market sales exposure and/or 4) further scaling up of development risk and capital expenditure. In addition, a weaker regulatory framework or a dilution of overall support for the sector could also exert downward pressure.

Key indicators

Alliance Homes Group	31-Mar-17	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22 (F)	31-Mar-23 (F)
Units under management (no.)	6,426	6,488	6,610	6,662	6,689	6,908	7,131
Operating margin, before interest (%)	24.8	20.7	25.3	21.5	23.0	21.4	24.5
Net capital expenditure as % turnover	(1.6)	7.4	23.5	21.0	(2.8)	81.7	35.3
Social housing letting interest coverage (x times)	8.0	7.1	0.9	2.4	2.6	1.9	2.7
Cash flow volatility interest coverage (x times)	8.4	9.6	1.6	4.9	5.3	3.7	4.9
Debt to revenues (x times)	1.3	1.3	2.0	2.0	2.1	2.1	2.3
Debt to assets at cost (%)	37.1	34.8	37.8	39.8	37.9	44.1	46.0

Source: Moody's, Alliance

Detailed credit considerations
The credit profile of Alliance, as expressed in the A1 stable rating, combines (1) a baseline credit assessment (BCA) for the entity of a2 and (2) a strong likelihood of extraordinary support coming from the UK government in the event that the entity faces acute liquidity distress.

Very strong interest cover ratios
Alliance's interest cover ratios are expected to remain strong relative to other Moody's rated English housing associations (HAs). Social housing lettings interest cover (SHLIC) has slightly improved, rising to 2.6x in fiscal 2021 from 2.4x in fiscal 2020. SHLIC is expected average at 2.4x over the next three fiscal years, reaching a low of 1.9x in fiscal 2022, primarily driven by higher maintenance spend as a result of the pandemic backlog and a 20% increase in the interest expense as additional debt will be drawn to fund the development programme. However, the three-year average SHLIC remains slightly above the A1 peer median of 2.3x for the same period.

Alliance's cash flow volatility interest cover (CVIC) was 5.3x in fiscal 2021, an improvement from 4.9x in the prior year. We do note that CVIC is expected to weaken to 3.7x in fiscal 2022, due to additional spend on existing stock and a higher interest expense. Nonetheless, the metric is projected to remain among the strongest of UK-rated peers, averaging 4.5x over the next three years, relative to the A1 peer median of 3.2x.

Low debt to revenues, simple debt profile and strong unencumbered assets position
Alliance's debt to revenue is expected to remain at low levels, as the growth in turnover will match the increase in debt. Debt to revenues has slightly increased to 2.1x in fiscal 2021 from 2.0x in the prior year due to a slight drop in revenues from other social

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housing activities. The metric is expected to remain stable and among the strongest of UK-rated peers, averaging 2.3x, in-line with A1 rated peers.

Alliance has a straightforward debt profile, strong covenant headroom and a large unencumbered asset base. As of November 2021, unencumbered assets could provide additional borrowing capacity of approximately £195 million, which compares favorably to the five year net funding requirement of around £92 million.

Gearing has reduced to 38% in fiscal 2021 relative to 40% in the prior year, as no debt has been drawn over fiscal 2020 and 2021, while reserves grew through additional surplus. However, further debt will start to be in drawn from fiscal 2022, with gearing anticipated to reach 46% in fiscal 2023, compared to the A1 peer median of 31.4% for the same period.

Liquidity coverage has weakened in fiscal 2021, reaching 1.3x or the equivalent of maintaining facilities to cover approximately 32 months of net capital expenditure. The weakening reflects the front-loaded development programme, with net capital expenditure relative to turnover in fiscal 2022 and 2023 reaching 82% and 35% respectively, significantly above historical levels. However, after fiscal 2023, net capital expenditure relative to turnover will average at 35%.

As of November 2021, Alliance held approximately £19 million in cash and cash equivalents as well as immediately available facilities of £29 million. Given the increasing spending on the development programme, Alliance is planning to secure additional funding in June 2022 in order to meet their liquidity golden rule which stipulates maintaining facilities to cover 18 months of cash needs.

Strong governance and management with clear strategy

Alliance demonstrates strong governance and management for its size, including a well-defined strategy, strong financial controls and comprehensive risk management. The development plan and strategy going forward continues to emphasize social housing lettings (SHL), with no plans to develop properties for outright sale, a credit positive.

Moreover, we do note the strong risk management practices which provide some counterbalance to the development ambitions, such as maintaining a liquidity buffer of 18 months with a 24 month trigger and maintaining comfortable cash balances, with a golden rule of £5 million and a trigger at £8 million. While the golden rule relating to interest coverage is generally weaker than other rated HAs, there is substantial covenant headroom, which is expected to be maintained going forward.

The clear strategy is also reinforced by Alliance completely exiting its care operations in November 2021, which will reduce both financial and reputation risk associated with this tenure and consequently enable it to focus on its core SHL operations as demonstrated within its development plan.

Lastly, risk awareness and management is embedded throughout the organisation and risk reporting is clear and comprehensive. In particular, we note the strength of Alliance's stress test reporting.

Supportive institutional framework in England

The sector's credit quality will continue to benefit from the strong institutional framework governing English housing associations (HAs) reflected in an Operating Environment score of a2 and a Regulatory Framework score of a1. These scores are assigned at a national level and reflect the following credit considerations:

The English regulator maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and by undertaking biennial In-Depth Assessments (IDAs) for large and complex HAs. In response to the pandemic, the regulator adapted some aspects of its oversight temporarily, for example, extending its liquidity monitoring, briefly pausing the programme of IDAs and delaying regulatory submissions to reduce the operational burden on HAs. 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 HAs has improved under more supportive policies for social rent increases and capital grant. Following four years of social rent reductions, HAs now benefit from a return to inflation-linked rent increases from April 2020 for five years. In addition, the government has committed to increased capital grant on more flexible terms for new social housing.

Counterbalancing the improvements, we expect policy to drive increased borrowing and development risk in the sector as it responds to the government's objective to deliver a significant increase in the construction of new homes.

Weak profitability

Alliance's operating margin is expected to remain largely stable at 24% over the next three years, above the A1 peer median of 22% for the same period but below the overall rated peer median of 26%. The operating margin is largely a result of the less profitable SHL activities relative to our rated peers, which are expected to generate a margin of 22% over the next three years and the relatively low anticipated margin on first tranche ownership sales with the margin averaging at 18% for the same period, as more land-led development is being pursued. However, the exit from care will remove some downward pressure from the operating margin, as it is a traditionally low margin activity.

Increased debt to support new strategy, higher development risk

Alliance will increase borrowing over the next few years to fund their development programme, although debt metrics are expected to remain strong. Debt levels have stayed relatively constant over fiscal 2020 and 2021 at approximately £90 million. Additional debt will start to be drawn from fiscal 2022, with debt expected to reach approximately £159 million in fiscal 2025. Development ambitions are reflected in the high net capital expenditure relative to turnover figure. Proceeds from drawn debt will be mainly used to build homes across three primary tenures from fiscal 2022 to 2025: general needs (39%), affordable housing (29%), shared ownership (30%) and others (2%).

As part of the 10-year development strategy, the Board has approved a more varied approach to growth in fiscal 2020, including acquiring land and procuring a construction contractor, building on existing land, and acquiring new homes through S106 partnerships with developers. Previously, growth was centered around S106 purchases but securing schemes has become competitive. In addition, in response to more generous capital grant during the last fiscal year, the group has rebalanced its tenure split in favour of more social rented development.

Outright sales were initially considered in 2018 to cross subsidize development scheme viability in response to low grant levels, representing a departure from the previous risk appetite. However, as grant rates improved, the board removed any outright sales from the 2020 development plan. Therefore, market sales exposure will be concentrated solely on shared ownership with no immediate plans for outright sales over the next few years. The Plan A corporate plan for 2017-2022 is coming to completion, with a new plan being rolled out covering the next five years, with the key strategic priorities focused on customer experience, affordability and investment into existing stock.

Extraordinary Support Considerations

The strong level of extraordinary support factored into the rating 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 (Aa3 stable) is willing to support the sector, as housing remains a politically and economically sensitive issue. The strong support assumption also factors increasing exposure to non-core social housing activities in the sector, that 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 Alliance and the UK government reflects their strong financial and operational linkages.

ESG considerations

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

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 Alliance, the materiality of ESG to its credit profile is as follows:

Environmental considerations are 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. Alliance has a comparatively lower risk to decarbonisation costs with 80% of its stock at EPC C rating or higher (as of February 2022).

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. 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 "Detailed credit considerations" 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 a2 is the same as the scorecard suggested BCA for FY2021.

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

Alliance Homes Group, 31 March 2021

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%	6,689	baa
Factor 3: Financial Performance			
Operating Margin	5%	23.0%	baa
Social Housing Letting Interest Coverage	10%	2.6x	aa
Cash-Flow Volatility Interest Coverage	10%	5.3x	aaa
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	2.1x	a
Debt to Assets	10%	37.9%	baa
Liquidity Coverage	10%	1.3x	a
Factor 5: Management and Governance			
Financial Management	10%	a	a
Investment and Debt Management	10%	a	a
Scorecard - Indicated BCA Outcome			**a2**
Assigned BCA			**a2**

Source:Moody's, Alliance

Ratings

Exhibit 4

Category	Moody's Rating
ALLIANCE HOMES GROUP	
Outlook	Stable
Issuer Rating -Dom Curr	A1

Source: Moody's Investors Service

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