

**CREDIT OPINION**

15 October 2024

Update

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**RATINGS**

**Paragon Asra Housing Ltd**

Domicile	United Kingdom
Long Term Rating	A3
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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**Paragon Asra Housing Ltd (United Kingdom)**

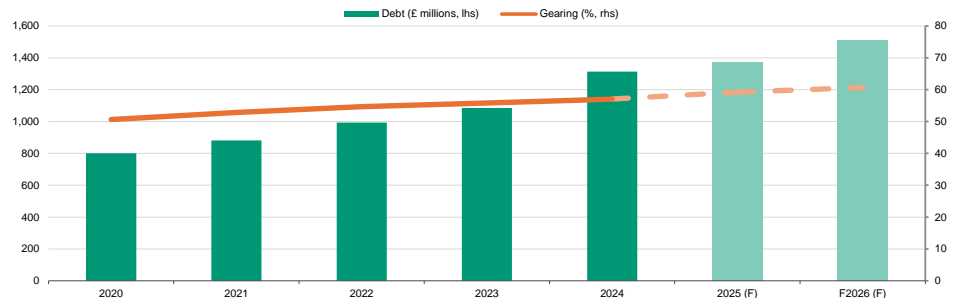
Update to credit analysis

**Summary**

The credit profile of [Paragon Asra Housing Ltd](#) (PA Housing, A3 stable) reflects its strong liquidity and its recent focus on efficiency and risk reduction. It also reflects the weaker operating performance, induced by fire safety costs and impairments, and the increase in debt, both weighing negatively on interest coverage ratios. PA Housing also benefits from the strong regulatory framework governing English housing associations (HAs), and our assessment that there is a strong likelihood that the government of the [United Kingdom](#) (UK, Aa3 stable) would act in a timely manner to prevent a default.

Exhibit 1

**Gearing will continue to increase to fund PA Housing's development programme**



(F): Forecast.

Source: PA Housing and Moody's Ratings

**Credit strengths**

- » Solid liquidity to be maintained because of its robust treasury policies
- » Focus on social housing lettings
- » Supportive institutional framework

**Credit challenges**

- » Debt to continue increasing, weighing negatively on debt and interest cover ratios
- » Weakened operating performance, anticipated to improve with efficiency plans

## Rating outlook

The stable outlook reflects the expected recovery in the operating performance, balancing the high debt.

## Factors that could lead to an upgrade

Upward pressure on PA Housing's ratings could result from a material reduction in debt or a significant increase in government support for the sector, especially significantly higher levels of capital grants.

## Factors that could lead to a downgrade

Downward pressure on PA Housing's ratings could result from a failure to remediate the fire safety risk as planned, a prolonged weakening in operating performance, increased development ambitions, debt growing more quickly than forecasts or weaker liquidity. Lower government support for the sector or a dilution of the regulatory framework could also lead to downward pressure on the ratings.

## Key indicators

Exhibit 2

PA Housing							
	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23	31-Mar-24	31-Mar-25 (F)	31-Mar-26 (F)
Units under management (no.)	21,901	22,312	22,591	23,467	23,810	24,375	25,082
Operating margin, before interest (%)	26.2	23.2	23.0	18.7	16.5	25.7	27.3
Net capital expenditure as % turnover	76.1	66.3	80.2	62.7	63.8	78.9	58.5
Social housing letting interest coverage (x times)	1.2	1.3	1.1	0.9	1.0	0.9	1.0
Cash flow volatility interest coverage (x times)	0.4	1.2	1.1	1.9	-0.6	0.7	0.9
Debt to revenues (x times)	5.4	5.6	5.9	6.0	6.3	6.1	6.2
Debt to assets at cost (%)	50.6	52.9	54.7	55.8	57.1	59.2	60.7

F: Forecast.

Source: PA Housing and Moody's Ratings

## Detailed credit considerations

PA Housing's A3 stable rating combines (1) its Baseline Credit Assessment (BCA) of baa2 and (2) a strong likelihood that the UK government would act in a timely manner to prevent a default.

### Baseline Credit Assessment

#### Solid liquidity to be maintained because of robust treasury policies

PA Housing has a robust liquidity policy, mitigating treasury risk. Golden rules state that the group will hold sufficient cash and liquid resources to cover at least the next 18 months' forecast net cash requirement excluding 50% of committed market sales proceeds, mitigating market sales exposure risk. They also state that the HA should commence work to secure new facilities 24 months before the funding needs.

Its liquidity coverage ratio was strong at 1.2x as of June 2024, with £16 million in cash and £374 million in secured undrawn facilities available within 48 hours. Including an additional £100 million available within 72 hours, the liquidity coverage ratio would have been 1.5x. PA Housing also benefits from a strong unencumbered assets position, which supports additional borrowing capacity of £468 million, which combined with its undrawn and charged position, compares well with funding needs.

Its treasury policy includes a specific mark-to-market policy requiring a separate liquidity buffer covering an adverse movement of interest rates of 50 basis points. PA Housing reports a large swap portfolio, with a total stand-alone notional value of £260 million and a negative mark-to-market value of £5 million, as of August 2024. This mark-to-market exposure is covered by properties, reducing the impact of potential margin calls.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

**Focus on social housing lettings**

Social housing lettings are projected to represent 85% of PA Housing's turnover over fiscal 2025-29. The high proportion of revenue derived from social housing is credit positive because it generates stable and predictable operating cash flows. PA Housing reduced its internal maximum sales exposure to 15% of turnover, from 25%. PA Housing does not want to develop outright sales schemes because of the higher risks involved and the lack of grants available.

PA Housing's development programme, including regeneration schemes, is supported by grants via its two strategic partnerships with Greater London Authority and Homes England.

PA Housing has a development target to build 5,000 units by 2030, having built 1,300 units to date, however the HA maintains flexibility in reducing this target if necessary to prioritize investment in existing assets. Along with other changes in its operating model, PA Housing reviewed its development strategy, to reduce risk. This includes the preference to work with bigger contractors with larger sites. Additionally, PA Housing is reducing the number of shared ownership units it is building to focus on social and affordable rent units.

In addition to its development programme, PA Housing will dedicate £57 million of capital spending over the next five years on retrofitting and energy efficiency works. On existing stock, PA Housing continues to progress towards its internal target of all stock at EPC-C by 2029. The HA currently reports 79% of its stock at EPC-C.

**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 a3 and a Regulatory Framework score of a1. These scores are assigned at a national level and reflect the following credit considerations:

The regulator maintains strong oversight through quarterly returns, long-term business plans, annual reviews, and regular programmed inspections for HAs with more than 1,000 units. The regulator has a strong track record of intervention in cases of mismanagement or financial stress.

The operating environment for English housing associations remains supportive. Demand for social housing is very high and English housing associations retain some expenditure flexibility, with a track record of controlling costs to mitigate lower income. The UK government confirmed that for fiscal 2026, rent increases within the English sector will be pegged at the September Consumer Price Index (CPI) plus 1%. The one-year extension of the rent settlement is positive, although it doesn't provide clarity over the medium-term.

**Debt to continue increasing, weighing negatively on debt and interest cover ratios**

PA Housing plans to materially increase its debt to fund its development programme and investment in existing assets. Gross debt is planned to increase to £1.7 billion by fiscal 2027 from £1.3 billion in fiscal 2024 weighing on the PA Housing's debt metrics. The future increase in debt depends on the pace of the development programme, which was slower than expected in the past three years due to contractor failures and challenging operating environment. PA Housing recently chose to slow its development starts to focus on existing assets and re-start stalled development sites.

PA Housing's debt metrics have already weakened as the group steadily grew its debt over the past five years. Debt/revenue was high at 6.3x in fiscal 2024 partially due to increased drawing of debt to repay some facilities after year end, but nonetheless comparing negatively with the A3-rated peer median of 4.6x. Gearing (debt/assets at cost) also weakened to 57%, comparing negatively with the A3-rated peer median of 52%. Gearing is anticipated to worsen to 61% by fiscal 2027, well above that of peers, a credit negative. Similarly, debt/revenue is expected to remain high compared to peers, reaching 6.4x in fiscal 2027.

In line with the debt increase, net interest costs are projected to increase to £60 million by fiscal 2027 from £40 million in fiscal 2024, which will weigh on PA Housing's interest cover ratios. PA Housing's social housing letting interest coverage (SHLIC) was in line with the A3 peer median in fiscal 2024 at 1.0x, while its cash flow volatility interest coverage (CVIC) suffered significantly in 2024 at -0.6x compared to the A3 peer median at 1.4x, due to inventory, weakening cash flows from operations in fiscal 2024. Whilst we expect the CVIC to recover, both metrics will be negatively impacted by the increased debt burden and associated rising interest expenses.

### Weakened operating performance, anticipated to improve with efficiency plans

PA Housing's operating margin decreased to 16% in fiscal 2024, explained by increased maintenance spending related to fire and building safety and impairment charges. Fire and building safety costs represented £5 million of operating costs, of which £4 million are attributed to waking watch and fire safety cover costs. The operating margin will continue to be impacted by fire safety works until fiscal 2026, as PA Housing plans for most of the works to be done by then.

PA also faced impairments of £15.6 million caused by contractor failures and impaired land bank sites which PA expects to dispose of in the future. Excluding both, the operating margin would have been 24%, compared to 22% the year before (excluding safety costs), an improvement despite higher repairs and maintenance costs.

PA Housing has established an internal target of 25% of operating margin on social housing lettings, having achieved 23% in fiscal 2024, dropping its previous target of 30%. PA Housing worked to reduce its cost base through a restructuring plan, plus renegotiating and exiting contracts, improvements around its procurement platform, merging resident teams and building its in-house recruitment and maintenance teams. Some of the savings achieved are reinvested to improve the quality of existing assets and the service provided to tenants.

On the other hand, margins on market sales remained stronger than peers, at 28% in fiscal 2024. PA Housing's market sales exposure is moderate at an average of 12% of turnover annually in the next three years. Unsold units remain high compared to peers, but high values margins are achieved when sold.

### Extraordinary support considerations

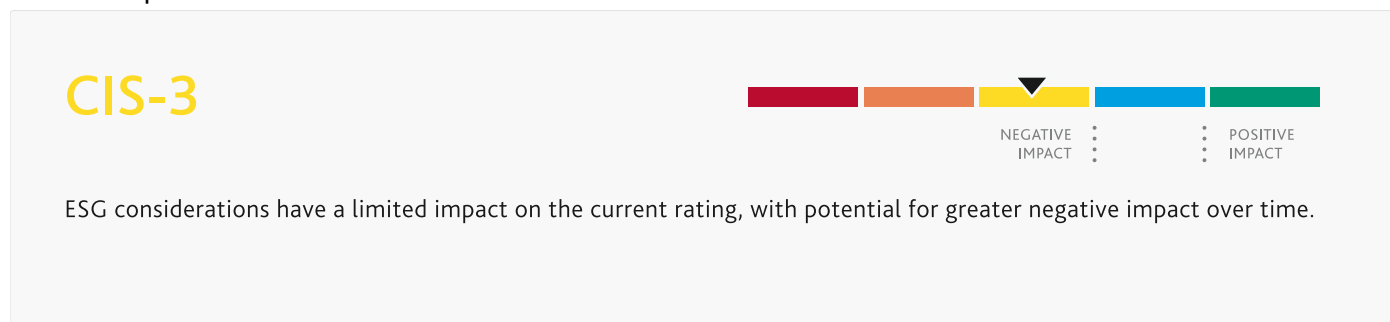
The strong level of extraordinary support factored into the rating reflects the wide-ranging powers available to the regulator in cases of financial distress, with the possibility of a facilitated merger or a transfer of engagements. However, the process can be protracted and is reliant on HAs agreeing to merge, which could be more challenging in a weakening operating environment. 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 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 PA Housing and the UK government reflects their strong financial and operational linkages.

## ESG considerations

### Paragon Asra Housing Ltd's ESG credit impact score is CIS-3

Exhibit 3

#### ESG credit impact score



Source: Moody's Ratings

PA Housing's **CIS-3** reflects our view that ESG risks have a materially negative impact on its rating. In particular, expenditure requirements related to the carbon transition and building safety will weaken margins and increase financing needs.

Exhibit 4

## ESG issuer profile scores



Source: Moody's Ratings

### Environmental

PA Housing has a material exposure to environmental risks (**E-3**) relating to a significant proportion of its stock requiring retrofit (21% as of fiscal 2024) to meet energy efficiency standards by 2035 (carbon transition risks), leading to increased expenditure.

### Social

PA Housing is highly exposed to social risks (**S-4**) through sector-wide legislative requirements to improve the safety of existing housing stock (responsible production risks) for which PA Housing has considerable expenditure requirements which will weigh on its margins and interest coverage over the medium term. PA Housing is also affected by cost of living or affordability pressures on social tenants (demographic and societal trends) which led to the UK government capping social rent increases below inflation in fiscal 2024 in England, which will also have a negative impact on margins.

### Governance

PA Housing has limited governance risks (**G-2**). Its governance is fit for purpose, with strong financial management policies and processes, detailed reporting and a simple organisational structure. The regulatory framework also supports good governance in the sector.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

### Rating methodology and scorecard factors

The assigned BCA of baa3 is one notch below the scorecard-indicated BCA of baa2.

The methodologies used in this rating were [European Social Housing Providers](#), published in July 2024, and the [Government-Related Issuers Methodology](#), published in January 2024.

Exhibit 5

## Fiscal 2024 scorecard

## Paragon Asra Housing Ltd

Baseline Credit Assessment	Sub-factor Weighting	Value	Score
<b>Factor 1: Institutional Framework</b>			
Operating Environment	10%	a	a
Regulatory Framework	10%	a	a
<b>Factor 2: Market Position</b>			
Units Under Management	10%	23,810	a
<b>Factor 3: Financial Performance</b>			
Operating Margin	5%	16.5%	baa
Social Housing Letting Interest Coverage	10%	1.0x	baa
Cash-Flow Volatility Interest Coverage	10%	-0.6x	b
<b>Factor 4: Debt and Liquidity</b>			
Debt to Revenue	5%	6.3x	b
Debt to Assets	10%	57.1%	b
Liquidity Coverage	10%	1.2x	a
<b>Factor 5: Management and Governance</b>			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	baa	baa
<b>Scorecard - Indicated BCA Outcome</b>			<b>baa3</b>
<b>Assigned BCA</b>			<b>baa2</b>

Source: PA Housing and Moody's Ratings

## Ratings

Exhibit 6

<b>Category</b>	<b>Moody's Rating</b>
<b>PARAGON ASRA HOUSING LTD</b>	
Outlook	Stable
Baseline Credit Assessment	baa2
Issuer Rating -Dom Curr	A3
Senior Secured -Dom Curr	A3
<b>PARAGON TREASURY PLC</b>	
Outlook	Stable
Senior Secured -Dom Curr	A3

Source: Moody's Ratings

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