FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms A2Dominion Housing Group Limited at 'A'; Outlook Stable

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Fitch Ratings - London - 02 Nov 2021: Fitch Ratings has affirmed A2Dominion Housing Group Limited's (A2D) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDR) at 'A' with Stable Outlooks. A full list of ratings is detailed below.

KEY RATING DRIVERS

Fitch assesses A2D's performance as strong despite the challenges that have affected the sector over recent years. Continued high demand for social and affordable housing, cost-efficiency measures and diversification into non-core business should allow A2D to maintain sufficient revenues for debt servicing, as well as cross-subsidising its core business. Its Standalone Credit Profile (SCP) is assessed at 'a-'

SCP Under the Revenue Supported Rating Criteria

Revenue Defensibility: 'Stronger'

Demand for social housing (SH) remains strong and any change in the rents that RPs are able to charge would be unlikely to materially affect demand. Nevertheless, our assessment of revenue is somewhat constrained by the lack of control RPs have on rents. The supportive regulatory regime aims to maintain compensation at a level that would consistently support the solvency of not-for-profit providers of essential public services.

However, Fitch expects revenue from housing benefits as a percentage of total revenue to eventually fall, due to increased revenue from non-SH activity. RPs have the flexibility to collect enough non-SH revenue to cover all costs.

Operating Risk: 'Stronger'

A2D has well-identified cost drivers and low potential volatility in major items. It has material capex in its development plans in the medium term but has flexibility to scale back committed schemes, defer uncommited schemes as well as switch tenure from sale to market rent. It has fairly low rigid staff costs in comparison to peers', equating to less than 30% of operating costs.

A2D owns or manages 99 high-rise buildings, which could be subject to fire safety costs. All have had intrusive fire-safety inspections. A2D anticipate costs of around GBP135 million to remediate its stock, with GBP55 million anticipated from the Governments Building Safety fund. A2D will use their stock rationalisation proceeds to reinvest in existing stock and develop new assets, and expects proceeds of around GBP200 million from selling non-core assets.

A2D has already stress-tested and run multi-variable scenarios for its business plan (BP). The scenarios include loan portfolios being repriced at higher lending margins, sales prices falling, delays in sales, inflation, increasing arrears and bad debt as well as political factors such as further rent reductions. To mitigate these effects and to be able to comfortably meet covenants, A2D has put forward corrective measures, including pre-emptive and responsive actions. Fitch will continue to monitor the resilience of A2D and assess its ability to overcome possible further turmoil. We will also closely review the robustness of its stress-testing relative to its ratings, including the impact of the Brexit vote on its business plan, and assess its flexibility to adapt to new market conditions.

Financial Profile: 'Stronger'

We expect A2D's performance to improve, aided by a mixed-tenure development plan that aims to deliver housing for sale as well as affordable housing and market-rent properties. Profits from the sale of private units will be re-invested in the RP to continue to build and provide affordable social units.

A2D is now one of the largest RPs in London and the south-east of England with just over 38,000 units. It reported GBP322 million operating revenue in financial year to March 2021 and EBITDA of GBP110 million. Debt at FYE21 remained stable at GBP1.7 billion and is expected to decrease to GBP1.6 billion by FYE26. Fitch expects net debt/Fitch-calculated EBIDTA to remain below 12x after FYE23. Our rating case forecasts operating revenue on average at about GBP400 million over the five years to FY26.

A2D has no group covenants. However, there are interest cover and gearing covenants within its two main subsidiaries, A2D Homes and A2D South. These covenants are met within the BP and in the stress- tested BPs, albeit with diminished headroom. Over the last decade, A2D has developed over 7,500 properties, and currently has almost 5,500 in their development pipeline. The tenure split is expected to be 30% affordable rent, 17% shared ownership, 6% private rent and 47% private sale. A2D has formed a strategic partnership with the GLA, securing GBP121 million in grant funding, or around GBP60,000 per unit delivered. A2D's profile is supported by high-value assets based in London, with significant sale values, if needed, to maintain operations and repay debt, as well as EBITDA/cash interest coverage above 1.5x across the rating case.

Under Fitch's Revenue-Supported Debt Criteria, the combined assessment of 'Stronger' revenue defensibility, operating risk and financial profile leads to an 'a-' SCP for A2D.

DERIVATION SUMMARY

A2D's 'a-' SCP under our Revenue Supported Debt Criteria (up to three notches away from the UK's sovereign of 'AA-/Stable'), and a support score of 12.5 points under our Government-Related Entities (GRE) Criteria lead to a bottom-up rating approach plus one notch under our notching guideline table.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-A sustained improvement in net debt/ EBITDA towards 10x in the medium term or a favourable change to our assessment of key rating factors.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-A multi-notch downgrade to the sovereign's ratings, deterioration of net debt/ EBITDA to above 12x on a sustained basis or an adverse change to our assessment of key rating factors.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING			PRIOR
A2Dominion Housing Group Limited	LT IDR	A Rating Outlook Stable	Affirmed	A Rating Outlook Stable
•	ST IDR	F1+	Affirmed	F1+
•	LC LT IDR	A Rating Outlook Stable	Affirmed	A Rating Outlook Stable

ENTITY/DEBT	RATING			PRIOR
•	LC	F1+	Affirmed	F1+

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Government-Related Entities Rating Criteria (pub. 30 Sep 2020)

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 01 Sep 2021) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

A2D Funding II plc	UK Issued, EU Endorsed
A2D Funding plc	UK Issued, EU Endorsed
A2Dominion Housing Group Limited	UK Issued, EU Endorsed

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