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Ratings

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Research Update:

Housing Finance Corp. Ltd. 'A/A-1' Ratings Affirmed; Outlook Stable

September 27, 2023

Overview

- Despite inflationary pressure and high interest rates, we believe credit quality of The Housing Finance Corp. Ltd. (THFC) will remain strong.
- We expect THFC's management policies and governance standards will support the company's robust capitalization, and strong funding and liquidity ratios.
- We therefore affirmed our 'A/A-1' long- and short-term issuer credit ratings on THFC and maintained the stable outlook.

PRIMARY CREDIT ANALYST

Ekaterina Ermolenko
Stockholm
46 708 770 286
ekaterina.ermolenko
@spglobal.com

SECONDARY CONTACT

Abril A Canizares
London
+ 44 20 7176 0161
abril.canizares
@spglobal.com

ADDITIONAL CONTACT

Sovereign and IPF EMEA
SOVIPF
@spglobal.com

Rating Action

On Sept. 27, 2023, S&P Global Ratings affirmed its 'A/A-1' long- and short-term issuer credit ratings on funding agency The Housing Finance Corp. Ltd. (THFC). The outlook is stable.

We also affirmed 'A' long-term and 'A-1' short-term issuer credit ratings on THFC's core subsidiary, THFC Sustainable Finance PLC.

At the same time, we affirmed our 'A' issue ratings on debt issued by THFC's three orphan funding subsidiaries: T.H.F.C. (Funding No. 1) PLC, T.H.F.C. (Funding No. 2) PLC, and T.H.F.C. (Funding No. 3) PLC. These ratings mirror the 'A' long-term issuer credit rating on THFC.

The 'AA' issue rating on debt issued by THFC's subsidiary Affordable Housing Finance PLC (AHF) reflects the exclusive guarantee by the U.K. government, which we consider as timely, unconditional, and irrevocable.

Outlook

The stable outlook indicates that S&P Global Ratings expects THFC to remain a leading U.K. Social Housing aggregator, despite strong competition in the sector and a 2% year on year decline in the balance sheet. In our view, THFC's very conservative risk management practices will enable it to maintain a strong financial risk profile notwithstanding high inflation and pressure on the social housing providers in the U.K.

Downside scenario

We could lower our rating if credit quality in the U.K. social housing sector deteriorated significantly, eroding the company's reserves. We could also lower the rating if THFC's risk management policies became less prudent and the company's balance sheet diminished.

Upside scenario

We could raise the rating if the company's market position strengthened significantly following the pick-up in the borrowing needs from the U.K. social housing associations with the risk management standards remaining strong.

Rationale

The 'A' issuer credit rating is based on THFC's strong financial profile and adequate enterprise profile.

Our rating on THFC reflects our view of the low industry risk of the U.K. social housing sector, to which the company lends. Having said that, we expect the U.K. social housing sector in general to face increased costs caused by inflation and the need to achieve energy efficiency and fire safety targets. Together with elevated interest rates, this could result in financial and debt metrics weakening across the sector. However, we believe THFC's prudent risk management policies will likely help mitigate the pressure coming from the weakening credit quality of the social housing sector in the U.K.

The rating also indicates that THFC maintains a solid market position compared with that of other U.K. aggregators, with a loan book of £8.13 billion or 7.8% of the social housing sector's total debt stock as of March 31, 2023.

The company's strong capitalization and robust funding and liquidity ratios support the rating.

Enterprise risk profile: Relevant role in a competitive market, with robust risk management practices that protect the group against sector pressure

Our U.K. Public-Sector Industry Risk and Country Risk Assessment (PICRA) benefits from low cyclicality, high barriers to entry, and strong government oversight via regulators. The PICRA also considers the wealthy, open, and diversified U.K. economy. Although we believe that higher leverage has increased risks to the U.K. social housing sector, we project that debt metrics will improve and we still consider the U.K. social housing sector to be low risk, which supports the THFC's rating.

We believe the THFC loan portfolio growth will likely be modest because we estimate incremental borrowing demand from U.K. social housing providers will reduce as they prioritize investments in existing stock by reducing development of the new homes. Nevertheless, we believe the company will likely preserve its market share and will remain the largest aggregator in the market. As of the fiscal year 2023 (ended March 31, 2023), THFC had a loan book of £8.13 billion, slightly decreasing from £8.22 billion in fiscal 2022 and providing funding to 159 borrowers. THFC accounted for 7.8% of the social housing sector's total debt stock and for about 2.2% of the sector's funding needs in fiscal 2023 compared with 9% in fiscal 2022. We believe this decline is temporary and THFC will resume its lending in the medium term. The company is by far the most successful aggregator, partly thanks to its historic position but also because of its ability to offer better pricing and bring new products to the sector, such as deferred drawdowns and installment fee solutions, which provide more flexibility to borrowers.

In our view, THFC's management has expertise and experience in operating its major business lines. It continues enhancing internal processes and introducing innovative products to adapt to market needs. THFC also enjoys a robust governance framework since, unlike other U.K.-based public-sector funding agencies, the group has board nominees from the regulator of the English social housing sector and from the National Housing Federation, the English housing sector's trade body.

Given that lending is broadly at the same interest rates and on the same repayment schedule as the funds that it borrows, THFC has no interest-rate risk. The group follows a strict matched-funding approach to minimize asset-liability risk. It also does not have currency risk; its funding and lending are both denominated in pound sterling. It also receives payments from borrowers up to a month before payments to investors become due, providing a timing cushion.

Financial risk profile: Consistently strong financial indicators, combined with robust risk management policies to mitigate potential risks on asset quality

We assess THFC's capital adequacy as very strong, supported by a strong risk-adjusted capital (RAC) ratio, its business construct as a cash-flow pass-through vehicle, and robust collateralization on its loan book through physical collateral and debt service reserves.

The RAC ratio has further strengthened to 21.1% from 20.1% in fiscal 2023 following the accumulated reserves, which increased to £57 million as of March 31, 2023, because of the £5.8 million profit after tax. Furthermore, after adjusting for single-name concentration on the loan book, the RAC ratio strengthened to 14.7% in fiscal 2023 from 13.9% in fiscal 2022.

Of THFC's portfolio, £3.2 billion or almost half of the loan portfolio, benefits from the double-guarantee scheme the U.K. government provides to its subsidiary, AHF. Therefore, given we perceive the central government is more creditworthy than the social housing sector, we believe that the guarantee reduces the exposure to the sector significantly.

We assess THFC's funding and liquidity position as strong, supported by a robust capacity to cover its liabilities, even under severe liquidity stress scenarios. Furthermore, conservative match-funding policies ensure that liquidity ratios will remain structurally well above 1x, meaning that the group has ample cushion to cover its liabilities under a severe liquidity stress scenario without accessing capital markets. Further supporting this view is a one-month gap between the group's obligation to pay investors and payments received from its borrowers.

Key Selected Indicators

Table 1

The Housing Finance Corp. Ltd. -- Selected Indicators

	--Year ended March 31--					
(Mil. £)	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**
Business position						
Total adjusted assets	8,359.8	8,549.1	8,004.4	7,572.6	7,456.8	7,108.0
Gross receivables	8,129.8	8,220.5	7,874.1	7,453.8	7,333.0	6,991.5

Table 1

The Housing Finance Corp. Ltd. -- Selected Indicators (cont.)

	--Year ended March 31--					
(Mil. £)	**2023**	**2022**	**2021**	**2020**	**2019**	**2018**
Growth in loans (%)	-1.1	4.4	5.6	1.7	4.9	18.8
Interest revenue	279.9	267.6	262.0	261.5	258.6	237.2
Noninterest expenses	6.5	6.0	5.2	5.2	4.6	4.3
Capital and risk position						
Total liabilities	8,302.9	8,496.8	7,957.9	7,530.9	7,418.7	7,073.4
Total adjusted capital	56.8	52.3	46.4	41.6	38.0	34.5
Assets/capital	147.1	163.4	172.5	181.9	196.3	206.1
RAC ratio before diversification (%)	21.1	20.1	18.6	17.8	16.6	15.8
RAC ratio after diversification (%)	14.7	13.9	12.4	11.4	10.7	11.9
Funding & liquidity						
Liquidity ratio with loan disbursement (one year)	1.4	2.9	1.2	2.3	1.6	1.7
Liquidity ratio without loan disbursement(one year)	1.4	2.9	1.2	2.3	1.6	1.7
Deposits to total financial liabilities						
Funding ratio (one year)	1.5	3.3	1.5	2.5	1.8	1.9

RAC--Risk-adjusted capital.

Ratings Score Snapshot

Table 2

The Housing Finance Corp. Ltd. -- Ratings Score Snapshot

Issuer credit rating	**A**
Stand-alone credit profile	a
Enterprise risk profile	Adequate (3)
Public-sector industry risk and country risk assessment	Low risk (2)
Business position	Adequate
Management & governance	Adequate
Financial risk profile	Strong (2)
Capital adequacy	Very strong
Funding and liquidity	Neutral and Strong
Support	0
Government-related entity support	0
Group support	0

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Governments | International Public Finance: Public-Sector Funding Agencies: Methodology And Assumptions, May 22, 2018
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Non-U.S. Social Housing Providers Ratings Risk Indicators: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot: March 2023, March 27, 2023
- Non-U.S. Social Housing Providers Ratings History: March 2023, March 27, 2023

Ratings List

Ratings Affirmed	
Housing Finance Corp. Ltd. (The)	
Issuer Credit Rating	A/Stable/A-1
THFC Sustainable Finance PLC	
Issuer Credit Rating	A/Stable/A-1
T.H.F.C. (Funding No. 1) PLC	
Senior Secured	A
T.H.F.C. (Funding No. 2) PLC	
Senior Secured	A
T.H.F.C. (Funding No. 3) PLC	
Senior Secured	A

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.