S&P Global
Ratings

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Research Update:

The Housing Finance Corp. Ltd. Upgraded To 'A+'; Outlook Stable; Off UCO On Implementation Of Revised PSFA Criteria

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Overview

- On July 26, 2024, S&P Global Ratings published its revised "Methodology For Rating Non-U.S. Public-Sector Funding Agencies," (PSFA methodology) and placed its ratings on The Housing Finance Corp. Ltd. (THFC) under criteria observation (UCO).
- Under our updated PFSA methodology, we are more closely linking our analysis of PSFAs to the credit risks of the underlying sector or sectors.
- We assess the risks associated with THFC's lending portfolio as overall low, supported by sovereign guarantees against more than 40% of its loan book.
- Having completed our review of THFC, we have raised our long-term issuer credit rating on the company by one notch to 'A+' from 'A'. We also upgraded THFC's core subsidiary, THFC Sustainable Finance PLC, to 'A+' and raised our issue ratings on debt issued by THFC's three orphan funding vehicles to 'A+': 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. We have removed all the ratings from UCO.
- The outlook is stable.

Rating Action

On Sept. 19, 2024, S&P Global Ratings took the following rating actions:

- Raised its long-term issuer credit ratings (ICRs) on THFC to 'A+' from 'A' and affirmed the short-term ICR at 'A-1'.
- Raised its long-term debt rating on THFC's core subsidiary THFC Sustainable Finance PLC to 'A+' from 'A' and affirmed the short-term ICR at 'A-1'.
- Raised its issue ratings on debt issued by THFC's three orphan funding subsidiaries to 'A+' from 'A': 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.
- Removed the ratings from UCO, where they were placed on July 26, 2024.

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

The outlook is stable.

Outlook

The stable outlook indicates that THFC's leading U.K. Social Housing pass-through vehicle (which operates under a match-funding principle) position and its low-risk operating environment will offset the pressure coming from the strong competition from banks and own-name placements by the social housing providers and some decline in THFC's balance sheet over the past two years.

Downside scenario

We could lower the rating if THFC's risk management policies became less prudent and if the company's relevance diminished, reflected by a substantial decrease of THFC's loan portfolio. We could also lower our rating if credit quality in the U.K. social housing sector deteriorated significantly.

Upside scenario

We could raise the rating if THFC significantly strengthened its market position while maintaining strong risk management standards and asset quality.

Rationale

The rating actions follow a revision to our methodology for rating PSFAs (see "Methodology For Rating Non-U.S. Public-Sector Funding Agencies," published July 26, 2024).

Under our updated PFSA methodology, we are more closely linking our analysis of PSFAs to the credit risks of the underlying sector or sectors. THFC's sector risk profile (SRP) benefits from the low industry risk in the social housing sector globally, and also from the fact that 42% of its loan book is guaranteed by the U.K. government and ultimately carries the risks of an 'AA' entity.

Our rating on THFC also reflects THFC's prudent risk management policies, diversified pool of borrowers, and the company's robust funding and liquidity ratios.

Sector risk profile: underpinned by direct exposure to U.K. based social housing providers and supported by guarantees from the U.K. government. We view the overall SRP of THFC as strong. THFC's loan book has direct exposure to U.K. social housing providers (45% to English providers, small shares in Scotland and Northern Ireland, and 7% to Welsh providers), with the rest being ultimately guaranteed by the U.K. government (AA/Stable/A-1+). Because of this, we apply a weighted-average approach to assess the SRP of the company.

For the unguaranteed part of the loan book, we generally view the industry risk for all U.K.-based social housing sectors as low, which forms the starting point of our assessment. We negatively adjust the SRP component for English social housing providers, to reflect country specific adverse considerations, which are captured in our regulatory framework assessment (see "Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks," published Oct. 23, 2023). Conversely, we think the regulatory frameworks under which SHPs in the devolved regions operate are stronger, and the risk exposure to them is well captured within the sector low industry risk.

The remaining 42% of the loan book (£3.2 billion), is lent via AHF and benefits from a guarantee that complies with our Guarantee Criteria Conditions. We therefore consider this part of the portfolio to carry very low sector risk profile.

Individual credit profile: projected modest loan portfolio growth is counterbalanced by the prudent risk management and robust liquidity thanks to the assets and liabilities matching principle.

We believe the THFC loan portfolio growth will likely be modest in the near term. U.K. social housing providers have scaled down their development programs as they prioritize investments in existing stock. Nevertheless, we believe the company will likely preserve its market share and will remain the largest pass-through vehicle in the market. As of the fiscal year 2024 (ending March 31, 2024), THFC had a loan book of £7.95 billion, slightly decreasing from £8.1 billion in fiscal 2023 and providing funding to 160 borrowers. THFC accounted for about 7% of the social housing sector's total debt stock and for only 0.1% of the sector's funding needs in fiscal 2024 compared with 2.2% in fiscal 2023. We believe this decline is temporary and THFC will resume its lending in the medium term. The company has the longest track record compared with other peers and has historically enjoyed strong portfolio growth. We think future growth will be supported by new products offerings and flexibility to borrowers.

While THFC's loan portfolio underperformed management's targets for the past two years, we expect this to be temporary and anticipate some rebound in the medium term. We think this will be supported by THFC's continued strategy to enhance internal processes and introduce innovative products to adapt to market needs and conditions.

In our view, THFC's management has expertise and experience in operating its major business lines. We understand that there is clear succession planning following several changes in the executive management team recently, and that changes were prepared for and included a transition period.

THFC also benefits from 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. THFC's credit and risk team closely monitors the performance of its borrowers by reviewing their reports and business plans. It also oversees the borrower watch-list and has its own grading system. The team scrutinizes all loan proposals and also provides a credit opinion.

THFC's business model limits interest-rate, currency, and funding risks. This is because lending is broadly at the same interest rates and on the same repayment schedule as the funds that it borrows. 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.

We now assess THFC's initial capital adequacy as adequate, because it operates as a pass-through vehicle and we therefore view it as neutral for our rating on THFC. While under our updated criteria we don't calculate the risk-adjusted capital ratios for pass-through vehicles, we note that THFC has increased its reserves to £63 million in fiscal 2024 from £57 million a year ago.

We assess THFC's funding and liquidity position as strong, supported by its 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.

Selected Indicators

Table 1

The Housing Finance Corp. Ltd. -- Selected Indicators

	--Year ended March 31--					
(Mil. £)	2024	2023	2022	2021	2020	2019
Business position						
Total adjusted assets	8,147.0	8,359.8	8,549.1	8,004.4	7,572.6	7,456.8
Customer loans (gross)	7,952.0	8,129.8	8,220.5	7,874.1	7,453.8	7,333.0
Growth in loans (%)	(2.2)	(1.1)	4.4	5.6	1.7	4.9
Interest revenues	281.0	282.0	267.6	262.0	261.5	258.6
Noninterest expenses	7.2	6.5	6.0	5.2	5.2	4.6
Capital and risk position						
Total liabilities	8,085.0	8,302.9	8,496.8	7,957.9	7,530.9	7,418.7
Total adjusted capital	63.0	56.8	52.3	46.4	41.6	38.0
Assets/capital	129.3	147.1	163.4	172.5	181.9	196.3
Gross nonperforming assets/gross loans	0.0	0.0	0.0	0.0	0.0	0.0
Funding & liquidity						
Liquidity ratio with loan disbursement (one year)	4.0	1.4	2.9	1.2	2.3	1.6
Liquidity ratio without loan disbursement(one year)	4.0	1.4	2.9	1.2	2.3	1.6
Funding ratio (one year)	4.3	1.5	3.3	1.5	2.5	1.8

Ratings Score Snapshot

Issuer credit rating	**A+/Stable/A-1**
Sector risk profile	Strong
Individual credit profile:	
Business position	Adequate
Management & governance	Adequate
Capital adequacy	Adequate
Funding & liquidity	Strong
Anchor	**a+**
Overriding factors and caps	0
Holistic analysis	0

Stand-alone credit profile	**a+**
Extraordinary support	0

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Non-U.S. Public-Sector Funding Agencies, July 26, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- 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

- Ratings On The Housing Finance Corp. Ltd. Placed Under Criteria Observation After Publication Of New Criteria, July 26, 2024
- U.K. Social Housing Borrowing 2024 Borrowing capacity remains constrained, March 6, 2024
- Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks, Oct. 23, 2023
- Housing Finance Corp. Ltd. 'A/A-1' Ratings Affirmed; Outlook Stable, Sept. 27, 2023

Ratings List

Upgraded

	To	**From**
T.H.F.C. (Funding No. 1) PLC		
Senior Secured	A+	A
T.H.F.C. (Funding No. 2) PLC		
Senior Secured	A+	A
T.H.F.C. (Funding No. 3) PLC		
Senior Secured	A+	A

Upgraded; Ratings Affirmed

	To	**From**
Housing Finance Corp. Ltd. (The)		
Issuer Credit Rating	A+/Stable/A-1	A/Stable/A-1
THFC Sustainable Finance PLC		
Issuer Credit Rating	A+/Stable/A-1	A/Stable/A-1