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CREDIT OPINION
27 October 2023

Update

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RATINGS

Riverside Group

Domicile	United Kingdom
Long Term Rating	Baa1
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

Maylis Chapellier +44.20.7772.1429
Analyst
maylis.chapellier@moodys.com

Sebastien Hay +34.91.768.8222
Associate Managing Director
sebastien.hay@moodys.com

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Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Riverside Group (United Kingdom)

Update following downgrade to Baa1 stable

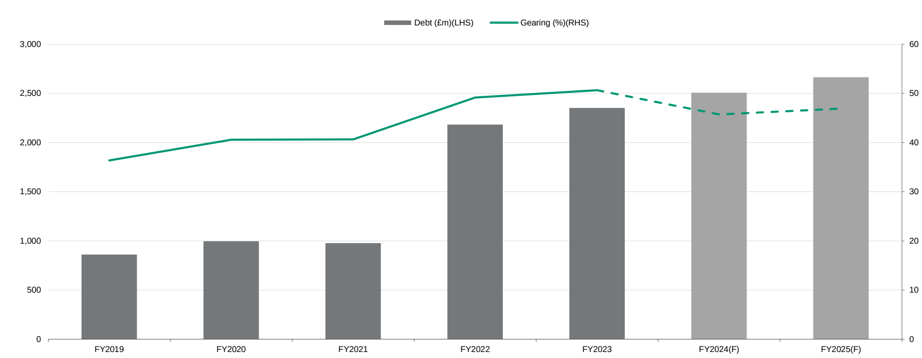
Summary

The credit profile of Riverside Group (Riverside, Baa1 stable) reflects its strong market position, its debt metrics in line with peers and adequate liquidity. It also incorporates a weaker operating performance after its merger in December 2021 with One Housing Group (OHG) and the increased treasury risks resulting from the merger, including refinancing, covenant and interest rate. Whilst Riverside plans to improve OHG's performance and to reduce treasury risks, the weakened economic environment intensifies downward pressures on its operations and increases risk of higher refinancing costs. The rating also incorporates a strong likelihood that the government of the United Kingdom (UK, Aa3 stable) would intervene if the group were to face liquidity distress.

Exhibit 1

Riverside is expected to maintain adequate debt metrics despite the jump in debt following the merger

Debt (£m)(LHS) and gearing (%)(RHS), FY2019-2025(F)



F: here indicates forecast based on Moody's projections. FY2019-2021 are Riverside only, FY2022-2025 show the merged entity, the key driver behind the jump in debt.
Source: Riverside, Moody's Investors Service

Credit Strengths

» Large housing association with nationwide operations and strong policies

» Debt metrics in line with rated peers

» Supportive institutional framework in England

Credit Challenges

» Treasury risk following the merger with OHG

- Low operating margin and interest cover ratios
- Weak performance on market sales but future exposure reduced

Rating Outlook

The stable outlook reflects adequate debt metrics and the proactive steps taken to reduce risk, including generating savings from the merger, scaling back development and reducing the exposure to market sales.

Factors that Could Lead to an Upgrade

Upward pressure on the ratings could result from a marked improvement in operating performance beyond the level currently projected, a reduction in indebtedness and a debt restructuring that effectively reduces the risk posed by the current portfolio combined with an improvement in interest coverage ratios.

Factors that Could Lead to a Downgrade

Downward pressure on the ratings could result from a weakening in financial performance, a ramp-up in risk appetite, including a higher exposure to market sales than the moderate level currently projected, or an increase in indebtedness, including gearing sustained at levels above 60%. A weakening of the regulatory framework or dilution of the overall level of support from the UK government could also lead to downward pressure on the ratings.

Key Indicators

Exhibit 2
Riverside Group

Riverside	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23	31-Mar-24 (F)	31-Mar-25 (F)
Units under management (no.)	56,089	58,360	57,077	75,089	75,088	72,339	73,726
Operating margin, before interest (%)	18.5	15.4	19.8	13.0	5.1	12.2	14.4
Net capital expenditure as % turnover	17.4	56.3	14.7	41.8	43.2	41.2	31.1
Social housing letting interest coverage (x times)	1.1	1.1	1.6	1.0	0.3	0.5	0.6
Cash flow volatility interest coverage (x times)	1.3	1.9	2.7	0.4	0.9	1.0	1.3
Debt to revenues (x times)	2.4	2.8	2.6	4.9	3.8	3.3	3.5
Debt to assets at cost (%)	36.4	40.6	40.6	49.2	50.6	46.0	47.3

F: Forecast based on Riverside's latest business plan. Merged entity from December 2021 (FY2022) onwards, Riverside as standalone entity in prior years. FY2022 income statement incorporates only 4 months of OHG, because of the timing of the merger. FY2023 onwards show the consolidated entity.
Source: Riverside, Moody's Investors Service

Detailed Credit Considerations

On 25 October 2023, Moody's downgraded Riverside's rating to Baa1 from A3 and changed its outlook to stable from negative. The downgrade followed Moody's change in outlook of the Government of the United Kingdom's Aa3 rating to stable from negative on 20 October 2023.

Riverside's rating combines: (1) its Baseline Credit Assessment (BCA) of baa3, and (2) a strong likelihood of extraordinary support coming from the UK government in the event that Riverside faced acute liquidity stress.

Baseline Credit Assessment

Large housing association with nationwide operations and strong policies

Riverside merged with OHG on 1 December 2021, gaining 15,339 additional units, which meant Riverside became the sixth largest HA in the UK with 75,000 units in FY2023. The substantial size of the newly merged entity strengthens its already-strong market position, enhances its political influence over smaller HAs and opens opportunities for further development activity.

The group's strong market position was illustrated in September 2021 when Riverside was selected as a strategic partner for Homes England, thereby securing additional funding (£81 million) that will limit debt growth going forward, a credit positive. Similarly, OHG and Riverside will both receive grants from the Greater London Authority for London-based schemes (respectively £42 million and £19 million). Riverside is politically engaged with dedicated public policy staff in order to ensure its views are heard.

Riverside's credit quality is also supported by its strong financial management controls. We view Riverside's stress-tests and tiered mitigations as more sophisticated than peers. Riverside brought forward by one year (March 2023 instead of March 2024) the transfer of engagements from OHG, to reduce covenant risk and accelerate the merger savings, a credit positive.

Riverside has started to simplify its organisational structure and will continue to do so over the next 2-3 years. The future simplification is required as Riverside inherited from OHG's very complex organisation with multiple joint ventures (JVs).

Debt metrics in line with rated peers

We expect Riverside's debt to revenue to average 3.5x over the next three years, stronger than rated peers (median expected at 4.1x over the same period) a credit positive. Riverside's debt to revenue stood at 3.8x in FY2023, lower than the previous year as FY2023 is the first year with 12 months of OHG. Going forward, Riverside will benefit from the additional income expected to be gained from a full year of trading in the newly merged entity.

Riverside's debt will increase to £2.8 billion by FY2026 (Moody's projections) from £2.4 billion in FY2023 to support the committed development programme. Debt to assets increased to 51% in FY2023, above rated peers 48%. It should decrease in the next few years as grants increase faster than debt.

Riverside's has an adequate level of liquidity as of June 2023, in line with its treasury policy which requires immediately available liquidity to meet cash requirements for the next 18 months. Riverside's liquidity was bolstered by a £300 million bridge funding in December 2022. The HA is planning a debt issuance to consolidate its debt, reduce exposure to variable rate and align its covenants, as well as to fund its development programme. Besides, the group benefits from a solid unencumbered asset position.

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 by undertaking biennial In-Depth Assessments (IDAs) for large and complex 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 remains supportive. Demand for social housing remains very high and the government has committed to increased capital grant on more flexible terms for new social housing. English HAs retain some expenditure flexibility and have a track record of reducing costs to mitigate lower income.

However, due to presently very high rates of inflation, the government has intervened on social rent policy with a 7% ceiling on social rent increases to be implemented from April 2023 for one year. The ceiling of 7% will likely result in an adverse differential between rental income and cost growth, driving lower margins and interest coverage. The intervention introduces policy volatility to the sector as the ceiling will supersede the allowable increase of consumer price inflation (CPI) plus 1% under the current rent standard, which is in place until March 2025.

Treasury risk following the merger with OHG

Following the merger with OHG, Riverside inherited from a higher share of variable debt and a higher refinancing risk than rated peers. As of August 2023, 31% of Riverside's debt was at variable rate, compared to a median of 11% for rated peers. This is risky given the current environment rapidly rising interest rates. Over the next five years, 37% of Riverside's drawn debt will mature, an added risk given the tightening funding conditions. Riverside's debt is complex with many lenders and non-harmonised covenants, which also adds risks. The covenant risk is mainly around interest covers. Despite a recent switch to EBITDA-only from EBITDA MRI, the covenant headroom remains tight after FY2024. We capture those higher risks than peers in our assessment of investment and debt strategy at ba.

Riverside's goal is to simplify its debt, reducing the number of lenders and targeting to have 90% of its debt as long-term and fixed, 10% short-term and variable. The HA plans to continue to reimburse early small loans and to have a smaller number of lenders with harmonised covenants. A £300 million bridging facility was issued in December 2022 to boost liquidity and accelerate the refinancing.

We will monitor the progress and risk reduction, as well as negative externalities. Given the increased interest rates, Riverside may face higher interest payments following its debt consolidation than planned, which will weigh on its interest cover ratios.

Low operating margin and interest cover ratios

Riverside's operating margin is projected to remain very weak at 14% on average over FY2024-2026. This is lower than peers, 25% over the next three years, and will depend on Riverside's sale of one its poorly performing care businesses. Riverside's projections include a higher degree of conservatism than peers having assumed rent cap at 5% for April 2024 and significant salary, overheads and service charge contingencies. While the HA could outperform its pessimistic forecast, we still expect the HA to have among the worst operating margin in our portfolio.

Whilst the HA experiences the same inflationary pressures as peers and the same 7% social rent ceiling, its margin will be weaker primarily due to fire safety costs. The group identified 78 high rise buildings with potential flammable cladding issues, and expects to spend £238 million over the next 5 years on fire/building safety as well as other compliance costs, an average of 7% of turnover per year. Riverside also faces further impairments on OHG's market sales schemes. Besides, Riverside provides care and supported housing, which tend to display lower margins than social housing lettings due to the labour-intensive nature of the work.

Riverside is committed to improve its operating performance and has made significant progress in accelerating the integration of OHG, which will generate savings. Riverside's operating margin could return to a 20% level by FY2030, however this is contingent on the timely realisation of fire safety works, within budget.

The fire safety works, inflation pressures (especially on repair and maintenance), high service costs in relation to the supported housing activities, and the social rent ceiling underpin Riverside's much weaker Social Housing Letting Interest Coverage (SHLIC), 0.3x the lowest among rated peers. Whilst Riverside may outperform its pessimistic forecast (as highlighted above), we anticipate its SHLIC to remain well below rated peers (median of 1.2x over FY2024-26), and below historical performances.

Riverside's cash flow volatility interest coverage (CVIC) stood at 1x in FY2023, which compares adversely to the peer median of 1.7x.[1] We expect CVIC to remain weaker than peers going forward, averaging 1.2x over the next three years as Riverside continues to face challenges on its operations and is also exposed to interest rate risk as it aims refinances debt in less favorable market conditions.

Weak performance on market sales but future exposure reduced

In FY2023, Riverside's operating margin on market sales (first tranche shared ownership and outright sales) stood at 7%, comparing negatively with the median of 17% for our rated portfolio. Over the past three years, Riverside has reported one of the lowest operating margins on market sales of our portfolio, a credit negative.

Riverside will maintain a moderate exposure to market sales, averaging 12% of turnover over the next three years, roughly in line with FY2023. Outright sales will account for half.

Riverside revisited its development programme following the rent cap and the inflationary pressures, slowing down to focus on committed development only and focus on social rented tenure. The group now anticipates to build an average of 875 units each year.

With the slowdown, net capital expenditure (net capex) will average 33% of turnover over the next three years, below the A3-rated peer median.

Capex include retrofitting of existing housing stock, as Riverside aims to improve 1,100 units to EPC C through fabric first measures. This is expected to cost £25 million, and Riverside obtained a £12.7 million of grant via the Social Housing Decarbonisation Fund (SHDF) to contribute towards the cost.

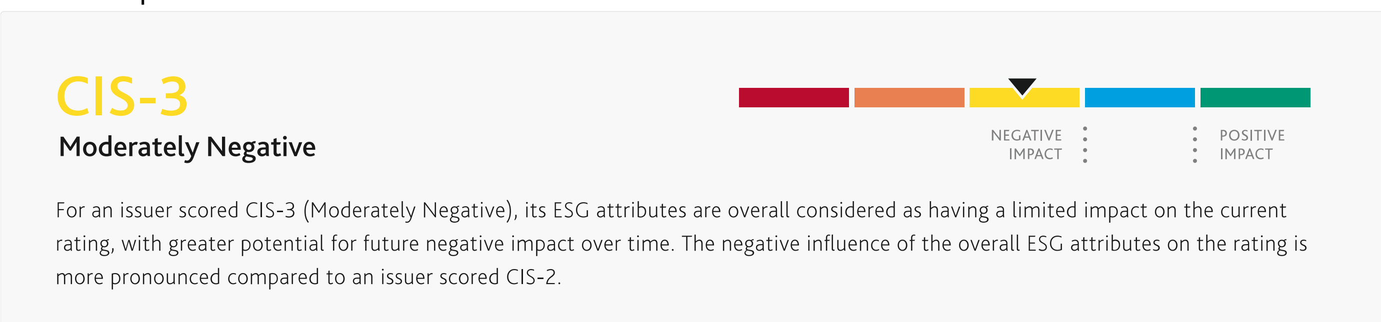
Extraordinary Support Considerations

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 Riverside and the UK government reflects their strong financial and operational linkages.

ESG considerations

Riverside Group's ESG Credit Impact Score is Moderately Negative CIS-3

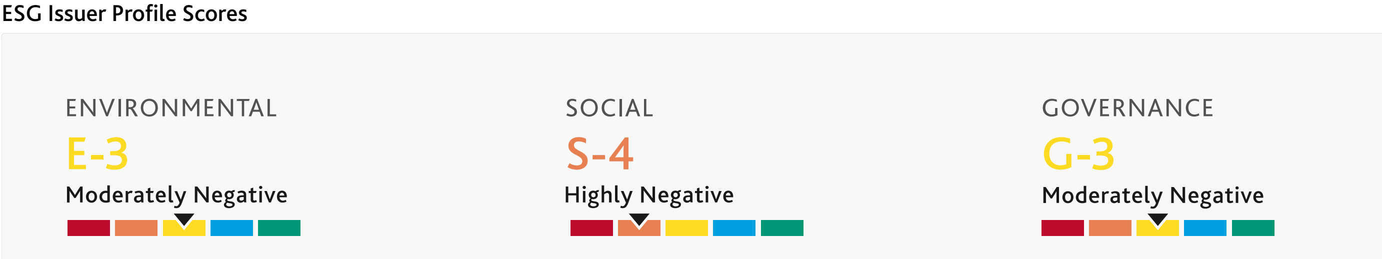
Exhibit 3
ESG Credit Impact Score



Source: Moody's Investors Service

Riverside'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, as well as affordability constraints for low-income tenants which have led to government-imposed sub-inflationary rent caps. Riskier debt structure than peers will weaken credit quality.

Exhibit 4
ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

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

Social

Riverside 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 Riverside has considerable expenditure requirements, following its merger with OHG, which will weigh on its margins and interest coverage over the medium term. Riverside 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. Riverside also has a significant care and support business, which generates lower margins, and is exposed to cost pressures from its ability to recruit skilled staff.

Governance

Riverside has higher governance risks than most of the sector (**G-3**) due to a debt structure that is riskier than is the norm for the sector, inherited from the merger with OHG. Besides, Riverside has a more complex group structure than peers, mostly inherited from One Housing Group. The HA is looking at simplifying both. Somewhat counterbalancing these risks, we view Riverside's management as strong and experienced, with sound policies.

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 in line with the scorecard-suggested BCA of baa3 for FY2023.

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

Exhibit 5

Fiscal 2023 scorecard

Riverside			
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%	75,088	aa
Factor 3: Financial Performance			
Operating Margin	5%	5.1%	ba
Social Housing Letting Interest Coverage	10%	0.3x	b
Cash-Flow Volatility Interest Coverage	10%	1.0x	ba
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.8x	baa
Debt to Assets	10%	50.6%	b
Liquidity Coverage	10%	0.7x	baa
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	ba	ba
Scorecard - Indicated BCA Outcome			**baa3**
Assigned BCA			**baa3**

Source: Riverside and Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
RIVERSIDE GROUP	
Outlook	Stable
Baseline Credit Assessment	baa3
Issuer Rating -Dom Curr	Baa1
RIVERSIDE FINANCE PLC	
Outlook	Stable
Senior Secured -Dom Curr	Baa1

Source: Moody's Investors Service

Endnotes

1 CVIC reflects the ability of pre-interest cash flow from operations, adjusted by the historical volatility (using the standard deviation of pre-interest cash flow from operations over the last three years) to cover net interest. In Riverside's case, it is distorted in FY2023 (1x) as it compares one year of the merged two years of Riverside only and FY2022 with the impact of the merger.

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