S&P Global Ratings

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Research Update:

U.K.-Based Social Housing Provider Aster Group Ltd. Downgraded To 'A' On Weaker Performance; Outlook Stable

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Overview

- We forecast Aster Group Ltd. (Aster)'s credit metrics will weaken as it continues to invest in existing stock while taking on new debt to fund its development program in the higher interest rate environment.
- We think the integration of mergers could create some cost efficiencies, but this might take time to achieve.
- We expect the group's investments in existing homes will further pressure its financial performance.
- We therefore lowered our long-term issuer credit rating on Aster to 'A' from 'A+'. The outlook is stable.

Rating Action

On Dec. 18, 2023, S&P Global Ratings lowered its long-term issuer credit rating on Aster to 'A' from 'A+'. The outlook is stable. At the same time, we affirmed our 'A-1' short-term issuer rating on Aster.

We also lowered our issue rating on the senior secured debt and £1 billion senior secured medium-term note program issued by Aster Treasury PLC, which we consider to be a core subsidiary of the group, to 'A' from 'A+'. We affirmed our 'A-1' short-term rating on Aster Treasury PLC's commercial paper program.

Outlook

The stable outlook reflects our view that Aster's experienced management team will likely take proactive actions should credit metrics come under further pressure.

Downside scenario

We could downgrade Aster if its financial metrics do not recover as we currently expect them to. This could be a result of additional investments in existing assets and new homes development combined with persistently high inflation and challenges associated with integrating recently merged entities. If management fails to effectively control its cost base, or increases its appetite for development, debt metrics could further weaken and pressure the ratings.

Upside scenario

We could raise the ratings if Aster restores its financial metrics to the stronger historical level by improving its margins and containing debt.

Rationale

The downgrade reflects our view that Aster's financial metrics will weaken more than we previously forecast. We anticipate the group will increase social rent adequately and that this will compensate for potential cost inflation in the two years after the rent cap in financial year 2024 (FY2024 ending March 31, 2024). Nevertheless, we expect the group's investments in existing homes will steadily increase, leading to a muted recovery in its financial performance. We also think cost efficiencies from integrating recent mergers will be gradual.

Although the group is moderating its development spend, we project its debt burden will remain elevated to support continued new homes development. The weaker nonsales EBIDTA interest cover also reflects additional costs for its carbon neutral agenda and the currently higher interest rates.

Enterprise profile: Focus on traditional social housing rentals supports credit quality

Aster remains focused on predictable and countercyclical social housing activities in England. The group's sales exposure is largely skewed toward shared ownership, supplemented by outright sales (primarily via joint ventures). Although the level of exposure historically has been close to one-third of total revenue, the group has tightened its risk tolerance so that sales income will be contained below this level on average in the coming two to three years.

We view demand for Aster's properties as strong. Its general needs rents are a fairly low 57% of the prevailing market rents, supporting demand for the group's rental units. Aster's vacancy rate, which averaged about 1.2% of rent and service charges over the past three years, also evidences the strong demand. We consider this rate on par with the sector in England.

In our view, Aster has a stable senior leadership team and good track record of financial management. We think it has robust risk management practices to navigate through current challenges that could stretch its financial and operational capacity. These challenges include business expansion and integration through mergers with three entities since 2020, additional spend on existing stock, continued new homes development and sales, and rising cost of debt. The three merged entities focus on lower margin activities, mainly supported housing and care, and all have weaker financial profiles than Aster. Cecil & Central Housing Trust (CCHT), based in London, has different market dynamics than the rest of Aster's properties. While we believe Aster has sufficient expertise and experience to manage the risks that come with this, integration benefits might take time to materialize.

We assess the regulatory framework under which registered providers of social housing in England operate as strong (see "Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks," published Oct. 23, 2023, on RatingsDirect).

Financial profile: Financial metrics recovery could be prolonged by increasing investments in existing homes and development ambition

We forecast the group's increasing investments in existing homes will continue to depress its financial performance. This keeps our projected adjusted EBITDA margins modestly above 20% in the coming two to three years. Aster's investments in existing homes will start to increase owing to its updated plan based on the latest stock condition surveys. These investments will cover building and fire safety involving remediation works at some of CCHT's properties, and energy efficiency--including all homes achieving Energy Performance Certificate C or above before the U.K. government's 2030 target. The investments are in line with the sector to meet the increased regulatory focus and customer demand for housing quality. Also, we forecast the group will need to continue to stabilize Enham Trust's operations in the near term, which will incur additional costs. While we acknowledge Aster is improving services in this small community, there is significant uncertainty on the perceived long-term financial benefits.

We forecast the group's debt metrics overall will be weaker than our last forecast, but still anticipate they will recover through FY2026. As the group continues to progress with its development plan, we project Aster will build up a moderate level of new debt to fund capital expenditure, despite grant support from Homes England and the proceeds from disposing of some existing properties. While we expect the group will keep most debt at a fixed rate, the higher interest rate environment means the recent medium-term note has a fixed rate that is higher than the historical level. We think the currently higher interest rates will add an extra burden to the group's debt metrics in the near term.

We view Aster's liquidity as very strong. Its liquidity sources will cover uses by approximately 2.3x in the next 12 months. This is based on our forecast of liquidity sources of about £804 million--comprising cash, undrawn and available revolving credit facilities, asset sales, grant receipts, and cash from operations (adding back the noncash cost of sales) that will cover liquidity uses of about £352 million (mainly capital expenditure and debt service payments). At the same time, we believe Aster retains satisfactory access to external liquidity when needed.

Government-related entity analysis

We believe there is a moderately high likelihood that Aster would receive timely extraordinary support from the U.K. government, through the Regulator of Social Housing (RSH) in case of financial distress. This provides a one-notch uplift from the stand-alone credit profile. As one of the key goals of the RSH is to maintain lender confidence and low funding costs across the sector, we believe it is likely that the RSH would step in to try and prevent a default in the sector. We base this view on previous records of the RSH mediating mergers or arranging liquidity support from other registered providers in cases of financial distress and think this would also apply to Aster.

Selected Indicators

Table 1

Aster Group Ltd.--Financial statistics

	--Year ended March 31--				
Mil. £	2022a	2023a	2024bc	2025bc	2026bc
Number of units owned or managed	35,068	36,414	37,185	38,013	39,059
Adjusted operating revenue	240.3	300.2	312.9	354.6	399.4
Adjusted EBITDA	63.9	61.3	66.2	77.0	93.0
Nonsales adjusted EBITDA	57.9	51.0	60.1	70.5	82.0
Capital expense	192.1	250.3	263.9	276.9	275.7
Debt	1,099.0	1,202.2	1,323.7	1,442.5	1,482.0
Interest expense	35.4	38.8	54.1	59.5	58.4
Adjusted EBITDA/Adjusted operating revenue (%)	26.6	20.4	21.2	21.7	23.3
Debt/Nonsales adjusted EBITDA (x)	19.0	23.6	22.0	20.5	18.1
Nonsales adjusted EBITDA/interest coverage(x)	1.6	1.3	1.1	1.2	1.4

a--Actual. e--Estimate. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N.A.--Not available.

Ratings Score Snapshot

Table 2

Aster Group Ltd.--Ratings Score Snapshot

	Assessment
Enterprise risk profile	3
Industry risk	2
Regulatory framework	3
Market dependencies	3
Management and governance	3
Financial risk profile	3
Financial performance	4
Debt profile	4
Liquidity	2
Stand-alone credit profile	a-
Issuer credit rating	A

S&P Global Ratings bases its ratings on nonprofit social housing providers on the seven main rating factors listed in the table above. Our "Methodology For Rating Public And Nonprofit Social Housing Providers," published on June 1, 2021, summarizes how the seven factors are combined to derive each social housing provider's stand-alone credit profile and issuer credit rating.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | General: Methodology For Rating Public And Nonprofit Social Housing Providers, June 1, 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: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Non-U.S. Social Housing Sector Outlook 2024: At A Turning Point?, Nov. 29, 2023
- Non-U.S. Social Housing Providers Ratings Risk Indicators: November 2023, Nov. 15, 2023
- Non-U.S. Social Housing Providers Ratings Score Snapshot: November 2023, Nov. 15, 2023
- Regulatory Framework Assessment: Social Housing Providers In The U.K. Benefit From Strong Regulatory Frameworks, Oct. 23, 2023
- United Kingdom 'AA/A-1+' Ratings Affirmed; Outlook Stable, Oct. 20, 2023
- U.K. Social Housing Providers' Credit Headroom Could Tighten If The Operating Environment Deteriorates, Oct. 4, 2023
- European Housing Markets: Sustained Correction Ahead, July 20, 2023
- U.K. Social Housing Borrowing 2023: On Pause, March 28, 2023
- Non-U.S. Social Housing Providers Ratings History: March 2023, March 27, 2023
- U.K. Social Housing Providers Set Their Sights On Cyber Risks, Dec. 16, 2022

Ratings List

Downgraded; Outlook Action

	To	From
Aster Group Ltd.		
Issuer Credit Rating	A/Stable/A-1	A+/Negative/A-1

Downgraded

	To	From
Aster Treasury PLC		
Senior Secured	A	A+

Ratings Affirmed

Aster Treasury PLC		
Commercial Paper	A-1	A-1