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CREDIT OPINION
16 February 2024

Update

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RATINGS

Orbit Group Limited

Domicile	United Kingdom
Long Term Rating	A3
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.

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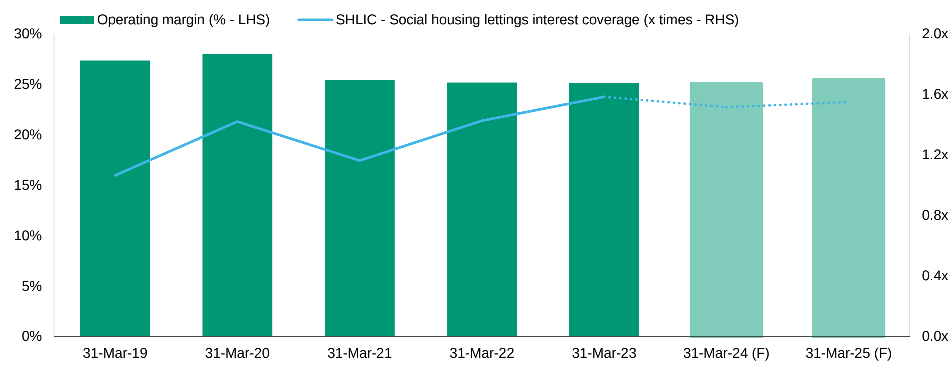
Orbit Group Limited (United Kingdom)

Update to credit analysis

Summary

The credit profile of Orbit Group Limited (Orbit, A3 stable) reflects its strong financial performance, strong liquidity, stable debt metrics and robust risk management practices. Counterbalancing its strengths are its sizeable development programme and high exposure to market sales. Orbit benefits from the strong regulatory framework governing English housing associations and our assessment that there is a strong likelihood that the government of the United Kingdom (UK, Aa3 stable) would act in a timely manner to prevent a default.

Exhibit 1
Orbit's financial performance is expected to remain stable over the next few years



(F) = indicates forecast
Source: Orbit and Moody's Investors Service

Credit strengths

» Stable financial performance

» Strengthened debt metrics and strong liquidity

» Adept management and governance alongside robust risk management practices

» Supportive institutional framework in England

Credit challenges

» High market sales exposure, albeit with good performance to date

Rating outlook

The stable outlook reflects the expected gradual reduction in inflation and associated cost pressures as well as the proactive actions taken by the issuer to mitigate the adverse effects of the weaker operating environment.

Factors that could lead to an upgrade

Upward pressure on the rating could result from a significant improvement in operating performance, a material reduction in debt or a significant increase in government support for the sector.

Factors that could lead to a downgrade

Downward pressure on the rating could result from a prolonged weakening in operating performance, debt growing more quickly than forecast, weaker liquidity or a failure to adapt strategies and risk appetite to mitigate weaker economic conditions. Lower government support for the sector or a dilution of the regulatory framework could also lead to downward pressure on the rating.

Key indicators

Exhibit 2

Orbit Group

	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.)	43,470	44,753	45,702	46,529	47,429	47,502	48,050
Operating margin, before interest (%)	27.3	28.0	25.4	25.2	25.1	25.1	25.4
Net capital expenditure as % turnover	57.8	47.0	14.6	50.3	10.2	45.8	23.3
Social housing letting interest coverage (x times)	1.1	1.4	1.2	1.4	1.6	1.5	1.5
Cash flow volatility interest coverage (x times)	0.5	0.3	1.4	0.5	2.3	1.7	2.5
Debt to revenues (x times)	4.6	4.6	4.8	4.2	3.8	4.3	4.0
Debt to assets at cost (%)	51.5	50.4	48.6	48.8	47.1	49.0	48.1

Fiscal 2019 and 2021 include one-off loan breakage costs of £27.6 million and £15.9 million, respectively. If we omit these one-off costs, SHLIC would have been 1.6x in fiscal 2019 and 1.5x in fiscal 2021.
Source: Orbit and Moody's Investors Service

Detailed credit considerations

Orbit's rating combines: (1) a baseline credit assessment (BCA) for the entity of baa1 and (2) strong likelihood that the UK government would act in a timely manner to prevent a default.

Baseline credit assessment

Stable financial performance

While profitability has been deteriorating across the sector due to rent policies and increasing spending pressures, Orbit's operating margin has been broadly stable over the last three years at around 25%. It now stands above the A3 median of 23%, demonstrating its strong management and cost control. The operating margin on social housing activities is strong - with an average margin of 37% over the past four years and only a small deterioration over this period, from 40% in fiscal 2020 to 35% in fiscal 2023. The overall margin is limited by its high exposure to market sales, which are typically less profitable than social housing lettings.

We expect margins to remain stable over the medium term because of Orbit's relatively limited expenditure needs on fire safety and decarbonisation. This reflects a proactive approach to completing remedial works as well as the characteristics of its housing stock. Orbit started work on energy efficiency in 2017, with more than 84% of its stock now at EPC-C or above compared with a median of 75% across rated UK HAs.

Orbit expects to maintain decent margins on market sales at around 14%. This may become more challenging due to the current housing market downturn as well as cost inflation. However, we note that Orbit exercises strong cost control on its development sites, which enables it to pause development if market conditions are not favourable.

Orbit's interest coverage is stronger than peers, with social housing lettings interest coverage (SHLIC) at 1.6x as of fiscal 2023, above the A3 peer median of 1.0x. Orbit has benefited from its large portfolio of stand-alone and embedded swaps as interest rates have risen, with 99% of its debt fixed or hedged to fixed rates with a very low mark to market position. We expect its SHLIC metric to remain strong in line with its stable debt metrics and financial performance. That said, Orbit intends to increase its reliance on variable rate debt, which will expose it to volatility in interest rates.

Strengthened debt metrics and strong liquidity

Orbit's debt metrics have strengthened in the last three years as higher receipts from market sales and asset disposals have reduced the amount of debt required to fund capital expenditure. As of FYE 2023, its total outstanding debt was £1.6 billion, equivalent to 3.8x revenue (A3 peer median: 4.4x) and 47% of its assets (A3 peer median: 51%). We expect its debt-to-revenue ratio to stabilise at around 4.0x and gearing at 48% on average over the next three years.

Orbit has limited refinancing risk with 13% of drawn debt due for refinancing within the next five years. In addition, Orbit has strong headroom on its interest cover covenants with 150 basis points of headroom over its tightest covenant.

Orbit has strong levels of liquidity in line with its liquidity policy, which includes the need to retain a minimum level of liquidity of 12 months net cash needs in cash and immediately available facilities, and 24 months in cash and committed (but unsecured) facilities. As of December 2023, Orbit held £450 million in cash and immediately available facilities, covering 1.6x net cash needs for the next two years. It also has significant additional borrowing capacity of another £1.3 billion, based on its unencumbered asset position.

Adept management and governance alongside robust risk management practices

Orbit is one of the largest housing associations in the UK, managing around 47,000 units with a strong presence across the Midlands, East of England and South East regions. Its large balance sheet provide better resilience to financial stress relative to smaller housing associations. Its group structure is simple, consisting of the parent company (Orbit Group Limited), the registered provider, a subsidiary providing design and build services to the group, and the two treasury vehicles.

Orbit's financial, debt and investment management is adept in enabling strong oversight and managing financial and operational risk through well articulated policies and practices. Risk management is detailed, with generally conservative golden rules and risk appetite codified and reported against on a frequent basis. One of the golden rules addresses Orbit's risk appetite for market sales, with a cap of 40% of turnover on these tenures. We consider this to be high risk for the sector, however note that performance on these tenures is good.

Supportive institutional framework in England

The sector's credit quality benefits 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 is very strong 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 very high rates of inflation in 2022, the government introduced a 7% ceiling on social rent increases from April 2023 for one year. The ceiling resulted in an adverse differential between rental income and cost growth, which we expect will drive lower margins and interest coverage across the sector in fiscal 2024. The UK government has confirmed that English HAs will be able to return to rent increases of consumer price inflation (CPI) plus 1% in fiscal 2025, which will be favourable, considering the recent reduction in inflation.

High exposure to market sales, albeit with good performance to date

Orbit has one of the highest exposure to market sales among rated HAs, highlighting its higher risk appetite than peers. In fiscal 2023, sales accounted for 36% of its turnover, including 21% from outright sales and 15% from first-tranche shared ownership sales. The high exposure to market sales leads to more volatility in operating cash flows: the group's cash flow volatility interest coverage (CVIC) averaged 1.4x over the last three years compared to 1.5x for the median of A3-rated peers.

Orbit has scaled back its development programme in response to the deterioration in the macroeconomic environment, including high cost inflation and elevated interest rates, demonstrating its proactive risk management. It plans to develop 5,182 new units over the next five years, down from its previous programme of 6,010.

Orbit will maintain a very high exposure to market sales in the next five years, with 64% of new units planned for market sales (shared ownership and outright sales). However, the group has shifted its market sales programme towards first-tranche shared ownership (42%), which we consider to be less risky than outright sales as it is typically less affected by factors such as rising interest rates and falling house prices. In addition, we note that market sales have performed well historically, the number of unsold units remains low and the HA retains a high level of control over development.

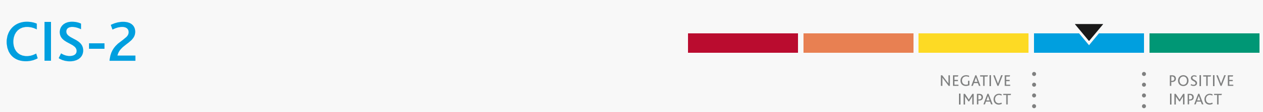
Extraordinary support considerations

The strong level of extraordinary support factored into the rating reflects our view of the UK government's support for the housing association sector due to its political, economic and social importance. Extraordinary support for the sector is predominantly exercised through sector regulators whose wide-ranging powers in cases of financial distress include facilitating mergers. However, this process can be protracted and is reliant on HAs agreeing to merge, which is more challenging in a weakened operating environment, with high expenditure pressures and high borrowing costs. In addition, our assessment that there is a very high default dependence between Orbit and the UK government reflects their strong financial and operational linkages.

ESG considerations

Orbit Group Limited's ESG credit impact score is CIS-2

Exhibit 3
ESG credit impact score



ESG considerations do not have a material impact on the current rating.

Source: Moody's Investors Service

Orbit's **CIS-2** reflects that ESG risks have a limited impact on its rating. Orbit faces limited carbon transition risks as the majority of its stock already meets required energy efficiency standards. Its high social risks - in line with the rest of the sector - are mitigated by its strong governance and management. In addition, the supportive regulatory framework for the sector also mitigates ESG risks.

Exhibit 4
ESG issuer profile scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-2	S-3	G-2

Source: Moody's Investors Service

Environmental
Orbit has limited exposure to environmental risks (**E-2**). English housing associations have the legislative requirement to improve the energy efficiency of their existing houing stock by 2035 (carbon transition risks), leading to increased expenditure. However, we assess that Orbit has a low exposure to this risk as the vast majority of its housing stock already meets the required efficiency standards.

Social
Orbit has material exposure to social risks (**S-3**) through sector-wide legislative requirements to improve the safety of its existing housing stock (responsible production risks) which weights on expenditure and operating margins, and the impacts of 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.

Governance
We assess its G issuer profile score as neutral to low (**G-2**). Governance in the sector is generally fit for purpose, with good oversight of business risks, strong financial planning and risk management processes, detailed reporting and simple organisational structures. The regulatory framework also supports good governance in the sector.

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

Output of the Baseline Credit Assessment Scorecard
The assigned BCA of “baa1” is one-notch below the scorecard-indicated BCA outcome in fiscal 2023.

The methodologies used in this rating are European Social Housing Providers, published in April 2018, and Government-Related Issuers, published in January 2024.

Exhibit 5
Orbit's 2023 scorecard

Orbit Group			
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%	47,429	a
Factor 3: Financial Performance			
Operating Margin	5%	25.1%	a
Social Housing Letting Interest Coverage	10%	1.6x	a
Cash-Flow Volatility Interest Coverage	10%	2.3x	a
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.8x	baa
Debt to Assets	10%	47.1%	ba
Liquidity Coverage	10%	1.6x	a
Factor 5: Management and Governance			
Financial Management	10%	baa	baa
Investment and Debt Management	10%	a	a
Scorecard - Indicated BCA Outcome			**a3**
Assigned BCA			**baa1**

Source: Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
ORBIT GROUP LIMITED	
Outlook	Stable
Baseline Credit Assessment	baa1
Issuer Rating -Dom Curr	A3
ORBIT CAPITAL PLC	
Outlook	Stable
Senior Secured -Dom Curr	A3

Source: Moody's Investors Service

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