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CREDIT OPINION
2 November 2022

Update

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RATINGS

Jigsaw Homes Group Limited

Domicile	United Kingdom
Long Term Rating	A2
Type	LT Issuer Rating - Dom Curr
Outlook	Negative

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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Jigsaw Homes Group Limited (UK)

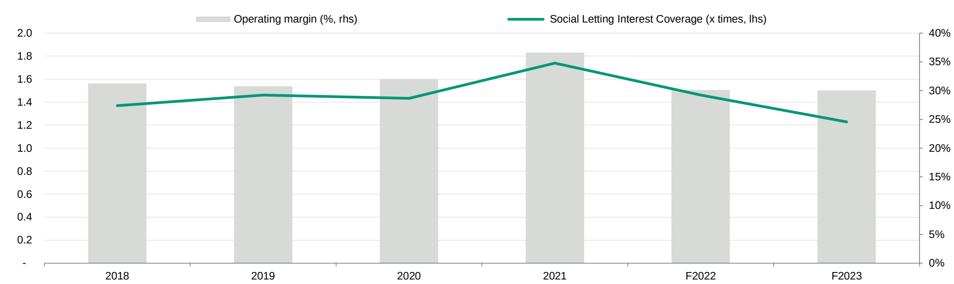
Update following outlook change to negative from stable

Summary

The credit profile of Jigsaw Homes Group Limited (Jigsaw, A2 negative) reflects the group's strong financial metrics and improved financial management, with a modest appetite for market sales. It also incorporates the group's moderate debt metrics, set to increase, as well as its increased development ambitions, although they are less risky than those of its peers. Jigsaw also benefits from the strong regulatory framework governing English housing associations (HAs), and our assessment of a strong likelihood that the government of the United Kingdom (UK, Aa3 negative) would intervene if Jigsaw faces acute liquidity stress.

Exhibit 1

Strong operating margins underpin Jigsaw's strong interest cover ratios



F: Forecast.
Source: Jigsaw and Moody's Investors Service

Credit strengths

» Strong financial performance

» Risk-averse financial management with a modest appetite for market sales

» Supportive institutional framework

Credit challenges

» Increased development ambitions, but liquidity coverage remains adequate

» Debt burden is moderate but will increase in the next three years

Rating outlook

The negative outlook reflects the high exposure to weaker economic and financial conditions in the UK. A potential ceiling on social rent increases in England and Wales combined with high cost inflation will weigh on operating margins over the next 12 to 18 months. At the same time, rising interest rates and tightening financing conditions will further weaken interest coverage ratios.

Factors that could lead to an upgrade

A rating upgrade is unlikely due to the negative outlook. The negative outlook could be stabilised if Jigsaw is able to maintain relatively stable financial metrics over the medium term. This could be driven by operating performance improving more than presently anticipated, including the ability to contain cost pressures, and reductions in development plans leading to lower debt levels than previously anticipated.

Factors that could lead to a downgrade

The ratings could be downgraded as a result of one or a combination of the following: a failure to adapt strategies to mitigate against weaker economic conditions; a sustained weakening in operating margins and interest coverage ratios; increases in debt levels beyond that currently anticipated; significant deteriorations in liquidity; significant scaling up in market sales exposure or material deterioration in market sales performance; or any weakening of the regulatory framework or dilution of the overall level of support from the UK government. A downgrade of the UK sovereign rating would also place downward pressure on the ratings.

Key indicators

Exhibit 2

Jigsaw Homes Group Limited

	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22 (F)	31-Mar-23 (F)
Units under management (no.)	33,945	34,442	34,696	35,198	35,939	36,784
Operating margin, before interest (%)	31.3	30.8	32.0	36.6	30.1	30.0
Net capital expenditure as % turnover	29.4	5.7	13.5	1.1	41.9	51.4
Social housing letting interest coverage (x times)	1.4	1.5	1.4	1.7	1.5	1.2
Cash flow volatility interest coverage (x times)	2.0	2.0	2.0	2.4	1.6	1.4
Debt to revenues (x times)	3.9	3.7	3.9	3.6	3.7	4.7
Debt to assets at cost (%)	51.4	49.6	48.5	47.1	48.0	50.0

*Cash flow volatility interest coverage (CVIC) for fiscal 2018 and 2019 use a proxy, because fiscal 2019 is the first year of operations for Jigsaw as a merged entity, and therefore 2018 is a restated statement. F: Forecast.
Source: Jigsaw and Moody's Investors Service

Detailed credit considerations

On 25 October 2022, Moody's changed the outlook to negative from stable and affirmed Jigsaw's ratings. The change in outlook followed Moody's change in outlook of the Government of the United Kingdom's Aa3 rating to negative from stable on 21 October 2022.

Jigsaw's A2 rating combines a Baseline Credit Assessment (BCA) of a3 and a strong likelihood of extraordinary support from the UK government in case of acute liquidity stress.

Baseline credit assessment

Strong financial performance

Jigsaw's financial performance is strong, with a 37% operating margin in fiscal 2021, significantly outperforming its initial budget and its peers with an A2 rating (median of 29%). The group's operating margin increased significantly from 32% in 2020 through efficiency savings and pandemic-induced delays in costs. Similar to its peers, Jigsaw experienced a maintenance backlog because of

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lockdowns, but it caught up with this backlog in September 2021. We expect Jigsaw to continue to outperform its peers — although not as significantly as in fiscal 2021 because of the backlog recovery — averaging 31% over the next three years.

Jigsaw's performance in the social housing letting business has been strong, with an average margin of 37% over the past three years. However, its margin on first-tranche shared ownership (FTSO) decreased to 16% in fiscal 2021 from 26% the year earlier because of disruptions to the housing market caused by the pandemic. Underpinned by strong margins, Jigsaw's SHLIC of 1.7x and CVIC of 2.4x are both in line with peer medians.

Risk-averse financial management with a modest appetite for market sales

Jigsaw is characterised by its stable strategy with moderate development targets as well as low and well-defined risk appetite underpinned by established golden rules to maintain the entity's financial resilience. Jigsaw focuses on low-risk social housing, averaging 84% of turnover over the past three years; and it has a minimal appetite for higher-risk market sales. Social housing lettings tend to generate stronger and more stable financial performance than market sales activities, as demand for social housing remains high across the country, and as a significant proportion of social or affordable rents are paid via government transfers in the form of housing benefits. Market sales exposure peaked at just 8% of turnover as of fiscal 2021. The exposure will decrease to a low 4% of turnover over the next five years, significantly below the A2 peer median of 18% over the same period.

Jigsaw has streamlined its structure and governance since its creation in April 2018, following the merger of New Charter Group and Adactus Housing. The group now has four registered providers (RPs, including the group and three other RPs covering different locations), a development provider, a support entity and a treasury vehicle. The group also participates in two joint ventures, both for social housing with one to deliver projects on employment and the other dealing with procurement. Despite the relatively complex organisation, Jigsaw was awarded a G1/V1 rating by the regulator.

Jigsaw also streamlined its debt structure by establishing a treasury vehicle, which simplifies monitoring processes because most of its debt is now under one set of covenants. This has also allowed the Group to release additional borrowing capacity from over-secured loans and has removed restrictive debt covenants from its main loan agreement. Further simplification of the debt structure is likely, which is a credit positive.

Supportive institutional framework

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 consultation on a ceiling on social rent increases to be implemented from April 2023 for a minimum of one year. The proposed ceiling of 5% 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.

Increased development ambitions but liquidity coverage remains adequate

Jigsaw's liquidity coverage stood at 1.1x as of February 2022 despite the expected increase in capital spending. The HA holds cash and cash equivalents of £67 million and additional immediately available facilities of £136 million.

Jigsaw plans to increase its capital spending to around 40% of turnover over the next three years, compared with the average of 7% over the past three years. The increase is in line with two of its corporate priorities; to (1) achieve 800 units per annum by fiscal 2022, compared with 536 units in fiscal 2021 and to (2) become a carbon neutral business by fiscal 2050.

Jigsaw's development programme includes around 3,700 units between fiscal 2022 and 2026. Of these, 83% are likely to be for social or affordable rent and 17% for shared ownership. Jigsaw is likely to fund a significant proportion, 28%, of its five-year development programme with operating cash flow, relying on its highly cash-generative core social housing business. The HA also expects grant funding to cover an additional 23% its development, through its continued market engagement with Homes England, a credit positive as it limits debt funding.

The increase in capital spending also reflects the estimated costs to retrofit social housing stock and other energy efficiencies to achieve carbon neutrality by year 2050, in line with Jigsaw's Sustainability Strategy.

Despite the increased capital spending, liquidity risk is limited because of Jigsaw's treasury policies. Jigsaw's third golden rule is to maintain liquid funds equal to its forecast net cash outflow for a rolling-six-month period, plus a contingency amount of £5 million, and short-term funds equal to its forecast net cash flow outflow for a rolling-12-month period. Its treasury management strategy states that the group will ensure that it has sufficient liquidity to meet its contractually committed obligations in less than 18 months. This is in line with peers' and supports its credit profile. Jigsaw's fourth and last golden rule is to retain capacity to cope with a sudden 10% increase in operating costs or stop additional development programmes, which further support its ability to cope with economic shocks.

Debt burden is moderate but will increase in the next three years

Jigsaw's drawn debt was £697 million as of fiscal 2021, a slight decrease from £702 million in fiscal 2020. The debt burden is moderate with debt/revenue at 3.6x, below those of its peers with an A2 rating (median of 4.1x), and gearing (debt to assets at costs) at 47%, in line with those of its peers with an A2 rating.

Jigsaw plans to increase its debt to fund its development programme and retrofitting expenses. We expect Jigsaw's debt metrics to weaken to 4.6x revenue and 51% gearing by fiscal 2024. This will be weaker than the level for its peers with an A2 rating, with medians of 3.9x and 50% forecast in fiscal 2024.

Jigsaw's debt structure is relatively low risk, with a low proportion of variable-rate debt (22% as of September 2021, in line with its first golden rule, which limits the exposure to 30%) and moderate refinancing risk, with 23% of drawn debt maturing in the next five years, but very few bullet maturities (8% of total drawn debt).

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

ESG considerations

Jigsaw Homes Group Limited's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 3
ESG Credit Impact Score

CIS-2
Neutral-to-Low

NEGATIVE IMPACT
POSITIVE IMPACT

For an issuer scored CIS-2 (Neutral-to-Low), its ESG attributes are overall considered as having a neutral-to-low impact on the current rating; i.e., the overall influence of these attributes on the rating is non-material.

Source: Moody's Investors Service

Jigsaw's CIS is neutral-low reflecting moderate exposure to environmental and social risks, low-neutral governance profile, as well as a supportive regulatory framework and support from the UK government.

Exhibit 4
ESG Issuer Profile Scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-3	**S-3**	**G-2**
Moderately Negative	Moderately Negative	Neutral-to-Low

Source: Moody's Investors Service

Environmental

Its overall E issuer profile score is moderate (**E-3**), reflecting moderately negative exposure to environmental risks, primarily due to carbon transition risk from the legislative requirement for English housing associations to improve the energy efficiency of their existing housing stock by 2035, leading to increased expenditure. We consider that Jigsaw has a material exposure to this risk due to a significant proportion of its stock requiring retrofit.

Social

We assess its S issuer profile score as moderate (**S-3**), reflecting exposure to risks from responsible production and demographic and societal trends. Responsible production risks include the legislative requirement to improve the safety of its existing housing stock which will increase expenditure over the medium term. Demographic and societal trends risks reflect the vulnerability of the sector to tenant affordability challenges and to government policy which controls rent setting in England and Wales, which weighs on revenue. The government's recent intervention on social rent policy with a consultation on a ceiling on social rent increases introduces policy volatility to the sector and will have a negative impact on financial performance.

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. The regulatory framework also supports good governance in the sector. Jigsaw has a more complex structure than peers but this is mitigated by the group's strong governance, illustrated in its G1/V1 ratings.

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 a3 is in line with the scorecard-indicated BCA. 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 2021

Jigsaw Homes Group Limited			
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%	35,198	a
Factor 3: Financial Performance			
Operating Margin	5%	36.6%	aa
Social Housing Letting Interest Coverage	10%	1.7x	a
Cash-Flow Volatility Interest Coverage	10%	2.4x	a
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.6x	baa
Debt to Assets	10%	47.1%	ba
Liquidity Coverage	10%	1.1x	a
Factor 5: Management and Governance			
Financial Management	10%	a	a
Investment and Debt Management	10%	baa	baa
Scorecard - Indicated BCA Outcome			**a3**
Assigned BCA			**a3**

Source: Jigsaw and Moody's Investors Service

Ratings

Exhibit 6

Category	Moody's Rating
JIGSAW HOMES GROUP LIMITED	
Outlook	Negative
Baseline Credit Assessment	a3
Issuer Rating -Dom Curr	A2
JIGSAW FUNDING PLC	
Outlook	Negative
Senior Secured -Dom Curr	A2

Source: Moody's Investors Service

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