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CREDIT OPINION
13 February 2023

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.

Contacts

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

Laura Balkarova +44.20.7772.5629
Associate Analyst
laura.balkarova@moodys.com

Sebastien Hay +34.91.768.8222
Senior Vice President/Manager
sebastien.hay@moodys.com

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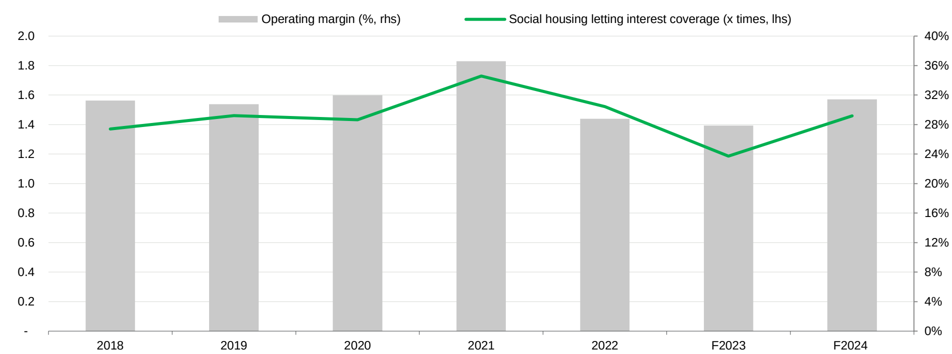
Jigsaw Homes Group Limited (UK)

Update to credit analysis

Summary

The credit profile of Jigsaw Homes Group Limited (Jigsaw, A2 negative) reflects the group's strong financial metrics and risk-averse 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. 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 7% ceiling on social rent increases in England combined with high cost inflation and sizeable levels of mandatory expenses (quality, fire and building safety, decarbonisation) will weigh on operating margins over the next 12 to 18 months. This could be worsened by additional below-inflation caps on social rent increases. At the same time, higher interest rates and tightening financing conditions will further weaken interest coverage ratios. Further declines in home prices and sale volumes in the UK could affect HAs' profitability and surpluses from market sales and further weaken their credit profile.

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 currently anticipated.

Factors that could lead to a downgrade

Jigsaw's rating could be downgraded as a result of one or a combination of the following: failure to adapt strategies to mitigate against weaker economic conditions; a further weakening in operating margins and interest coverage ratios; increases in debt beyond levels that are 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 Jigsaw's rating.

Key indicators

Exhibit 2

Jigsaw Homes Group Limited	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23 (F)	31-Mar-24 (F)
Units under management (no.)	33,945	34,442	34,696	35,198	35,732	36,529	37,422
Operating margin, before interest (%)	31.3	30.8	32.0	36.6	28.8	27.9	31.4
Net capital expenditure as % turnover	29.4	5.7	13.5	1.1	19.7	44.4	23.0
Social housing letting interest coverage (x times)	1.4	1.5	1.4	1.7	1.5	1.2	1.5
Cash flow volatility interest coverage (x times)	2.0	2.0	2.0	2.4	2.0	1.6	1.9
Debt to revenues (x times)	3.9	3.7	3.9	3.6	3.6	3.9	3.8
Debt to assets at cost (%)	51.4	49.6	48.5	47.1	45.1	47.0	47.3

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

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 remains strong, with a 29% operating margin in fiscal 2022, down from 37% in fiscal 2021, but still outperforming its A2-rated peers (median of 23%). In fiscal 2022, the group's operating margin was broadly in line with expectations, impacted by the catch up on maintenance and major repairs works delayed due to Covid-19, as well as the shortages in the availability of skilled labour and materials. In fiscal 2021, the group's performance was exceptionally strong owing to the maintenance backlog experienced as a result of lockdown restrictions. We expect Jigsaw to continue to outperform its peers, with its margins averaging 31% over the next three years.

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Similar to peers, Jigsaw's performance will continue to be pressured by cost inflation as well as development delays due to labour and material shortages, although its margin is expected to remain strong, at 28% in fiscal 2023. As of Q2 2023, Jigsaw's operating margin was at 33%, in line with its budget for the same period. In response to the anticipated cost pressures, the group has entered into long-term procurement contracts. Jigsaw also aims to achieve savings in areas such as staff costs, and will continue its focus on in-house repairs and online services delivery.

The group's SHLIC decreased to 1.5x in fiscal 2022, from 1.7x the year before, but remained in line with the peer median. The group's CVIC also decreased, reaching 2.0x in fiscal 2022, compared to 2.4x in the prior year, and falling behind the A2-rated peers median of 2.2x. Both metrics are expected to decline over the next three years, due to the increased debt burden. SHLIC is expected to average 1.4x, versus a median of 1.6x, over the next three years, while CVIC will average 1.8x, versus 2.1x.

Risk-averse financial management with a modest appetite for shared ownerhip 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 85% 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. The group's market sales (FTSO) represented only 5% of turnover in fiscal 2022. The exposure will average 3% of turnover over the next five years, significantly below the A2 peer median of 17% 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 is also involved in two joint ventures, without financial or development risk, both for social housing with one to deliver projects on employment and the other dealing with procurement. Whilst Jigsaw continues to have more RPs than rated peers, we note that all entities have a purpose and that 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 would be credit positive.

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.

Increased development ambitions but liquidity coverage remains adequate

Jigsaw plans to increase its net capital spending to 30% of turnover over the next three years, compared with the average of 11% over the past three years. The increase is due to the group's more ambitious development targets introduced from fiscal 2022, although net capex is expected to remain broadly in line with A2-rated peers. It 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.

Jigsaw's development programme includes around 4,300 units between fiscal 2023 and 2027. Of these, 80% are likely to be for social or affordable rent and 20% for shared ownership. The HA expects grant funding to cover 25% of its development, through its continued market engagement with Homes England, a credit positive as it limits debt funding. Jigsaw targets to build energy efficient units, with EPC rating of B and above. Only 9% of Jigsaw's development spending is currently committed over the next five years, a mitigant as it can allow the HA to scale back if required.

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. Jigsaw's liquidity coverage stood at 3.0x as of Q2 2023 supported by the strong liquidity policy.

Jigsaw's unencumbered asset position currently supports £125 million of additional borrowing capacity. Whilst this is relatively low compared to peers, Jigsaw does not require any additional funding until May 2028. The group plans to increase its borrowing capacity to £394 million by fiscal 2027, thanks to 4,000 additional units built over the next five years as well as the release of over-collateralisation on existing facilities and the switch to MVT (Market Value subject to Tenancies) valuations.

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

Jigsaw's drawn debt stood at £689 million as of fiscal 2022, a slight decrease from £698 million in fiscal 2021. The debt burden is moderate with debt/revenue at 3.6x, slightly above those of its A2-rated peers (median of 3.5x) and gearing (debt to assets at costs) at 45%, in line with A2-rated peers (median of 45%).

The group plans to increase its debt, although at a lower pace than previously anticipated, reaching £920 million by fiscal 2027. In April 2022, Jigsaw secured a £360 million sustainability bond, with £100 million retained, to fund its development programme and retrofitting expenses. We expect Jigsaw's debt metrics to weaken to an average of 3.9x over the next three years, above the A2-rated peers median of 3.6x. The group's gearing is also expected to increase, but will remain in line with the A2-rated peers, averaging 47% over the next three years.

Jigsaw's debt structure is relatively low risk, with a low proportion of variable-rate debt (4.3% as of September 2022, well below its first golden rule, which limits the exposure to 30%) and low refinancing risk, with of 4.6% drawn debt maturing in the next five years.

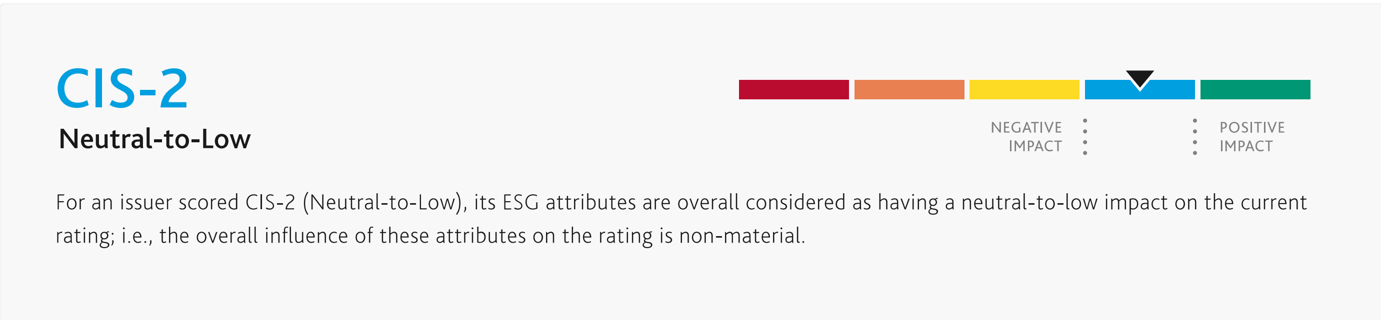
Extraordinary support considerations

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

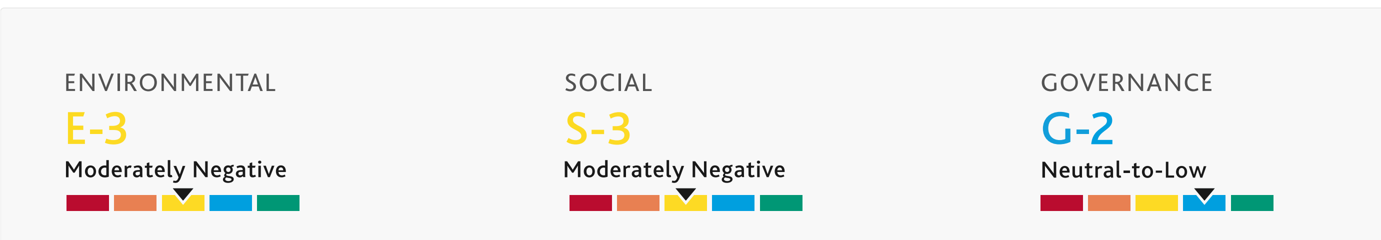
Exhibit 3
ESG Credit Impact Score



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



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 government policy which controls rent setting in England and Wales. The government's recent intervention on social rent policy with 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 2022

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%	35,732	a
Factor 3: Financial Performance			
Operating Margin	5%	28.8%	a
Social Housing Letting Interest	10%	1.5x	a
Cash-Flow Volatility Interest Coverage	10%	2.0x	baa
Factor 4: Debt and Liquidity			
Debt to Revenue	5%	3.6x	baa
Debt to Assets	10%	45.1%	ba
Liquidity Coverage	10%	1.4x	a
Factor 5: Management and			
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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