Research Update:

Kainga Ora-Homes and Communities Ratings Affirmed; Outlook Stable

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Overview

- Kainga Ora-Homes and Communities is a New Zealand government (Crown) agency deeply integrated in implementation of the government's social housing policy. We expect the agency's financial performance to be better than we previously anticipated, due to government directives that will reduce operational expenditure plus increasing rental revenue from developments as they reach completion.
- Strengthening EBITDA margins and improving interest coverage led us to change our assessment of Kainga Ora's stand-alone credit profile (SACP) to 'a-' from 'bbb+'. We equalize our ratings on Kainga Ora with our sovereign credit ratings on New Zealand.
- We therefore affirmed our long-term 'AA+' foreign-currency and 'AAA' local-currency issuer credit ratings on Kainga Ora. We also affirmed our 'A-1+' local- and foreign-currency short-term issuer credit ratings.
- The stable outlook on the long-term ratings reflects that on the New Zealand sovereign.

Rating Action

On Feb. 11, 2025, S&P Global Ratings affirmed its 'AA+' foreign currency and 'AAA' local currency long-term issuer credit ratings on Kainga Ora-Homes and Communities, a New Zealand-based social housing provider. At the same time, we affirmed our 'A-1+' local- and foreign-currency short-term issuer credit ratings on the agency. The outlook on the long-term ratings is stable.

Outlook

The stable outlook on Kainga Ora reflects that on the New Zealand sovereign as well as our expectation that the role of Kainga Ora will remain critical and its link to the New Zealand government will stay integral over the next two years.

Downside scenario

We may lower our ratings on Kainga Ora if we perceive the agency's role or link to the Crown to be weakening. We could also downgrade Kainga Ora if we were to take the same action on the New Zealand sovereign.

Upside scenario

We could raise our foreign-currency long-term rating on Kainga Ora during the next two years if we were to upgrade the New Zealand sovereign, all else being equal.

Rationale

We equalize our ratings on Kainga Ora with those on New Zealand because we believe the likelihood of direct, timely, and sufficient extraordinary support from the sole owner of Kainga Ora, the Crown, is almost certain in a stress scenario.

We believe Kainga Ora's financial risk profile is improving. Over the past year, the agency has simplified its strategic direction to focus on managing social housing. Under a Crown directive, Kainga Ora aims to improve its financial position by maintaining a portfolio of about 78,000 homes rather than growing its asset base. Slowing its construction pipeline should lower expenditure, improving its financial ratios. Additionally, increased rental revenue from developments the agency is completing is positive for its financial performance and interest coverage. We therefore changed our assessment of Kainga Ora's SACP to 'a-' from 'bbb+'.

We view the agency's management and governance expertise as neutral for the ratings. A Crown-initiated strategic review in 2024 led to an unprecedented replacement of most of the board as well as the appointment of a new interim chief executive. Strong Crown influence means management has less influence on the ratings than in the past.

Enterprise profile: Quasi-monopoly footprint and prudent management underpin agency.

Kainga Ora is New Zealand's largest residential landlord, owning or managing about 76,000 properties as of June 2024. Its large portfolio and geographically diversified footprint help it minimize operating volatility.

Globally, we classify social housing as a low-risk industry. It tends to be stable, with relatively high barriers to entry and ongoing government subsidies in many jurisdictions. Demand for Kainga Ora services is high, with about 22,000 applicants on New Zealand's public housing register as of September 2024. A persistent undersupply of housing and strong population growth in recent years contributed to declining affordability.

Relative to international peers, Kainga Ora benefits from a very supportive regulatory framework. As a Crown agency, its public policy mandate is enshrined in legislation (Kainga Ora-Homes And Communities Act 2019).

Kainga Ora's management and governance is a neutral credit factor. In 2024, an independent review examined the agency's financial viability, asset procurement and tenancy management, and remit and institutional arrangements. The review resulted in a series of recommendations, including a refresh of the board, a simplified strategic direction, and development of a plan to improve financial performance. In mid-2024, the government appointed six new members of the board, which then appointed Mr. Matt Crockett as interim chief executive. These leadership changes are yet to produce a track record of public policy outcomes, in our view.

Furthermore, strong Crown influence has left management with less influence on the ratings than in the past. We believe Kainga Ora's fluctuating financial outcomes and SACP in recent years, including its weakening financial position and declining SACP between 2021 and 2023, was due to implementation of the former government's mandate to expand the agency's housing developments. Similarly, the change of direction of SACP to 'a-' primarily reflects new Crown policy.

Kainga Ora's reset plan, its third public housing plan since inception, outlines the agency's focus on its core business of providing good quality social housing. The agency is concentrating on improving its management of tenants, reducing building costs, and enhancing its financial focus. It is curtailing development of new housing projects in favor of maintaining a fixed portfolio of 78,000 homes.

Financial profile: Reduced development pipeline and rising revenue should strengthen fiscal ratios and slow debt growth.

We forecast Kainga Ora's financial performance will improve. Its adjusted EBITDA margin rose above 20% in 2024, from 13% in 2023. We expect this to remain above 20% across our forecasts to 2027. This is due to a slowing development pipeline leading to lower operational costs, along with improving revenue as newly completed construction developments are rented.

Following the independent review in 2024, Kainga Ora is identifying and implementing cost reductions in line with the change in its strategic positioning. We understand new capital developments will increase much more slowly compared with our previous expectations as Kainga Ora's construction development pipeline peaks in 2024 and tapers. The agency will continue to maintain and retrofit its existing stock of housing supply.

Kainga Ora's revenue streams are reliable because it receives most of its operating revenue directly or indirectly from the Crown. Most tenants pay no more than 25% of their net income on rent; the Crown then pays to Kainga Ora the difference between market rent and the tenant's income-related rent, in the form of an income-related rent subsidy.

Gross debt and interest coverage ratios should improve compared with our previous expectations. We project Kainga Ora's non-sales adjusted EBITDA-to-interest ratio will rise to about 1.1x in 2025, from 0.8x in 2024. We estimate Kainga Ora's non-sales adjusted debt-to-EBITDA ratio is very high and will average about 32x for fiscal 2023 (ending June 30, 2023) to fiscal 2027. These ratios incorporate all the group's commercial and Crown debt.

In November 2022, the New Zealand government announced that Kainga Ora will conduct all future borrowing through the sovereign debt management office, rather than in commercial markets in its own right. For the preceding four years, Housing New Zealand Ltd. (HNZL, a core subsidiary of the Kainga Ora group) had directly issued New Zealand-dollar denominated bonds to wholesale investors on behalf of the group.

The financing switch itself does not affect our ratings on Kainga Ora. We assume the refinancing will be gradual (as HNZL's outstanding bonds mature and the agency refinances them with Crown loans), and the New Zealand Debt Management office does not buy back outstanding bonds.

The Kainga Ora group spreads its outstanding commercial debt across seven tranches of fixed-rate and inflation-indexed bonds with maturities ranging from June 2025 to September 2040.

The agency's liquidity position remains strong, supported by an increase in expected ongoing debt financing and equity injections by the Crown to cover capital investment needs. The working capital facility with the New Zealand Treasury remains unchanged at NZ$500 million. Kainga Ora has sources of liquidity of NZ$4,656 million to cover uses of liquidity of NZ$4,180 million, resulting in a liquidity coverage ratio of 1.1x for the 12 months ending Jan. 31, 2026.

Sources of liquidity for the period include:

- Our forecast of cash generated from continuing operations (as proxied by adjusted EBITDA) of NZ$799 million.
- Cash and short-term liquid investments of NZ$751 million.
- Proceeds from asset sales of NZ$10 million.
- An undrawn working capital facility with the New Zealand Treasury of NZ$500 million.
- Our estimate of Crown financing of about NZ$2,595 million.

Uses of liquidity over the same period include:

- Forecast capital expenditure of NZ$2,533 million.
- Forecast principal and interest payments of NZ$1,646 million.

Kainga Ora benefits from strong access to external liquidity through the Crown's debt management office and, historically, New Zealand's local capital markets. Kainga Ora manages its debt maturities so that no more than 25% of total debt matures in any 12-month period. The earliest of HNZL's medium-term notes will mature in June 2025, which will be refinanced via the Crown.

Government-related entity analysis

We equalize our ratings on Kainga Ora with those on New Zealand because we believe the likelihood is almost certain that direct, timely, and sufficient extraordinary support would be forthcoming from the sole owner of Kainga Ora, the Crown, in a stress scenario. We base our assessment on Kainga Ora's following characteristics:

- Critical role, given it is mandated by and operates on behalf of the Crown to provide a key public service (provision of social housing to the most vulnerable segments of the New Zealand population) and enable, facilitate, and deliver housing and urban development projects.
- Integral link with the Crown due to its status as a Crown agency that we consider an extension of the government. The Crown is responsible for appointing all Kainga Ora's board members, and Crown subsidies and appropriations represent the bulk of the agency's operating revenue. The Crown does not require Kainga Ora to pay it dividends. It conducts all borrowing through loans from the sovereign debt management office, further solidifying our view of Kainga Ora's integral link with the Crown.

We do not believe the likelihood of support is subject to any transition risk or negative intervention from the Crown.

Selected Indicators

Table 1

Kainga Ora-Homes and Communities--Key statistics

	--Year ended March 31--				
(Mil. NZ$)	**2023a**	**2024a**	**2025bc**	**2026bc**	**2027bc**
Number of units owned or managed	72,035	75,640	78,440	78,440	78,440
Adjusted operating revenue	2,030	2,374	2,563	2,910	3,077
Adjusted EBITDA	265	477	680	885	874
Non-sales adjusted EBITDA	265	453	665	885	874
Capital expense	3,577	4,516	3,000	2,200	2,000
Debt	12,303	16,526	19,210	19,925	20,377
Interest expense	344	538	597	579	602
Adjusted EBITDA/Adjusted operating revenue (%)	13.1	20.1	26.5	30.4	28.4
Debt/non-sales adjusted EBITDA (x)	46.4	36.5	28.9	22.5	23.3
Non-sales adjusted EBITDA/interest coverage(x)	0.8	0.8	1.1	1.5	1.5

a--Actual. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

Kainga Ora-Homes and Communities--Ratings score snapshot

	Assessment
Enterprise risk profile	2
Industry risk	2
Regulatory framework	1
Market dependencies	1
Management and governance	3
Financial risk profile	4
Financial performance	4
Debt profile	5
Liquidity	3
Stand-alone credit profile	a-
Issuer credit rating	AA+

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

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 2025: Quality Maintenance Constrains Recovery, Jan. 14, 2025
- Comparative Statistics: Non-U.S. Social Housing Providers Ratings Risk Indicators: Ratings Pressure Has Eased, Oct. 31, 2024
- Non-U.S. Social Housing Providers Ratings History: October 2024, Oct. 31, 2024
- Regulatory Framework Assessment: New Zealand Crown-Owned Social Housing Providers Operate Under Uniquely Strong Policy Mandate, June 29, 2023

Ratings List

Ratings Affirmed	
Kainga Ora-Homes and Communities	
Issuer Credit Rating	
Foreign Currency	AA+/Stable/A-1+
Local Currency	AAA/Stable/A-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.