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Civitas Social Housing

REITs | Update | 17 May 2021

On firm footing

The leading UK social housing investor, Civitas Social Housing (CSH), is on a firm footing as it steps up its growth plans. It has the investment firepower to grow its portfolio after securing new debt facilities. Significantly, it has also attained an investment grade credit rating that not only gives it access to the bond market and cheaper debt, but provides a big vote of confidence for the lease-based model in the social housing sector.

Strong operational performance, including a rent collection rate that was unaffected by the pandemic, coupled with the planned growth of the portfolio, has given the board the confidence to raise its dividend target for the year to March 2022 above inflation forecasts.

Income and capital growth from social housing

CSH aims to provide its shareholders with an attractive level of income, together with the potential for capital growth from investing in a portfolio of social homes. The company expects that these will benefit from inflation-adjusted long-term leases and that they will deliver a targeted dividend yield of 5% per annum on the issue price, with further growth expected. CSH intends to increase the dividend broadly in line with inflation.

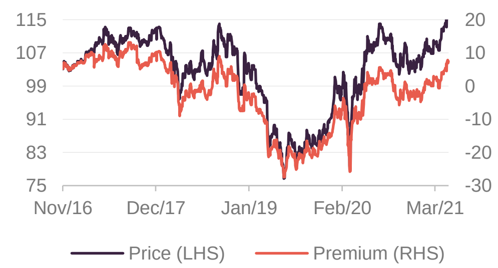
Year ended	Share price total return (%)	NAV total return (%)	EPRA earnings per share (pence)	Dividend per share (pence)
31/03/2018*	(0.6)	10.7	1.44	4.25
31/03/2019	4.2	6.2	3.63	5.0
31/03/2020	6.6	5.4	4.63	5.3
31/03/2021	17.6	4.9		5.4

Source: Morningstar, Marten & Co. Note *: From launch on 18 November 2016

Sector	Property – UK residential
Ticker	CSH LN
Base currency	GBP
Price	116.4p
NAV	108.3p
Premium/(discount)	7.5%
Yield	4.6%

Share price and discount

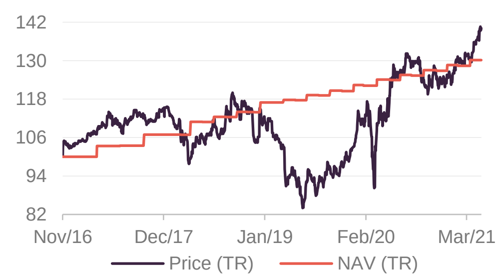
Time period 18/11/2016 to 13/05/2020



Source: Morningstar, Marten & Co

Performance since launch

Time period 18/11/2016 to 13/05/2020



Source: Morningstar, Marten & Co

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Domicile	England and Wales
Inception date	18 November 2016
Manager	Civitas Housing Advisors
Market cap	£723.9m
Shares outstanding	621.9m
Daily vol. (1-yr. avg.)	1.46m shares
Loan to value	35.0%

Click here for our most recent annual overview note

Click here for an updated CSH factsheet

Click here for CSH's peer group analysis

Click here for a link to share trading platforms

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Market update

CSH has put in place the building blocks that should see net asset value (NAV) and earnings growth take off this year. In February 2021, the group finally secured new debt facilities with M&G Investment Management (which were delayed due to the COVID-19 pandemic – more details on page 5) that brought it up to its loan to value (LTV) target of 35% and gave it around £75m to invest in new acquisitions. Significantly, the company also secured an investment grade credit rating from Fitch Ratings that will open up access to cheaper finance through new lenders and the bond market.

This, on top of a strong operational performance, has helped cement its place as the leading UK investor in supported social housing. We explained the structure of the specialist supported housing market in the UK in our October 2020 annual overview note. To recap, substantial savings are available to local authorities if they can rehome a person in need of supported living (for example, people with learning disabilities, autism, mental health issues or physical disabilities) from a hospital into a property adapted to their needs. Research has also shown that these tenants then have an improved quality of life and better medical outcomes. Local authorities turn to care providers to manage the day-to-day welfare of the tenant and to housing associations to provide the accommodation. The housing associations lease property on a long-term basis from the likes of CSH.

Lack of supply and huge demand underpins the strength of the supported living sector

The fundamentals that underpin the supported living sector – namely, the chronic shortage in supply of appropriate accommodation for the delivery of mid- to higher-acuity care, and growing demand; the better health outcomes that specialist supported housing brings to occupants; and the substantial cost saving to government – are only intensifying. Demand for this specialist accommodation is growing at a rate of around 2% to 5% a year, with between 170,000 and 250,000 people already housed in supported living facilities like those provided by CSH.

Portfolio development

In April 2021, CSH made the first acquisition financed with the proceeds from the M&G debt facility. It bought 15 supported living and care facilities (providing a total of 51 beds) in South Wales for £10.9m. The properties are subject to 25-year leases with existing tenant Auckland Home Solutions C.I.C., with rents adjusted annually in line with CPI over the full term, subject to a lower limit of inflation of 0% per annum and a maximum indexation of 4% per annum.

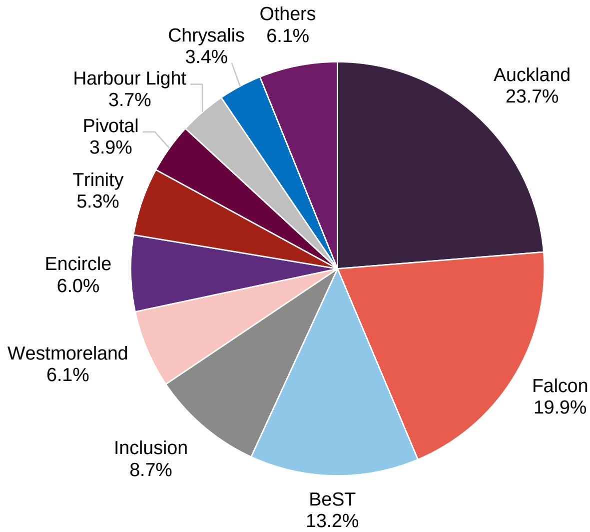
CSH now provides homes for 4,346 working age adults with long-term care needs, in 634 bespoke properties that are supported by 119 specialist care providers, 16 approved providers and working with over 172 individual local authorities.

Figure 1: Portfolio growth over time

	31 Dec 2017	30 June 2018	31 Dec 2018	30 June 2019	31 Dec 2019	30 June 2020	31 Dec 2020
Investment (£m)*	431	508	674	761	771	793	803
Properties	384	440	557	594	608	616	619
Tenancies	2,405	2,845	3,746	4,094	4,153	4,241	4,295
Local authorities	99	123	144	158	161	164	164
Housing associations	10	12	15	15	15	15	16
Care providers	59	71	98	113	115	118	118

Source: Civitas Social Housing. * excluding purchase cost

Figure 2: Rental income by housing association at 31 March 2021



Source: Civitas Social Housing

Acquisition pipeline worth in excess of £200m

CSH has an ongoing pipeline of investment opportunities worth in excess of £200m, primarily coming from extensive relationships with housing associations, care providers and local authorities.

Expansion into homeless accommodation

Demand for supported housing is growing and expanding to also cover a wide range of underlying needs faced by people who are battling homelessness, addiction or who are stepping down from the NHS into a more appropriate supportive care environment. To this end, CSH is making significant steps in the homeless accommodation sector. It has partnered with Barnet Council in North London to repurpose three of CSH's properties into specialist accommodation for the homeless. In all, the three projects will provide 80 to 100 beds and cost CSH between £400,000 and £500,000. Barnet Council will be paying CSH income during the refurbishment period and will provide the accommodation to local homelessness charities, which will lease the properties from CSH. The manager said that this local authority tie-up would be replicated across the country and it was already receiving enquiries.

Debt facilities

An equity raise had been mooted by the manager last year, and this remains an option for the company this financial year. It is likely that this will be done through smaller equity raises, to avoid cash drag.

Debt facilities give CSH £75m firepower for acquisitions

In the short term, the company will use the new debt facilities secured with M&G Investment Management to acquire new assets. In February 2021, it announced it had secured a new seven-year-term, interest-only loan facility of £84.55m from M&G Investment Management (£75m net to invest). The facility is priced at 2.75% above a fixed rate set by reference to the LIBOR swap rate of the loan term, and is repayable seven years from the date of utilisation. It is secured by an existing portfolio of specialist supported living assets. CSH had been in negotiations with M&G more than 18 months ago, but securing the loan was delayed due to M&G's decision to pause lending to new clients as they assessed the impact of COVID-19. The manager says that the M&G debt facility will be the last piece of conventional debt it uses for the foreseeable future, following the investment grade credit rating it received in March 2021 and the favourable finance options open to it as a result.

Impact of investment grade credit rating

Investment grade credit rating expected to materially reduce cost of debt

Receiving an investment grade credit rating was a big milestone for CSH and a vote of confidence for the lease-based model in the social housing sector, with acknowledgement that the ultimate security of income comes from government and not the housing association counterparties.

The manager says it will look to replace some of its existing debt facilities with the issue of a bond. It has two revolving credit facilities – a £60m facility with Lloyds that expires in November 2021 and a £100m facility with HSBC that expires in 2022 – that can be replaced. It expects to benefit from a material reduction in the cost of debt finance and an increase in the term length. One option that it is investigating is issuing a green bond, based on the company's strong ESG credentials – especially the positive social impact of its portfolio (more detail below). The manager says that the level of demand from institutional investors for ethical bonds is strong, while interest rates are lower.

Boosting ESG credentials

Investment in supported living has an obvious positive social impact. The lives of people who live in the homes owned by CSH are enhanced due to the secure, long-term, high-quality nature of the housing, whether of a general nature or as a base for the provision of more specialist housing and care.

CSH's portfolio produces £114m of social value every year

Every year, social advisory firm The Good Economy publishes a report examining the social impact of CSH's investments. Due to COVID-19, it has not been able to publish one since 2019, but is due to publish one this year. The 2019 report found CSH to be an "authentic impact investor" in accordance with the International Finance Corporation Principles for Impact Management. As part of the report, the Social Profit Calculator (SPC) – a social value consultancy that specialises in calculating the additional value of social, economic, and environmental impact –

calculated the social value of CSH's portfolio in monetary terms and found the portfolio to have produced £114m of social value per year. This equates to £3.50 of social value being created for every £1 of annualised investment.

CSH is also pressing ahead with plans to increase the environmental credentials of its portfolio. It intends to roll out initiatives such as the installation of PV solar panels on the roofs and the introduction of heat pumps at some of its properties. It will look to take advantage of government grants that are available and is in early discussions with national contractors to carry out works across its portfolio. The manager says that the works should provide a small incremental improvement to the value of the portfolio, as well as the obvious environmental improvements.

Dividend target increased

Dividend target for FY 2022 increased to 5.55p per share

CSH's board is targeting a dividend of 5.55p per share for the financial year ending 31 March 2022, 2.8% above the 5.4p per share it has paid for the year to 31 March 2021.

The board said that the increase (above current CPI inflation estimates of 2.0%) reflects its confidence in the future performance of the company due to strong operational and financial performance, stability of rental collection and target gearing (35% gross assets) now in place.

Going forward, the board said that the dividend would grow in line with inflation as measured by CPI.

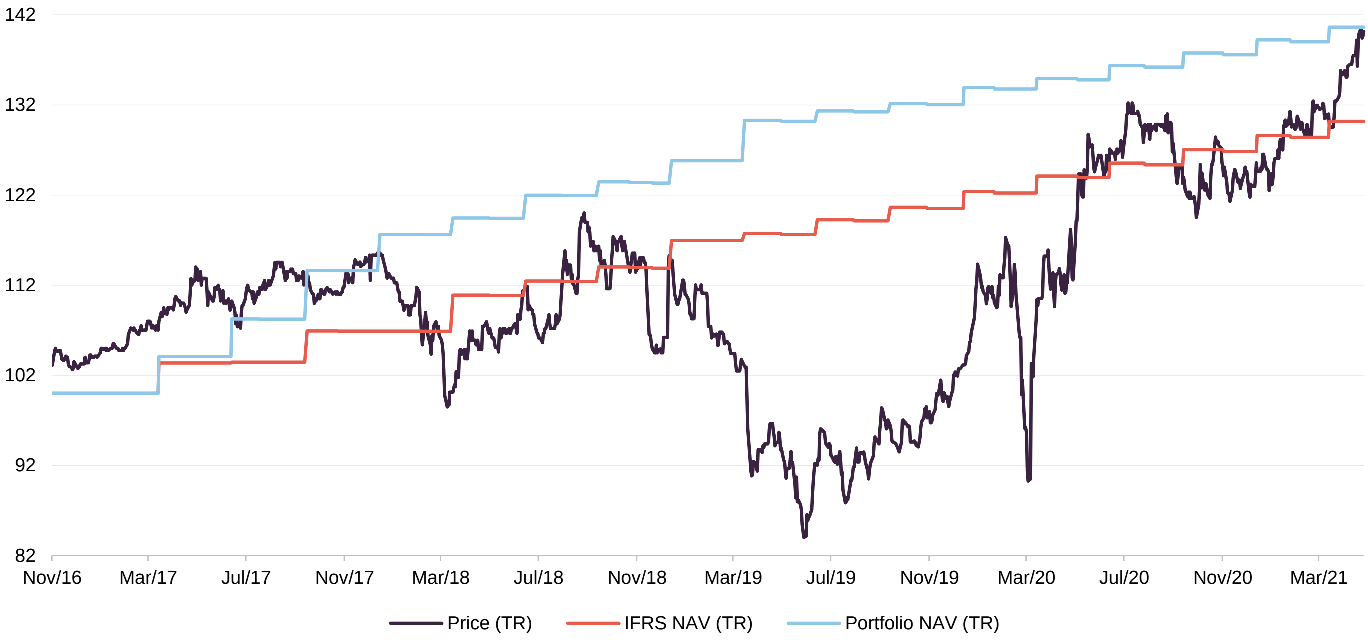
Performance

CSH publishes two NAVs – an International Financial Reporting Standards (IFRS) NAV, which reflects the value of the portfolio if it was sold off on a piecemeal basis, and a portfolio NAV, which is based on the value if it were to be sold as a single portfolio. This is generally higher than the IFRS NAV, reflecting the fact that the properties are held in special purpose vehicles and attract a lower tax charge than selling properties individually.

At 31 March 2021, the IFRS NAV was £673.5m or 108.3p per share. On a portfolio basis, the NAV was £736.8m or 118.47p per share.

CSH's share price has been on an upward trajectory since June 2019, apart from the COVID-19 induced blip in March 2020 when its share price crashed as part of a wider sell-off due to fears over the pandemic. The share price quickly regained all its losses as investors recognised the strength of its government-backed income. Unlike most other REITs, CSH has not seen a drop-off in its rent collection rates throughout the COVID-19 pandemic.

Figure 3: CSH performance since launch



Source: Morningstar, Marten & Co

Peer group comparison

CSH sits within a small group of listed peers comprised of Triple Point Social Housing REIT (SOHO), Home REIT (HOME) and Residential Secure Income REIT (RESI). CSH is by far the largest fund in this peer group.

Figure 4: Peer group comparison

	Market cap (£m)	Premium/ (discount) (%)	Yield (%)	Launch date	NAV total return 1 year (%)*	Price total return 1 year (%)*
Civitas Social Housing	723.9	7.5	4.6	18/11/16	4.9	17.6
Residential Secure Income REIT	163.5	(9.5)	5.2	12/07/17	1.7	14.4
Triple Point Social Housing REIT	422.9	0.1	4.9	08/08/17	4.5	16.7
Home REIT	276.7	8.4	2.2	12/10/20	4.8**	14.8**

Source: Morningstar, Marten & Co. Note *: to 31 March 2021. Note**: From launch on 12 October 2020

RESI's focus is more on retirement properties and shared ownership housing (without leases), whilst HOME launched in October 2020 and is solely focused on providing homeless accommodation. Therefore, SOHO may provide a better direct comparison. CSH is larger and has a longer track record than SOHO, a comparable yield and a better performance over one year in both price and NAV terms.

Premium/(discount)

CSH's shares initially traded at a premium to its IFRS NAV, but moved to trade at a discount due to the concerns that the regulator highlighted regarding some of the housing associations in its portfolio. As the company demonstrated the underlying fundamentals supporting growth in the supported living sector and its leading position in it, the discount narrowed from July 2019. As the company and the sector proved resilient during the pandemic, helped by secure government-backed income, it returned to a premium rating in the second half of 2020 and as of 13 May 2021 was at a premium of 7.5%.

Figure 5: CSH's premium/(discount) to IFRS NAV since launch

Source: Morningstar, Marten & Co

CSH is authorised to repurchase up to 14.99% of the issued share capital (renewal of this authority is sought annually at the company's AGM). Any shares repurchased may be cancelled or held in treasury and later resold. Shares will not be resold from treasury at a discount to NAV unless as part of an offer that is being made to all shareholders on a pro-rata basis.

In March 2021, CSH sold 250,000 shares from treasury at a price of 109.8p and at a premium to the prevailing NAV.

Fund profile

The company's website is civitassocialhousing.com

CSH has invested £803m to amass a portfolio of diversified supported social housing assets since it launched on 18 November 2016. It raised £350m at IPO and expanded in November 2017, raising an additional £302m through a C share issue (whereby C share investors own a separate class of shares which has its own portfolio). These two pools were merged together in December 2018.

Attractive yield, growing with inflation, plus capital growth from a portfolio of social homes

CSH aims to provide an attractive yield, with stable income growing in line with inflation and the potential for capital growth. Its diversified portfolio is let to housing associations and local authorities (referred to as registered providers) on long-term lease agreements, typically 25 years. It buys only completed homes, which includes acquiring new developments on completion, but it does not get involved with forward funding deals (putting up money to finance the construction of new social homes), or the management of social homes directly.

CSH's portfolio has a low correlation to the general residential and commercial real estate sectors, as the supply and demand demographics driving the social home sector do not move in line with that of the wider real estate market. It is a real estate investment trust (REIT), giving it certain tax advantages. As a REIT, it must distribute at least 90% of its income profits for each accounting period.

The adviser – Civitas Investment Management

CSH is advised by Civitas Investment Management (CIM), previously named Civitas Housing Advisors, a business established in 2016. Many of the 25-strong team have long experience of working in the sector and in specialist healthcare, and collectively, they have been involved in the acquisition, sale and management of more than 80,000 social homes in the UK.

Previous publications

QuotedData has published five previous notes on CSH. You can read them by clicking the links below or by visiting the QuotedData.com website.

Figure 6: QuotedData's previously published notes on CSH

Title	Note type	Date
Socially beneficial investing	Initiation	18 June 2018
Regulatory action is positive	Update	19 February 2019
Targeting full dividend cover	Annual overview	12 September 2019
Proved its mettle	Update	15 April 2020
Solid foundations for future growth	Annual overview	22 October 2020

Source: Marten & Co

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