MORhomes PLC

MORhomes PLC

£5,000,000,000

Secured Euro Medium Term Note Programme

Questions and Answers

Disclaimer

IMPORTANT: YOU ARE ADVISED TO READ THE FOLLOWING CAREFULLY BEFORE READING, ACCESSING OR MAKING ANY OTHER USE OF THIS DOCUMENT.

This document does not constitute or form part of, and should not be construed as, an offer to sell, or the solicitation or invitation of any offer to buy or subscribe for, any senior notes of MORhomes PLC ("MORhomes") in any jurisdiction or an inducement to enter into investment activity.

The information contained in this document has been prepared to assist interested parties in making their own evaluation of MORhomes and is believed to be in all material respects accurate, although it has not been independently verified by MORhomes and does not purport to be all-inclusive. Neither MORhomes nor any of its representative directors, officers, managers, agents, employees or advisers makes any representations or warranties (express or implied) or accepts any responsibility as to or in relation to the accuracy or completeness of the information in this document (and no one is authorised to do so on behalf of any of them) and (save in the case of fraud) any liability in respect of such information or any inaccuracy therein or omission therefrom is hereby expressly disclaimed in particular if for reasons of commercial confidentiality information on certain matters that might be of relevance to a prospective purchaser of any senior notes has not been included in this document.

This document and any accompanying materials are furnished on a confidential basis for information purposes only. The information contained herein may include estimates, projections and other forward-looking statements which as such may not relate strictly to historical or current facts and involve significant elements of subjective judgment and analysis. No representations are made as to the accuracy of such estimates, projections or other forward-looking statements or that all assumptions relating to such estimates, projections or other forward-looking statements have been considered or stated or that such estimates or projections will be realised. Investors are cautioned not to place undue reliance on forward-looking statements. The management of MORhomes does not expect to update or otherwise revise the information contained herein.

No representation or warranty is given as to the achievement or reasonableness of any projections, estimates, prospects or returns contained in this document or any other information. Neither MORhomes nor any other person connected to it shall be liable (whether in negligence or otherwise) for any direct, indirect or consequential loss or damage suffered by any person as a result of relying on any statement in or omission from this document or any other information and any such liability is expressly disclaimed. This document includes certain statements, estimates and projections prepared and provided by the management of MORhomes with respect to its anticipated future performance. Such statements, estimates and projections reflect various assumptions by MORhomes' management concerning anticipated results and have been included solely for illustrative purposes. No representations are made as to the accuracy of such statements, estimates or projections or with respect to any other materials herein. Actual results may vary from the projected results contained herein.

Without the express prior written consent of MORhomes, this document and any information contained herein or disclosed or delivered therewith may not be (i) reproduced (in whole or in part), (ii) copied at any time, (iii) used for any purpose other than your evaluation of MORhomes or (iv) furnished to any other person, except your employees and advisors, on a need to know basis, who are advised of the confidentiality of the information. This document (as well as other material that may be provided by MORhomes) remains the property of MORhomes and, upon request, it is to be returned promptly and any copies made by the recipient must be destroyed.

Any senior notesissued by MORhomes will not be registered under the U.S. Securities Act of 1933, as amended (the "Securities Act"), or the laws of any state or other jurisdiction of the United States, and may not be offered or sold within the United States, or for the account or benefit of, U.S. Persons (as such terms are defined in Regulation S under the Securities Act), absent registration or an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state laws.

This document is made to and directed at: (i) those persons who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order"); (ii) those persons falling within Article 49 (2)(a)-(d) of the Order; and (iii) to persons outside of the United Kingdom only where permitted by applicable law (all such persons together being referred to as "Relevant Persons") and must not be acted on or relied on by persons who are not Relevant Persons. Any person who is not a Relevant Person should not act or rely on this document or any of its contents.

1. Visibility and Maintaining credit quality

While we can see the quality of the initial borrowers, how can we be sure that the credit quality of the loan book will not decline as we have no control over future borrowers?

The credit policy at MORhomes has been designed specifically to address this problem. It does this in two ways:

a. The loan limits (Lending Levels) imposed on individual borrowers.

These are set using a transparent credit model that awards larger borrowing limits to borrowers with stronger credits on a scale of 1 to 4 (below4 is a fail), thus weighting the portfolio to higher quality borrowers.

The credit model that sets the Lending Levels uses ratios (published on its website) that are based on Rating Agency methodology though with a heavier weighting towards liquidity and asset availability. Ratios are applied to 5 years historic performance and 5 years' future performance as set out in the borrower's business plan submitted to the regulator (FFR or equivalent). The look-forward numbers are time-weighted.

MORhomes believes the operation of this model provides investors with two benefits not available when investing in a public own name bond issue

- MORhomes' access to non-public information in the FFR when making its credit decisions
- MORhomes' ability to monitor the quarterly performance of the borrower against the FFR and intervene to take remedial action in the event of any deterioration. Borrowers are also obliged to notify MORhomes if they change their business plan in a way that could lead to a downgrade of their MORhomes' Lending Level

b. The portfolio management policy determining the single name and combined Lending Level exposures

This is designed to ensure that the loan portfolio is

- Always weighted in favour of the stronger borrowers by imposing limits on aggregate debt. (These are set out on page 105 of the Programme Agreement). Thus, for example, only 20% of the debt outstanding can be at level 4 and a maximum 50% at Levels 3 and 4.
- Subject to concentration rules to ensure that MORhomes has a broadly diversified loan portfolio that avoids the risk of dependence on a small group of borrowers

MORhomes provides diversification as, subject to credit clearance, it will lend to organizations ranging from 2,000[1] to over 50,000[2] units and expects a mix across that range as illustrated by the initial borrowers. It is also worth noting that there is a popular conception that the larger the association the stronger it is, but based on our credit scoring smaller and mid-sized organizations

[1] The Board has discretion to vary this number which it has done in the case of a registered subsidiary (which is the borrower) of larger unregistered but not for profit group.

[2] There is no upper size limit

often display better credit metrics and in some cases better credit ratings – for instance two of the HAs with the strongest public ratings from S&P (Local Space & RHP) might traditionally be considered small associations.

2. Adverse Selection

The structure naturally will provide incentives for only the smaller or the less well rated HAs to use MORhomes, where larger credits will fund themselves individually. How can this adverse selection be avoided?

How can investors get comfortable that you are lending to small HAs in the portfolio? Portfolio concentration controls are not applicable until at least the second issuance (£500m).

MORhomes has set a limit on the minimum size of a borrower. This is 2,000 units[3], which is well above the current level at which English HAs attract increased oversight from the regulator. (In Northern Ireland and Wales, all HAs are under more uniform scrutiny).

It is clear that the shareholders and borrowers in MORhomes represent a wide spread of HAs when judged on the basis of size, type or geography. What they share is a requirement for non-"benchmark" funding on a reasonably regular basis – i.e. a regular, annual funding requirement of below £250m.

By investing in MORhomes, investors are gaining exposure to a portfolio of borrowers, and diversification away from the relatively frequent HA issuers in the public market.

MORhomes borrowers go through a rigorous credit process (as set out on page 104 of the Programme Memorandum) taking into account financials and more subjective matters such as management which can be a risk in a growing association. MORhomes have taken a number of members through the credit process who have public credit ratings. This has helped MORhomes to validate its process against these ratings. Broadly MORhomes' assessments have been in line with or slightly lower than the available public ratings.

MORhomes will continue to publish the borrowers in each tranche. You will see that for the first issue, the larger borrowers are publicly rated and at a very strong level.

3. Financial Arbitrage

Isn't MORhomes designed to provide borrowers with the benefits of financial arbitrage at the expense of the investor?

Unlike other aggregators, MORhomes at inception offers access to a significant level of junior debt and capital to support its borrowing – equal to at least 5% of the total debt outstanding – as well as liquidity to support any interruption in payments.

This provides credit support to investors in any senior notes. Scenario testing indicates they are repaid in cases of serious loan default other than a significant sector-wide systemic collapse.

Clearly MORhomes hopes that this will be reflected in the price of any senior notes issued by MORhomes. However, the motivation behind the structure is not driven by financial arbitrage but a desire to offer a robust and sustainable structure

- With a minimal risk of bond default
- That can issue in meaningful volume if demand is sufficient
- While protecting the capital ratios.

4. Conflict of interest

Are there not conflicts of interest and governance issues with Shareholders being Borrowers?

MORhomes has been designed to align the interests of shareholder/Borrowers and Investors by

[3] See Note 1 above

- Requiring Borrowers to put capital at risk by purchasing ordinary shares in MORhomes and subscribing for Subordinated Debt.
- Having a board with a majority of independent members
- Complying with the UK Corporate Governance Code.

During the process of establishing its governance structure, MORhomes consulted a specialist governance adviser (Wedlake Bell).

5. Business Model

Can you give colour on expected funding volumes over time?

Is MORhomes going to meet its business plan of £1bn issuance a year?

According to Homes England Data, the sector has over £70bn[4] of debt; estimates of the sector's annual funding requirement are around £4bn pa[5] over the next few years based on a requirement for new debt and maturing facilities.

This will be MORhomes' debut transaction which it is launching from it long term, sustainable funding programme. It is very conscious of the need to manage this responsibly and would therefore not be expecting to market a further benchmark issue until later in the year. MORhomes' target is to build up to £1bn per year over the next couple of years, across all maturities and other markets, such as the US Private Placement market, where it can access sterling, based upon these expected future finance needs of our Borrowers and the sector more broadly. MORhomes was set up in response to the fact that whilst government is encouraging HAs to increase their development programmes, the number of funding alternatives has reduced: the AHF and EIB programmes have finished and THFC No 3 is no longer issuing large benchmark issues. At the same time, few borrowers want to access the bond market in their own name given their annual needs.

HAs can use the funds as a source of new finance or to refinance maturing or restructured facilities. It has over 60 shareholders, most of whom would qualify to borrow through MORhomes.

Is MORhomes a sustainable model following a single issuance? What level of issuance is needed going forward in order to maintain/grow the equity buffer?

Yes, MORhomes has been stress tested for a single issue and it can be run with very low running costs. Moreover, MORhomes is able to reclaim ongoing costs from its borrowers.

The equity buffer would still grow but at a slower rate. However, MORhomes has a range of other mechanisms to conserve cash through the lock up provisions and the Subordinated Debt can be converted to equity as explained in the Programme Memorandum.

Why would a multi-maturity model work for borrowers in the medium and long-term (ie. will demand for MORhomes issuance follow and keep them growing)

HAs have been borrowing from the bank and capital markets for over 30 years. Until the financial crisis, they generally borrowed very long term, and mainly from the banks. Since 2007/08, they have tended to shift to a mixed funding approach - banks offering shorter term flexible facilities and the capital markets longer term debt. This has required HAs to manage finance and treasury more actively.

Their business model has also changed so that their portfolios are less static – more active asset management, shared ownership, property for sale and private rent. As a result, many HAs are looking to vary the maturity of their debt.

While the banks will continue to offer the most flexible form of shorter term debt, there will be times when borrowing 5-7 year money from the capital markets will also be attractive. MORhomes aims in time to offer this type of maturity.

[4] Global Accounts for Private Registered Providers 2018
[5] S&P "UK Social Housing Providers to borrow £12bn of new debt by 2020, Total debt to reach £89bn" This note, published in March 2018, assumes 90% of this debt is borrowed by housing associations.

Explain the appeal to MORhomes for HAs vs. standalone / other forms of financing

Apart from any cost benefit over time, MORhomes believes that HAs see the advantages as follows:

- Availability and amount - The ability to borrow £10-20m at a time is very useful to borrowers – firstly for managing cash requirements, and because over time they will be able to better manage their repayment schedule to greatly reduce carry cost. Public bond issuance now appears to require a minimum of £150m sale and a private placement needs to be £40-50m to ensure a competitive process
- Predictability of credit process – Borrowers see and use the MORhomes credit model and if their application is agreed, they will be given an annual Lending Level
- Speed to market – the ability to charge the majority of assets after issue, materially cuts down on lead time, reducing market risk
- Efficient use of security – housing associations increasingly run mixed tenure portfolios; they want to charge a range of assets albeit on lower LTVs than social housing
- Access to range of maturities on standardized documentation
- Operational issues – Time and resources, high fixed and variable incidental costs, public bond ongoing compliance – these are all things that deter borrowers from accessing own name issues and incline them to use MORhomes
- Credit Rating/listing - Many borrowers do not have a credit rating and they do not want the obligations of a public bond issue.
- Another source of funding – HAs will still use a full range of funding sources including public and private bonds; however, MORhomes offers another alternative.

6. Peer comparison

Why do you think MORhomes is as good a credit as THFC or bLEND?

What are the key differences of the MORhomes model to the THFC/bLEND/GB Social Housing

THFC has done a fantastic job for housing associations but its model was designed many years ago and THFC No 3 is only used today when its bonds stand at a large premium to par, reducing the security per £ raised to more modern levels.

MORhomes believes that its ownership and capital model is a very attractive structure (for the reason described below), but that it clearly hasn't the trading history and track record, and has therefore been notched down by S&P. MORhomes wanted to establish an inclusive, sustainable model and was not convinced that the Moody's methodology used by bLEND was ideal for this.

MORhomes believes it has the following advantages in terms of credit

- MORhomes starts with proportionately (measured against loan book) twice the capital as THFC has accumulated after 30 years of trading (1.65% vs 0.80%) while GB Social Housing was operating with capital to loans of 0.21%.[6]
- MORhomes' capital can immediately be used to support any defaulting borrower, not just the borrower that has provided the capital.
- The capital is provided by the sector and particularly the borrowers themselves – they have skin in the game to each other.
- MORhomes also starts with immediate liquidity as the equity contributions of borrowers are held in cash, and a large proportion of profits are retained.
- MORhomes initially has an unsecured liquidity facility from four lenders in aggregate currently totaling well in excess of one year's interest receivable on the loan book, which along with MORhomes' own cash (initially £1.3m from borrower equity contributions) can be used to resolve cashflow issues created by any loan in the portfolio.

[6] Based on THFC and AHF 2018 Accounts (Statements of Financial Position): THFC Group loans excluding AHF loans £3.58bn; THFC Group equity less AHF equity £28.47m
GB Social Housing 2017 Accounts (Balance Sheet): Loan book £266m and Shareholders funds £0.561m

MORhomes' credit model is designed to ensure quality, and be consistent with credit rating agency ratios. It is transparent to investors and borrowers, and minimum lending terms cannot be amended unless MORhomes is satisfied that the rating of the notes will not be adversely affected. As the credit models of THFC and GB Social Housing are not fully transparent, it is not possible for MORhomes to comment on it.

GB Social Housing has done an excellent job in offering facilities for smaller HAs. MORhomes' ambition has always been to build on the strength of the sector and it therefore has to appeal to a very broad group of potential borrowers. Its shareholder base demonstrates that it has achieved this.

bLEND is a very different structure and depends on the weighted average credit rating of the underlying portfolio. This limits access and might lead to less diversification in the portfolio.

MORhomes also aspires to provide more "Investor Friendly" product through

- Its commitment to transparency and investor relations
- A desire to establish a curve,
- Issue benchmark sized issues, and
- By engaging with a broad dealer group.

How can investors get comfortable with the outsourced credit evaluation process?

The credit evaluation process is overseen and set by the Board and the Credit Committee from start to finish. The credit policies are set by MORhomes Board, and the Credit Model has been designed for and is controlled by MORhomes.

MORhomes' in-house team conducts an initial review of the Credit Model data. The role of Edison in the process is to write an independent due diligence report for the Credit Committee based on a review of the model, and interview with the borrower. The report will conclude with a recommendation of a Lending Level. . The Credit Committee can accept or reject it or ask for further information. The Lending Level is approved by either the Board of MORhomes or the Credit Committee provided that it complies with the policy set by the Board.

7. Unsecured period

Why are you giving an unsecured period at no real additional cost? Is the fee really an incentive?

Organising security charging is one of the most onerous part of any bond issuance process for HAs, depending on responses from local authorities and the Land Registry which can result in delays beyond the control of the HA. The process can delay issuance so long that the market may have changed in the meantime.

MORhomes therefore wants to make access to the market faster for HAs while ensuring it is putting in place protections for investors. It does this by

- Conducting extensive due diligence on the look-forward business plan (FFR),
  - Liquidity and available assets are a focus for the credit report and
  - Are heavily weighted in the credit ratios, and
  - The credit report is reviewed by the Credit Committee which currently comprises both credit professionals and those with first hand HA treasury experience.
- Reviewing management accounts every quarter with continued focus on available assets and liquidity;
- Requiring
  - a legal certification as a CP to drawdown of funds that the borrower has sufficient uncharged eligible security available to meet the asset cover ratio by the Required Charging Date (as defined in the Programme Memorandum) , and
  - an ongoing covenant that it will continue to maintain sufficient uncharged eligible security to meet the asset cover ratio.
- Currently, having unsecured liquidity facilities available from 4 banks to cover income shortfalls

- Requiring cash collateral to be pledged within 5 business days of request by MORhomes if the borrower's Lending Level falls and its lending limit is breached
- Demanding fees at a rate which increases over time to be paid over the unsecured period.

It may also be worth noting that MORhomes takes a fixed charge on *de minimis* security at the point of making its loan to each borrower so that it is notified and would enable MORhomes or the Trustee to direct MORhomes to participate in any moratorium arrangement.

As MORhomes grows, the proportion of borrowing without charged assets will fall as each cohort of borrowers begins the charging process.

8. Collateral

Why don't the HAs have to pledge security over social housing?
Security selection and methodology – how do you prevent receiving 'the worst stock' from each HA?

Eligible security

- At least half (by value) of the eligible security HAs are pledging has to be social rented, affordable rented, sheltered or supported housing. Subject to this condition being satisfied, Borrowers are also permitted to pledge shared ownership housing (which is also social housing and must be valued using the EUV-SH methodology of the RICS), and certain other types of property: HAs do much more than provide rented social housing, and MORhomes wants to represent the sector as a whole. At its absolute discretion, it can accept other core assets of HAs, including care assets, and head offices. The valuation basis must be agreed by MORhomes.

- In MORhomes' view, the advantage of taking this type of asset is that not only does it increase social impact for the HA, but some of these assets tend to be easier to sell if the Trustee ever needed to direct MORhomes to enforce security over them.

- Shared ownership is a more complex asset class but has a long track record of strong performance. It is also an area attracting most interest from private sector providers, potentially broadening the market for the stock.

Adverse selection

- In a number of cases, MORhomes may be participating in a security trust with numerical apportionment.
- MORhomes will require the same due diligence in terms of chargeability of stock as any other lender.
- MORhomes will provide instructions to the valuers. MORhomes will discuss stock with the valuers and will reject properties that are not Eligible Properties as defined in the Programme Memorandum.
- The valuation requirements will ensure that any 'poor' quality stock will automatically be reflected in the valuation. Stock is regularly revalued and borrowers are under an obligation to maintain the asset cover at all times after the unsecured period, pledging additional security if necessary.
- Indications of the stock to be pledged for the first tranche are that it broadly reflects borrowers' overall mix of stock and is predominantly (over 90%) social housing.[7]

9. Value of Structure

Why do you think your structure is so valuable?

[7] Based on responses to a survey of prospective borrowers in first tranche

In the rare case that an HA encounters financial challenges it is typically because cash balances run low and its assets are not easily realisable. It is, therefore, very important to have time to resolve a problem.

MORhomes has been set up to manage severe breaks in liquidity resulting from major interest payment defaults. The capital structure, liquidity regime and waterfalls are all designed to ensure payments are maintained on any senior notes whilst problems on any loans are resolved.

Structural enhancements include:

- Capital at risk
  - Equity in a public limited company provided by HA shareholders and largely by the borrowers themselves
  - Borrower equity subscriptions are retained in cash
  - MORhomes should build retained earnings as its policy is to distribute no more than 25% of earnings
  - As MORhomes has proven, it is also possible to return to shareholders with a rights issue
  - Subordinated Debt, also provided by borrowers, adds a further layer of capital at risk
  - New borrowers must also provide initial equity subscriptions.
- Junior secured capital
  - Second Secured Debt, subordinated to any noteholders and with the capability of rolling up interest to preserve cash in MORhomes
- Liquidity facility
  - Initial unsecured liquidity facility provided by four banks which can be drawn when underlying loans are in default
- Cash lock ups
  - Apart from the waterfall of payments – which is on a look forward basis - various events trigger cash lock ups:
    - A payment default on a single loan will stop dividend payments
    - Whilst a drawing on the liquidity facility will stop Subordinated Debt and dividend payments.

10. Collateralisation of the notes

The senior notes are secured on secured loans. How does the collateralisation work?

The senior notes have the benefit of a floating charge over all of MORhomes' assets, including a pool of RP loans which in turn are secured on property (and possibly cash). The collateral requirements for the RP loans vary depending on the nature of the security with the lowest asset cover requirement being 1.05x for assets valued on an EUV SH basis. Please see page 117 of the Programme Memorandum for more details.

There is also a level of overcollateralization on the senior bonds when measured against the aggregate principal of the RP loans. This is because the proceeds from any senior notes are initially expected to fund c.95% of the loans with the balance of the funding coming from a combination of second secured debt and Subordinated Debt, while there will also be cash retained from the equity subscribed by the borrowers.

11. Corporate Covenants

Why don't you think corporate covenants are important?

MORhomes will only lend to regulated housing associations (either direct or via a group funding vehicle) and aims to have a portfolio reflecting the strength of the sector rather than biased towards the business model of particular housing associations.

MORhomes considers that it protects itself better by limiting the amounts it will lend; having an asset management policy that weights it towards better rated entities and remediation policy involving active engagement and that requires collateral to be pledged.

MORhomes considers covenants a two edged sword – while they may put limitations on the borrowers' capacity to borrow, they create a performance risk that may well fetter its business. MORhomes considers the most important credit factor is the borrower's liquidity and capacity to generate returns from its business.

Moreover, MORhomes is under an obligation to report to investors on a quarterly basis about the state of its portfolio as set out in Conditions 7(j) and (p) of the Programme Memorandum.

Will MORhomes hold an annual noteholders' meeting?

MORhomes intends to host a meeting or call for noteholders on an approximately annual basis. Further details will be provided by the Issuer via RNS closer to the relevant time.

12. Rating

Why is the rating worse than THFC?

Given all these enhancements, why is the rating so low?

MORhomes has a strong investment grade credit rating, with a positive outlook. It is rated under S&P's Public Sector Funding Agency methodology which includes not only THFC and GB Social Housing but also issuers such as MuniFin and Kommuninvest.

This is a risk adjusted capital model where the score is then notched up or down for a variety of other factors. Key to S&P's analysis is how much equity or quasi equity is in the vehicle.

MORhomes exceeds the required equity amount but as it has the top score for financial strength, it can gain no explicit mark up for additional capital liquidity cushions. Rather these are taken into account in the more subjective analysis.

MORhomes was then notched down for being a 'start-up' and therefore it was unable to benefit from any score for "Business Risk" for the same reason.

However, S&P have given the overall structure a very positive write-up, and reflected this strength in the Positive Outlook.

It is worth noting that a similar vehicle to MORhomes, HI-C Issuer Trust (HIT), a new Canadian public-sector funding agency that lends to affordable and social housing providers, has just been rated in Canada. This has quasi government equity and a higher capital base, but is still rated A- (stable).

13. Sovereign Risk

What would you expect the impact of a sovereign downgrade to be on the rating?

MORhomes has no benefit from government support in the same way that some HAs are notched up as government supported entities.

However, the risk adjusted capital is based on ratings of underlying borrowers. The fact that MORhomes is "overcapitalised" and is weighted to stronger borrowers, and has a positive outlook, may give some protection against a downgrade in line with underlying borrowers.

14. Second Rating

Will MORhomes obtain a second rating?

Yes that is our intention to seek a second rating in due course.

15. Start up

If the start-up nature is so penal, why did you not get established management to run MORhomes?

The model is also an innovation, so it is not simply about management experience. 62 shareholders want MORhomes to be established as an alternative route to market so it is confident that its offer will appeal to borrowers.

MORhomes believes that with the experience on its board, its management and its outsourcing partners, it is very robust, and unlike other models is subject to scrutiny from shareholders.