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CREDIT OPINION
31 May 2018

Update

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RATINGS

UPP Bond 1 Issuer PLC

Domicile	United Kingdom
Long Term Rating	Baa1
Type	Senior Secured - Dom Curr
Outlook	Stable

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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UPP Bond 1 Issuer PLC

Annual update

Summary

UPP Bond 1 Issuer PLC's (the Issuer) (part of the UPP Group Ltd (UPP, not rated)) credit benefits from: (1) the long-term concessions held by subsidiaries (AssetCos) of its parent, UPP Bond 1 Limited (ParentCo), to provide student accommodation and facilities management at seven UK universities, (2) stable revenue given close to 100% occupancy of the portfolio since UPP's involvement, (3) the partnership approach to the concessions, reflected by protective covenants and upside sharing under the concession contracts but also by the support provided by the universities to UPP's projects, (4) the diversification of the portfolio, which mitigates asset-specific risks, (5) the Issuer's exposure to the world-class UK Higher Education (HE) sector, which demonstrates robust demand characteristics and (6) UPP's solid track record in the HE sector.

However, credit risks include: (1) the Issuer's exposure to price and demand risk, albeit this is well mitigated, (2) some uncertainty in relation to medium-to-long term student demand trends, (3) the Issuer's financial structure, which includes a super-senior inflation-linked swap and (4) the ability to raise additional indebtedness to fund new AssetCos, which could be of a weaker quality than the existing portfolio, although this is somewhat mitigated by certain conditions which need to be met.

Exhibit 1
Project overview

Project description	The provision of on-campus or near student accommodation and certain facility management at seven established UK universities
Site overview	11,693 rooms of new build and estate transfer self-catering student accommodation.
Issuer	UPP Bond 1 Issuer PLC
ParentCo	UPP Bond 1 Limited
AssetCos	UPP (Alcuin) Limited, UPP (Broadgate Park) Holdings Limited, UPP (Kent Student Accommodation) Ltd, UPP (Nottingham) Limited, UPP (Oxford Brookes) Limited, UPP (Plymouth Three) Limited, and UPP (Exeter) Limited
Universities	University of York, University of Nottingham, University of Kent, Nottingham Trent University, Oxford Brookes University, Plymouth University, and University of Exeter
Construction completion	1998-2012
PA lease terms	35-45 years
Construction contractor	Estate transfers, subsidiaries of Balfour Beatty plc, Jarvis plc, and others
Operator	UPP Residential Services Ltd (soft and hard facilities management) (URSL) [1]
Lifecycle risk	Borne by AssetCos
Price and demand risk	Yes, but somewhat mitigated by contractual provisions.
Senior debt	£307.1 million 4.9023% fixed rate notes, £75 million 2.729% index-linked notes, and £149.7 million 1.037% index-linked bonds (together, the Bonds)
Debt maturities	2040, 2047, and 2049
Projected ADSCR metrics	Minimum 1.33x (August 2031) Average 1.51x (2018 - 2047) and 1.75x (2018 - 2049)
ADSCR covenants	Lockup 1.15x, and Default 1.05x

[1] At the University of York, soft facilities management is provided by the university.
Source: Project documents

Credit strengths

» Strong student demand and on or near campus locations support high occupancy rates

» Portfolio diversification and cross-collateralisation between the AssetCos

» Various positive contractual provisions in the concession agreements including protective covenants, nominations agreements and rent setting mechanisms

» Positive partnership approach between UPP's projects and the universities

» Satisfactory operational and financial performance with no deductions

Credit challenges

» Exposure to price and demand risk

» Some uncertainty in relation to medium-to-long term student demand trends

» Structural weaknesses including a super-senior inflation-linked swap and the ability to raise additional indebtedness to fund new AssetCos

Rating outlook

The rating outlook is stable reflecting our expectation that the project will continue to achieve high occupancy rates over the terms of the Bonds, with rents and costs modestly increasing over time.

Factors that could lead to an upgrade

Moody's could upgrade the rating if: (1) occupancy and rent increases consistently outperform our base case projections as outlined in our pre-sale report for the Issuer and (2) greater certainty develops around longer term demand dynamics.

Factors that could lead to a downgrade

Moody's could downgrade the rating if: (1) the Issuer fails to achieve target occupancy or rent increases as set out under our base-case scenario, (2) projected student demand for accommodation results in a forecast student-to-bed ratio of less than 2.0x, (3) there is a significant increase in supply of student accommodation which is not directly procured by the universities, or (4) there is poor service performance at individual concessions.

Key indicators

Exhibit 2
ADSCRs and historical occupancy levels

	2017 [1]	2016 [1]	2015 [1]	2014 [1]	2013 [1]
ADSCR	1.37x	1.38x	1.39x	1.30x	n/a
Occupany levels (%)	99.9%	99.9%	99.7%	100.0%	99.5%

[1] August year-end
Source: Annual investor reports

Profile

The Issuer is a 100% subsidiary of ParentCo and part of UPP, the largest provider of on-campus student accommodation to universities in the UK. ParentCo holds, through the ownership of seven AssetCos, certain university accommodation concessions with established UK universities.

In March 2013, the Issuer raised £307.1 million 4.9023% fixed-rate notes maturing in 2040 and £75 million 2.729% index-linked notes maturing in 2047 and on-lent the proceeds to the AssetCos through six on-loan agreements which benefit from cross-collateralisation. In December 2014, the Issuer raised £149.7 million, 1.037% index-linked bonds maturing in 2049 to finance the addition of a seventh AssetCo, UPP Exeter.

The seven AssetCos have entered into long-term leases, largely ranging from 35 to 45 years, with seven universities being the University of Kent, the University of Nottingham, Nottingham Trent University, Oxford Brookes University, Plymouth University, the University of York, and the University of Exeter. Under the terms of the leases, which cover a total of 11,693 rooms of self-catering student accommodation located on or close to the respective campuses, the universities are responsible for marketing and allocating the accommodation and also for collecting rent that is then passed to the AssetCo. URSL provides maintenance and lifecycle services for all AssetCos until the end of each concession period, when the buildings will be handed back to the respective universities. URSL also typically provides soft facilities management services (e.g., cleaning and security) at each concession.

Detailed credit considerations

Recent developments

UPP has successfully converted to a UK REIT

On 01 March 2018, UPP converted to a UK Real Estate Investment Trust (REIT). Please see https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1104904 for further details.

We believe that the corporate reorganisation of UPP to facilitate the REIT conversion will not adversely impact credit quality.

Performance and contractual terms

Whilst applicant numbers have fallen nationally student demand remains strong supporting high occupancy rates

In 2017/18, as reported by UCAS, the total number of applicants for HE full-time enrolments was approximately 3.7% lower than the prior year. According to ProjectCo, this was expected, in line with the demographic decline of 18-24 year olds in the UK.

Despite this decline, we still consider demand for HE robust. The total number of HE full-time enrolments has grown year-on-year by approximately 1.2% since the sharp decline in 2012/13, which coincided with the introduction of higher tuition fees from £3,290 to £9,000 per annum. According to the Higher Education Statistics Agency (HESA), in 2016/17, full-time student enrolments increased by 3.3% compared to 2015/16 and is 4.5% higher than the previous peak in 2011/12, where students sought to commence HE prior to the introduction of higher tuition fees.

Average occupancy across the portfolio in 2016/17 was 99.8%. All of the AssetCos have achieved 100% occupancy for 2017/18. The portfolio has consistently experienced high occupancy rates averaging above 99.8% over the past five years. In 2015/16, the portfolio had an average student to bed ratio, an industry measure of demand for university controlled accommodation, of 2.9x.

The properties in the portfolio also have a strong competitive advantage in terms of location. All accommodation blocks are located on or adjacent to campus, are generally custom-designed for students' needs and are furnished as self-catering accommodation. In a number of cases the concessions have bars, shops and other amenities for students.

Positive partnership approach between the AssetCos and the universities and various contractual provisions mitigate demand risk

Although the universities do not hold any ownership of the AssetCos, they do have significant interest in the project, not least in ensuring that the accommodation meets the needs of their students.

There are restrictive covenants in place, which restrict the universities from building additional accommodation or entering into agreements with other accommodation providers unless certain conditions have been met. Furthermore, the majority of concessions contain a revenue-sharing mechanism whereby the relevant universities benefit from revenue in excess of that originally forecast.

Rent for each concession is set annually based on the respective mechanism set out in the individual concession/headlease agreements between the AssetCo and the university.

UPP and URSL have a successful track record in managing the projects and have good working relationships with the universities for which UPP provides accommodation.

Operational performance has been satisfactory with no deductions despite cladding defects at UPP (Exeter) Limited which are being resolved

The AssetCos' revenues are derived from rents collected from tenants. Although the universities take credit and void risk once the student has entered into the rental agreement, the universities do not guarantee a minimum level of occupancy.

The project consists of 11,693 rooms across seven universities, demonstrating its significant size in comparison with peer projects. This scale and diversity helps mitigate against volatility in occupancy and expenses. UPP has negotiated rent increases across the portfolio in line with RPI for academic year 2017/18. Underlying rental income increase is forecast at 1.7%.

URSL incurred no deductions for unavailability or poor performance in the 12 months to August 2017, which is consistent with the level of performance since URSL took over operation and maintenance responsibilities of each concession. In 2015, a latent non-fire-related construction defect was identified at UPP Exeter in relation to external paneling of the accommodation buildings. Operations have been unaffected, with occupancy at 100% in 2017. UPP has worked closely with Exeter University and the construction contractor, a

subsidiary of Balfour Beatty plc, to develop a satisfactory rectification plan. Works began in the summer vacation period of 2017 and are progressing. All associated costs are expected to be borne solely by the construction contractor.

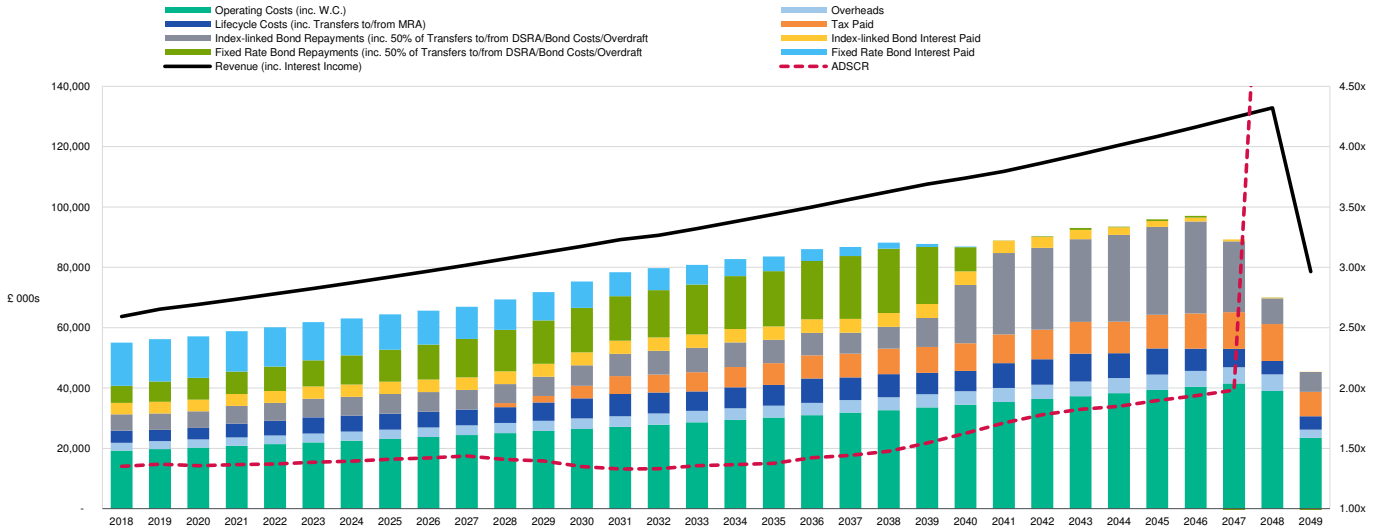
Financial analysis

Financial performance is satisfactory

The annual debt service coverage ratio (ADSCR) for 2016/17 was 1.37x compared to a lock-up ADSCR of 1.15x. Under our base-case scenario, the minimum and average ADSCRs (excluding years 2048 and 2049) is 1.33x (occuring in 2031) and 1.51x, respectively. Our long-term base-case occupancy assumption is supported by current occupancy rates of 98%-100% and covenants at each of the seven concessions, which impose restrictions on the universities' ability to develop additional student accommodation or enter into agreements with other accommodation providers.

Exhibit 3

Cash flow projection summary



Source: Issuer's financial model

Liquidity analysis

As at 28 February 2018, all of the Issuer's mandatory reserves were fully funded. The balance of the six-month debt service reserve account (DSRA) equalled approximately £15.6 million and the combined capital expenditure reserve stood at approximately £11.8 million.

Rating methodology and scorecard factors

The principal methodology used in these ratings was Global Housing Projects published in December 2015. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

Exhibit 4

Methodology grid

Global Housing Projects	
Factor 1: Financial Position (65%)	**Score**
a) Debt Service Coverage	Baa
b) Liquidity & Reserves	Ba
c) Diversity & Sources of Revenues	Baa
Factor 2: Market Position (20%)	
a) Demand Drivers	Baa
b) Project Size	Aa
Factor 3 : Property Management (15%)	
a) Ownership / Affiliation	Aa
b) Project Management	A
Rating	
a) Indicated Rating from Grid	Baa1
b) Actual Rating Assigned	Baa1

Source: Moody's Investors Service

Ratings

Exhibit 5

Category	Moody's Rating
UPP BOND 1 ISSUER PLC	
Outlook	Stable
Senior Secured -Dom Curr	Baa1

Source: Moody's Investors Service

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