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SL Green Realty Corp. (SLG)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Thank you, everyone, for joining us; and welcome to SL Green Realty Corp.'s Third Quarter 2022 Earnings Results Conference Call. This conference is being recorded.

At this time, the company would like to remind listeners that during the call, management may make forward-looking statements. You should not rely on these forward-looking predictions of future events, as actual results and events may differ from any forward-looking statements that management may make today. All forward-looking statements made by management on this call are based on their assumptions and beliefs as of today. Additional information regarding the risks, uncertainties and other factors that could cause such differences to appear are set forth in the risk factors and MD&A sections of the company's latest Form 10-K and other subsequent reports filed by the company with the Securities and Exchange Commission.

Also, during today's conference call, the company may discuss non-GAAP financial measures as defined by Regulation G under the Securities Act. The GAAP financial measures most directly comparable to each non-GAAP financial measure discussed in the reconciliation of the differences between each non-GAAP financial measure and the comparable financial measure can be found on both the company's website at www.slgreen.com by selecting the press release regarding the company's third quarter 2022 earnings and then the supplemental information included in our current report [indiscernible] (00:01:19) relating to our third quarter 2022 earnings.

Before turning the call over to Marc Holliday, Chairman and Chief Executive Officer of SL Green Realty Corp., I would ask that those of you participating in the Q&A portion of the call, please limit yourself to two questions per person. Thank you.

I will now turn the call over to Marc Holliday. Please go ahead, Marc.

Marc Holliday

Chairman & Chief Executive Officer, SL Green Realty Corp.

Thank you. Good afternoon, everyone. We appreciate you dialing in today, and we look forward to giving you an overview of our quarter's results, taking your questions. Just want to remind everyone that since 2019, we faced many new challenges, which in turn caused us to raise our bar even higher and respond in ways that have been beneficial for our tenants, our shareholders and our community.

In less than three years, we signed over 5 million square feet of office leases, we completed two dozen individual sale transactions at a gross price at share of $5 billion. We developed and acquired new world-class assets; oversaw and executed $2.25 billion of physical construction projects for on-time deliveries; reduced our DPE balance to $663 million at quarter end. We created a new iconic global entertainment destination, SUMMIT.

We managed our portfolio in a safe, secure and efficient manner; launched a portfolio-wide hospitality and amenity program. And we did all of this throughout by working five days a week from office, the only possible way we could have realized these extraordinary accomplishments. I want to once again express my extreme gratitude to the amazing and talented workforce here at SL Green, who came together, all of us on the floor of the New York Stock Exchange to ring the closing bell and celebrate 25 years of excellence in improving the way which New Yorkers live, work and play.

And this momentum carried through into the most recent quarter. I'm extremely, extremely pleased with the leasing performance in Q3, highlighted by the Franklin Templeton deal at One Madison Avenue and Memorial Sloan Kettering Deal at 885 Third Avenue, which took a total of over 750,000 square feet of vacancy out of the SL Green portfolio [indiscernible] (00:03:48) economic terms that were consistent with our expectations.

As pleased as I am with the leasing performance in Q3, I'm just as happy that we were able to retire $800 million of maturing public bonds through a series of paydowns and financings that were done on attractive terms. Furthermore, we're highly focused on implementing strategies to mitigate our exposure to rising interest rates by executing on a series of swaps, caps and debt repayment. Understandably, a lot of the focus from the market is on the leasing performance and tenant demand. And on that front, we feel quite good about where we are given the portfolio is highly improved and our overall asset quality has never been better.

We continue to amenitize our best assets to attract top tenants. And as a result, the portfolio is still well occupied today at 92%. And we have marketing and capital plans in place that we believe will enable us to operate during this market cycle at or above 90% or better until things begin to turn around. Rising interest rates, on the other hand, are more of a concern, given the impact it has on our earnings, making interest rate hedging and debt reduction our number one priority for the foreseeable future.

I think, Matt and his team have done an excellent job with this, as evidenced by the $1.25 billion of corporate swaps entered into during third quarter to hedge future floating rate exposure. In addition, during the most recent quarter, we entered into cap contracts in another $270 million of variable rate property debt. And just yesterday, we swapped another $200 million on a floating rate mortgage.

Notwithstanding the current interest rate environment, the underlying New York City economy is still chugging along based on employment data showing that NYC added 24,000 private sector jobs in August and is now 100,000 jobs ahead of New York City OMB's original 2022 forecast. More to the point, 22,500 office-using jobs have been created in just the last three months reported, now bringing the total office-using jobs recovery to 104%, a pre-pandemic high-water mark. And contrary to what you may see in the media, I expect September's numbers, due out momentarily, to show positive as well.

The numbers confirm what we feel, that New York City is finally back to normal. The road, sidewalks and commuter trains are packed and the subways are coming back. Tourism and hospitality are near pre-pandemic levels. Residential rental market remains tight. And the enablement of conversion of office to resi to help solve this problem is gaining momentum at the state and city levels. Meetings, conferences, parties, they fill the calendars, and the rhythm of New York's social life has returned.

Before opening up the line for questions, I want to acknowledge a few other milestone moments for the company. First, SUMMIT One Vanderbilt is celebrating its one-year anniversary tomorrow. We will all be there to recognize the successful launch of this world-class attraction that has quickly become one of New York's hottest experiences, having welcomed 1.4 million guests to SUMMIT during the first year of operation, with far more expected next year.

During the third quarter, we prevailed in consolidating ownership and control of 245 Park Avenue, a trophy asset in the SL Green corridor of owned properties after a contentious bankruptcy litigation. We have plans to improve 245 Park over the next 24 months to make it one of the most desirable buildings on Park Avenue. Last week, we received the excellent news that Le Pavilion received a Michelin Star, less than 18 months after opening during the pandemic.

And finally, this morning, we announced a partnership with Caesars Entertainment to pursue a downstate casino license for a world-class gaming hotel and entertainment venue in the heart of Times Square. In connection with this effort, we have formed a coalition for a better Times Square that seeks to make significant investment in security, traffic mitigation, mass transit improvements and accelerate economic recovery for surrounding businesses and create good-paying jobs for local New Yorkers.

With that summary, we'd like to open up the line for questions on the quarter and whatever else is on people's minds.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Alexander Goldfarb with Piper Sandler. Your line is open.

Alexander Goldfarb
Analyst, Piper Sandler & Co.

Q

Oh, good afternoon. So, two questions. First, just taking a look at bringing on, converting the DPE positions for 5 Times Square and 245 Park. Just want to understand, one, the earnings impact, because I think, you were getting close to 11% on the DPE positions previously. I'm not sure how that equates to a cap rate on the buildings. Two, I think you have some large vacancies coming in 245 Park. So, maybe, Matt, if you could just talk about how we should think about the economics and impact to earnings from converting those two positions.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

Sure. I'll let Steve address the 245 Park vacancy question you had. As to earnings, obviously, we'll be giving guidance for 2023 on December 5 at our investor conference, so you'll get more detail then. You alluded to the DPE balances rolling off. That's about $367 million of debt and preferred equity investments combined between 245 and 5 Times that were rolling off it, just short of 11%.

You're right, the properties do not generate that equivalent return on their face. 5 Times is in redevelopment and lease up. We only own 30% – 32% roughly of that; and 245, we own 100% of. There will be finalization of GAAP adjustments and those types of things done over the coming weeks leading into our guidance for 2023. But the roll-off is substantial at $367 million at near 11%.

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

And then with regards to vacancy – or pending vacancy at the building, we really don't have as much as I think you may suspect. The JPMorgan space, which is 17 floors in the building, 15 of those floors were either previously leased to [indiscernible] (00:11:01), or while we were doing the leasing for HNA, we had pre-let five of the floors to Houlihan Lokey. So, that only leaves us two floors to really deal with, when we get that space back late next year.

Other than that, there's about 120,000 square feet of current vacancy. There's another block in the building that we get back late this year – I'm sorry, late next year, Major League Baseball, which had roughly five floors. We had pre-leased most of that space on short-term leases to either Rockefeller Group or Houlihan Lokey. So, we'll now get it back, mid to end of next year. Other than that, there's a smattering of floors throughout the building and that sort of roll over the next couple years, is what's justifying the capital program that were in design for the building right now, which we're really excited about.

Just to remind everybody, this product is exactly what the world is looking for today. It's side core design, has a four-plate design that has actually six corners on it, the way it's configured; sits directly – catty-cornered to JPMorgan's new headquarters; has direct access to Grand Central Terminal. Our development plan, which is going to be a spectacular transformation of the building from the plaza, to the lobby, to amenities being added is, I think, very forward-thinking. And we're already trading paper with prospective tenants. So, I have the greatest of confidence that this building will outperform.

Alexander Goldfarb
Analyst, Piper Sandler & Co.

Q

Okay. And then, the second question is, Matt, on the swaps, lot of news and press reports about the rise and cost of swaps, but you guys have been quite active. Can you just give us some perspective, how much pricing has changed? And should we think about swaps being prohibitive or based on the fact that you guys are still executing them earlier this week that prices may have gone up, but in the scheme of things, given debt costs, still plenty of availability and cost effectiveness on the swaps for your debt?

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

Yeah, certainly the latter, not the former. And I think Marc alluded to the fact that we're going to continue to target reducing future floating rate debt exposure through caps and swaps. You talk about cost. Technically the way it works, cost for a swap is built in through a credit charge, which is just measured in basis points on top of the rate that you swap. In the $1.250 billion, it was roughly five basis points on average, so not much. Haps have an upfront cost and those costs are based on the term and the benchmark.

So, yeah, there has been some press about increasing cost. I think cost of everything has gone up. But certainly the savings we're realizing by executing on these trades far exceeds whatever incremental cost may be embedded in them. Just to put that in perspective, on the $1.250 billion that we did and was included in the press release, that was done more than 100 basis points tighter than where you would do those today. On $1.250 billion, you can do the simple math, 100 basis points, $1.250 billion over the course of several years, that's a lot of money; well worth a couple basis points.

Alexander Goldfarb
Analyst, Piper Sandler & Co.

Q

Thank you.

Operator: One moment for our next question. Our next question comes from Steve Sakwa with Evercore ISI. Your line is open.

Steve Sakwa
Analyst, Evercore ISI

Q

Thanks. Good afternoon. I guess, Steve, I was just wondering if you could comment a little bit more on kind of where the pipeline sits today, given that big tech has sort of gone on hold, I'm just curious what parts of the market are you seeing the most demand in, whether it'd be size of tenants or what part of New York. Is it Midtown South, Midtown? Any color on leasing would be great.

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Sure. Well, we've got a pipeline that's about 700,000 square feet. Obviously, that number is down as a result of the two big leases that we recently signed. But I think the good news in that pipeline is we're seeing a lot more activity from the small to medium-sized tenants, which is a change from where the market was for the past six to nine months, because a lot of the leasing activity, although the year is doing – broadly speaking, the market, the market is doing well compared to the prior two years, velocity is still down compared to sort of the 10-year average.

But the success in the market this year has been driven largely by the bigger tenants. And I think the new, news, like you I said, is that they were starting to see these small to medium-sized tenants coming back into the market as the bigger tenants, the higher price point tenants that are signing leases were the first ones into the market; the small to medium-sized guys were sitting on the sidelines. And as the big guys are bringing their employees back to the office, you're now seeing those smaller guys follow them into the office. And that's driving a lot more leasing activity. So, some of our Third Avenue, Lexington Avenue product, we have more towards trading paper and signing leases today than we have been in the past year or so, so I think that's positive.

I think Midtown is still, without a doubt, the driver of the overall leasing velocity in the marketplace. Financial Services is some 41%, 42% of total leasing that was signed in the third quarter. [ph] Tuck (00:17:03) is still out there, but obviously in a much smaller, diminished way. They're kind of 8% to 10% of total leasing. But financial services, which in the past couple years was sort of in that 30% range, they're now 40% plus. And I think there doesn't seem to be any slowdown in that segment's demand.

You're also seeing law firms, a lot more active today than they were a year ago. And I think that same demographic is what we're seeing within our portfolio of the core pipeline, about 17% is financial services, 12% is tech and the balance is, everything from government, to health care, to service.

Steve Sakwa
Analyst, Evercore ISI

Q

And if I could ask just a quick follow-up on that. Do most of these requirements, are they kind of downsizing; are they kind of including growth space; are they just kind of musical chairs moving out of 150,000 foot into another; or just what can you say about size?

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Well, there's an unusual amount of relocations taking place in the city as tenants reinvent their workplaces. Typically, about 30% of leases that get signed are relocations. Third quarter, it was over 40% of the leases that were signed were relocations. And I think that's a function of tenants that are continuing to densify. That was a pre-COVID phenomenon that never stopped. And they're reinventing how they want to use their workplace.

So more amenities, more space per employee and a more hospitality vibe in their design. And without a doubt, people are – most businesses are still very unsettled about what their ultimate footprint is going to be. They just don't know. So, they're building in a lot of flexibility on ability to grow and ability to downsize as time goes by because the world is still figuring itself out.

Steve Sakwa
Analyst, Evercore ISI

Q

Got it. And then, Marc, I know it's early, and you just put out the press release, with Caesars on the gaming license. I guess, I'm just trying to sort of think through that. Building's obviously encumbered with a large tenant. And I'm just trying to think through sort of the concept of a vertical casino in New York versus one that's more horizontal. I mean, can you just kind of share any thoughts with us about that?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

Steve, There'll be lots coming out over the course of the next several months. We expect the RFP out sometime in December, but that's not official or formal or announced from the state. That's just our expectation, could be before or could be after. Suffice it to say, we have, what we and Caesars think is an excellent plan for bringing gaming, entertainment and, and hotel right to the heart of Times Square.

I think we wouldn't do anything less than a world-class facility laid out in a way that we think will be extremely successful and desirable and additive to Times Square, which I think really could use a boost right now. So, I would say, stay tuned for those details. Will be more to come and stuff that I and the team are really excited about. But thanks for the question.

Steve Sakwa
Analyst, Evercore ISI
Q

Great. Thank you.

Operator: One moment for our next question. [Operator Instructions] Our next question comes from Michael Griffin with Citi. Your line is open.

Michael A. Griffin
Analyst, Citigroup Global Markets, Inc.
Q

Yeah. Hey, thanks. Let me go back to the refinancing for a moment. Definitely debt maturities coming up. Is there any ability to get longer-term refinancing on some of these? Were the expectations more of a shorter-term floating rate [indiscernible] (00:21:07) kind of similar to the $400 million term loan.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

Yeah, I would – I mean, at the moment the CMBS market for single assets is not as compelling as the shorter-term market. So, you'll probably see us use the shorter-term market at the moment. As soon as that single-asset CMBS window reopens, which no dealer has been able to tell us exactly when it'll happen, but hopefully, it'll be by the first of the year. Then we'll start to avail ourselves of longer term fixed rate financing.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.
A

And just with regard to the $400 million corporate facility, remember we're trying to accomplish there, we are ultimately going to – we had to pay off maturing bonds $500 million, which we've done. And we were doing that in a way that can be repaid one year from now when we get money from our partners at One Madison, just short of $600 million. The bank financing market for that kind of term is well inside of what any bond execution will look like, probably 200 basis points inside. So, that's why we went that route.

Michael A. Griffin
Analyst, Citigroup Global Markets, Inc.
Q

Got it. That's definitely helpful. And then, we saw some details recently around Local Law 97 in New York. I understand things are still preliminary, but can you give a sense of how it could impact your portfolio? I mean, can you highlight any [indiscernible] (00:22:32) make sure your portfolio is going to be in compliance?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

This is Local Law 97?

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.
A

Yeah.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

Yeah. No, I mean, this is – the rules were formally adopted recently, but this is something we've been preparing for, for years and it's been out there. The first measurement date, we think, the bulk of the portfolio, if not all the portfolio, will pass in compliance without penalty. And then, in the 2030 date, we're going to be working obviously over the next seven, eight years on making additional investments and exploring ways to use renewable energies, and credits, and everything that'll be available to try and limit or eliminate entirely whatever penalties there will be in 2030.

We'll probably go into more detail on this in December at the Investor Conference to give people a better sense of where the issues lie, A range of quantifications. But we don't have that here now. And I would say that until 2030, at the earliest, we expect it to be of no financial consequence. Not because the rules are not rigorous, but simply because we've invested so much in the portfolio, and we have – so many of our buildings are LEED-designated, WELL-designated, ENERGY STAR recipients, et cetera, that we score very well on the current metrics.

Michael A. Griffin
Analyst, Citigroup Global Markets, Inc.
Q

So, this is evolving?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

Yeah, those rules will evolve over time. And we'll see what the state of play is in seven or eight years, but we're preparing as though what's been promulgated is what we'll have to live with.

Michael A. Griffin
Analyst, Citigroup Global Markets, Inc.
Q

Okay. That's it from me. Thanks for the time.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.
A

Thank you.

Operator: One moment for our next question. Your next question comes from Anthony Paolone with JPMorgan. Your line is open.

Anthony Paolone
Analyst, JPMorgan Securities LLC

Q

Yeah. Thank you. I guess, first question is for Marc. Can you talk about where you think the balance sheet leverage should be? Over time, you mentioned the priority of debt pay down. And so, just wondering how you're thinking about it and especially in the context of the asset-light strategy you guys have articulated.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah. Just on the issue of debt pay down, it's not so much a leverage ratio question in my mind. I think we are very fairly leveraged and maybe [indiscernible] (00:25:26) leveraged relative to what I think a loan to – a proper loan to value would be in this market. The debt reduction really is pointedly towards preserving and protecting our earnings from increasing rates and variable rate debt. So, it's – at a leverage point, we feel and have always felt very comfortable where we sit today with our leverage relative to an asset base that we think has a value far, far in excess of where the stock trades today, and even given where the stock trades today.

However, we have about, Matt, I want to say maybe $2 billion or so unhedged at this point. So, we're over 80% hedged at the moment, right. And so, therefore, what we're talking about is managing the risk, if you will, on that, whatever that is – 17%, 18% unhedged position, which I would like to reduce further. Again, not from a credit or balance sheet table, but purely from an earnings standpoint to protect ourselves from volatile increases in interest rates.

Anthony Paolone
Analyst, JPMorgan Securities LLC

Q

Okay. Got it. And then, just follow up, on the DPE book, a lot of it is set to mature next year. I mean, should we think about this as being the end? And also, did you anticipate just getting paid back on all this, I guess, outside of $625 million, perhaps; or do you think other properties might have to come onto the books?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

It's definitely not the end. This has been a very important program for us. It's returned us terrific IRRs over the course of the program. We tend to invest at the bottom of the cycle, so debt investments are most effective when we can make them in distress-type situations. And if we do see those type of situations, we will definitely be taking advantage of them in the debt book.

In terms of the maturities, they'll – time will tell what the refinancing markets look like, what the property markets look like. Sitting here today, we can't predict sort of what's going to happen in the future at existing loan maturities. But we were happy with the outcomes, obviously on 245 Park and 5 Times Square. And I definitely wouldn't call the book defunct by any stretch.

Anthony Paolone
Analyst, JPMorgan Securities LLC

Q

Okay. Thank you.

Operator: One moment before our next question. Our next question comes from John Kim with BMO. Your line is open.

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

Thank you. You guys talked about the improvement that you can make at 245 Park over the next couple of years, and the former owner was capital-constrained. So I was wondering if you can comment on how much CapEx will be needed to upgrade the building? And also, if you can comment on the timing of finding a joint venture partner.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

I would say, needed is – there's a lot you can work into what's needed at the property. I mean, the property leases in its current state. And we've done actually a lot of leasing. How much, Steve?

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Probably 200-plus thousand square feet.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah, we've done about 200,000 square feet plus. The building's a very good building, but – and I don't think needs were much. However, what – to bring it up to where we want it to be to its full potential and be consistent with some of the great properties within the portfolio that have extensive amenities, et cetera, we're going to go in sort of selectively and voluntarily, I would expect any program of size to be under $100 a foot. So, I don't mean that to sound de minimis. It's a big building. It's up to 1.8 million square foot building.

And that's the beauty of the situation here is we can amortize some substantial improvement dollars over a very large asset and for relatively, I'll call it, modest incremental investment per square foot, we can take our already low basis for a Park Avenue asset of, I think, about $1,100 a foot, if I'm not mistaken, maybe even slightly under that.

And like I said, make a very large dollar amount, but a small relative per square foot improvement amount for improvements, beautification, efficiencies, new lobby, plaza amenities and still have a basis very low by Park Avenue standards, and I think have one of the best buildings, with one of the best views sitting right on top of access to Grand Central Station. Thanks.

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

And the timing of a JV partner?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

I mean, we're looking. I mean, we'll begin those conversations in this quarter. And that's one of our priorities for – we'll be one of our priorities for 2023 – will be identification closing of a JV partner but we're – we, I guess, already have begun fielding inbound and will be sort of proactively marketing outbound this quarter.

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

Okay. My second question is...

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

It doesn't mean it's going to close this quarter, just means we're going to start the process this quarter. These processes generally could take anywhere from four to six months, I would say on balance.

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

Got it. On the Caesars joint venture, can you provide any more color on the structure of the JV? Is it just going to be you and Allianz on the real estate and Caesars as the operator, and that's completely separate or will it be co-ownership both?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

What is this...

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

And if you could also confirm that this is an exclusive to both you and Caesars for a New York casino license?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah. In terms of – maybe I'll sort of do a blanket statement for the many questions that may follow. Any details of the of the project, the bid, the structure, all that, is going to be something that we're going to address as other bidders will address over time and in response to an RFP that hasn't been issued yet. So, I want to put an emphasis on that there. There is no RFP from the state right now for a downstate casino license award that is anticipated to occur.

So, the answer to your second or third question was, yes, we are exclusive with Caesars on this casino site. And we're going to be putting, both of our mutual best efforts behind it to make it happen, because we think it's not just a big opportunity for the state and city, but it's almost a – it's a rallying point for Times Square to have a catalyst of something very positive, to help redirect some of the degradation we've seen in that area. And we know Times Square as best, there's nothing better in the world. It's the best entertainment district in the world, bar none.

But there are moments in time, particularly coming on the heels of this pandemic, where an area like Times Square – it's not the only area in New York city, but an area like Times Square needs help. And needs to reboot itself. And I think we can rally around the casino and make that the engine and economic engine around which we could really have a Times Square renaissance much in the way that you've seen a Grand Central renaissance over the past few years.

John P. Kim
Analyst, BMO Capital Markets Corp.

Q

Great. Thank you.

Operator: One moment for our next question. Our next question comes from Tom Catherwood with BTIG. Your line is open.

Thomas Catherwood
Analyst, BTIG LLC

Q

Thanks so much. Steve, let me turn over to One Madison. Obviously, two kind of anchor tenants in there at this point in time. Now that you've reached this kind of 55% plus level of pre-leasing, how does your marketing program shift at all? Do you become more selective with tenants? Are you able to start pushing rents at this point in time? Is there anything that changes once you reach this level?

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Yeah, we've already raised rents as a result of the leases that we've signed. But first and foremost, is to remind the brokerage community that we still have space. I think a lot of people are under the impression that we're fully leasing the building. So, we're out there reminding people that we've still got space to offer.

We're actively trading paper with a couple of tenants now in the tower of the building. And we're still seeing a pretty strong tour activity. You know, I think it's going to pick up even further towards the end of this year once we start to have the steel in place for the new tower and we can do site tours. Up until this point, all of our marketing has really been done out of our boardroom, off of renderings, and off of a presentation deck and really not with site visits.

And what we saw, One Madison – or One Vanderbilt Avenue is that once we could do site tours, the place just really exploded because people got so excited about the quality of the development, with the views [indiscernible] (00:36:00), with the volume of space really feels like, and it takes on a whole different character and pace to the leasing program. So, we top out steel in November of this year. And I think we'll be doing site tours towards the end of the year or early next year. And so, that's really where the thrust of our focus will be.

Thomas Catherwood
Analyst, BTIG LLC

Q

Got it. Appreciate that. And then, maybe Marc or Andrew, when you're thinking of sources and uses going forward, obviously, one of the big priorities has been repaying the unsecured bonds. You got that resolved. But the new projects obviously add more capital requirements, whether it's 450 Park, or 245 Park, or 5 Times Square. How do you think about allocating capital to those while at the same point in time kind of reducing your floating rate debt? What gets prioritized or kind of where do you hit a challenge in that capital allocation, if at all?

Andrew W. Mathias
President, SL Green Realty Corp.

A

So, I think the primary source of capital will be asset sales. And in terms of specifics, 5 Times Square will be zero incremental capital that, that deal was sort of fully funded at capitalization with new cash equity that will not come from our side of the ledger. It came from the other partners in the deal. So, there's zero incremental capital needs there. And then, as we've said, 245 Park, where we have this active search for a joint venture partner ongoing, and we'd expect the proceeds of that joint venture sale to cover most, if not all, of the capital required by that build.

Thomas Catherwood
Analyst, BTIG LLC

Q

Got it. Thanks to both.

Operator: One moment before our next question. Our next question comes from Michael Lewis with Truist. Your line is open.

Michael Lewis
Analyst, Truist Securities, Inc.

Q

Great. Thank you. I have a question about the term loan and the swaps,. And I'm wondering if there was any change in the amount or the composition of the banks that kind of came to the table to help you get that done. Because we've heard that some large lenders have pulled back on commercial real estate lending. So, I'm wondering not just about the pricing of that, but kind of the availability of capital in market.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

Yeah. Mike, it's Matt. No question, it's tough out there. A lot of banks are pulling back in various areas. So, to hit the mark with a facility like this is not without its challenges. But we went to very close relationship institutions who stepped into it. They are all participants in our existing credit facility. Some are participants in the One Madison financing. And given that this facility is pursuant to funds coming from One Madison, they have a great deal of certainty around the success of that project, and therefore, the funds coming in. But yeah, there's plenty of nos in this environment, just because capital allocation or restrictions are keeping a lot of banks handcuffed.

Michael Lewis
Analyst, Truist Securities, Inc.

Q

Okay. Thanks. And my second question, kind of piecing together, I guess, some of the other questions that were already asked. As you look at JV partners and maybe selling some assets. What's kind of the depth of that market, right? So, with interest rates up, leverage buyers under pressure, is there capital out there to get those deals done? And does the pricing take a significant hit or do you feel pretty good about what you'll be able to do those deals at?

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

Well, I mean, I think we feel good relative to the kind of product we're bringing to the JV market. It's still sort of irreplaceable Class-A often, trophy-like assets. And for that, I'd say, there's almost always demand in every market. That demand often shifts from, investor to investor or from country of origin to country of origin.

But I think that for the balance of 2022, you're not going to see – a lot of people are going to have more limited capacity. But in 2023, there, we believe, will be certainly new investment mandates to put money to work, but only in best markets, best properties, best sponsorship. I mean, it's like almost anything in a dislocated market or a challenged market because of what Mathias talked about on the debt front. Only the best deals are going to get done in the Grade A markets with very confident sponsorship. So, in that regard, we go into it very confidently that we've got the right product, the right returns for this market, the right valuation levels. The proof will be in the execution.

Andrew W. Mathias
President, SL Green Realty Corp.

A

In the case of 245, the right in place financing.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

Yeah, well, that said, it's a great point Andrew makes. It's a fully financed deal, so that certainly helps. But with or without it...

[indiscernible] (00:41:09) [audio gap] (00:41:10-00:41:26)

Andrew W. Mathias
President, SL Green Realty Corp.

A

That's it. It's taken off the table in 245 Parks.

Michael Lewis
Analyst, Truist Securities, Inc.

Q

It makes sense. Thank you.

Operator: One moment for the next question. Our next question comes from [ph] Daniel Tuccio (00:41:49) with Scotiabank. Your line is open.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Oh, hi. Nick Yulico here. So, it's a question on 245 Park. How are you guys – so, you talked about some of the capital plans. But how should we think about how you underwrote a stabilized yield on that building, post renovation?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Well, stabilize – what kind of yield cash on cost, unlevered IRR, levered IRR just what specifically?

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Yeah, cash on cost will be great.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Stabilized cash on cost, would have to – I think we've got – let me sort of go back to front. We've got levered returns on our basis that I think would exceed 50% based on where we can execute for a great HOP multi-office property right across from JPMorgan's new world headquarters. How does that translate...

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

SL Green, it's low-6s [indiscernible] (00:42:46).

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Okay. Great, thanks. And I guess just going back to the – in that case, you do have the in place there on the building, which is attractive, low 4%. Well, if you think about that building or another building in New York trading right now, you have to put a new acquisition debt on it. [indiscernible] (00:43:10) on that, even if you can get it's going to be somewhere over 6%. But then, how is that in your mind affecting values in the market? Because, I mean that starting cap rates for New York in that type of situation, if you have to finance it over 6%, starting cap rates have to be closer to 7% or higher.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

No. No chance. I mean, this – no different than you have inverted interest rates. You're going to have cap rates below financing rates because New York Class A [indiscernible] (00:43:45) office is not going to be a seven cap. You're looking – a cap rate is a perpetual in place expected rate of return over a spread to treasuries minus growth rate based on long-term treasuries. That has no – for me, you're talking about discount rates. There's no bearing to a cap – or New York City cap rates today I still think are, solidly, for the best assets in the 4s; maybe for a more mid-market product in the 5s. I haven't heard anything about 7s. And is that – do you have a transaction in mind that traded in Midtown to north of 7%?

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Well, no, that's I think part of the problem is that there aren't that many transactions. But everything we're hearing is that, you know, negative leverage is a problem, particularly for office if you're underwriting the market.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

No, negative leverage is a fact of New York City. Been doing this for 37 years. Negative leverage is often the case in New York City. It's called – often, in people...

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

[indiscernible] (00:44:50) vacancy, there's going to be negative lever.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Yeah, or even – people will generally be making long-term 10, 15-year investments, ideally. I mean, you'd love to be in a strong, positive leverage going on. I'm not arguing that. But it is not unusual in New York to buy negative leverage and work your way up on cash on cost to get to even a positive leverage to create – depends on the market, but high-single-digit IRRs. So, no, I wouldn't say it's – not for trophy, I mean, it's 400 million, 410 million square feet of assets in New York, not all the same. I'm just told – you said a building, yeah, like a 245, so I'm responding to that, a 7% plus cap rate would be, I think, empty set.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Okay. Even if someone could put that on that building today would have to replace that at well over 6%, even if you can get...

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

I don't know where debt would be. That's your debt. I don't know...

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Just spreads. I mean, spreads in the market.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

A

I hear you. But you know something? We just closed a corporate facility about how much? 140 over. Now, in your mind, maybe it's like 7% plus, but...

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

No, no, no. I understand you used a term loan, staying in the market to get properties.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Nick, please, you asked me a question. I'm going to give you my opinion, if you don't agree.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Okay. I just want to make sure I understand. So you still think cap rates in New York are more stabilized? That does not turn around asset or somewhere...

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

No, no, no, no, no. I'll be very specific, but then I'm going to move on to the next question.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Okay.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

I think stabilized cap rates – well, let's say, cap rates for assets like 245 as improved with us at the helm in this market across from JPMorgan's $5 billion to $6 billion investment, few blocks up the road from One Vanderbilt, down the street in 325 Park carries a sub-5% e cap rate and does not carry a 7.5% cap rate. That's it. No other words on that. That's my feeling on it. And if you disagree, you disagree, which is what makes a market. I have no problem with that. I'm just saying that's my opinion.

Nicholas Yulico
Analyst, Scotia Capital (USA), Inc.

Q

Okay. Thank you.

Operator: One moment for our next question. Our next question comes from Blaine Heck with Wells Fargo. Your line is open.

Blaine Heck
Analyst, Wells Fargo Securities LLC

Q

Thanks. Good afternoon. Marc, you talked a little bit about this in your prepared remarks. But now that we've moved past Labor Day, I'm curious what you guys are seeing in terms of tenant space usage or utilization, days in the office per week and maybe even times of day that are most active at the office?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah. I'd say that like many others are experiencing right now, there's two workweeks. There's the Tuesday, Wednesday, Thursday workweek, where I'd say we're almost back to close to pre-pandemic levels. This is how it feels like and the numbers are in excess of 60%. Pre-pandemic, our full occupancy might have been 70% or 70 some odd percent. We don't have exact numbers on [indiscernible] (00:48:07).

Certain buildings are higher than that where the tenant base is more back to work. Then we have certain tenants that may be more remote, so it fluctuates a bit, but I'm giving you the averages. And then Mondays and Fridays, particularly Fridays, you might see physical occupancy at, 30%. Now, all those numbers are increasing, and we see that in the numbers we're getting.

Fridays, we're often late, in New York City. So, we're not measuring against 100% on Fridays in New York City. I mean, people are out PTO, traveling, doing business, et cetera. So, it has the feel for three to almost four days a week like a pre-pandemic market. And I come off the train the other day. I mean, that train is full. That platform is full. You can't – the time it took to get out the doors into the main theater at Grand Central was measured in minutes – many minutes not seconds because the platform is packed. And it has a very good feel right now in my opinion. I don't know, anybody Steve.

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Well, I'll add to it. I mean just statistically Metro-North ridership is, if I remember the stat correctly, is like 9% greater than it was pre-pandemic. Car traffic is 5.5% or 6% greater than it was pre-pandemic. We're still less than COVID numbers. There's a lot on railroad and still at a lower number. But to Marc's earlier point, the trend line is such that ridership, and people coming back in the city and people occupying the offices is on the upward slope, and we're seeing that consistently improve week-over-week.

Blaine Heck
Analyst, Wells Fargo Securities LLC

Q

Thanks, guys. That's helpful. Second question, it seems as though the highest quality and highest rent price points were certainly the most active during the pandemic, and I assume that can't last forever. So, I'm wondering how the pace of leasing activity has trended in some of your lower-rent buildings. Are you guys seeing much of a pickup in activity there relative to kind of what you saw during the pandemic?

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.
A

Well, as I said earlier, we're seeing more tours, and proposals, and lease sightings in our in our sort of mid-price point buildings, which I think are largely dominated by the smaller to mid-size tenants. That's not yet translated into enough signed leases to really move the needle. But just off of a tour activity and expressions of interest, it's improved. It's still a struggle because those small and medium sized guys are late to the game.

Blaine Heck
Analyst, Wells Fargo Securities LLC
Q

Great . Thanks, Steve.

Operator: One moment for our next question. Our next question comes from Tayo Okusanya with Credit Suisse. Your line is open.

Tayo Okusanya
Analyst, Credit Suisse Securities (USA) LLC
Q

Yes, good afternoon. Two quick ones for me. First of all, in regards to the swaps and earlier comments about, again, just having more hedging going forward, I mean, could you just talk to just how much you kind of ultimately expect to be hedged by, given you have about $3 billion of kind of variable debt between the consolidated and unconsolidated JVs?

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.
A

Yeah. So, let's talk those numbers first here. We had about $2.4 billion unhedged floating on just short of $12 billion of debt. Our target floating rate ratio is kind of 15% to 20%. So, we're already at or below that number, but we're going to target all of our existing floating rate debt, as much of it as we possibly can, because we don't unilaterally control some of it to hedge. So, we just – beyond the end of the quarter, we did another $200 million swap offloading to fixed yesterday.

We're zoned in on another almost $400 million of property level floating rate debt, and then there will be debt pay down. We want to look at the credit facility – our revolving credit facility. And our goal is always have that near zero. So, with proceeds from asset sales or other activity, we'll try and get that down to zero. That's also floating rate debt. So, it's a combination of caps, swaps and debt repayment, as Marc said in his opening comments. And we are – even though we are at or below our target, we're going for more because we want to protect earnings and cash flow.

Tayo Okusanya
Analyst, Credit Suisse Securities (USA) LLC
Q

Got it. Because that's helpful. And then 717 Fifth Avenue and 650 Fifth Avenue with the debt maturities there and the ongoing kind of conversations with the lenders. I mean, what's kind of the ultimate kind of goal there with those two assets?

Andrew W. Mathias
President, SL Green Realty Corp.

A

Well, we're not managing partner at 717 and we have very small [indiscernible] (00:53:33) there. So I think the hope is to get an extension from the existing lender group. And I would say 1552 is much the same. Times Square retail has obviously been heavily impacted by the pandemic. And we expect the lender to be appreciative of those impacts.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

And you mentioned 650 Fifth, we did a short-term extension.

Tayo Okusanya
Analyst, Credit Suisse Securities (USA) LLC

Q

Right. But after the six-month extension that expires like in April or so next year right. So I think longer term, is the idea [indiscernible] (00:54:07)?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Yeah. Part of the exercise, part of the exercise with the extensions is evaluating the financing market at the time. So we felt with the lender, the best thing to do at this point was extended six months. And in six months we'll consider it again and maybe do another six months, another 12 months until we get to a more comfortable position right. And if the markets are cooperative, we'll do something longer term.

Tayo Okusanya
Analyst, Credit Suisse Securities (USA) LLC

Q

Got you. Thank you.

Operator: One more before our next question. [Operator Instructions] Our next question comes from Anthony Powell, Barclays. Your line is open.

Anthony F. Powell
Analyst, Barclays Capital, Inc.

Q

Hi. Good afternoon. Marc, I think you mentioned the prospect of office to residential conversions. Have you talked in, any context, with people at the mayor and the governor? Are there plans in place to maybe just systematically reduce some of the office, I guess, availability of their up stock in New York [indiscernible] (00:54:58)? Could something be announced in next few quarters?

I'm curious because I think this issue of maybe obsolescence [indiscernible] (00:55:04) something that comes up a lot in our conversations. So if the plan's in a way to kind of get that started, that would be super helpful. So, what's your view on that prospect for the next few quarters?

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

So, just so I understand the question, the question is, what do I think is the real timeline or prospect of getting something accomplished at state and city level? Is that...

Anthony F. Powell
Analyst, Barclays Capital, Inc.

Q

Yeah. And certainly just a broad office to residential or office conversion program.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

Okay. I think the best – this is one of the topics that we're going to be featuring in about six weeks at the investor conference, stepping through what it takes to get a building from office to resi, from a physical standpoint, from a zoning standpoint, from building code standpoint. It's very doable. We've done it. Many have done it.

There are ways to make it easier, better, more efficient to turn right now with a very small pipeline of office to resi into a much larger pipeline of office to resi. Obviously, one of those big elements, would be a tax break along the line of what 421-g was Downtown, when Downtown had substantial problems after 9/11. And that in and of itself is being looked at, but it's being looked at in coordination with the kind of changes that I mentioned.

Some of which will take time to implement. So I think that a program can come about in 2023 in terms of directional but in terms of actually seeing buildings converted, I would guess that's 2024 and beyond. But I do think that you could see upwards of 10 million square feet off of office sort of taken out of the equation for conversion, pursuant to a new program if the economics and the zoning are there to make it happen. So it's a much longer discussion – it's a detailed discussion that, Anthony, if you don't mind, I want to defer until our investor conference when we're going to be speaking to that directly.

Anthony F. Powell
Analyst, Barclays Capital, Inc.

Q

All right. Great. Thank you.

Operator: One moment for next question. Our next question comes from Ronald Kamdem with Morgan Stanley. Your line is open.

Ronald Kamdem
Analyst, Morgan Stanley & Co. LLC

Q

Hey. Great. Two quick ones for me. Just when you're thinking about those 2023 lease roll, at this point, any commentary on how much is rolled, how much is left to do? What that's shaking out?

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

Well, we're as you can imagine, we've been, for the better part of this year, working on the 2023 expirations already. So we have very good clarity of every single tenant as to who's likely to stay or not. We're actually going through our budgets, building our budgets for next year. So, we have a granular tenant-by-tenant assumption for everybody that's rolling in each piece of vacancy that we have today. And I don't think there's any surprises, as we sit here today, as to where we thought which tenants were going to stay or go compared to where we saw those – how we saw those tenants probably 12 months ago.

Ronald Kamdem
Analyst, Morgan Stanley & Co. LLC

Q

And any chance – any way to quantify that? Is it 20%, 10%. Any sort of high-level numbers or....

Steven M. Durels
Executive Vice President & Director-Leasing and Real Property, SL Green Realty Corp.

A

I don't have it at my fingertips, so that'd be pure speculation. It's something that I think we'll have -when we're done with our budgets over the next week or two, we'll have a very good ability to communicate that. And maybe perhaps that's something we would talk about at investor conference as well.

Ronald Kamdem
Analyst, Morgan Stanley & Co. LLC

Q

Sure. [indiscernible] (00:59:28). So, my second question was just on asset sales. I think you talked about historically about sort of JV-ing One Vanderbilt. Maybe can you talk about how that's going, and are there other assets beyond that, that you're contemplating as well in the portfolio?

Andrew W. Mathias
President, SL Green Realty Corp.

A

Well, we are marketing some assets for sale. We have other assets we're evaluating for sale and the One Vanderbilt JV process is still sort of in discussions. So, we're active on the disposition front. We're going to use those proceeds to retire debt and to fund some of the capital needs of some of the projects. And there's still an active market out there, as we showed with Memorial Sloan Kettering. And there's a bunch of other trades that have happened in the market.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

A

I think on balance, we feel pretty good in our ability to execute, which is why we're basing our plan on redeployment of those proceeds. If we feel good about those executions, then, you know, we have a different plan. But working hard and trying to convert. And we got a lot done this year, I referenced, 44 sale transactions either entire or partial interest, several of which were this year and more of which will be in the next few quarters.

Ronald Kamdem
Analyst, Morgan Stanley & Co. LLC

Q

Thank you.

Operator: And I'm not showing any further question at this time. Like to turn the call back to management for any closing remarks.

Marc Holliday
Chairman & Chief Executive Officer, SL Green Realty Corp.

No, let's that it. Thanks for everybody that's left on the phone, appreciate you hanging in there for the duration. And we will see, I hope, many, or most or all of you on December 7.

Matthew J. DiLiberto
Chief Financial Officer, SL Green Realty Corp.

5th.

Marc Holliday

Chairman & Chief Executive Officer, SL Green Realty Corp.

5th. I'm sorry about that. On December 5th, Monday. See you then.

Operator: Ladies and gentlemen, this does conclude today's presentation. You may now disconnect and have a wonderful day.