



October 16, 2015

## **Fitch Affirms SL Green's IDR at 'BBB-'; Outlook Stable**

NEW YORK--(BUSINESS WIRE)-- Fitch Ratings has affirmed the Issuer Default Rating (IDR) for SL Green Realty Corp. (NYSE: SLG) and its subsidiaries SL Green Operating Partnership, L.P., and Reckson Operating Partnership L.P. at 'BBB-'. The Rating Outlook is Stable. A full list of rating actions follows at the end of the release.

### **KEY RATING DRIVERS**

The affirmation of the ratings and Outlook reflects SLG's credit strengths, including its high-quality New York office portfolio, manageable lease maturity and debt expiration schedules and growing unencumbered asset pool. These positive elements are balanced by relatively weak unencumbered asset coverage of unsecured debt, concerns regarding the midtown Manhattan office leasing environment, which remains somewhat dependent on the growth of large financial institutions and supporting industries such as law and accounting firms, as well as the continuing lag in the suburban office portfolio.

### **APPROPRIATE LEVERAGE**

SLG's leverage ratio is consistent with a 'BBB-' rating for a REIT owning primarily Midtown Manhattan office assets, as the company's leverage ratio (excluding the effects of consolidating 388-390 Greenwich Street) was 7.4x as of June 30, 2015, down from 7.6x as of Dec. 31, 2014 and level with 7.4x as of Dec. 31, 2013. Leverage has been aided by the incremental NOI from repositioning and leasing of assets within the company's growth portfolio, which consists of value-add properties purchased over the past few years. Fitch expects that leverage will temporarily increase from historical levels due to the recent acquisition of 11 Madison Avenue, the purchase of which will be largely funded with proceeds from asset sales. Fitch expects leverage will decline modestly post-dispositions to the mid-7.0x's (inclusive of 388-390 Greenwich Street) due to incremental NOI from the Company's redevelopment/growth portfolio. Fitch defines leverage as net debt divided by recurring operating EBITDA, including Fitch's estimate of recurring cash distributions from joint ventures.

### **EXCLUSION OF 388-390 GREENWICH FROM LEVERAGE RATIOS**

The rationale for excluding the consolidating effects of this asset is due to Citibank having the option to acquire this property from SLG as early as December 2017. It is Fitch's expectation that it will exercise this option, and thus the leverage impact for this property is relatively short-term.

### **APPROPRIATE FIXED-CHARGE COVERAGE**

SLG's fixed-charge coverage ratio was 2.1x for the 12 months ended June 30, 2015, up from 1.9x in 2014 and level with 2.1x in 2013. The improvement in coverage has been driven by the reduction in free rent periods offered to tenants, combined with slightly lower leverage and improved funding costs, particularly with the company's unsecured credit facility. Fitch expects coverage to remain relatively flat as growth in cash flow is partially offset by an environment in which landlords will continue to offer attractive tenant improvement packages. Fixed-charge coverage is defined as recurring operating EBITDA - including Fitch's estimate of recurring cash distributions from joint ventures - less recurring capital expenditures and straight-line rents, divided by interest incurred and preferred stock distributions.

### **LOW UNENCUMBERED ASSET COVERAGE OF DEBT**

The ratings are hindered by SLG's unencumbered asset value coverage of unsecured debt (UA/UD). Consolidated unencumbered asset coverage of net unsecured debt (calculated as annualized 2Q 2015 unencumbered property net operating income divided by a stressed 7% capitalization rate) results in coverage of 1.6x, down from 2.1x as of year-end 2012. This ratio is weaker when compared to similarly-rated companies, particularly given that the stressed capitalization rate applied to SLG's NOI is the lowest across Fitch's rated universe. However, when considering that Midtown Manhattan assets are highly sought after by secured lenders and foreign investors, the results are a stronger contingent liquidity relative to most asset classes in other markets. Fitch expects this ratio will improve modestly as the company unencumbers additional assets with relatively high debt yields; however, should this ratio sustain below 2.0x, this could have a negative impact on SLG's rating or outlook.

### **STRONG MANAGEMENT TEAM**

The ratings also consider the strength of SLG's management team given their knowledge of the Manhattan office sector and their ability to maintain occupancy and liquidity throughout the downturn. This expertise has also been demonstrated by the company's ability to identify off-market acquisition opportunities, and its maintenance and growth of portfolio occupancy and balance sheet liquidity throughout the downturn and into the current cycle. The management team has also led the company towards an even greater property focus within Manhattan, not only within the office segment, but expanding to the potentially highly profitable retail segment as well.

#### MIDTOWN LEASING CONCERNS

Offsetting these strengths are Fitch's concerns regarding the uncertain Midtown Manhattan leasing environment. While the New York City leasing environment has strengthened over the last few years and net effective rents are higher, the company continues to incur significant costs in the form of tenant improvements, leasing commissions and free rent incentives as tenant inducements, which has placed pressure on the company's fixed charge coverage. A downturn in space demands from the financial services industry, which accounts for 33% of SLG's share of base rental revenue, may result in reduced cash flows or values of SLG's properties. Further, emerging competitive pressure from the Hudson Yards development and newer and redeveloped downtown assets (i.e., Brookfield Place and World Financial Center assets) could result in larger tenants vacating Midtown. Despite these headwinds, SLG has maintained strong leasing volume and has improved occupancy.

#### LOW LIQUIDITY COVERAGE

SLG has weak liquidity. For the period from July 1, 2015 to Dec. 31, 2016, the company's sources of liquidity (cash, availability under the company's unsecured revolving credit facility, and Fitch's expectation of retained cash flows from operating activities after dividends and distributions) covered uses of liquidity (pro rata debt maturities, Fitch's expectation of recurring capital expenditures and non-discretionary development expenditures) by 0.9x. This stressed analysis assumes that no additional capital is raised to repay obligations; SLG has demonstrated good access to a variety of capital sources over time, mitigating refinance risk. Under a scenario where the company refinances 80% of maturing secured debt, liquidity coverage improves to 1.3x, which would be adequate for the rating.

SLG's liquidity is strengthened by its conservative common dividend policy, which enables it to retain substantial operating cash flow. Fitch expects the company's projected AFFO payout ratio to center around 45%, which is low relative to the broader equity REIT universe. The lower payout ratio should provide the company with additional financial flexibility, which is of high importance given it will need to fund significant capital costs related to recently-signed renewal leases for Viacom and Citibank, and projected growth redevelopment portfolio costs prior to year-end 2016.

#### ONE VANDERBILT DEVELOPMENT SPEND LOOMING

SLG has obtained the approvals necessary to commence its ground-up development project at One Vanderbilt Avenue, and it has commenced demolition for the project. The total cost and the company's equity funding commitment for the project remain uncertain, and the company has stated it may consider joint venture alternatives to reduce its exposure. The degree and timing of the company's ultimate funding requirements could have a meaningful negative impact on the company's liquidity and headline credit metrics.

#### STRONG, ALBEIT RELATIVELY CONCENTRATED TENANT BASE

SLG's portfolio has a modest degree of tenant concentration, with the top 10 tenants representing 33.4% of annual base rent. This compares to the contribution from the top 20 tenants of Boston Properties and Vornado Realty of 30% and 27.8%, respectively. Despite the concentration, the largest tenant Citigroup, Inc. ('A' IDR with a Stable Outlook by Fitch) comprises 10.5% of SLG's share of annual cash rent, and all three of SLG's Fitch-rated top 10 tenants have strong investment grade ratings.

#### MANAGEABLE LEASE EXPIRATION PROFILE

SLG has a manageable lease expiration schedule with only an average of 5.2% of consolidated Manhattan rents expiring annually through 2019. While an average of 10.2% of the company's consolidated suburban property rents expire during that same period, the suburban portfolio represents a limited portion of the company's total assets and only 9.2% of annualized cash rent.

#### LADDERED DEBT MATURITIES

Further supporting the ratings is SLG's manageable debt maturity schedule. Over the next five years, 2017 is the largest year of debt maturities with 17.5% of pro rata debt expiring, with no other year greater than 10.4%. The 2017 maturities are primarily comprised of \$1.4 billion of non-recourse mortgage debt and \$355 million of unsecured debt. Additionally, SLG's ratios under its unsecured credit obligations' financial covenants do not hinder the company's financial flexibility at this point in time.

## RECKSON'S IDR LINKED TO SLG'S

Consistent with Fitch's criteria, 'Parent and Subsidiary Rating Linkage' dated May 23, 2015 and available on [www.fitchratings.com](http://www.fitchratings.com), Reckson's IDR is linked and synchronized with SLG's due to strong legal, operational and strategic ties between SLG and Reckson, including each entity guaranteeing certain corporate debt of the other.

## JUNIOR SUBORDINATED NOTES NOTCHING

The one-notch differential between SLG's IDR and junior subordinated notes (trust preferred securities) is consistent with Fitch's criteria for corporate entities with an IDR of 'BBB-'. Based on Fitch Research on 'Treatment and Notching of Hybrids in Nonfinancial Corporate and

REIT Credit Analysis', available on Fitch's Web site at [www.fitchratings.com](http://www.fitchratings.com), these securities are senior to SLG's perpetual preferred stock but subordinate to SLG's corporate debt. Holders of such notes have the ability to demand full repayment of principal and interest in the event of unpaid interest.

## PREFERRED STOCK NOTCHING

The two-notch differential between SLG's IDR and preferred stock rating is consistent with Fitch's criteria for corporate entities with an IDR of 'BBB-'. Based on Fitch Research on 'Treatment and Notching of Hybrids in Nonfinancial Corporate and REIT Credit Analysis', available on Fitch's Web site at [www.fitchratings.com](http://www.fitchratings.com), these preferred securities are deeply subordinated and have loss absorption elements that would likely result in poor recoveries in the event of a corporate default.

## STABLE OUTLOOK

The Stable Outlook reflects Fitch's expectation that SLG will maintain a strategy and leverage and coverage metrics consistent with the rating. While these quantitative metrics are nominally weaker than most REIT issuers with investment-grade ratings, the Outlook considers that Midtown Manhattan office assets consistently trade at lower capitalization rates and are more liquid and financeable in economic downturns than typical office assets, bolstering the contingent liquidity of the company's portfolio.

## KEY ASSUMPTIONS

Fitch's key assumptions within the rating case for SLG include:

--Annual same-store NOI increases of between 1.0% - 3.0% for 2015-2017;

--The \$2.4 billion acquisition of 11 Madison Avenue is financed by \$1.4 billion in secured debt with the remainder financed via proceeds from asset dispositions;

--\$400 million of additional acquisitions in 2015 (not including 11 Madison Ave.) at a 4% capitalization rate;

--\$475 million of asset sales in 2016 (not including sales related to 11 Madison Ave.) at a 5% capitalization rate;

--Projected annual recurring capital expenditures of \$140 million for the remainder of 2015, \$175 million for 2016, and \$165 million for 2017;

--2015-2017 secured maturities are refinanced dollar-for-dollar;

--Annual unsecured bond issuances between \$250 - 350 million at yields between 4.5% - 5.0% during 2015-2017;

--Common equity issuances of \$285 million in 2015 and \$178 million in 2017 via the company's ATM/DRIP programs, though Fitch notes issuance is at management's discretion and the common shares are currently trading at a 12% discount to consensus mean net asset value according to SNL Financial LC.

## RATING SENSITIVITIES

The following factors may have a positive impact on SLG's ratings and/or Outlook:

--Fitch's expectation of leverage sustaining below 7x (leverage was 7.9x for TTM ended June 30, 2015 and 7.4x excluding the effects of 388-390 Greenwich Street);

--Fitch's expectation of fixed-charge coverage sustaining above 2.25x (coverage was 2.1x for TTM ended June 30, 2015);

--Growth in the size of the unencumbered pool.

The following factors may have a negative impact on SLG's ratings and/or Outlook:

--Fitch's expectation of UA/UD sustaining below 2.0x;

--Fitch's expectation of leverage sustaining above 8x;

--Fitch's expectation of fixed-charge coverage sustaining below 1.5x;

--A sustained liquidity shortfall (base case liquidity coverage was 0.9x for the period July 1, 2015 to Dec. 31, 2016).

#### FULL LIST OF RATING ACTIONS

Fitch has affirmed the following ratings:

SL Green Realty Corp.:

--IDR at 'BBB-';

--Senior unsecured notes at 'BBB-';

--Perpetual preferred stock at 'BB'.

SL Green Operating Partnership, L.P.

--IDR at 'BBB-';

--Unsecured line of credit at 'BBB-';

--Senior unsecured notes at 'BBB-';

--Exchangeable senior notes at 'BBB-';

--Junior subordinated notes at 'BB+'.

Reckson Operating Partnership, L.P.

--IDR at 'BBB-';

--Senior unsecured notes at 'BBB-'.

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

#### Applicable Criteria

Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage (pub. 17 Aug 2015)

[https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=869362](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869362)

Recovery Ratings and Notching Criteria for Equity REITs (pub. 18 Nov 2014)

[https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=813628](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=813628)

Treatment and Notching of Hybrids in Non-Financial Corporate and REIT Credit Analysis (pub. 25 Nov 2014)

[https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=821568](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=821568)

## Additional Disclosures

### Dodd-Frank Rating Information Disclosure Form

[https://www.fitchratings.com/creditdesk/press\\_releases/content/ridf\\_frame.cfm?pr\\_id=992439](https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=992439)

### Solicitation Status

[https://www.fitchratings.com/gws/en/disclosure/solicitation?pr\\_id=992439](https://www.fitchratings.com/gws/en/disclosure/solicitation?pr_id=992439)

### Endorsement Policy

<https://www.fitchratings.com/jsp/creditdesk/PolicyRegulation.faces?context=2&detail=31>

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK:

[HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE '[WWW.FITCHRATINGS.COM](http://WWW.FITCHRATINGS.COM)'. PUBLISHED RATINGS, CRITERIA AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE 'CODE OF CONDUCT' SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

View source version on [businesswire.com](http://www.businesswire.com): <http://www.businesswire.com/news/home/20151016005816/en/>

#### Fitch Ratings

##### Primary Analyst

Stephen Boyd, CFA

Director

+1-212-908-9153

Fitch Ratings, Inc.

33 Whitehall Street

New York, NY 10004

or

##### Secondary Analyst

Steven Marks

Managing Director

+1-212-908-9161

or

##### Committee Chairperson

Monica Aggarwal

Managing Director

+1-212-908-0282

or

##### Media Relations:

Sandro Scenga, New York, +1 212-908-0278

Email: [sandro.scenga@fitchratings.com](mailto:sandro.scenga@fitchratings.com)

Source: Fitch Ratings

News Provided by Acquire Media