FITCH AFFIRMS PECONIC LANDING AT SOUTHOLD, INC. (NY) REVS AT 'BBB-'; OUTLOOK STABLE

Fitch Ratings-New York-05 November 2015: Fitch Ratings has affirmed the 'BBB-' rating on the following bonds issued on behalf of Peconic Landing at Southold, Inc. (Peconic):

--$20,415,000 Southold Local Development Corporation revenue bonds, series 2015 (Peconic Landing At Southold, Inc. Project);
--$28,825,000 Suffolk County Economic Development Corporation revenue refunding bonds series 2010 (Peconic Landing at Southold, Inc. project).

The Rating Outlook is Stable.

SECURITY
Gross revenue pledge, mortgage interest on the land and all buildings except the ILU/Co-op units and a debt service reserve fund.

KEY RATING DRIVERS
PROJECT PROGRESSING: Peconic is in the midst of an expansion project that is adding 46 new independent living (IL) apartments, 16 memory care units, and 16 skilled nursing beds. The project, funded by a 2015 debt issuance and $5 million in equity, is slightly behind schedule due to the harsh 2015 winter but is currently tracking under-budget. The delay is not a concern and the new target date for opening is May 2016. Peconic reports strong pre-sales with all of the 46 new IL apartments reserved with a 10% deposit.

CONSISTENT OPERATING PERFORMANCE: Over the last four audited years, Peconic's financial profile has been consistent, with many of its financial ratios comparing well to Fitch's 'BBB' category medians. In particular, its operating ratio has averaged 92.2%, relative to a median of 96.1%, a strong figure for a Type 'A' facility.

SOLID HISTORICAL DEBT COVERAGE: With the issuance of the series 2015 bonds, Peconic's maximum annual debt service (MADS) increased to $3.6 million from $2.1 million. However, Peconic will not be tested on the higher MADS until it reaches stabilized occupancy, which is expected in 2017. Thus, debt service coverage on actual debt service of $2.1 million was a solid 2.6x in 2014 and 1.8x in the nine-month 2015 interim period. Fitch expects the additional revenue from new units to raise Peconic's coverage closer to the 2x median once stabilization is reached.

HIGH IL OCCUPANCY: IL occupancy has averaged 95% over the last four audited years. The high occupancy has kept operations steady and shows evidence of good demand for services as Peconic looks to fill its expansion project in the second half of 2016.

ADDITIONAL CREDIT STRENGTHS: Peconic has limited competition in a very good service area, and benefits from a large and attractive campus, which includes a private beach, located on the North Fork of eastern Long Island.

RATING SENSITIVITIES
PROJECT COMPLETION AND FILL: Peconic Landing at Southold, Inc. (Peconic) is drawing down a $16.5 million bank construction loan to help fund the project construction, with repayment dates in December 2016 and December 2017. The loan will remain a credit concern until it is paid

off. Mitigating some of this concern are the strong pre-sales and Peconic's good liquidity relative to the loan amount, which would enable Peconic to endure a longer period of fill-up, if necessary.

LONGER-TERM OUTLOOK: Should fill-up on the new units progress as planned, the added revenues, coupled with Peconic's already solid balance sheet and consistent operating profile, could lead to positive rating pressure.

CREDIT PROFILE
Peconic is located on the North Fork of Long Island and consists of 109 single-story cottages, 141 apartments, 26 enriched housing units (assisted living units), and 44 skilled nursing beds. In 2014, Peconic had total operating revenues of $24.4 million.

Stable Financial Profile
Peconic finished 2014 with a 90.6% operating ratio and a 13% net operating margin - adjusted (NOMA). The operating ratio was better than Fitch's 'BBB' median, but the NOMA trailed the 'BBB' median of 20.5%. The 13% NOMA is in line with historical performance and the below-median NOMA reflects Peconic's refundable contract, including the appreciation on the value of the resold units.

Nine-month 2015 results show the operating ratio remaining good at 97.6% and NOMA at 12.5%. Operating revenues were off budget slightly due to the impact of the 'two midnight' rule, which affected the inpatient status of hospital referrals discharged to Peconic's health center. This rule led to an increase in the number of observation patients at area hospitals, and those observation patients are ineligible for Medicare reimbursed rehabilitation, when discharged to a skilled nursing center.

Early in 2015, Peconic had a number of its own residents who were in hospitals, classified as for observation and discharged to Peconic. As a result, Peconic was able to collect only the monthly Type 'A' service fees, which are much lower than the daily Medicare reimbursement rates. This differential had a negative impact on skilled nursing revenues, although it was offset by an increase in private-pay patients. Peconic worked to educate area hospitals on this issue and reports better results in the second half of the year in health center revenues.

Peconic had an unusually high level of IL turnover this year, but has been able to refill units. Peconic was budgeting for 20 to 25 sales in 2015 and is projecting closer to 35. Overall, occupancy across all levels of care continues to be strong. At Sept. 30, 2015, IL, assisted living unit (ALU), and skilled nursing (SNF) occupancies were 94%, 89%, and 97%, respectively.

Peconic's liquidity metrics weakened with the debt issuance, but remain solid for the rating level. At Sept. 30, 2015, Peconic had $28 million in unrestricted cash and investments which equated to 466 days cash on hand, a cushion ratio of 7.7x, and 58.8% cash-to-debt, all of which are near or above their respective 'BBB' medians.

Capital Project Update
Peconic is in the middle of a major repositioning and expansion project to renovate and expand its health center, build a new 16-unit memory care area, and add 46 new IL apartments. The project was delayed slightly due to bad weather in the 2015 winter but is moving forward, and Fitch does not view the delay as a credit concern.

The project is expected to cost $43 million and is being funded by a $19.5 million in fixed-rate debt (issued in 2015), a $16.5 million short-term bank construction loan, which has been almost fully drawn, and $7 million of equity and philanthropy. Peconic has already contributed its share of the equity and raised approximately $4.3 million in philanthropic contributions to date.

Fitch continues to view the project positively believing the long-term strategic and revenue gains will outweigh the near-term construction risk and additional debt. The new memory care units will add a much needed service to the campus and the additional skilled nursing beds and renovated health center will advance an already strong service line at Peconic.

Fitch has noted in previous press releases that Peconic is unusual in the number of cottages it has relative to apartment units. The additional 46 units will bring the number of apartments up to 187, which provides a better balance with its 109 cottages. Peconic is also exploring adding a Type 'C' contract, which would help market the cottages, which generally attract younger residents who are better suited for the Type 'C' contract.

Fitch also notes as a credit positive that 46 of the 46 new IL units have a 10% deposit. Over the last year, approximately 14 of the depositors dropped from the list as they moved into other available units at Peconic; however, Peconic was able to refill their spaces on the list. In addition, the waitlist for Peconic's current IL apartments remains strong at 120.

Debt Structure/Debt Burden
All of Peconic's long-term debt is fixed. The short-term construction loan, which is with Citizen's Bank, is floating rate, and if fill-up occurs on schedule, will be fully paid down by 2017. The operating covenants provided to the bank are not materially different from the covenants provided to the series 2015 bondholders. In addition, Peconic has a strong liquidity position relative to the debt it needs to pay down.

Debt metrics, which assume the paydown of the construction loan, show Peconic's debt levels as elevated. At Sept. 30, 2015, MADS as a percent of revenue of 15.4% and debt-to-net available of 9.3x were above the category medians of 12.4% and 12.9x. However, Fitch expects these figures to moderate as the debt amortizes and the projects are finished and come online, which will provide additional revenue and operating income.

Disclosure
Peconic covenants to provide to the Municipal Securities Rulemaking Board's Electronic Municipal Market Access System (EMMA) audited financial statements within 120 days after the end of each fiscal year and quarterly financials within 45 days after the end of each quarter.

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Applicable Criteria
Not-for-Profit Continuing Care Retirement Communities Rating Criteria (pub. 04 Aug 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=868824
Revenue-Supported Rating Criteria (pub. 16 Jun 2014)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=750012