RATING ACTION COMMENTARY

Fitch Assigns 'BBB-' IDR to Peconic Landing at Southold (NY); Affirms Revs; Outlook Stable

Tue 19 Oct, 2021 - 2:52 PM ET

Fitch Ratings - New York - 19 Oct 2021: Fitch Ratings has assigned a 'BBB-' Issuer Default Rating (IDR) to Peconic Landing at Southold, Inc. (Peconic Landing) and affirmed the 'BBB-' revenue rating on approximately $43 million in bonds issued by the Suffolk County Economic Development Corporation and the Southold Local Development Corporation on behalf of Peconic Landing. The Rating Outlook is Stable.

SECURITY

The bonds are secured by a gross revenue pledge, mortgage interest on the land and all buildings, except the ILU/Co-op units, and a debt service reserve fund.

ANALYTICAL CONCLUSION

The 'BBB-' rating reflects the expected resilience of Peconic Landing's financial profile through Fitch's forward-looking scenario analysis, within the context of the strength of its business profile, characterized by strong revenue defensibility, as a life plan community (LPC) provider, with an attractive location and limited local competition, and midrange operating risk, with good operating ratios (below 100%) for a largely Type 'A' LPC.
Peconic Landing's underlying operating performance has remained steady through the coronavirus pandemic, helped by independent living (IL) occupancy, which has remained above 90% through June 2021. However, thinner net entrance fee receipts related to the timing of sales and move ins caused by pandemic-related disruptions have led to weaker net operating margins - adjusted (NOMAs), softer maximum annual debt service coverage (MADS), and a decrease in unrestricted cash and investments. Peconic Landing's refundable contract (net of certain fees), which includes passing on a unit's appreciated resale value as part of the refunded portion of the entrance fee, has also contributed to the decline.

Fitch views this stress as near term, given the continued demand for services at Peconic Landing and the steady underlying operating performance and as further indicated by revenue-only coverage that has remained above 1x. Fitch's forward look shows net entrance fee receipts stabilizing to historical levels over the next few years, and with no major capital projects underway or expected, Peconic Landing's financial profile steadily improves through Fitch's moderate stress scenario, remaining consistent with the current rating level throughout.

**KEY RATING DRIVERS**

**Revenue Defensibility: 'a'**

Favorable Location and Limited Competition Support Strong Census

The strong revenue defensibility reflects IL occupancy above 90%, Peconic Landing's large and attractive campus on the North Fork of eastern Long Island, limited competition across the region, and solid local area demographics.

**Operating Risk: 'bbb'**

Steady Underlying Operations; Manageable Capital Needs

The midrange operating risk assessment reflects operating ratios below 100%, revenue only coverage consistently over 1x and ongoing investment in its plant.

**Financial Profile: 'bbb'**

Financial Profile Stable Through a Moderate Stress Scenario

At YE 2020, Peconic Landing had unrestricted cash-to-adjusted debt of about 60.6% and maximum annual debt service (MADS) coverage of 1.3x (as calculated by Fitch). Given
Peconic Landing’s strong revenue defensibility and midrange operating risk assessments and Fitch’s forward-looking scenario analysis, Fitch expects Peconic Landing’s key leverage and coverage metrics to remain consistent with current rating level through a moderate stress.

**Asymmetric Additional Risk Considerations**

No asymmetric risks were factored into the rating assessment.

**RATING SENSITIVITIES**

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Growth in unrestricted liquidity such that cash to adjusted debt stabilizes closer to 90%;

--Strengthening of the operating performance such that the operating ratio is closer to 95% and maximum annual debt service coverage (MADS) is consistently at or above 2.5x.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--An erosion in unrestricted liquidity such that cash to adjusted falls to below 50% and is not expected to improve;

--A deterioration in the operational performance such that MADS coverage is consistently at or below 1.7x.

**BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from ‘AAA’ to ‘D’. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit [https://www.fitchratings.com/site/re/10111579](https://www.fitchratings.com/site/re/10111579).

Peconic Landing is located on the North Fork of Long Island and consists of 109 single-story cottages, 187 apartments, 26 enriched housing units (ALUs), 16 memory care units (MCUs) and 60 SNF beds. Utilizing a co-op model, Peconic Landing primarily offers a Type-A contract. Under the co-op structure, co-op shares are issued to the resident by Peconic Landing.
Currently, when IL units are vacated and resold, Peconic Landing pays the resident or resident's estate the lower of (1) the purchase price by the new resident less certain fees or (2) the purchase price initially paid by the resident, plus inflation (if positive), less certain fees. If a new buyer is not identified within one-year, Peconic Landing pays the resident or the resident's estate the lower of (1) the most recent purchase price of a similar unit recently sold less certain fees or (2) the original purchase price less certain fees. In 2020, Peconic Landing had total operating revenues of $34.7 million.

Revenue Defensibility

IL occupancy averaged 93% over last four audited years. The solid occupancy reflects Peconic Landing's ongoing marketing efforts and focused initiatives, such as the dividing of larger cottages into two townhouse units. Despite the challenges in marketing and sales brought on by the coronavirus pandemic, Peconic Landing maintained IL occupancy of 93% in FY20 and 91% through the first six months of FY21. Assisted living (AL), memory care and skilled nursing occupancies, which had historically been above 90%, have fallen to the high 70% and low 80% range during the pandemic. Fitch expects these occupancies to rebuild as external short-term rehabilitation referrals into skilled nursing recover and AL and memory slowly return to historical levels.

Only two other LPCs are currently located in the vast Long Island market, both of which are outside Peconic Landing's primary market. The two LPCs are Jefferson's Ferry (BBB/Stable), which is located approximately 50 miles from Peconic Landing in in South Setauket, NY, and The Amsterdam at Harborside, which is located approximately 82 miles from Peconic Landing in Port Washington. Additionally, a third LPC currently in the development phase is located in Commack, NY. Fitch believes the limited competition, coupled with Peconic Landing's advantageous location, including access to a private beach, on eastern Long Island's North Fork, will continue to support strong demand across the continuum of care at Peconic Landing.

Peconic Landing's pricing is in line with its attractive location, strong local service area demographics in both the local Peconic/Greenport market and in Suffolk County overall, and the net worth of its incoming residents. Peconic Landing has consistently raised its entrance fees and month service rates. Overall, Fitch believes Peconic Landing's ongoing focus on marketing, its attractive product, and area demographic will continue support the strong revenue defensibility assessment.

Operating Risk
The vast majority of Peconic Landing’s residents have a lifecare (Type-A) contract, which requires an upfront entrance fee and ongoing monthly fees. Under the lifecare contract, residents pay the same monthly fees regardless of level of care needed, which shifts the healthcare burden to Peconic Landing. Fitch views Type-A facilities as having a more elevated operating risk.

Over the last five fiscal years, Peconic Landing has averaged 99.1% operating ratio, 4.7% net operating margin (NOM), and 12.5% NOMA, which are largely consistent with the midrange assessment. Despite pressures from the pandemic, Peconic Landing maintained a solid core performance through the six-month 2021 interim period as evidenced by its 90.4% operating ratio and 16.3% NOM. The operating performance was supported by improving AL, memory care and skilled nursing occupancies, as the year has progressed, reduced Medicaid census in the skilled nursing center, and good ongoing cost management efforts. The operating results do not include the proceeds of a $2.9 million Payroll Protection Program loan that was forgiven in the current year. The proceeds of that loan have kept Peconic's Landing's overall financial profile stable, helping to offset a negative $2.6 million in net entrance fee receipts through the first six months of 2021. Fitch expects the net entrance fee receipts to improve in the second half of 2021, as the timing on sales and move ins return to a more normalized flow.

Peconic Landing's capex has averaged about 83% of depreciation over the last five years, which is consistent with the midrange assessment. Capex spending has been well below depreciation in recent years. However, the lower level of spending is not a concern as Peconic Landing has very limited capital needs as it completed a sizable IL expansion and healthcare repositioning project in fiscal 2016 (capex spending was 252.7% of depreciation in 2016). The largest current project is a $1.5 million bistro that will add a new dining venue to the campus and will have water views. Fitch believes the $2 million to $3 million a year that Peconic Landing is expected to spend on capital over the next three years is sufficient to keep the campus marketable.

Peconic Landing’s capital-related metrics are consistent with the midrange operating risk assessment. MADS represented a moderate 9.1% of 2020 revenues and debt to net available was consistently below 4x through the four-year historical period, leading up to 2020. Revenue only coverage has averaged above 1x over the last four audited years, which is consistent with the midrange assessment and particularly good for a Type 'A' LPC, which generally have revenue only coverage below 1x. The steady revenue only coverage helps offset some of the volatility in Peconic Landing’s net entrance fee receipts.

Financial Profile
Given Peconic Landing’s strong revenue defensibility and midrange operating risk assessments and Fitch's forward-looking scenario analysis, Fitch expects key leverage metrics to remain consistent with the lower end of the 'BBB' category throughout the current economic and business cycle. At YE 2020, Peconic Landing had unrestricted cash and investments of approximately $25 million. This represents about 60.6% of total adjusted debt (when including approximately $37 million in debt service reserve funds). Peconic Landing has no debt equivalents. DCOH was at 286 days at YE 2020.

Fitch’s baseline scenario, which is a reasonable forward look of financial performance over the next five years given current economic expectations, shows Peconic Landing maintaining operating and financial metrics that are largely consistent with the current rating and with historical levels of performance (operating ratios below 100% and NOMAs generally near or above 15%). Capital spending is expected to remain near depreciation, and includes life cycle investments. Fitch assumes an economic stress (to reflect equity volatility), which is specific to Peconic Landing’s asset allocation. Despite the stress, Peconic Landing’s cash-to-debt levels remain at levels consistent with the rating level in the forward look. MADS coverage remains steady as well. DCOH remains near 200 days through the moderate stress which is neutral to the rating outcome.

Sources of Information

In addition to the sources of information identified in Fitch’s applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of ‘3’. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch’s ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

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VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

U.S. Public Finance Not-For-Profit Life Plan Community Rating Criteria (pub. 02 Mar 2021) (including rating assumption sensitivity)

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 01 Sep 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Portfolio Analysis Model (PAM), v1.3.2 (1)

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Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

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