SL Green Realty Corp. (SLG)

Updated July 20th, 2023 by Aristofanis Papadatos

Key Metrics

Current Price:	$35	**5 Year CAGR Estimate:**	19.7%	**Market Cap:**	$2.2 B
Fair Value Price:	$54	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	7/27/2023[1]
% Fair Value:	64%	**5 Year Valuation Multiple Estimate:**	9.2%	**Dividend Payment Date:**	8/14/2023
Dividend Yield:	9.3%	**5 Year Price Target**	$69	**Years Of Dividend Growth:**	0
Dividend Risk Score:	F	**Retirement Suitability Score:**	B	**Rating:**	Buy

Overview & Current Events

SL Green Realty Corp. (SLG) was formed in 1980. It is an integrated real estate investment trust (REIT) that is focused on acquiring, managing, and maximizing the value of Manhattan commercial properties. It is Manhattan's largest office landlord, with a market capitalization of $2.2 billion, and currently owns 60 buildings totaling 33 million square feet.

On June 26th, 2023, SLG sold its 50% stake in 245 Park Avenue for $1.0 billion. Since then, the stock has rallied 50%, as the sale signaled that the assets of the REIT are probably worth more than the market values them. To provide a perspective, the stock had a market cap of only $1.6 billion before the announcement of the above sale.

In mid-July, SLG reported (7/19/2023) financial results for the second quarter of fiscal 2023. Its same-store net operating income grew 3.6% over the prior year's quarter but its occupancy rate dipped sequentially from 90.2% to 89.8%. Given also the negative effect of some assets sales, its funds from operations (FFO) per share decreased -24% over the prior year's quarter, from $1.87 to $1.43, though they exceeded the analysts' consensus by $0.09.

SLG has been severely hit by the pandemic, which has led many tenants to adopt a work-from-home model. Occupancy of office space in New York remains near historic lows. This has caused an unprecedented tenant-friendly environment, which has lasted much longer than expected. SLG has not provided guidance for 2023. Moreover, high interest rates have greatly increased the net interest expense of the REIT, from $17 million in Q1-2022 to $41 million in Q2-2023.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
FFO	$5.16	$5.85	$6.38	$8.29	$6.45	$6.62	$6.99	$7.11	$6.80	$6.76	***$5.50***	***$7.02***
DPS	$1.49	$2.10	$2.52	$2.94	$3.14	$3.29	$3.44	$3.54	$3.64	$3.69	***$3.25***	***$3.40***
Shares[2]	95.3	99.7	103.7	104.9	103.4	91.5	86.6	74.3	69.9	68.7	***68.0***	***60.0***

SLG benefits from long-term growth in rental rates in one of the most popular commercial areas in the world, Manhattan. The REIT pursues growth by acquiring attractive properties and raising rental rates in its existing properties. It also signs multi-year contracts (7-15 years) with its tenants in order to secure reliable cash flows. SLG has grown its funds from operations per share at a 3.0% average annual rate in the last decade. Due to the effect of the pandemic on its business, funds from operations decreased in 2021 and 2022. The pandemic has subsided this year but the REIT has not begun to recover from the work-from-home trend yet. Nevertheless, we expect SLG to grow its funds from operations per share at a 5.0% average annual rate over the next five years off this year's 10-year low expected level.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/FFO	17.1	18.2	17.8	12.5	16.1	14.6	12.2	8.3	10.6	8.4	***6.4***	***9.9***
Avg. Yld.	1.7%	2.0%	2.2%	2.8%	3.0%	3.4%	4.0%	5.1%	5.0%	6.5%	***9.3%***	***4.9%***

[1] Estimated date.

[2] In millions.

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SLG has traded at an average price-to-FFO ratio of 13.6 during the last decade. Due to the impact of the work-from-home trend on its business and the impact of high inflation on its interest expense and its valuation, the REIT is currently trading at a nearly 10-year low FFO multiple of 6.4. In order to be conservative, we assume a fair price-to-FFO ratio of 9.9, which is equal to the 4-year average of the stock. If SLG reaches our fair valuation level in five years, it will enjoy a 9.2% annualized boost to its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	29%	36%	39%	35%	49%	50%	49%	50%	54%	55%	***59%***	***48%***

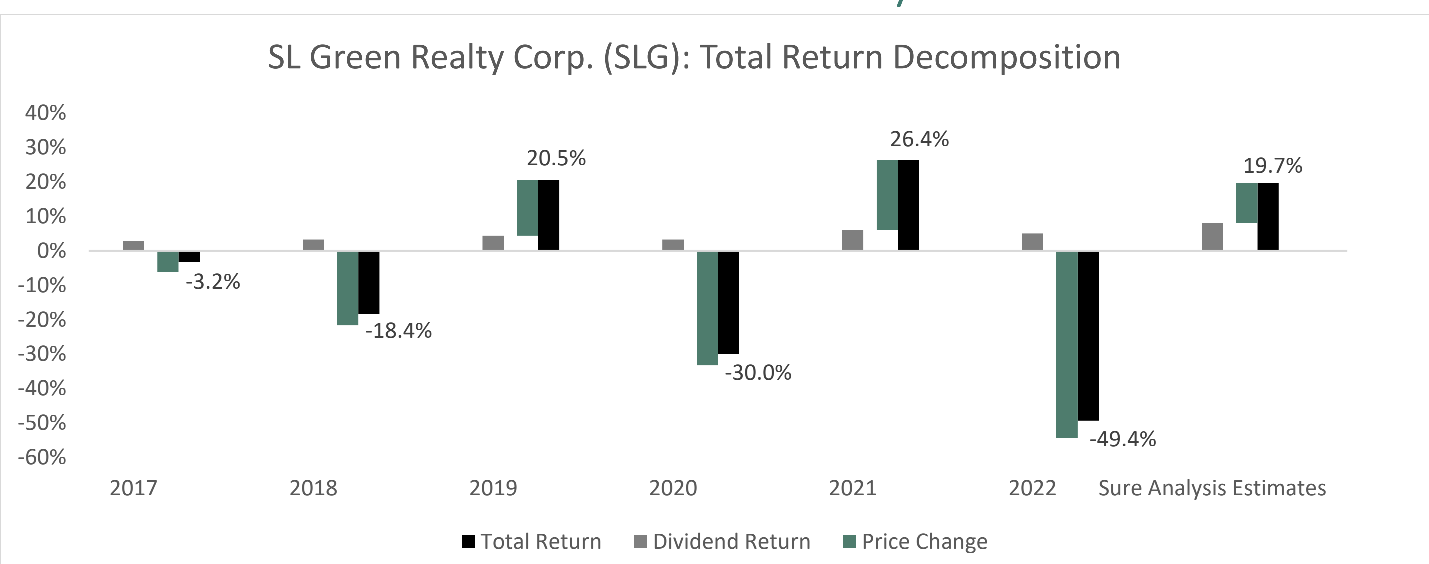
During the last 43 years, SLG has been operating, investing and developing several high-quality commercial properties in Manhattan. It has thus developed great expertise in the area, which constitutes a significant competitive advantage.

SLG is under pressure due to the work-from-home trend, which has resulted from the pandemic. However, it has a decent balance sheet, with a healthy BBB credit rating. As a result, it can endure the ongoing crisis and emerge stronger whenever the work-from-home trend subsides. It can also maintain its attractive 9.3% dividend, which is well covered by cash flows, with a healthy payout ratio of 59%. SLG is thus suitable for income-oriented investors who can wait patiently for the recovery of the REIT from the pandemic. On the other hand, we note that SLG recently issued a great amount of debt to buy new properties and thus its net debt climbed to $5.2 billion, which is about 14 times the annual FFO and more than double the market capitalization of the stock. We will continue monitoring the debt situation closely.

Final Thoughts & Recommendation

SLG is the largest landlord in the area of Manhattan and thus it is ideal for those who want to benefit from the reliable, multi-year growth in rental rates in this area. The stock is currently facing the headwind from the work-from-home trend and rising interest expense due to rising interest rates but we expect more people to return to offices and interest rates to subside in the upcoming years. Thanks to the aforementioned sale of an asset, the stock has rallied 35% since our last research report, in April, but it remains attractive. Thanks to its 9.3% dividend, 5.0% annual growth of FFO per share and a 9.2% potential valuation tailwind, SLG could offer a 19.7% average annual return over the next five years. We thus maintain our buy rating and advise investors to be patient.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	1,371	1,520	1,663	1,864	1,511	1,227	1,239	1,053	844	827
Gross Profit	859	988	1,096	1,269	941	779	780	664	497	488
Gross Margin	62.7%	65.0%	65.9%	68.1%	62.2%	63.4%	63.0%	63.1%	58.9%	59.0%
SG&A Exp.	86	92	95	100	100	93	101	92	95	94
D&A Exp.	358	400	588	846	419	290	284	325	228	223
Operating Profit	449	523	440	349	437	179	400	198	162	178
Operating Margin	32.7%	34.4%	26.5%	18.7%	28.9%	14.6%	32.3%	18.8%	19.2%	21.5%
Net Profit	138	521	291	261	113	259	281	380	457	(72)
Net Margin	10.0%	34.3%	17.5%	14.0%	7.5%	21.1%	22.7%	36.1%	54.2%	-8.7%
Free Cash Flow	386	490	526	644	543	442	376	554	256	276

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	14,959	17,097	19,728	15,858	13,983	12,751	12,766	11,708	11,067	12,356
Cash & Equivalents	207	281	255	279	128	129	166	266	251	203
Accounts Receivable	447	432	562	496	423	378	327	347	296	292
Long-Term Debt	6,920	8,179	10,275	6,482	5,855	5,542	5,508	4,929	4,017	5,512
Shareholder’s Equity	6,303	6,715	7,066	7,103	6,003	5,680	5,219	4,688	4,543	4,363
LTD/E Ratio	1.06	1.18	1.41	0.88	0.94	0.94	1.01	1.00	0.84	1.20

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	0.9%	3.2%	1.6%	1.5%	0.8%	1.9%	2.2%	3.1%	4.0%	-0.6%
Return on Equity	2.2%	8.0%	4.2%	3.7%	1.7%	4.4%	5.2%	7.7%	9.9%	-1.6%
ROIC	1.0%	3.4%	1.7%	1.5%	0.8%	2.0%	2.4%	3.4%	4.6%	-0.7%
Shares Out.	95.3	99.7	103.7	104.9	103.4	91.5	86.6	74.3	69.9	67.93
Revenue/Share	14.81	15.69	16.50	18.29	15.04	14.18	14.69	13.61	11.57	12.17
FCF/Share	4.17	5.06	5.22	6.32	5.40	5.10	4.46	7.16	3.51	4.06

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.