Mid-America Apartment Communities, Inc.
Conference Call 2Q09
August 7, 2009

Leslie Wolfgang:
Good morning. This is Leslie Wolfgang, Director of External Reporting for Mid-America Apartment Communities. With me are Eric Bolton, our CEO, Simon Wadsworth, our CFO, Al Campbell, Treasurer, Tom Grimes, Director of Property Management and Drew Taylor, Director of Asset Management.

Before we begin I want to point out that as part of the discussion this morning company management will make forward-looking statements. Please refer to the safe-harbor language included in yesterday's press release and our 34-Act filings with the SEC which describe risk factors that may impact future results. These reports, along with a copy of today's prepared comments, and an audio copy of this morning's call can be found on our website.

I'll now turn the call over to Eric.

Eric Bolton:
Thanks Leslie. Mid-America's strong operating performance in the second quarter supports our belief that we are well positioned to ride out the current weak leasing environment. With unemployment likely to remain high through next year, we expect that leasing will remain challenged in most markets this year and well into 2010. I expect it will be late next year before we have an ability to meaningfully start moving pricing power back our way. However, as supported by the solid second quarter performance, we don't expect to see a material deterioration from current leasing conditions across our overall portfolio of markets and properties. Our priorities remain focused on protecting occupancy, aggressively managing expenses, protecting asset value, and taking advantage of an improving environment for making new acquisitions.

As discussed during our first quarter call, we made a real effort to ensure we entered the busy spring and summer leasing season with strong occupancy in order to capture the best pricing performance and expense control we could in an environment of weak leasing fundamentals. We were pleased with the results. Overall same store average effective rent declined only 1.3% over the prior year and only 90 basis points from first quarter. Occupancy climbed 60 basis points over the prior year and 20 basis points over the prior quarter. And importantly, the strong occupancy and lower resident turnover helped to drive same store operating expenses down 1.1% as compared to the prior year.

As expected, during the second quarter our secondary markets continued to outperform our large tier markets. With physical occupancy in our secondary markets a very strong 95.9% at quarter end, revenues trended down only 10 basis points from second quarter of last year, with average effective rent declining only 1.0%. We're also very pleased with the performance of our large tier market segment with occupancy at a very solid 95.3% at quarter end and revenue growths declining only 1.3% as compared to last year. And as noted in our earnings release, occupancy in both our large tier and secondary market segments was up on both a prior year and a sequential quarterly basis. And, encouragingly, July same store occupancy closed at a very strong 95.7%.

While we likely have 3 to 4 quarters to go before we'll see meaningful improvement in overall pricing performance, we were encouraged by the fact that in the second quarter the pricing on leases written for new residents was consistent with the performance achieved in the first quarter, declining by 7.2%. The pricing on leases written for renewing residents remained positive with rents up a strong 2.1% over the prior year, but as expected is trending down slightly from the prior first quarter. It will take a return to positive year-over-year pricing on leases written for new residents before the overall pricing trend really improves and as noted, I expect it will be mid to late next year before that occurs. But the take-away point is that market pricing within our portfolio at least seems to have found a bottom and we're encouraged with the ability to capture such strong occupancy in the second quarter without further deterioration in pricing trends during our busy spring and early summer season.

We also were very pleased with performance in the area of collections. This is an area that we're keeping a very close eye on to ensure our leasing standards are not compromised in an effort to gain occupancy. In the second quarter, collection loss as a percent of net potential rent was only 0.36%, which is actually slightly better than the same point last year at 0.39%. As outlined last quarter, we believe the right approach in this weaker part of the leasing cycle is to trade pricing for occupancy, within reason, and not compromise credit quality standards.

In the second quarter we also wrapped up implementation of our new web-based Access 24/7 platform. This program now provides a fully automated platform over the internet for prospective renters to access the information they need to evaluate and rent from any one of our communities. In addition, our new online Resident Portal provides a fully automated platform for existing residents to make payments, request work orders and communicate with our staff. We expect to capture increasing cost efficiencies from these new web-based initiatives over the coming year. Implementation and roll-out of our new bulk cable initiative and resident statement billing is also making good progress and on track with expectations we have for this year.

In summary, we're pleased with second quarter operating results. A combination of our portfolio strategy and strong operating platform, coupled with a belief that the economy and job loss trends are nearing a bottom in most of our markets, should enable operating performance to hold up and not materially worsen from current levels.

As outlined in yesterday's earnings release, during the quarter we formed a new investment joint-venture with private capital and established Mid-America Fund II. We're excited about getting this new platform in place and believe it broadens our opportunity for value creation over the next couple of years. We've already closed on one new investment for the fund and are currently looking at several other opportunities. We continue to believe that the transaction environment is moving our way and as a 'value investor' we're optimistic about the likelihood of an increasing number of buying opportunities.

As Simon will detail in his comments, our first investment for Fund II is a brand new property that was acquired on a very attractive basis in Macon, GA, just south of Atlanta. A market we know very well. While this acquisition of a new lease-up property is outside of the primary focus of the new fund, which is aimed at older properties offering turn-around opportunity, given that we already have four other properties in the market and to avoid market concentration risks, we elected to make this investment via our new Fund II. This is an example of another way in which the Fund II platform will enable us to create value for our shareholders, create more efficiency for our operating platform and reduce risks for our shareholders' capital.

We also continue to pursue a number of acquisition opportunities that we would acquire as wholly owned investments for Mid-America. During the second quarter we closed on the acquisition of Sky View Ranch, 232 units located in Phoenix, AZ. Phoenix is a market obviously fighting through a tough leasing environment and we expect that the market may deliver additional opportunities over the next couple of years. New lease-up properties, such as Sky View Ranch, when acquired on a conservative basis with realistic lease-up expectations, offer a very compelling and attractive long-term investment opportunity as Phoenix is expected to be one of the top revenue growth markets in the country by 2011.

Mid-America's balance sheet remains in a solid position with $163 million of capacity under our existing credit facilities, a record high fixed-charge coverage ratio and one of the better dividend coverage ratios in the sector. We remain committed to our current dividend level. We of course are also committed to keeping the company poised to capture new investment opportunities. As noted in our first quarter report, any decision to raise additional new equity will be driven by the transaction environment and a belief that we can put new capital to work in a timely manner. While we did not issue any new common shares during the second quarter, our continuous equity program remains teed up and we continue to closely monitor our deal flow and the transaction environment. Should opportunities continue to emerge we are committed to positioning the balance sheet for growth, but based on anticipated needs at this point, we don't expect any significant shifts in the balance sheet to be necessary.

I'll now turn the call over to Simon.

Simon Wadsworth:
Our second quarter FFO per share of $0.98 cents was an all-time second quarter record, 5 cents ahead of the mid-point of our guidance and 3% ahead of the second quarter of 2008. This was entirely due to excellent property performance, with about half of the upside from our original guidance contributed by property revenues and the balance from favorable property operating expenses. As Eric mentioned, high occupancy, strong reimbursements, and excellent collections helped revenues. Expenses were helped by

lower property taxes and lower turnover than we anticipated. All of this contributed to great same-store NOI performance, which was down just 0.2% compared to a year ago.

Effective rent declined 1.3% from the second quarter of last year to $730. The average rent on all leases written was down only 4.2% over the same quarter a year ago; rent on leases written to new residents dropped by 7.2%, but rents on lease renewals were up an average of 2.1%.

Same store revenues declined just 0.6%, significantly better than our forecast, on record occupancy which was a 60 basis points increase over the second quarter of last year. An increase in reimbursement fees and continued improvement to systems helped boost our reimbursement collections, contributing to the great collections performance.

Same store expenses dropped by 1.1% compared to the second quarter of last year. Property operating expenses, before taxes and insurance, increased only 1.5%, as reduced turnover and tight control brought repairs and maintenance costs down 5%. Property taxes were down 6.6% for the quarter, as we had some favorable results from last year's tax appeals as well as success in negotiating lower assessments. We also continued to benefit from the lower insurance rates we negotiated a year ago.

So, our initiatives to maintain strong revenues and contain expenses helped us generate substantially better NOI than we had forecast at the beginning of the quarter, limiting the same store decline to a nominal 0.2%.

Traffic levels for the quarter continued to be good. Walk-in traffic was at almost exactly the same level as last year, which is excellent considering that our properties began and ended the quarter with record occupancy, and that the number of move-outs declined by 9.3%. Traffic from internet sources increased 43%, reflecting the strong impact of our internet initiatives.

Resident turnover in our same store portfolio decreased 9% for the quarter compared to the same period a year ago mainly because residents leaving us to buy a house dropped by 22%, from 25.0% of move-outs in the second quarter of 2008 to 21.5%. On a trailing 12-month basis, resident turnover is only 59.1% compared to 62.6% a year ago. House rental continues to be a very small part of our competition: the number of residents moving out to rent a house increased slightly from 4.3% of move-outs a year ago to just 4.8% of move-outs this quarter.

We had a couple of one time items that cost us almost a penny a share of FFO in the quarter. Firstly, as Eric mentioned, we acquired Sky View Ranch, and as required under new accounting rules, expensed the $107,000 in acquisition costs that we incurred. Secondly, we prepaid a tax-free bond, and as a result wrote off $140,000 in deferred finance costs, a non-cash charge.

We have one of the better dividend coverages of the sector, despite the dividend reductions and cash dividend cuts of some of the apartment REITS. For the quarter, AFFO was $0.73 per share, well ahead of our $0.615 dividend. We continue to feel comfortable with the current dividend level based on our internal projections for this year and for 2010.

On the transaction front, we announced the formation of Fund II. We anticipate the Fund investing up to $250 million over an 18 month period, of which approximately 30% to 35% will be equity. We're a 1/3 owner, and we'll receive normal fees acting as managing partner, which helps our returns. We anticipate a 6 year hold period for each asset, and returns to Fund II's equity of 13% – 15%. We're eligible for a promote after Fund II returns reach a threshold IRR.

As Eric mentioned we were pleased to be able to buy Sky View Ranch, a 232- unit apartment community in Phoenix, and I'll provide a little more information about the underwriting. We acquired the property mid-June for $17½ million, or $75,000/unit; to put this price in perspective, the tax assessor has this property appraised at $108,000/unit, which we think is reflective of development costs in Phoenix. The property closed the month at 81% occupied, up from 78% when we acquired it 2½ weeks earlier. Because of the difficult state of the Phoenix market, we underwrote it pretty conservatively, even projecting it to take 5 years to reach 94% occupancy, at which point we project it to be more or less stabilized at a 9½% NOI yield.

At the end of July, Fund II acquired Ansley Village, a 294-unit high-end property in lease-up that was completed in 2007. Fund II acquired it for $16.5 million, or $56,000 a unit from a bank who'd taken it back by deed in lieu of foreclosure, and we understand that the property was developed for $85,000 a unit. The property is currently 70% occupied, and we're projecting it to stabilize in year 4 with an 11% NOI yield. Fund II financed it with a non-recourse bank loan at approximately 65% loan-to-value, and anticipates replacing this with more permanent debt after the property reaches 90% occupancy.

We completed the sale of Riverhills a 96-unit property in Grenada, MS, in May. This 36-year old property was part of our IPO, and sold for $2.7 million, at around a 6.4% cap rate. We have one other property under contract for sale, River Trace, a 440-unit property in Memphis, which is now targeted to sell in September, with proceeds estimated in the $15 million range, around a 6.9% cap rate. River Trace was listed as 'held for sale' at quarter end. We haven't forecast additional dispositions in 2009.

Even in this transaction environment, we anticipate that the blended cap rate for all three properties we've sold or are planning to sell this year will be 7.1%. These properties are all in secondary markets, and average 29 years of age**,** almost double that of our portfolio average. That's an interesting perspective when we consider that these assets are obviously being culled off the bottom of our portfolio, yet the entire company is trading at a cap rate only slightly better than these sales.

We continue to have one of the stronger financial positions of the apartment REITs. On April 1st we paid off our only 2009 debt maturity, a $38.3 million bank loan. As of the end of the quarter, we had $163 million of unused capacity available under our credit facilities. In 2010 we have only our $50 million bank credit facility that matures which we expect to refinance with our current lenders, although we have capacity to take it out if needed. At June 30th, our debt to total gross assets was 50%, at the same level of a year ago, and about 300 basis points below the apartment sector median. Our fixed charge coverage in the second quarter was 2.71, well ahead of 2.51 a year ago, and also well ahead of the sector median of 2.39.

In 2009, we expect to pick up 2 cents a share of interest expense savings from debt re-pricing opportunities on the $38 million refinancing that we just completed. We have $65 million of debt that re-sets to variable rate on December 1st, and based on our refinancing assumptions, expect to pick up 7 cents a share of savings on a full 12-month basis.

As we've previously indicated, we have not been active with our continuous equity program. Our balance sheet is in great shape, and we have no need to issue equity for defensive purposes. However, we continue to monitor the capital markets and the investment environment, and are encouraged that we've managed to locate and acquire two very attractive investment opportunities in the past two months.

To provide a little more color on some of our expense items for 2009, as a result of our pro-active efforts to reduce assessments as well as appeals pending from 2008, we expect same-store real estate taxes to be approximately flat, substantially less than the 4½% increase that we forecast earlier in the year. We've also had good success in negotiating better insurance terms than we projected for our July 1st renewal. Our loss-control initiatives helped us offset the impact of what is a hardening insurance market, and we now expect same-store insurance costs for the balance of the year to be up less than 1%, compared to our prior expectation of a 5% increase. Because of our efforts to control expenses, we expect our combined G&A and property management costs to be down about 2% to 3% on a full-year basis compared to 2008.

The significant improvement in our outlook for property operations causes us to increase our full-year forecast of FFO per share by 8-cents to a range of $3.55 to $3.75. For 2009, we are now projecting a 2½% - 4½% reduction in same-store NOI, compared to our prior guidance of a reduction of 4% to 6%. At the mid-point, the decline in NOI is reduced from 5% to 3½%. This forecast is built on a 1% - 2 % reduction in same-store revenues, and an increase in expenses of approximately ½% to 1½%.

We project our average interest rate for the year at 4.4% compared to an average of 4.9% for 2008. We see Agency interest rates continuing to be favorable both overall and compared to Libor. At the end of the quarter, 78% of our debt was fixed or swapped, and a further 9% capped.

Excluding the redevelopment program, the quarter's total property capital expenditures at existing properties was $11.2 million, for a year to date spend of $16.6 million compared to our full year budget of $29.5 million, or 97 cents a share. Recurring capex is budgeted in the region of $21½ million, or 70 cents a share. We anticipate total expenditures on our redevelopment program of $9 million, about half the level of last year, of which $6.8 million is budgeted for the interior upgrade of 2,000 apartment units. In addition, we project full-year development funding of $9 million, down from $25 million last year, of which only $3 million remains to be funded.

We continue to anticipate that we'll invest approximately $75 million in new acquisitions, and contribute about $9 million for our share of the equity in Fund II.

Eric Bolton:
Thanks Simon.

Second quarter results provide further evidence that Mid-America remains well positioned to deliver stable results during this weak part of the cycle. A combination of our investment disciplines, portfolio strategy, strong operating platform and conservative financing strategy all play a part in Mid-America's ability to deliver stable performance during this phase of the cycle. We remain committed to the belief that part of the process in delivering superior long-term value growth for shareholders is to ensure that existing asset value and performance is protected during stress periods. Mid-America's ability to avoid the significantly dilutive equity issuances, dividend cuts and asset value write-offs that have been required by a number of REITs is validation of this strategy.

However, while we take comfort from an ability to ride out the current down-turn in strong fashion, it's the prospects over the next few years as the economy and employment markets recover that really excites our team. Mid-America is in a terrific position to capture new value growth and a significant recovery in operating performance as market conditions improve. With new supply trends expected to be very low over the next several years, with a focus on the most vibrant job growth region of the country, and with a sophisticated and efficient operating platform that puts us in a strong competitive position in our markets, we're excited about the prospects for Mid-America. We expect to deliver operating performance from our markets and portfolio that will continue to compare very well with the operating performance captured in the traditionally lower cap rate and higher investment cost markets, and as a result deliver more attractive returns on the capital invested.

At Mid-America our approach to creating value for shareholders is a straight-forward model, based on being a value investor and disciplined buyer, with an aggressive focus on operations geared towards property redevelopment and strong property management that matches the operating profile of our high growth markets. We believe the window of opportunity for this strategy continues to broaden and we look forward to capturing new value growth for our shareholders.

That's all we have in the way of prepared comments and operator we'll now turn the call back over to you for any questions.