CONFERENCE CALL TRANSCRIPT: 1Q2015
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Tim Argo
Good morning. This is Tim Argo, SVP of Finance for MAA. With me are Eric Bolton, our CEO, Al Campbell, our CFO, and Tom Grimes, our COO.

Before we begin with our prepared comments this morning, I want to point out, that as part of the discussion, company management will be making forward-looking statements. Actual results may differ materially from our projections. We encourage you to 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 will be available on our website.

During this call, we will also discuss certain non-GAAP financial measures. Reconciliations to comparable GAAP measures can be found in our earnings release and supplemental financial data.

When we reach the question & answer portion of the call, I would ask for everyone to please limit their questions to no more than two, in order to give everyone ample opportunity to participate. Should you have additional questions, please re-enter the queue or you are certainly welcome to follow up with us after we conclude the call. Thank you.

I'll now turn the call over to Eric.

Eric Bolton
Thanks Tim. We appreciate everyone joining us this morning.

We had a strong start to the year with first quarter results ahead of our expectations. The out-performance was driven by solid operating results with same store NOI growing 5.8% as compared to prior year. Tom will walk you through more specifics surrounding pricing and the factors driving revenue performance, but overall we continue to enjoy a favorable leasing environment as job growth and strong demand across our markets are more than off-setting new supply deliveries.

Continued progress in harvesting the opportunities coming out of our merger with Colonial is also contributing to operating momentum. The lift in performance we captured in the back half of last year from a number of operating improvements and scale benefits are continuing to generate solid year-over-year results. All aspects of our operations are now fully consolidated onto one platform and we're looking forward to continuing to improve and fine tune several processes that we believe will generate further lift in operating margin.

The balance sheet remains in a strong position and we expect to see coverage metrics continue to improve over the course of the year. In his comments Al will recap more details, but we are particularly pleased with the progress in growing the unencumbered asset base. With a higher level of asset sales and growing free cash flow, our overall debt level as a percentage of gross assets is declining and is also further strengthening the balance sheet.

As recapped in yesterday's earnings release, we had a very busy quarter with transactions. Including a group of properties that were sold earlier this week, we have completed the sale of 18 properties since the first of the year. We have an additional three properties under contract and are expecting to close on those sales later in the summer. As we outlined in last quarter's earnings release, we believe that market conditions and the transaction market supported an expedited execution of our plans to exit these 21 properties and smaller secondary markets. We're very pleased with the execution.

At an average age of 25 years and located exclusively in smaller markets, this group of 18 properties that has been sold has an average rent that is 21% below our same store portfolio average. Based on trailing twelve month NOI, total capital spending averaging approximately $1,200 per unit and a 4% management fee, we captured a 5.6% cap rate on the sale of these properties.

Going forward, as we've been doing for the past few years, we will continue to consider opportunities to recycle capital from properties and markets where we believe we can re-invest to capture more attractive long-term value. But it's worth noting that with the dispositions being completed this year, in addition to the significant volume of dispositions and capital recycling completed over the past few years, we've now sold over 11,000 units since 2010. As a result, you can expect us to execute our capital recycling on more of a match-funding basis going forward. In exiting an additional eleven markets this year we have now repositioned the portfolio for stronger and more efficient execution going forward.

I'd like to point out that as a result of this capital recycling, along with a number of other improvements we've made to both the operating and financing platforms for both the legacy MAA and CLP portfolios, we've seen MAA's same store NOI margin over the last five years improve 430 basis points. When considering capital spending on both recurring and revenue enhancing items, the same store NOI margin has improved 550 basis points since calendar year 2010.

On the acquisitions front we continue to underwrite a number of new opportunities and deal flow remains high, but extremely competitive. As we move further into the new supply delivery cycle I continue to believe that we'll see more investment opportunities that meet our long established investment hurdles. As noted in yesterday's earnings release, during the quarter we started a phase II expansion of our property in Fredericksburg, VA and are currently looking at starting additional expansions at properties we own in Orlando and in Charleston. We also remain active in discussions with developers on several opportunities to acquire properties on a pre-developed or lease-up status.

In summary, we like the momentum we are seeing and believe that the benefits being harvested from our merger, coupled with the capital recycling we've completed further supports a more efficient operation and higher internal growth profile. The balance sheet is also well positioned and we remain poised, but disciplined, to capture growth opportunities that we feel are likely to increase as we move further into the cycle.

That is all I have in prepared comments and I'll now turn the call over to Tom.

Tom Grimes
Thank you Eric and good morning everyone. Our 5% revenue growth was driven by strong average physical occupancy of 95.6%, up 60bps from prior year, coupled with average rent per unit growth of 3.9%, and good fee performance. April trends continue to be strong. Our 60 day exposure, which is current vacancy plus all notices for a 60 day period, is just 8.3%. This is down 130bps from the same time last year. Our blended year-over-year pricing for April is up 6% which is 200 bps higher than this time last year.

While expenses were better than we expected there are a few timing notes on the expense lines. Our personnel and marketing expenses reflect timing incongruities related to the discontinuation of legacy CLP programs last year. This affects first quarter comparisons only and we expect both line items to be below 3% for the full year.

The benefits of our strong operating platform on the legacy CLP communities continues to pay dividends. The more robust approach of our revenue management team has grown rents at CLP communities more than 150bps higher than their market peers. Our system customizations that allow for fees and collections to be automatically billed on the CLP platform has improved delinquency and fee collections this quarter.

We are excited about our new repair and maintenance inventory process. In this new initiative our vendor stocks and replenishes our onsite shops with their owned inventory. We then purchase the inventory when it is used by our teams. This maximizes our scale discounts and the speed of service to the resident. It minimizes the amount of time our teams spend on procurement and increases efficiency on site. This process gives us the right part at the right cost at the right time. This is another example of how our scale and operating sophistication creates value for our residents and our shareholders.

On the market front, the vibrant job growth of the Large markets is driving strong revenue results in places like Atlanta, Austin, Charlotte, and Tampa. In the Secondary markets, which have lower supply pressure, we are benefiting from accelerating job growth. In this group Charleston, Greenville, and Savannah stand out. Jacksonville's 4% revenue growth is also notable. Further illustrating the demand of that market is our newly developed 220 Riverside project. We delivered our first units last week and the 294-unit community is already 58% preleased with rents above pro forma.

We expect our 4 communities in Memphis to show year-over-year improvement as the year plays out and job growth builds. We are in very good shape in Houston but continue monitoring our portfolio closely and will remain sensitive to any changes in demand. During the quarter Houston generated 6.6% revenue and rent growth. Turnover for the quarter was down 8%. For the month of April Houston's average physical occupancy was 96.1%. Year-over-year blended rents for April were up 7.7%.

It was at this time last year that the heavy lifting of our system integrations and improvements began. A year later we are in a different place. Our platform is fully integrated, our people are having fun with the new systems and the benefits of the merger are being harvested. I'm excited about what our teams have accomplished thus far and am looking forward to what's to come. And now, I will turn the call over to Al.

Al Campbell
Thank you Tom, and good morning everyone. I'll provide some additional commentary on the company's first quarter earnings performance, balance sheet activity, and expectations for the remainder of the year.

FFO for the first quarter was $105.2 million, or $1.34 per share. Core FFO, which excludes certain non-cash and non-routine items was $95.6 million, or $1.32 per share, as compared to $89.5 million or $1.21 per share for the prior year. This Core FFO per share performance was $0.03 per share above the mid-point of our previous guidance, and represents a 9.1% growth over the prior year.

Core AFFO for the first quarter was $94.6 million, or $1.19 per share, producing solid coverage of our $0.77 per share quarterly dividend.

Strong results from our same store portfolio, as discussed by Tom, produced the majority of the favorability to our forecast, as both our revenues and expenses were slightly favorable to projections. Performance from our lease-up properties also progressed as planned and our overhead and interest expenses were essentially in line with expectations for the quarter. Our G&A expenses are a little "front loaded" this year, reflecting the timing of certain items, but we expect this to normalize over the course of the year, and we remain very confident in our projection for combined G&A and property management expenses of $56.5 to $58.5 million for the full year, fully reflective of the synergies captured from the Colonial merger.

During the first quarter, we acquired one 298-unit luxury property for $46.5 million and we sold four older properties for combined gross proceeds of $53.3 million. The vast majority of our recent disposition activity occurred during April, as we sold an additional fourteen communities for combined gross proceeds of $180 million, which will be used to pay down our line of credit during the second quarter.

We also continued construction on the two properties under development at year-end, and we began construction on a phase II expansion of an existing community located in Fredericksburg, VA. We funded $5.0 million of construction costs during the first quarter, and expect to fund an additional $24.4 million to complete these three projects. Our current plans anticipate $50 to $60 million of construction spending during 2015, based on additional expansion opportunities.

To prepare for the planned asset sales as well as to continue improving our balance sheet, during the first quarter we paid off $116 million of secured Fannie Mae debt, as well as an additional $15.2 million single mortgage. We incurred $3.4 million of debt extinguishment charges related to these payoffs, but the vast majority of this expense was non-cash write-offs of deferred financing costs. We also have about $315 million of debt maturities remaining for the year, primarily occurring in the fourth quarter. As mentioned before, we currently plan to utilize the public bond markets to refinance this later this year. The average interest rate for the majority of these maturities is well above 5%, which is projected to produce some fairly significant interest rate savings given the current markets.

At the end of the first quarter our balance sheet remains in great shape. Our total debt to market cap was 36.1%, our fixed charge coverage ratio was over 4.0 times, and our net debt to recurring EBITDA was 6.2 times. Over 70% of our assets are now unencumbered, which is a record for the company, and over 92% of our debt is fixed or hedged against rising interest rates. Given the level of asset sales and projected internal cash flow, our current plans for the year do not include a need for new equity. At quarter end, we had over $335 million of total cash and credit available under our line of credit at year-end supporting our liquidity, and we expect to end the year with our leverage on a net gross asset basis to be about 41%, down from 42.6% at the end of 2014.

Finally, we are maintaining our current guidance for Core FFO and AFFO for the full year. We were encouraged by the first quarter performance from our same store portfolio, as we continued to capture benefits from the Colonial merger. But, as mentioned in our last call, we do expect tougher comparisons in the back half of this year, as post-merger more "normalized" quarters begin to compare to periods of synergy capture last year. We feel good about our current operating momentum, but given that the bulk of our leasing activity and significant transaction activity are ahead of us for the year, we will wait to revisit guidance with our second quarter earnings report.

As a reminder, our Core FFO is projected to be $5.09 to $5.33 per share, or $5.21 at the mid-point, based on average shares and units outstanding of about $79.5 million. Core AFFO is projected to be $4.43 to $4.67 per share, or $4.55 at the mid-point, which is a 6.3% increase over 2014. The major components of this guidance are outlined in our supplemental data package that accompanied our press release. Also, I will point we added some additional detail regarding our operating expenses to our supplemental package disclosures (page S-3) this quarter, which we hope you will find helpful.

I'll now turn the call back to Eric.

Eric Bolton
Before opening the line for questions I want to extend my thanks and appreciation for the hard work and excellent service our associates working on site at our properties provide for our residents. Our company culture is based on a strong service oriented mind-set, for both those who directly serve our residents and those of us who support them in our corporate and regional positions. As a result of this focus, MAA will be recognized later today as first among apartment management companies across the country as having the best online reputation based on an independent Online Power Rankings survey conducted by J Turner Research. This recognition follows our designation earlier this year as having the best online reputation among the publicly traded apartment REITs. This recognition speaks to both our teams' dedication to serving our residents, as well as to the strength and sophistication of our operating platform.

That's all we have in the way of prepared comments. Leo, we'll now turn the call back to you for Q&A.