Mid-America Apartment Communities, Inc.
Conference Call 1Q10
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Leslie Wolfgang

Good morning. This is Leslie Wolfgang, Director of External Reporting for Mid-America Apartment Communities. With me are Eric Bolton, our CEO, Al Campbell, our CFO, 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 will be available on our website.

I'll now turn the call over to Eric.

Eric Bolton

Thanks Leslie and good morning everyone.

We were encouraged with the better than expected start to 2010. As we'll outline in our comments this morning, we now believe that same store NOI will be better than originally forecast. It seems likely that the high retention of existing residents, coupled with a steady recovery in leasing conditions, will support our ability to continue pushing rents in line with what we are forecasting this year, and reinforces our belief that improved revenue trends should begin to emerge late this year and into 2011.

Results for the first quarter were highlighted by better than expected revenues as occupancy, fee income and collections were all ahead of forecast. Same store occupancy was a strong 96.6% at quarter-end; putting the portfolio in a terrific position as we enter the busy summer leasing season. The occupancy performance was 120 basis points better than first quarter of last year and 140 basis points better than where we were at year end. As we think about the remainder of 2010, we now expect that occupancy will remain consistent with last year's very strong performance with rent increases in line with our original forecast. In his comments Al will outline for you the adjustments that we've made to our forecast for the remainder of the year.

In the first quarter, when comparing rents to the prior quarter and looking at trends on a sequential basis, traction for sustained rent growth is definitely beginning to take shape. Rents achieved on new leases for all of the first quarter were up an average of 0.5% as compared to the fourth quarter. The recovery trend continued in April, with new lease pricing up 1.2% as compared to March.

As expected, the trend for rents on renewal lease transactions are lagging the trend on new leases, but are likewise moving into a recovery mode. Renewal rents in the first quarter were on average down 1.9% as compared to pricing in the fourth quarter. But, when looking at the trends on a more real-time monthly sequential basis, April renewal rents were up 1.7% as compared to the pricing achieved in March and reflect an improving trend as well.

While it takes several months of re-pricing to capture meaningful impact in overall revenue results, we're encouraged by these trends and remain comfortable with our forecast assumption that pricing will steadily recover over the course of this year and build for strong performance momentum into 2011.

The solid performance in the first quarter was fairly wide spread across our markets with the secondary markets posting slightly better revenue results. Our large market segment performance in the first quarter was somewhat weighted down by the weaker performance out of Houston and Phoenix. These are two markets that we feel good about long-term and where we expect robust recovery over the next couple of years, but as Houston was a little late to feel the impact of the recession, our properties there will be challenged with tougher prior year comparisons than most of our markets. We continue to believe that our high growth Sunbelt markets will capture more robust job growth as the economy begins to find traction. The latest projections from the Bureau of Labor Statistics released a week ago forecast that our markets, on a weighted average basis, will exceed the national job growth projections and we're optimistic about the future rent growth prospects from our portfolio.

As noted in our release, we just closed on our third investment for Mid-America's Fund II. Broadstone Cypress is a newly developed property located in the northwest sub-market of Houston. We acquired the property from the construction lender who had taken it back through foreclosure. At $74 thousand a unit for this upper-end and brand new property, we acquired the property at a 15% discount to the construction loan, well below replacement costs and we believe that we made a terrific buy. We continue to have a very active pipeline of opportunities that we are reviewing and remain optimistic that we will be successful in capturing a number of new investments this year on both a wholly-owned basis for Mid-America's balance sheet, as well as for Mid-America's Fund II. As has been extensively discussed, there is a lot of investment capital chasing acquisition opportunities and as a result cap rates continue to hold up very well. For the high quality properties that we've been pursuing, we continue to see transactions execute in the 5.5% to 6% range throughout our markets.

In summary, we're excited about where Mid-America is positioned for the coming recovery cycle. While the company's performance over the last couple of years has demonstrated an ability to withstand a down cycle, we continue to believe that the comparative recovery opportunity within Mid-America's portfolio is somewhat under-appreciated. When considering the upside for job growth throughout the southeast and southwest markets, coupled with the muted new supply pressure for at least the next couple of years, we believe that our core growth will be very competitive within the apartment REIT sector over the coming recovery cycle. And on the external growth front, it's clear to us that the transaction market is picking up. Certainly cap rates have trended down and it appears to us that cap rates throughout our markets have pretty much trended in a fashion that is consistent with trends we've seen in other regions and markets across the country. We remain confident that our long record focused on the Sunbelt region, with ability to perform for Sellers, will enable the company to capture meaningful new growth while retaining the disciplines that have guided our investment. With solid prospects for recovery in pricing out of our existing asset base, and growing opportunities to capture new value from an increasingly active transaction environment, we believe Mid-America is in a terrific position to perform well over the coming recovery cycle, just like we did during the last up cycle.

That's all I have in the way of prepared comments and I'll turn the call over to Al.

Al Campbell

Our first quarter FFO per share of 99 cents was 8 cents ahead of the mid-point of our initial guidance. Same store NOI for the first quarter was projected to be down 7% compared to the prior year, but was down only 3.5% as occupancy, collections performance and fee income were all above expectations. Occupancy climbed well above 96% during the first quarter, which formed the basis for much of the favorable result. Low resident turnover continued to support the higher occupancy levels, reaching a historical low of 56.9% at the end of the first quarter, which was 3.7% below the prior year. Same store operating expenses, after netting bulk cable programs in revenue, also remained under control during the first quarter, growing only 0.6% over the prior year, which was slightly better than projections, primarily due to personnel costs, utilities, and real estate tax expenses.

Our balance sheet remains stronger than ever, and we made good progress on planned financing activities during the quarter. We were pleased to complete the renewal of our $50 million bank credit facility during the quarter, which was our only debt maturity during 2010. The new facility matures in two years, with a one year extension and has a $20 million expansion feature. We were pleased with the final terms, most significant being the borrowing cost of LIBOR + 275, which remains is within current market levels.

We entered two interest rate caps during the quarter, totaling $50 million, to replace a maturing interest rate swap hedging a portion of our variable rate borrowings. As consistent with our recent transactions, both caps have low cap levels (LIBOR of 4.5%) and mature in 7 to 8 years. We also entered a $19.5 million Freddie Mac fixed rate mortgage on a recent acquisition property during the quarter, which matures in 10 years and bears interest at just below 5.5%.

Our leverage (defined as debt to gross assets) ended the first quarter at 49% and our fixed charge coverage was 2.83 times EBITDA for the quarter, which is 2% above the previous year and more than 25% above the sector average of 2.23 times EBITDA. Our total average interest rate for the quarter was 4.1%, and we ended the quarter with 86% of our debt fixed or hedged against future interest rate rises. We also ended the quarter with over $175 million of current borrowing capacity and cash, providing flexibility and strength.

In April, we also fixed the rate on an additional $50 million of our Fannie Mae borrowings, adding another 3% interest rate protection, bringing the total fixed or hedged debt to 89% of our outstanding balance.

As announced in our release earlier this week, we called half of our outstanding Preferred H shares. The Preferred H shares are redeemable at $25 per share on June 2nd, for a total redemption price of $77.5 million, plus accrued dividends. We plan to use proceeds from our at-the-market, or ATM, program to fund this redemption. Through the end of April we raised almost $73 million through our ATM, at an average price of just over $52 per share, net of issuance costs. We have the ability under our current ATM program to issue up to 4 million shares, of which over 2 1/2 million shares are remaining. We plan to continue using our ATM program to fund a portion of the acquisition opportunities that emerge over the remainder of the year, in order to maintain our current balance sheet strength.

The preferred redemption is just another step toward strengthening our balance sheet, further preparing us for future growth. The preferred shares carry a relatively expensive 8.3% coupon rate, and this transaction lowers our total leverage (defined as debt + preferred to gross assets) by almost 3%, and increases our fixed charge coverage ratio by 10%. We are required to record a non-cash charge of about $2.6 million (or 8 cents FFO/share) related to the original issuance costs of these shares, and we expect to incur an additional 1 cent per share during 2010 executing the transaction. However, the redemption is expected to add between 3 and 3 ½ cents per share to FFO in 2011.

As noted in our release, we're raising our guidance for the year and providing guidance both before and after the Preferred H redemption. Overall, we expect to hold our solid occupancy through the year (in the 95% to 96% range), with pricing trends continuing to slightly improve over the next few quarters, beginning to show more improvement on a year-over-year basis late in 2010 and into 2011. We are now projecting same store NOI to decline in a range of 3% to 5%, compared to the prior guidance range of a 5% to 7% decline. Though there are other cross currents in our forecast, this 200 basis points improvement in projected same store results for the year produces about 12 cents per share in FFO which is the primary reason for raising our guidance. Thus, our revised guidance for the year, before the preferred redemption, is for FFO per share between $3.57 and $3.77 per share, 12 cents above our previous guidance at the mid-point. After considering the non-cash charge and execution costs for the preferred redemption, totaling 9 cents per share, FFO per share is projected to be between $3.48 and $3.68, which at the mid-point is still slightly above our initial guidance for the year.

That's all I have for prepared comments.