



CONFERENCE CALL TRANSCRIPT: 4Q2017
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Timothy P. Argo, SVP, Finance

Good morning. This is Tim Argo, SVP of Finance for MAA. With me are Eric Bolton, our CEO, Al Campbell, our CFO, Tom Grimes, our COO, and Rob DeIPriore, our General Counsel.

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 forward looking statements section in yesterday's earnings 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.

I'll now turn the call over to Eric.

H. Eric Bolton, Jr., Chairman and Chief Executive Officer

Thanks Tim. Good morning and thanks for joining our fourth quarter earnings call.

Overall same store and FFO performances for the fourth quarter were in line with our expectations. Leasing fundamentals and results reflect higher levels of new supply, primarily impacting the higher-end price point properties. Off-setting some of the supply pressure at our higher priced locations has been the steady results captured from our more moderate priced properties located mostly in suburban submarkets and a number of our secondary markets.

MAA's diversified and balanced portfolio strategy is performing as we would expect at this point in the cycle. As we consider 2018 we believe the year will unfold initially with leasing performance much in line with what we've seen over the last couple of quarters, as new supply continues to come on line. However, we continue to believe that based on moderating trends for the permitting of new construction that we are nearing the trough for this cycle and with continued good job growth we expect to capture improving pricing trends as we enter the peak leasing season.

Tom will highlight more details in his comments and while it is of course very early in the year, performance in January is in line with what we expected. January results continued with strong occupancy. In fact daily occupancy in January across the same store portfolio was 40 basis points ahead of the same point last year. Importantly, this strong occupancy provides the support needed for positive pricing traction and we're encouraged that effective pricing in January across the same store portfolio was slightly ahead of the growth rate in January of last year.

Our long established strategy built around a goal of optimizing results over the full cycle continues to deliver solid down side protection to MAA's earnings stream. And with the strengthening of the balance sheet that we've accomplished over the past few years, we're confident not only in the solid support for our various coverage ratios, but importantly we are also well positioned for any compelling investment opportunities that might emerge over the coming year.

We continue to feel that our focus on the strong job-growth Sunbelt region offers the best opportunity for capturing the superior full-cycle results that we're after. The continued strengthening of the economy and the growing appeal of the more affordable region and markets where we focus shareholder capital continue to support our strategy for long-term value creation.

Our development pipeline also continues to deliver new earnings growth at attractive yields. And while both our development portfolio and lease-up properties represent a drag on earnings in 2018, with almost 2,500 units this pipeline will become increasingly productive in 2019. We have a number of other development opportunities that we're currently underwriting, on both existing land sites we own as well as additional new opportunities and would expect to see a couple new projects or so get underway late this year or early 2019.

As described in our earnings release during the fourth quarter we closed on a new acquisition in Nashville in the very appealing West End submarket near downtown. The transaction is typical of the acquisitions we've made over the past few years, namely a property that had previously been under contract, actually in this case, a couple of different times, with a seller that was highly motivated and with a very short close window. We were successful in performing for the seller and closed on the acquisition the last week of 2017. We have several other opportunities under review, but pricing and competition does still remain very robust.

Final steps and activities surrounding the full integration of the MAA and Post operating platforms are underway and we expect to be fully consolidated on the same operating systems and platform later this year. We're making significant progress on the redevelopment opportunities within the legacy Post portfolio and our team plans to accelerate activity on this opportunity in 2018. We continue to feel very good about each of the variables we've previously discussed that drive the long-term value proposition associated with the Post merger.

Before turning the call over to Tom I want to thank all of our associates for their hard work and efforts surrounding the integration that has been completed to date in merging MAA and Post. You've accomplished a lot and great progress has been made. The MAA platform continues to build strength. The long-term value proposition offered by our strategy, the strengthening of our platform and the commitment our team has in generating value for those served by MAA is compelling. We look forward to executing on the growing opportunities in front of us during 2018.

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

Thomas L. Grimes, Jr., EVP, Chief Operating Officer

Thank you, Eric, and good morning everyone. Our operating performance came in as expected. Revenues for the fourth quarter were 1.8% over the prior year with 96.2% average daily occupancy and 1.7% effective rent growth. Expenses increased just 1.3% over the prior year and NOI increased by 2.2%.

Looking at revenue drivers by portfolio in the fourth quarter as compared to the prior year, the legacy MAA portfolio generated revenue growth of 2.6% with 96.3% average daily occupancy and effective rent growth of 2.4%. The legacy Post portfolio had slightly negative revenue growth with 95.8% average daily occupancy and flat effective rent growth. The slight improvement in the overall year over year revenue growth rate from the third quarter to the fourth quarter was the result of the steadily improving occupancy in the legacy Post portfolio.

Expenses continue to be a bright spot for both portfolios. While it takes time for the improvements in revenue management practices and pricing to show up in our revenues, our programs to more aggressively manage operating expenses have shown more immediate results. Including real estate taxes which were up 5.7%, overall expenses for the same store portfolio were up just 1.3% for the quarter. That was driven by improvements in personnel, repair and maintenance as well as property and casualty insurance. We still have room to run with our expense management

programs on the Post portfolio and expect continued progress in 2018. Our operating disciplines are now fully in place and at current run rates the savings will continue.

January results show the benefit of our consolidated platform. Overall same store average daily occupancy in January was 96.3% which is 40 bps higher than prior year. This is driven by a 50 bps year over year improvement in the legacy Post portfolio. Overall same store January blended lease over lease rates are up 1% which is 10 bps better than the blended rents in January of last year. Within the legacy Post portfolio, blended rents in January were up 0.4% and continue to lag the performance from the legacy MAA portfolio where blended rents were up 1.3%. Encouragingly, however, blended rents within the legacy Post portfolio in January were up 130 bps from the blended rents in January of the prior year. While we are facing higher supply pressures in the Post submarkets, the improvements in our operating practices at the legacy Post locations are allowing us to gain ground on year-over-year pricing trends.

Looking forward, our renewal trends are solid. Across the same store portfolio, January lease renewals were up 5.4% with February and March renewal transactions thus far capturing 5.3% growth.

Supply will continue to pressure our new leases. While the jobs-to-completions ratio improves from 6 to 1 in 2017 to 7 to 1 in 2018, the benefit is likely to be felt in the back half of the year. Deliveries for 2018 are front loaded with our markets seeing 52,000 deliveries in the first quarter declining each quarter to about half that amount in the fourth quarter. It is important to remember that in 2017, deliveries were lowest in the first quarter and peaked in the fourth quarter. Said another way, the fourth quarter of 2017 and first quarter of 2018 mark the high point for deliveries in our markets. Job growth is expected to remain robust in our markets at over 2% vs. the national average. Permitting is also improving for our markets, down 4% vs. the same time last year.

Dallas and Austin are facing the most pressure. In 2018 we expect 23,000 deliveries for Dallas and in Austin we expect 7,000 deliveries. We are encouraged that job growth has remained strong in both markets. Dallas job growth was at 2.3% in 2017 and expected to stay at the same strong level. Austin Job growth was 1.6% in 2017 and expected to grow to 2.1% in 2018.

While elevated supply levels moderated rent growth, we are still seeing good rent growth in many markets. Fort Worth, Raleigh, Phoenix, and Richmond stood out from the group.

Renter demand remains steady and move-outs by our current residents continue to remain low. Move outs for the overall same store portfolio were down 6% for the quarter. Move outs to home buying and move outs to home renting were down 10% and 9% respectively. On a rolling 12 month basis, turnover dropped to 50.1%.

As you know, the majority of the legacy Post locations are in the inner loop areas that are seeing the most supply. While this new supply puts pressure on the newer product, it creates opportunity on the older product in these excellent locations. There are 13,000 legacy Post units that have compelling redevelopment opportunities. We can make these great locations more competitive by updating the product. We have room to raise rents and still be well below the rates of the new product coming on line.

Momentum is building on the redevelopment program across the legacy Post portfolio. Through 2017 we have completed 1,700 units. On average we are spending \$8,600 and getting a rent increase that is 12% more than a comparable non redeveloped unit.

For the total portfolio, during 2017 we completed over 8,300 interior unit upgrades. On the legacy MAA portfolio, we continue to have a robust redevelopment pipeline of 10,000 to 15,000 units. On a combined basis with the legacy Post portfolio, our total redevelopment pipeline now stands in the neighborhood of 25,000 units.

As you can tell from the release, our active lease-up communities are performing well. Leasing has gone better than expected at Charlotte at Midtown in Nashville and it stabilized in the fourth quarter ahead of our original schedule.

We are actively leasing Post Afton Oaks in Houston which will stabilize on schedule this quarter. Our remaining pipeline of lease-up properties, The Denton II, Post South Lamar II, Post Midtown, Post River North and Acklen West End are all on track to stabilize on schedule.

2017 was a year of significant change for our organization. We started 2017 with two completely different operating platforms and teams. We are pleased that the bulk of the integration work of the Post portfolio is now behind us. We are starting 2018 with a much more aligned and cohesive operating platform and team. We are looking forward to continuing to capture value creation opportunities on both the revenue and expense sides of the equation as we finalize full integration activities in 2018.

Albert M. Campbell, III, EVP, Chief Financial Officer

Thank you Tom and good morning everyone. I'll provide some additional commentary on the company's fourth quarter and full-year earnings performance, balance sheet activity, and finally on initial guidance for 2018.

Net income available for common shareholders was \$1.08 per diluted common share for the quarter. FFO for the quarter was \$1.50 per share. Fourth quarter performance includes \$0.03 per share of non-cash income from the valuation of the embedded derivative related to the preferred shares issued in the Post merger. Excluding the impact of the embedded derivative, earnings results for the fourth quarter were essentially in-line with our expectations.

Net income available for common shareholders was \$2.86 per share for the full-year of 2017. FFO for the full-year was \$5.94 per share, which includes \$0.07 per share of non-cash income related to the preferred share valuation offset by \$0.17 per share of merger and integration costs during the year. AFFO for the full year was \$5.30 per share, which supported a healthy 66% dividend payout ratio, well below the sector average.

During the fourth quarter, we acquired one community for \$72 million and sold two communities for \$97 million in gross proceeds, completing our capital recycling plans for the full year. Total book gains of \$68 million were recognized related to the dispositions during the fourth quarter.

For the full year, we acquired two communities for a combined total investment of \$134 million, and sold five communities for combined gross proceeds of \$186 million, which produced an average 15% leveraged IRR for the disposition portfolio. These sales also produced \$127 million of recorded book gains, and \$132 million of combined tax gains for the year, which were deferred with 1031b transactions or covered with other tax planning methods, eliminating any special dividend requirement for the year.

During the fourth quarter, we completed two development communities on plan. Both were expansions of current communities, located in Austin and Kansas City, which are now included in our lease-up portfolio. During the quarter, we also funded \$28 million of additional development costs, bringing total development funding for the year to \$170 million. Our development pipeline at year-end now contains three communities with a total estimated cost of \$214 million, of which only \$46 million remains to be funded as of year-end. We expect NOI yields to average 6.3% on these development communities once completed and stabilized.

Our lease-up portfolio now contains five communities totaling 1,538 units, including the community acquired in lease-up during the quarter, with average occupancy for the group of

62.5% at quarter end. We expect to stabilize one of the communities in the first quarter of 2018, three during the second half of the year, and the final community early next year.

Our balance sheet remains in great shape at year-end. During the fourth quarter, we paid off \$130 million of secured debt as well as \$18 million of maturing unsecured notes with our line of credit. At quarter-end, our leverage, as defined by our bond covenants, was only 33.2%, while our Net Debt was just over 5.0 times Recurring EBITDA. At quarter-end, 83% of our debt was fixed or hedged against rising interest rates, with well laddered maturities averaging 4.7 years. We also had almost \$600 million of combined cash and borrowing capacity under our unsecured credit facility.

Finally, we are providing initial earnings guidance for 2018 with the release (detailed in our supplemental information package). We're providing guidance for net income per diluted common share, which is reconciled to FFO and AFFO in the supplement. We're also providing guidance on other key business metrics expected to drive performance for 2018, a number of which were outlined in our recent Investor Day presentation provided at NAREIT.

Net income per diluted common share is projected to be \$1.78 to \$2.08 for the full year 2018. FFO is projected to be \$5.85 to \$6.15 per share, or \$6.00 per share at the midpoint, which includes \$0.08 per share of final merger and integration costs related to the Post merger. AFFO is projected to be \$5.24 to \$5.54 per share, or \$5.39 at the midpoint.

The primary driver of 2018 performance is same store NOI growth, which is projected to be 2.0% to 2.5% for the full year, based on 1.75% to 2.25% revenue growth and 1.5% to 2.5% operating expense growth. Our revenue projections include continued strong occupancy levels through 2018 (ranging 95.75% to 96.25%), combined with projected average blended rental pricing on new leases and renewals in the 2.25% to 2.75% range for the full year. We expect revenue performance to begin the year near the bottom of our range and improve over the course of the year, as we expect supply pressure to moderate. We generally expect modest growth in operating expenses for 2018, with real estate taxes continuing to produce the only area of expected pressure. Though below the prior year level of growth, real estate taxes are expected to increase in the 3.5% to 4.5% range for the year.

We project acquisition volume to range between \$300 and \$350 million for the year, including several lease-up deals. Given the significant recycling of assets over the last several years, we aren't currently planning for any dispositions in 2018.

We expect to end 2018 with our leverage around 34% on a net-debt-to-gross assets basis, well within our long-term range. Also, another important consideration for 2018 is our projected average effective interest rate range of 3.8% to 4.0%, which is about 45bps to 50bps above the prior year at the mid-point which represents about \$0.18 per share impact to earnings. Nearly half of this projected increase is the impact of rising short-term interest rates on our variable rate debt, based on three interest rate increases by the Fed over the course of 2017 and our projection of three more during 2018. Declining interest capitalization as we complete the construction of the development pipeline produces another portion of the increase (about 1/4th), with the declining mark to market adjustment related to debt acquired from the Colonial and Post mergers producing the remaining portion of the increase for 2018.

Our guidance also assumes we incur final integration costs of \$8 to \$10 million, as we complete our systems integrations related to the recent Post merger, and that our total gross overhead costs (G&A and Property Mgmt Expenses combined) will range between \$89.5 to \$92.5 million, fully reflecting our planned \$20 million of overhead synergies, as compared to the combined stand-alone company costs projected for 2018.

Though we expect continued volatility related to the valuation of the preferred shares acquired with the Post merger, our projections do not include any valuation adjustments, as these adjustments are both non-cash and impractical to accurately predict.

That's all we have in the way of prepared comments, so Savannah we will now turn the call back to you for questions.