



## CONFERENCE CALL TRANSCRIPT: 2Q2015

July 30, 2015 9:00 AM CDT

### **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.

MAA posted strong second quarter results with same store NOI increasing 7.5% over the prior year, generating Core FFO per share of \$1.36, which is a record performance for the company. I attribute the strong results to three factors:

First, the demand for apartment housing is strong across our high growth region. The steady improvement in employment conditions, coupled with the surge in new rental household formations, are more than off-setting the higher levels of new supply. We feel that our approach of diversifying capital across a number of

markets in the high growth Sunbelt region, coupled with also diversifying the portfolio across suburban, inner loop and a growing number of more urban locations provides a more balanced platform that is better positioned for deflecting new supply pressure. It's worth noting that the 5.3% revenue growth captured this quarter from our secondary market segment of the portfolio is the strongest performance we've seen since the third quarter of 2011 and we're encouraged with the trends that we're seeing.

Secondly, our strong Q2 performance reflects various opportunities and synergies harvested from our merger with Colonial Properties. The 60 basis point improvement in same store NOI margin reflects improvements in revenue management practices and unit turn efficiencies within the legacy Colonial portfolio, as well as a number of opportunities driven by the larger scale of the company. As we've noted for the last couple of quarters, now that we've completed a full year of harvesting merger related operating benefits, and while there are some additional opportunities left to squeeze, there will be some year-over-year moderation from merger lift taking place over the back half of this year. However, it's important to note as outlined in our earnings guidance, we certainly expect to sustain the merger benefits that have been captured to date and retain the momentum in both improved occupancy levels and pricing trends that have been achieved.

And thirdly, our strong Q2 results and positive momentum reflect the growing benefits of the significant capital recycling that we've accomplished over the past few years. It's worth noting that MAA's same store NOI margin, after routine capital spending, has improved 570 basis points over the past five years. As we've steadily recycled capital from some of our older investments into newer and higher cash flow margin properties, which has also resulted in recycling capital into markets providing better long-term growth prospects and opportunity for enhanced operating efficiency, we've made a meaningful improvement in the cash flow growth prospects of our same store portfolio.

So on balance it was a good quarter, but more importantly, the trends that drove the great results are variables that we expect to hold onto and further improve.

On the transactions front our activity so far this year clearly reflects the environment that favors harvesting value from non-core investments, while requiring a lot of patience and discipline on the capital redeployment side of the equation. The pricing achieved on our planned asset sales for the year exceeded our expectations and resulted in strong investment returns for shareholder capital.

During the second quarter we initiated two new development projects in Orlando and in Charleston which are highly accretive expansions of existing communities, and closed on two new acquisitions located in Scottsdale and Richmond. The transaction market continues to be very active and we are underwriting quite a

few deals. However, acquiring properties on a basis that meet our investment hurdles remains a challenge. We continue to see some pretty aggressive pricing paid on both stabilized and pre-stabilized properties, with new development opportunities also requiring increasingly optimistic or aggressive assumptions. Accordingly, as noted in our updated guidance, we've slightly lowered our anticipated acquisition volume for this year. I continue to believe that we'll see some increasing opportunities for redeploying capital on an attractive basis as we move later into the cycle. Meanwhile, we will continue to stick to our disciplines and actively work the market looking for the unique opportunities that fit our parameters.

In summary, we like where the portfolio is now positioned and believe that we are well balanced to take advantage of the favorable leasing conditions across our high growth region. The operating platform is strong, more efficient and our property and asset management team is performing at a high level. Our redevelopment program continues to deliver strong value growth and the pipeline of new development and lease-up properties will generate attractive new growth in 2016. The balance sheet is in a strong position and we're excited about what I believe will be increasing opportunities to capture new growth as we work into 2016.

That is all I have and Tom will now give you some more details on our operating results for the quarter.

### **Tom Grimes**

Thank you Eric and good morning everyone. Our record results were driven by an increase in revenue per occupied unit of 5.3% up to \$1,100 and a 100bps increase in average physical occupancy. July trends continue to be steady. Our 60 day exposure, which is current vacancy plus all notices for a 60 day period is just 7.1% down 130bps from the same time last year. July blended rents on a lease over lease basis are up 5.6% or 20bps better than the same time last year.

The great results for the quarter pressured our personnel expenses as more of our property level teams are on track to meet their performance based compensation targets. Personnel costs less incentives were up just 3.7%. Property taxes also pressured expenses up 7% as municipalities, particularly in Texas, were aggressive in their valuations.

The benefits of our strong operating platform on the legacy Colonial communities continues to pay dividends. The more robust approach of our revenue management practices has allowed the Colonial communities to capture rent growth more than 180bps above their market peers. Our long term focus on average days vacant applied to this group brought the portfolio average down 20% for the quarter and to 22.8 days for the month of June.

On the market front, the vibrant job growth of the Large Markets is driving strong revenue results. In this group, 11 of our 13 markets had at least 6% revenue growth. Large market leaders included: Atlanta (10%), Orlando (8.6%) Austin (7%) and Raleigh (6.9%). The Secondary Markets, which have lower supply pressure, achieved 5.3% revenue growth. In these markets we also benefited from improved job growth, Colonial operating improvements and the advantage of a robust REIT operating platform in markets that don't see many REIT caliber platforms. Notable Secondary Market performers included: Charleston (8.0%), Savannah (6.8%), Greenville (6.7%) and Jacksonville (5%).

Turnover for the same store portfolio was again down for the quarter by -2.4%. On a twelve month rolling basis turnover is a low 53.6%. Move-outs to home buying were just 19.5%, well below historic norms. Move-outs to home rentals were down 14.5% and represent less than 8% of our total move-outs.

Year to date we have completed 2,400 redevelopment units, 1,400 were on legacy Colonial communities. We are on pace to renovate 4,000 units again this year and expect the mix to favor the legacy Colonial portfolio. As a reminder, on average we spend approximately \$4,300 per unit and receive \$95 rent increase over a comparable non renovated unit, which generates a year one cash return of over 20%.

On our last call we mentioned to you that we were ranked as the number one REIT in online customer service reputation by J. Turner Research. During the second quarter the same organization rated the top 50 operators of multifamily units and we earned a number one rating in that group as well. A focus on the customer is not a new idea at MAA. This is a result of our sophisticated customer service approach as well as our long term cultural focus on creating a home for our residents rather than just a place to live. We feel the results speak volumes about our team's ability to create value for our customers which is one of the key drivers of our ability to deliver steady long term performance for our shareholders.

## **Al Campbell**

Thank you Tom, and good morning everyone. I'll provide some additional commentary on the company's second quarter earnings performance, balance sheet activity, and our revised guidance for the full year.

FFO for the second quarter was \$112.4 million, or \$1.41 per share. Core FFO, which excludes certain non-cash and non-routine items was \$108 million, or \$1.36 per share, as compared to \$93.9 million or \$1.18 per share for the prior year, which is \$0.07 above the mid-point of our previous guidance, and represents a 15% growth over the prior year.

Recurring capital expenditures for the quarter were \$21.9 million, or \$0.28 per share, which produced Core AFFO for the second quarter of \$86.1 million, or \$1.08 per share, compared to the quarterly dividend rate of \$0.77 per share.

As Tom discussed, we were pleased with the strong operating performance for the quarter, which produced the majority of the favorability to our forecast, as pricing, occupancy levels, and fee income were all above our quarterly projections.

During the second quarter we acquired two new communities for a combined purchase price of \$111.3 million, bringing our total acquisition investment for the year to approximately \$158 million for three new properties.

During the second quarter, we also sold fourteen older communities for gross proceeds of \$180 million, and recorded book gains of \$105 million. Immediately following the end of the quarter, we closed on the sale of three additional older communities for gross proceeds of \$121 million, and expect to record additional book gains of approximately \$54 million during the third quarter. These sales complete our full year disposition plans, with 21 properties averaging 25 years of age being sold for \$354.3 million, representing a 5.8% economic cap rate (based on last twelve months' NOI, less a 4% management fee and actual capex). Notably this cap rate is only 30bps above the expected stabilized cap rate on the three new properties acquired thus far this year.

We also continued to make progress on our development plans during the quarter. We completed construction on an expansion of a community located in Nashville, and as Eric mentioned we began construction on two additional expansion opportunities, in Charleston and Orlando. The total construction costs for the four communities currently under development is expected to be \$118.8 million, of which only \$63.7 million remains to be funded at quarter end.

We have three communities, totaling 799 units, currently in lease-up with average occupancy of 76.6% at quarter-end. We expect all three of these communities to be stabilized by the first quarter of 2016.

At the end of the second quarter our balance sheet remains in great shape. Our total debt to market cap was 37%, our fixed coverage ratio was over 4 times, and our Net-Debt-to-Recurring EBITDA was 6.0 times. Over 70% of our assets are unencumbered, and over 92% of our debt is fixed or hedged against rising interest rates. We have about \$300 million of debt maturities later this year (primarily in the fourth quarter), which we currently expect to refinance with unsecured senior notes. In anticipation of this financing we have pre-locked the interest rate on \$100 million using forward interest rate swaps.

We expect the proceeds from our asset sales along with the additional \$80 to \$85 million of internal "free cash flow" produced this year to fully fund our

acquisition and development needs. Our current plans do not include a need for new equity this year. At quarter end, we had over \$360 million of total cash and credit available under our line of credit, supporting our liquidity, and we expect to end the year with our leverage (defined as Net Debt-to-Gross Assets) between 41% and 42%, below 42.6% reported at the end of 2014.

Finally, due to the strong operating performance and capture of benefits from the Colonial merger over the first half of the year, we are raising our guidance for Core FFO and AFFO for the full year. We're now projecting Core FFO for the full year to be \$5.25 to \$5.41 per share, or \$5.33 at the mid-point, representing a 6.8% growth over the prior year. Core AFFO is now projected to be \$4.60 to \$4.76 per share, or \$4.68 at the mid-point, representing a 9.3% growth from the prior year. Notably the expected AFFO growth rate is 250bps higher than the FFO growth rate, as we begin to see the asset recycling program impact our capital spending.

Same store NOI growth is now expected to be 4.5% to 5.5%, based on revenue growth of 4.5% to 5.5% and expense growth of 4% to 5%.

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