CONFERENCE CALL TRANSCRIPT: 3Q2016

October 28, 2016 8:30 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.

I'll now turn the call over to Eric.

Eric Bolton

Third quarter results were at the top end of our guidance as solid same store results, which were captured against a record occupancy performance of last year, coupled with favorable trends in G&A and interest expense, drove Core FFO per share of $1.49 representing an 8% jump as compared to Q3 of last year. As outlined in our earnings release, we have raised full year guidance for Core FFO to a range of $5.86 to $5.96 per share.

We continue to capture solid leasing trends across the portfolio. Average daily occupancy within the same store portfolio in the third quarter was a very strong 96.4% compared to the likewise very strong 96.5% occupancy in Q3 of last year. Effective rent per unit increased 4.2% with higher performances coming from Orlando, Tampa, Atlanta, Charlotte and Fort Worth.

As noted in our release we were successful in closing two acquisitions during Q3, one in Houston and one in Greenville, SC. Both transactions are newly constructed properties and represent compelling long-term investment opportunities for those two markets. We also were successful in completing the disposition of seven older properties in the third quarter as part of our efforts to steadily recycle capital to protect and enhance MAA's long-term earnings profile. Additionally, we currently have five other properties under contract for disposition and expect to close on these transactions in the fourth quarter.

Our merger with Post Properties is making good progress. Both companies have shareholder meetings scheduled for November 10th and we anticipate a closing of the merger effective December 1st.

Processes associated with integration of the two companies are well underway with the go-forward organization structure and team members now in place. As outlined in our announcement of the merger, we anticipate that upon completion of integration activities by the end of 2017, we expect to capture overhead synergies of $20 million. The specific line items and decisions associated with capturing this opportunity have been identified and we remain very confident in achieving this performance benchmark.

As we continue to engage in the more detailed tasks surrounding the integration of the two companies we remain very enthused and confident about capturing the improved operating margins and NOI lift from the legacy Post portfolio that is important to the overall value proposition of the merger. Our work to date associated with inventorying and comparing the more detailed operating practices of the two platforms, further assessing opportunities surrounding our larger scale and enhanced market efficiencies and evaluating the redevelopment opportunities, all combine to have us also feeling very confident about this aspect of the value proposition. We will begin to lay out more details upon closing the merger and as part of providing our initial guidance for calendar year 2017.

Before turning the call over to Tom I want to express my appreciation and thanks to the associates working at both MAA and Post for their hard work and great support during the past few weeks as we have worked through the difficult task of merging the organizational structures and preparing for consolidated operations, while also taking care of our residents and existing operations. Our newly combined company will have a number of strong attributes that position us well for the future. The professionalism and dedication that our combined team of associates demonstrates each day are key among these qualities.

Tom Grimes

Thank you Eric and good morning everyone. Our second quarter NOI performance of 3.7% was driven by revenue growth of 3.6% over the prior year. Revenues were up 1.5% sequentially, which is 30 bps higher than the sequential change last quarter. We have good momentum in rents as all in place effective rents increased 4.2% from the prior year. In the third quarter, new rents and renewal rents executed during the quarter increased 4.3% on a blended lease over lease basis. We achieved 96.4% average daily occupancy which is strong on an absolute basis but slightly lower than last year's record performance.

Fourth quarter trends continued the positive momentum. October's average daily physical occupancy of 96.1% is in line with October of last year. Our 60 day exposure, which is current vacancy plus all notices for a 60 day period is just 6.6%, below prior year by 55bps. New and renewal rents have built on the strong trends of the third quarter. On a blended lease over lease basis, October rents have increased a seasonally strong 3.3%.

On the market front, the vibrant job growth of the large markets is driving strong revenue results. They were led by Fort Worth, Orlando, and Atlanta.

The secondary markets continued to close the effective rent growth gap with the large markets. Since the third quarter of 2015, the rent growth gap between large and secondary markets has narrowed 80bps. Revenue growth in Jacksonville, Charleston and Memphis all stood out.

As mentioned, momentum is strong across our markets with occupancy, rent growth and exposure all showing positive trends. Our only market worry bead is Houston which represents just 4% of our current portfolio. It's worth noting that Houston will drop to less than 4% of NOI after the merger. We continue to closely monitor and protect occupancy in this market. As we approach the end of October, Houston's average daily occupancy is 95.9% and 60 day exposure is just 6.1%.

Our customer base remains stable. Move-outs for the portfolio were down for the quarter by 1.4% over the prior year and turnover remained low at 51.3% on a rolling twelve month basis. Move-outs to home buying remained at 20% of total move-outs. There was also little change in move-outs to home rental, which represents just over 7% of move-outs.

During the quarter we completed over 2,400 interior unit upgrades, bringing our total units redeveloped this year to just over 5,400. Our pre-merger redevelopment pipeline of 15,000-20,000 units remains robust. As a reminder, on average we are spending about $4,500 per unit and receiving average rent increases of approximately $100 over a comparable non-renovated unit, generating a year one cash return of well over 20%. Work is underway defining the scale and scope of redevelopment opportunity from the Post portfolio. Indications are that it will be a significant value creation opportunity. We are excited about adding units from the Post portfolio to our redevelopment pipeline.

Our active lease-up communities are performing well. Station Square at Cosner's Corner II and Cityscape at Market Center II both stabilized on schedule in the third quarter. Rivers Walk II will stabilize on schedule in the fourth quarter. Colonial Grand at Randal Lakes II in Orlando is 30% leased and on schedule to stabilize at the end of next year. Our three new acquisition communities in Tempe, Greenville and Houston are all on track.

We are pleased with our progress thus far on the Post merger. The operating structure of the combined companies has been finalized and communicated. There is a high degree of overlap in both systems and markets. We have enjoyed meeting the Post onsite teams and believe that adding these solid teams as well as excellent product and locations to our operating platform will create value for all of our stakeholders.

We are in good shape for Q4 and set up well for 2017.

Al Campbell

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

Net income available for common shareholders was $1.12 per diluted common share for the quarter. Core FFO for the quarter was $1.49 per share, which represents an 8% increase over the prior year. This performance was $0.04 per share above the mid-point of our previous guidance. Our same store performance continued to be solid, in-line with our expectations. About half of the outperformance, or $0.02 per share, was related to the favorable impact from the timing of our planned bond deal, previously projected for the third quarter, which has been postponed until early next year due to our merger activity (will discuss more on that in a moment). An additional penny per share is related to the timing of our transaction activity during the quarter, and the final penny per share is related to favorable G&A expenses for the quarter.

As Eric mentioned, we acquired two new communities during the third quarter. We invested a total of $133 million for these two new communities, bringing our total acquisition volume year-to-date to $264 million. We also sold seven communities, averaging 22 years of age, during the quarter for gross proceeds of $152 million, which represented a 6.3% cap rate. We also exited two additional secondary markets with these sales, Winston-Salem and Greensboro, NC. Our plans for the year include selling an additional five communities, which are expected to close during the fourth quarter.

We completed one community during the quarter, River's Walk phase II in Charleston, and we had three communities, all expansions of current properties, remaining under construction at the end of the quarter. We funded $13 million of construction costs during the third quarter, and have an additional $33 million to be funded on the existing pipeline. We continue to expect average stabilized NOI yields of about 7.5% for these communities once completed and stabilized.

During the third quarter, we paid off $75 million of maturing public bonds, which we expect to refinance as part of a public bond offering early next year. Also during the third quarter, Fitch upgraded our senior unsecured rating to BBB+ (stable outlook) and S&P placed our ratings (at BBB) on positive Credit Watch to reflect the anticipated increased strength of the balance sheet from the announced Post transaction. Given the merger announcement and related activities, we have postponed our original plans for a bond deal late this year in order to allow the merger to close, which we expect to provide support for a financing early next year.

Our balance sheet remains in great shape at quarter-end. Our leverage, defined as Net Debt to Gross assets, was 39.7%, 100bps below the prior year, while our Net Debt was only 5.6 times Recurring EBITDA. At quarter-end, 89% of our debt was fixed or hedged against rising interest rates at an average effective interest rate of only 3.9%, with well laddered maturities averaging 4.1 years. At quarter end, we had almost $570 million of combined cash and borrowing capacity under our unsecured credit facility providing both strength and flexibility. Given our current expectations for acquisitions and dispositions over the remainder of the year, along with our projection for excess cash, we do not expect any new equity needs (other than the shares issues for the merger transaction) this year. Also, we expect our leverage to decline upon the closing of the merger with Post, ending the year in the mid 30's as a percent of Gross Asset value.

Finally, as Eric mentioned, we are again increasing our earnings guidance for 2016 due to the stronger than projected performance. We're increasing our Core FFO projection by $0.06 per share at the mid-point, to reflect both the $0.04 per share third quarter outperformance and $0.02 per share for our revised expectations for the remainder of the year. We expect interest expense for the fourth quarter to be about $0.03 per share favorable due to the delayed timing of the planned bond deal, offset by about $0.01 per share of costs relating to clean-up from Hurricane Matthew. We were very fortunate to avoid significant damage from this recent storm, but we will incur some costs during Q4 for repairs and clean-up.

Core FFO is now projected to be $5.86 to $5.96 per share, or $5.91 at the mid-point, based on average shares and units outstanding of about 79.7 million. Core AFFO is now projected to be $5.16 to $5.26 per share, or $5.21 at the mid-point. The major components of our guidance, including same store growth, transaction and financing assumptions, remain similar to our prior guidance, with the one exception of the bond deal timing, as discussed.

As mentioned in our release, given the merger transaction is not yet approved, this guidance does not reflect the anticipated impact of the transaction. If the transaction closes as planned, we expect to end the year within this current guidance range, although near the lower end given the initial dilution expected from the merger transaction. We expect to provide guidance for 2017 and more details regarding the merger transaction with our fourth quarter press release. As discussed during our merger announcement call, we plan to capture synergies and additional earnings opportunities from the merger with Post that will recapture the initial dilution from the transaction over the first 12 to 18 months, and what we have seen thus far continues to support expectations. We plan to outline this further with our fourth quarter release.

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