CONFERENCE CALL TRANSCRIPT: 3Q2019
October 31st, 2019 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, Rob DelPriore, our General Counsel, Tom Grimes, our COO, and Brad Hill, EVP and Head of Transactions.

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. A presentation of the most directly comparable GAAP financial measures, as well as reconciliations of the differences between non-GAAP and comparable GAAP measures, can be found in our earnings release and supplemental financial data, which are available on the "For Investors" page of our website at www.maac.com.

I'll now turn the call over to Eric.

Eric Bolton

Thanks Tim. I appreciate everyone participating in our call this morning.

Performance during the important third quarter leasing season was strong with continued solid momentum in rent growth and high occupancy. Reflecting strong demand across our Sunbelt markets and the great work performed by our on-site associates, resident turnover remains at historically low levels despite lease renewal pricing that continues to run above 6%. We believe that at this point in the cycle our best strategy remains a focus on pushing rent growth. We're happy with the performance on rent trends and are encouraged with the momentum that we'll carry into next calendar year.

While we are currently in the process of compiling a detailed outlook surrounding the new supply pipeline in 2020 and the impact at each of our locations, at this point we expect the elevated new supply levels will likely persist in 2020. There is simply too much capital available to developers at this point to expect any sort of meaningful pull back. However, I also believe it is unlikely that we will see new supply levels pick up from current trends, as rising costs among other things will keep new development from accelerating. As we finalize our property specific budgeting process, I am sure we will have markets that will likely experience some increase in new supply next year and some markets that will experience a decline in new deliveries. We will have more to report on our specific expectations for 2020 surrounding new supply when releasing fourth quarter results, but at this point, we do not have any heightened concerns surrounding next year's leasing environment. And while new supply remains elevated, we continue to see strong demand fueled by job growth across our markets with growing population shifts and increased migration to the Sunbelt.

We closed on the disposition of a property located in the Little Rock, Arkansas market during October and expect to close on the sale of the four remaining properties in that market before year-end. Based on current contract pricing we expect to capture a 5.4% cap rate on this portfolio of properties that has an average age of 21 years.

We are currently negotiating several one-off property acquisitions and are hopeful that we will close on one or more of these deals by year-end. As has been the case over the past few years, each of the opportunities we are underwriting are new properties in initial lease-up. The acquisition market remains very competitive, but we continue to see a high volume of lease-up transactions and expect that we will have some success with acquisitions over the next few months.

As noted in our supplemental schedules to the earning release, we now have six new development projects underway and expect to start an additional two projects, located in Orlando and Houston, before year-end.

And, finally, we continue to capture great performance out of our redevelopment pipeline. In addition to our very earnings accretive unit-interior upgrade program, we are planning to initiate in calendar year 2020 more extensive redevelopment efforts at several of the legacy Post property locations. We believe our expanding focus on redevelopment initiatives will generate very accretive returns on capital and further boost earnings growth from our existing asset base over the next few years.

I want to send a big thank you to our team of associates for their work and great results over the busy summer leasing season. We are building positive momentum across multiple fronts of our platform and I appreciate all the hard work and great progress.

I'll turn it over to Tom, now.

Tom Grimes

Thank you Eric and good morning everyone. Our operating performance for the third quarter was strong and exceeded our expectations. With the steady demand for apartments and our enhanced platform, we have continued momentum in rent growth, strong average daily occupancy and improving trends.

Same store effective rent growth per unit was 3.9% for the quarter. This is the sixth straight quarter of year over year improving ERU growth. As a result, our year-over-year same store revenue growth was 4%, the highest it has been since 2016. Revenue also increased 200 bps sequentially. The acceleration in revenues was widespread across our markets. The year-over-year revenue growth rate for the third quarter exceeded the year over year growth rate of the second quarter in 16 of our 21 markets.

Revenue performance was led by steady momentum in blended new and renewal lease pricing, up 4.9% for the quarter, which is 190bps better than this time last year. The improvement in blended pricing seen in Atlanta, Austin, Nashville and Dallas was particularly impactful.

In addition to the great traction in blended lease over lease pricing, average daily occupancy during the quarter remained strong at 96.1%.

Same store operating expenses were in line with our guidance but higher than they have been recently. As we have mentioned on prior calls, we have captured the benefits of the improved expense management platform on the Post portfolio, the comparisons are now more normalized, and year to date expense growth is now 3%. As a reminder, our annual operating expense growth rate since 2012 has been just 2.4%, well below the sector average. This is reflective of our long-term focus on driving efficiencies into our operation.

The favorable same store trends continued into October. As we have discussed, we feel that in this part of the cycle when demand is strong we should prioritize rent growth over higher occupancy. Average daily occupancy for the month was strong at 95.6% as compared to 96.1% in October of last year. October's blended lease over lease rents are up 4% month to date, which is well ahead of the 2.2% blended rent growth posted in October of last year, and will support continued momentum in effective rent growth for the portfolio, which is important for steady and sustained revenue growth.

On the redevelopment front, in the third quarter we completed about 2,700 units, which keeps us on track to redevelop about 8,000 units in 2019. This is one of our best uses of capital. On average year to date, we spent $5,700 per unit and achieved an additional 10% in rent, generating a year one cash on cash return in excess of 20%. Our total redevelopment pipeline now stands in the neighborhood of 14,000 to 15,000 units.

Our technology platform continues to expand. Our overhauled operating system and new website have aided our ability to attract, engage and create value for our residents. The results are evident in our blended pricing traction. Our tests on SmartHomes are going well. The technology has been installed at 15 communities with minimum disruption and has been well received by our residents. We are also exploring a range of AI, Chat, Customer Resource Management and prospect engagement tools.

Our teams have handled the busy season very well and have us well positioned to move forward. We are pleased to have the integration work of 2017 and 2018 in the rear view mirror. We are encouraged with the momentum in rent growth and excited about the opportunities ahead.

Al Campbell

Thank you Tom and good morning everyone. I'll provide some brief commentary on the company's third quarter earnings performance, balance sheet activity, and finally on our updated guidance for the remainder of the year.

Reported FFO per share of $1.72 for the third quarter included a couple of significant "non-core" items outlined in the release, which added $0.16 per share of non-cash earnings to FFO. Excluding these items, FFO for the quarter was $1.56 per share, which was $0.01 per share above the mid-point of our guidance and analyst consensus.

This outperformance was primarily the result of continued favorable pricing trends, as outlined by Tom, which produced the acceleration in total revenue growth for the quarter. Overall operating expenses also remained well under control with real estate taxes and repair and maintenance expense producing the primary areas of pressure for the quarter. These were offset by reductions in marketing and moderation in personnel costs. We expect real estate taxes to continue producing some expense pressure for the year, as aggressive final valuations recently received in certain markets will produce RE tax expense growth near the top end of our range outlined for the full year (4.25% to 5.25%). Repair and maintenance expenses for the third quarter were impacted by difficult prior year comparisons, but are projected to increase in range of 3.25% to 3.5% for the full year.

We continued to make progress on our development and lease-up portfolio during the quarter, funding $31 million toward the completion of our current pipeline. This brings our year to date funding to $72 million, with $125 to $150 million total projected for the full year.

During the third quarter we were fairly active on the financing front. We re-opened the bond series initially issued in February to issue an additional $250 million of unsecured notes at an effective interest rate of 2.9% over the remaining term of about 10 years. We used the proceeds to pay off a $150 million variable rate term loan which was due early next year, utilizing this low rate environment to fix more and extend the maturity of our debt portfolio which is seven years on average. The remaining proceeds were used to pay down our line of credit balances at the end of the quarter.

Finally, we are increasing both our FFO and same store guidance for the full year to reflect the strong third quarter performance. We're now projecting FFO per share for the full year to be in a range of $6.46 to $6.54 per share, or $6.50 at the mid-point, which includes the $0.16 of third quarter net favorable "non-core" items and $0.02 per share related to the fourth quarter land sale gain mentioned in the release. Our updated fourth quarter guidance assumes no further impact from the preferred share valuation or activity from the unconsolidated affiliate. We are now projecting our same store revenues, expenses, and NOI to all grow in the range of 3.0% to 3.5% for the full year, which produces a 25bps increase in our SS NOI expectations for the full year, at the mid-point. This adds an additional $0.02 per share to the full year FFO (Q3 and Q4 combined), which is partially offset by a penny per share reduction for the year related to G&A and Interest expense changes combined.

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