



## CONFERENCE CALL TRANSCRIPT: 1Q2016

May 5, 2016 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**

As detailed in our earnings release, MAA started 2016 with solid first quarter operating results that were ahead of expectations. Average daily physical occupancy at 96.2% and effective rent growth at 4.5% drove same store revenues higher than forecasted. We expect the solid momentum in leasing across our portfolio to continue over the balance of the year.

As Tom will outline in his comments, in the first quarter our properties continued to post low resident turnover, strong occupancy and captured solid pricing performance. Importantly, we enter the busy summer leasing season with the portfolio well positioned to take advantage of the favorable leasing conditions.

Given the strong start to the year, we have raised the mid-point of our earnings guidance for Core FFO for the full year to \$5.81 per share.

Investor interest in apartment real estate remains high across our markets and we continue to find the acquisitions environment challenging, with pricing reflecting strong demand from private and institutional buyers. Cap rates continue to hold up despite a higher volume of new supply coming into the market. Our deal flow and transaction pipeline is more robust than we've seen over the last couple of years and we're certainly underwriting a higher volume of opportunity, but seller pricing expectations have been hard for us to support. We continue to believe that as we work later into the cycle we will likely find more opportunities that meet our underwriting criteria. Until then, we plan to remain disciplined and deploy capital only when we are comfortable with the value proposition and earnings accretion to be captured.

As AI will recap, our balance sheet remains in a very strong position and we continue to build capacity for future growth. As noted in our earnings release, Moody's recently moved MAA's current Baa2 rating to a positive outlook. We believe our established record of producing steady value growth and strong operating performance, coupled with credit and coverage metrics that are stronger than at any point in our company history, has MAA well positioned to continue to build on long-term competitive advantages across our footprint.

After several years of strong operating performance, questions surrounding the sustainability of the current leasing environment is certainly a hot topic. Based on what we are experiencing across our portfolio, which is diversified across urban, inner loop, suburban and satellite city sub-market locations, in both Large and Secondary markets, demand does not appear to be weakening and all indications are that we will continue to capture good leasing velocity over the next few quarters. Conversations with a number of developers suggest that construction financing is becoming increasingly harder to secure, and those pressures coupled with much higher land and construction costs, are raising the bar to justify new starts. It's worth noting that new construction permitting across our markets is down so far this year compared to the trends we've seen over the last two years. We continue to believe that new supply trends are unlikely to materially disrupt the positive momentum for apartment leasing. Across our portfolio, the outlook for the ratio of new job growth to new apartment deliveries actually improves in 2017 as compared to this year. And while our crystal ball is certainly no better than anyone else's, and I do still believe our business retains cyclical patterns, it is difficult to see any sort of near-term significant deterioration of leasing fundamentals. While our occupancy comparisons get harder in the back half of the year, given the essentially full occupancy status of the portfolio last year, the rent trends remain encouraging.

So, overall, our focus for the balance of year remains centered on taking full advantage of the great operating fundamentals to drive earnings and build

platform strength and capacity, while remaining very active in the transaction market and disciplined in our assessment of new growth opportunities.

Before turning the call over to Tom, I want to thank our MAA associates for their focus and hard work in preparing for the upcoming busy summer leasing season. You have the portfolio well positioned and I very much appreciate all of your hard work and great results.

### **Tom Grimes**

Thank you Eric and good morning everyone. Our fourth quarter NOI performance of 7.1% was driven by revenue growth of 5.5% over the prior year and 1.1% sequentially. We have good momentum in rents and saw effective rents increase 4.5% on a year over year basis. Strong average physical occupancy contributed 60bps of revenue over the prior year.

Overall expenses remain in line, up just 2.9%. Expense discipline has been a hallmark of our operation for years. Our industry leading initiatives such as our vendor owned inventory shop stocking program, which will be completed this year, have allowed us to keep the expense line consistently in check.

April demand trends continue the positive momentum. Average physical occupancy of 96.2% ran 40 bps ahead of last year. Our 60 day exposure, which is current vacancy plus all notices for a 60 day period is just 8.2%, in line with the same time last year. April blended rents on a lease over lease basis are up 4.8%. Occupancy, exposure and pricing are all in good shape as we head into our summer leasing season.

On the market front, the vibrant job growth of the large markets is driving strong revenue results of 5.9%. They were led by Orlando, Fort Worth, Atlanta and Charlotte.

The secondary markets achieved 4.6% revenue growth. In these markets we are benefiting from improved job growth as well as a sophisticated operating platform that has competitive advantages across our footprint and markets. Revenue growth in Charleston, Greenville, Savannah and Jacksonville stood out.

As mentioned above, 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 3.5% of our portfolio. We will continue to monitor closely and protect occupancy in this market.

Move outs for the portfolio were down for the quarter by 4.4% over the prior year and turnover remained low at 52.2% on a rolling twelve month basis. Move outs to home buying were down 4.6%. Move outs to home rentals were down 14% and represent less than 7% of our total move outs. Our focus on minimizing the

time between occupants again paid off. The decrease in the average days vacant between occupants for the quarter helped drive the first quarter average physical occupancy to 96.2%.

During the quarter we completed over 1,400 interior unit upgrades. We expect to redevelop approximately 5,000 units this year. As a reminder, on average we spend about \$4,500 per unit and receive an average rent increase of \$95 over a comparable non renovated unit. This generates a year one cash return of well over 20%.

Our active lease-up communities are performing well. You will notice in the supplemental data that we completed the construction of Station Square at Cosner's Corner II during the quarter. It is currently 94.2% occupied and due to the stronger than expected lease up, we have moved the stabilization date forward one quarter to the third quarter of 2016. Cityscape at Market Center II is leasing well. They are 84% leased and expected to stabilize on schedule in the third quarter of this year.

We are off to a solid start and are well positioned as we headed into the summer leasing season.

## **AI Campbell**

Thank you Tom and good morning everyone. I'll provide some additional commentary on the company's first quarter earnings performance, balance sheet position, and finally on the revised earnings guidance for 2016.

Core FFO, which excludes certain non-cash and non-routine items, was \$1.44 per share for the quarter, which represents a 9% increase over the prior year. This performance was \$0.05 per share above the mid-point of our previous guidance. The strong performance for the quarter was primarily produced by favorable property revenues, which was broad based. Average occupancy, average effective rents, fees and collections were all slightly better than expectations for the quarter, producing about 2/3rds of the favorability. Operating expenses, interest, and G&A expenses combined to produce the remainder of the favorability.

During the first quarter, we acquired one new community, located in Fredericksburg, VA, for a total investment of \$61 million, which was stabilized on acquisition. We also sold one commercial property during the first quarter, Colonial Promenade Nord du Lac, located in Covington, Louisiana, which included both operating retail and land parcels. Total proceeds for the disposition were \$33.2 million, and we recorded a total gain on sale of \$2.4 million related to the transaction. This property represented the final wholly-owned operating commercial asset acquired from Colonial.

During the quarter, we completed the construction of one new community, Station Square at Cosner's Corner Phase II, located in Fredericksburg, VA, which remains in lease-up and was 78% occupied at quarter end. We have four communities, all phase II expansions, remaining under development at the end of the quarter. We funded an additional \$13 million of construction costs during the quarter, and expect to fund about \$63 million to complete the current development communities over the next year or so. We continue to expect NOI yields in the 7.0% to 7.5% range for these communities once completed and stabilized.

We also invested \$6.2 million in our interior redevelopment program during the first quarter, capturing rent increases of 9% above non-renovated units.

Our balance sheet remains in great shape. As Eric mentioned, during the quarter Moody's affirmed MAA's unsecured debt rating of Baa2 and revised the outlook on the company to positive from stable. Now two of the three primary rating agencies have a positive outlook on MAA, which further exhibits the strength of our balance sheet.

At quarter end, our leverage, defined as Net Debt to Gross Assets, was 40.7%, and defined as Total Debt/Market Capitalization was 29.7%. Our recurring EBITDA covered our fixed charges over 4.2 times. At quarter-end 93% of our debt was fixed or hedged against rising interest rates, at an average effective rate of 3.7%, with well laddered maturities averaging 4.6 years. We also had over \$645 million of total cash and credit available at quarter-end providing flexibility.

Finally, as Eric mentioned, we are revising our earnings guidance for 2016 with this release. We are increasing our Core FFO projection by \$0.03 per share, at the mid-point, to reflect both the strength of the first quarter results, and also the offsetting impact of revised transaction volume and timing. Core FFO is now projected to be \$5.71 to \$5.91 per share, or \$5.81 at the mid-point, based on average shares and units outstanding of about 79.6 million. Core AFFO is projected to be \$5.01 to \$5.21 per share, or \$5.11 per share at the mid-point. You may notice in our release that we introduced one additional metric this quarter, Funds Available for Distribution, or FAD, which represents Core FFO less all capital spending, including discretionary items such as redevelopment and revenue enhancing capital, as well as corporate and casualty loss expenditures. The intention is to show the overall strength of our earnings and cash flow. For the full year, we expect our FAD (or FFO less all internal capex) to be sufficient to cover our total annual dividend (\$3.28/share) with \$90 to \$95 million remaining for investment or to build capacity for future growth.

We are maintaining our guidance range for same store NOI for the full year, along with the other components of previous guidance, with the one exception of projected acquisition volume, which we now expect to be between \$250 and

\$350 million for the year. Our current plans do not include any need for new equity during 2016, and we now expect to end the year with our leverage about 150bps below the 2015 year-end level.

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