



## CONFERENCE CALL TRANSCRIPT: 2Q2017

July 27, 2017 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, Tom Grimes, our COO, and Rob DelPriore, 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 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**

Thanks Tim. Good morning. We were pleased with the solid results for the second quarter with FFO performance ahead of our expectation. Pricing momentum continues to move in a favorable direction and occupancy remains strong. Our portfolio of properties balanced across various sub-markets and price points of the Sunbelt region, combined with our strong operating platform, continues to demonstrate an ability to better tolerate the elevated pockets of new supply present in several markets.

The integration of the Post portfolio is making terrific progress and as expected the emerging positive trends in higher rents and occupancy are starting to build momentum. The initial opportunities surrounding expense synergies, resulting from our reconciling operating practices and taking advantage of our larger scale, have yielded some early wins on operating expense performance. We expect these trends to continue over the balance of the year and into 2018.

While it's clear that current new supply trends have caused some moderation from the last year's rent growth results, especially for new move-in residents, we continue to believe that at this point in the cycle, our legacy MAA portfolio locations continue to offer some off-setting balance, or protection, against the new supply pressures which are more evident within the legacy Post sub-market locations. Our property teams are doing a great job in taking care of our existing residents with renewal lease pricing across the Combined Adjusted Same Store portfolio continuing a solid trend in the 6% range with a steady pattern of improvement in renewal pricing being generated out of the legacy Post portfolio. Resident turnover remains low with our 12-month rolling turnover rate at 50.9% half-way through the year, essentially matching last year's performance of 50.8%. So, overall, while leasing conditions have become more competitive when compared to prior year, we continue to believe that a combination of our balanced portfolio focused on the solid employment growth markets of the Sunbelt, coupled with the growing margin expansion opportunities from our merger with Post, will yield continued FFO growth and NOI performance that are in line with our expectation.

The transaction market remains highly competitive as investor capital and interest in the multifamily market continues to outpace opportunities being brought to market. As noted in our earnings release, we did not make any acquisitions during the second quarter. However, we continue to underwrite quite a few deals and will continue to be patient and disciplined in our underwriting as more new development projects are brought to market over the back half of the year.

Our lease-up and development pipelines are making solid progress. The six new properties currently in lease-up, were 82.5% occupied at the end of the second quarter and we expect to stabilize four of these communities in the current third quarter. Our six projects remaining under construction are also making solid progress with initial leasing just getting underway in Austin at Post South Lamar Phase II and in Atlanta at Post Millennium Midtown.

So in summary, we like the momentum we're seeing during our peak leasing season and remain excited with the upside opportunities to capture over the next couple of years from our merger with Post Properties. Our balanced portfolio of properties and strong operating platform continue to demonstrate an ability to deliver stable results through the cycle.

Before turning the call over to Tom I do want to express my appreciation to our entire team here at MAA. I appreciate your efforts over the busy summer leasing season in not only delivering great performance today, but also your extra efforts focused on completing our merger and consolidation activities which are further strengthening MAA's platform for the future. And with that, I'll now turn the call over to Tom.

## Tom Grimes

Thank you Eric and good morning everyone.

The progress made since the first quarter is encouraging, and we're especially pleased with the improvement in pricing trends emerging from the legacy Post portfolio. For the second quarter, on a lease over lease basis, blended rents, which include both new and renewal leases, for the Combined Adjusted Same Store portfolio grew by 2.6 percent, an improvement of 130 basis points from the performance in the first quarter.

Breaking that down a little bit, lease over lease rents for new resident leases written during the second quarter were down 70 basis points, this is a significant 250 basis point improvement from the performance in the first quarter. This positive momentum on new lease pricing for the Combined Adjusted Same Store portfolio continued in July with new lease pricing turning positive, now up 30 basis points. Renewal lease pricing within the Combined Adjusted Same Store portfolio remained strong during the second quarter, growing 6.3 percent.

The positive trends are most evident within the legacy Post portfolio as blended rents, on a lease over lease basis improved 150 basis points from the first quarter to the second quarter. The trend continued in July with Post blended lease over lease rents growing 2.6 percent. July's blended rent performance represents a 370 basis point improvement in rents from the first quarter result for the legacy Post portfolio. These improvements drove the blended rent growth for the Combined Adjusted Same Store portfolio up to 3.1% in July.

The trends are similar for average daily occupancy. In July, the MAA portfolio remained steady at 96.1 percent and the Post portfolio, which ran 90bps behind legacy MAA in the second quarter, closed the gap to 50bps at 95.6 percent. 60 day exposure, which is all vacant units and notices for a 60 day period, for both portfolios is now just 7.4 percent, very strong for this time of the year.

We expect the gap between the portfolios on both rents growth and occupancy to continue to narrow as the benefits of our operating approach come to bear on the Post communities. We have completed most of the foundational work associated with repopulating our revenue management system with updated data from the legacy Post locations, and they are benefiting from the improved occupancy and exposure positioning. We are pleased with the improvement of this portfolio in our critical busy summer season and believe it will be well positioned as we head into the slower winter months.

Expense performance follows a similar pattern. R&M costs were down by 2.2% led by a few early wins in the Post portfolio. As a result of the improved scale, our national account pricing improved in both portfolios but was more impactful in the Post results. In addition, the renegotiation of in-market contract services

such as interior paint vendor and pool cleaning services aided the Post results. We have improvements still to come. At the end of the second quarter, the Post communities are still running 25% higher on a maintenance cost per unit basis than the legacy MAA portfolio. We expect this gap to close as our approach to turning units, which is less reliant on expensive contract labor, takes hold.

Driven by these improvements in revenue and expense, the NOI margin on the Post portfolio increased 130bps from the second quarter of last year.

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

In both portfolios, Houston remains our only market level worry bead and represents just 3.7% of our NOI. We will continue to monitor closely and protect occupancy in this market. Currently, our combined Houston market's daily occupancy is 95.3% and 60 day exposure is just 7.9%.

Renter demand remains steady and our current residents continue to choose to stay with us. Move outs for the portfolio are in line with prior year and turnover remained at a low 50.9% on a rolling twelve month basis. Move outs to home buying and move outs to home renting remained consistent at 20% and 6% of move outs.

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

Momentum is building on the Post redevelopment program. Through June we have completed 423 units. On average we are spending \$8,600 and getting a rent increase that is 13% more than a comparable non redeveloped unit.

For the full MAA portfolio, during the quarter we completed over 2,300 interior unit upgrades. On legacy MAA, our redevelopment pipeline of 15,000 to 20,000 units remains robust. On a combined basis, our total redevelopment pipeline is in the neighborhood of 30,000 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 that stabilization date has been moved up a quarter to Q4 of this year. Innovation in Greenville and Residences at Fountainhead in Phoenix stabilized on schedule during the quarter. Our four communities scheduled to stabilize in the third quarter are all on track to do so.

We are actively leasing The Denton II, Post South Lamar II, Post Millennium Midtown and they are progressing well.

It has been a busy quarter for our teams and we are pleased with our progress. The momentum building in the Post portfolio is particularly encouraging. We look forward to continuing to capture value creation opportunities on both the revenue and expense sides of the equation. AI?

## **AI 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 finally on guidance for the remainder of 2017.

Net income available for common shareholders was \$0.42 per diluted common share for the quarter. FFO for the quarter was \$1.48 per share which was \$0.07 per share above the mid-point of our guidance for the quarter. The earnings outperformance was primarily related to favorable interest, G&A, and integration costs during the quarter, with each producing about \$0.02 per share of favorability. An additional \$0.01 per share was provided by favorable performance in our lease-up and development properties, which are included in our non-same store portfolio. Our Combined Adjusted Same Store NOI performance was in-line with expectations for the quarter. The integration expense savings were mainly related to timing of costs, which we expect to incur over the remainder of the year. I will outline our revised guidance for the full year in just a moment.

During the quarter, we completed the construction of two communities, Post Parkside at Wade Phase II located in Raleigh, and Post Afton Oaks, located in Houston. We also began construction on one new community, a phase II expansion of 1201 Midtown, a community located in Charleston that we acquired late last year.

During the second quarter, we funded an additional \$50 million of development costs, bringing our year-to-date funding to \$110 million. Our current development pipeline now contains six projects with a total projected cost of \$396 million, with only \$103 million remaining to be funded. The six projects are expected to produce an average 6.5% stabilized NOI yield once completed and leased-up, with four of the projects projected to be completed by the first quarter of 2018, and the remaining two completed in the back half of 2018.

Just after quarter-end, we sold three wholly-owned communities, located in Lakeland, FL, Montgomery, AL, and Fort Worth, TX. The total proceeds of \$88.4 million represented strong pricing for 28 year old assets (on average), and

produced a 5.3% economic cap rate. We also exited two tertiary markets with these sales.

During the second quarter, we successfully used our enhanced credit ratings to complete a public bond offering. We issued \$600 million of 3.6% unsecured ten year notes at an issue price of 99.58%, using the proceeds to pay down our line of credit. During the quarter we also prepaid \$156 million of secured mortgages, further increasing our unencumbered assets to 83% of our total gross assets.

Per our bond covenants at quarter-end, our leverage (defined as Debt to Total Assets) was 34.0% and our consolidated income covered our debt service by 5.2 times. We also had over \$877 million of combined cash and capacity under our credit facility to provide protection and support for our business plans.

Finally, we increased our earnings guidance for the full year to reflect the second quarter performance and updated expectations for the remainder of the year. We are updating guidance for net income per diluted common share, which is reconciled to updated FFO and AFFO guidance in the supplement.

Net income per diluted common share is now projected to be \$2.69 to \$2.89 for the full year 2017. FFO is now projected to be \$5.77 to \$5.97 per share, or \$5.87 at the mid-point, which includes \$0.15 per share of merger and integration costs for the full year. AFFO is projected to be \$5.18 to \$5.38 per share, or \$5.28 at the mid-point.

We are maintaining our guidance expectations for the Combined Adjusted Same Store portfolio, which is expected to produce NOI growth for the year in the 3.0% to 3.5% range.

In summary, we are increasing our FFO guidance for the full year by \$0.03 per share, representing the addition of the strong second quarter performance discussed earlier partially offset by the \$0.02 per share of integration costs now expected to be incurred later in the year (timing related variance), along with an additional reduction of \$0.02 per share related to revised acquisition timing and yields for the year. Given the competitive environment Eric mentioned earlier, we now expect our remaining acquisition opportunities to occur later in the year and all to be lease-up communities.

Our guidance for acquisition volume and total merger and integration expenses for the full year remains unchanged. We did increase our range for disposition volume, as our actual pricing expectation is exceeding our initial estimates. We also narrowed the ranges of expected G&A costs and development investment for the full year.

We remain on track to capture the full \$20 million of overhead synergies related to the Post merger, on a run-rate basis, by year-end. And we also expect to

continue capturing additional NOI opportunities (included in our forecast), primarily in the later part of this year, as the operating practices and platforms become fully integrated.

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