Mid-America Apartment Communities, Inc.
3Q08 Conference Call Comments

Good morning. This is Leslie Wolfgang, Director of External Reporting for Mid-America Apartment Communities. With me are Eric Bolton, our CEO, Simon Wadsworth, our CFO, Al Campbell, Treasurer, Tom Grimes, Director of Property Management and Drew Taylor, Director of Asset Management.

Before we begin I want to point out that as part of the discussion this morning company management will make forward-looking statements. Please 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 can be found on our website.

I'll now turn the call over to Eric.

Eric

Thanks Leslie and thanks for joining our call this morning. We were pleased with FFO results for the third quarter. Despite continued weakness in the economy, extraordinary volatility in the debt markets, very challenging prior year expense comparisons and steps taken to further strengthen the balance sheet, FFO was better than we expected. FFO for the quarter was driven by stable revenue performance, lower G&A costs and lower financing costs. Excluding the expenses associated with Hurricane Ike, FFO was two cents above the mid-point of our guidance, and equal to the record high third quarter FFO result reported last year.

Revenue growth in the third quarter was driven by stable occupancy and strong results in collections. Same store occupancy ended the quarter at a very solid 95.4%. When compared to last year's exceptionally strong 96.4%, the 100 basis point decline did pressure year-over-year revenue performance, but given the more difficult economic environment, we are encouraged with the results. 95% occupancy is pretty strong. Helping to offset some of the moderation in leasing conditions is lower resident turnover and vacancy loss from move-outs as compared to last year.

As we indicated would be the case in our second quarter conference call, we believe it will be difficult to push pricing aggressively on new resident leases over the next few quarters. We were encouraged however by the performance in pricing renewal leases as effective pricing on leases renewals was up 4% as compared to prior year. Capturing that level of price increase, while at the same time reducing resident turnover by 6% is pretty strong performance and brings further support to our belief that revenue performance from Mid-America's portfolio should hold up over the next few quarters.

It is also important to point out that two markets across the portfolio were largely responsible for the overall moderation in our year-over-year revenue growth: Atlanta and

Jacksonville. Atlanta is a market where weak employment trends earlier in the year became significantly more pronounced in the third quarter. Year to date job losses in Atlanta are 53,000, with 35,000 of those losses coming in the third quarter. This pressure generated a 240 basis point decline in effective occupancy for our Atlanta properties. Jacksonville has battled a combination of new supply that came on earlier this year and weak employment conditions with 22,000 jobs lost year to date. This generated a 250 basis point decline in effective pricing for our Jacksonville group of properties. We expect both of these markets will show improving trends next year as new supply pressure moderates and job loss trends bottom out.

While our outlook for revenue growth over the next few quarters will be impacted by weaker job growth trends, remember that Mid-America's portfolio is not materially exposed to the over-supplied single-family home and condo markets. And given our investment in a number of secondary markets in the southeast that are not experiencing the volatility in employment conditions seen in the larger markets, we expect Mid-America's portfolio performance will not experience as much pressure as others. As detailed in the earnings release, you'll note that Mid-America's stable income and smaller market segment outperformed the other two segments of the portfolio.

Overall, same store leasing traffic was up on a year over year basis, resident turnover was down, occupancy is holding up and pricing weakness is largely isolated to new resident leases. As a result, we believe Mid-America is well positioned to weather this slowdown in the economy. Longer term, with the continued shift of more households to apartments and away from the single-family market, along with the dramatic decline in new apartment starts, once we get some positive traction back into the employment trends, leasing conditions should turn positive and do so quickly.

As expected, same store operating expenses in the third quarter reflected higher than normal year-over-year growth, as we were comparing against an unusually low prior year benchmark of only 0.3% growth in operating expenses. In addition, the quarter's results were also pressured by expenses incurred from Hurricane Ike. Simon will give you more details on the various components driving the expense performance, but we are comfortable that after another tough comparison in the upcoming fourth quarter with a prior year benchmark of negative expense growth of 1.2%, we will see property operating expenses trend more in line with our historical norms.

In addition to questions about the leasing environment, the other item under focus in this market is of course the balance sheet. This is another component of our platform and strategy that places Mid-America in a solid position. Of the total $1.4 billion in outstanding financing, we have only $39 million, or roughly 3% of our total debt facing refinancing next year. Further, in 2010 we again only have another 4% of our debt program facing refinancing. Mid-America has one of the strongest dividend and fixed charge coverage ratios in the sector. And, we've raised $104 million of additional equity this year, prior to the recent collapse of the capital markets. All together, this puts us in a solid position to be more disciplined in our management of asset sales and in our pursuit of new growth opportunities. Mid-America does not have the pressure of liquidity concerns and the exposure to the current debt markets associated with securing financing commitments for new development and material refinancing requirements.

We're very pleased with the acquisitions completed in the third quarter and we remain active in the market looking at a number of opportunities. Obviously, given the dramatic shift in the capital markets and the rise in the cost of capital over the last couple of months, we are being very careful in our analysis and decisions about any current use of capital. We continue to believe there are going to be some terrific buying opportunities over the next year.

In summary, we believe Mid-America is well positioned to weather this period of moderating leasing conditions and volatility in the capital markets. With our exposure to a wide range of markets and a proven operating platform, we like our situation. We have several new initiatives underway for next year that we believe will further boost our internal growth prospects including a new bulk cable program, a fully integrated on-line leasing program, and new resident utility billing programs. Our interior redevelopment program continues to make steady progress and will make an increasing contribution to revenue growth. We have a number of lease-up and new development projects underway that are diluting 2008's FFO by 16 cents per share. These investments will all become productive next year. The balance sheet is in terrific shape. We have the ability to selectively and carefully pick opportunities for capturing new value for our shareholders. In all, we believe that Mid-America is in a good position to play defense as needed during this period, with the added capability to jump on opportunities that these markets will undoubtedly create.

That's all I have and I'll now turn the call over to Simon.

Simon

We were pleased that our third quarter FFO was ahead of our internal forecast, given the economic issues, the impact of Hurricane Ike, and our reduced leverage. Our top line was softer than we anticipated, and property expenses showed a temporary spike, but these were more than offset by less G&A and interest expense.

As Eric mentioned, revenues were weak in Atlanta and especially in Jacksonville, and excluding these two markets, our revenue performance was more in line with our expectations, with same-store revenue growth of 2½%. We stepped up our marketing efforts after the slow down in traffic we experienced in June, and walk-in traffic was up by 2.7% over the same quarter a year ago on a same-store basis. We saw leasing conditions become more challenging as although our lease applications rose, the number of credit turn-downs increased by 5%. Physical occupancy ended the quarter at 95.4%, which was solid performance, as the level we achieved at the end of September a year ago was exceptionally high. Effective rent increased by 1.6%, which was the major contributor to our same store revenue increase of 1.4%.

Our bad debt expense continued to improve, with net delinquency down 9% to 0.5% of net potential rent, although we think credit will become more challenging as we go into next year, and so we're taking early steps to combat this potential pressure. The same-store concession rate dropped from 2.2% to 0.8% of net potential rent, as we migrate towards net effective pricing at most of our properties. We continued to see a reduction in the number of our residents leaving us to buy a house, down 22% from 25% of move-outs in the third quarter of 2007 to 21.5% in the third quarter of 2008. The number of our residents that left to rent a house is insignificant, at 4% of move-outs. Quarterly resident turnover on an annualized basis dropped from 77% to 71%, or from 63% to 62% on a trailing 12-month basis.

Same-store operating expenses were above the level we'd projected. As mentioned in the release two events, Hurricane Ike and the large credit to real estate taxes last year, contributed 2.5% of the increase. A further 0.8% was due to higher personnel and make-ready costs we discussed in the release; in other words without these unusual or one-time items, our same store expense increase would have been 3.6%, more in line with our normal expectations. As Eric mentioned, these issues should work their way through by the fourth quarter, or at least by the first quarter of 2009; we've noted before that expense comparisons with the fourth quarter of last year will be tough, a period when our same store expenses dropped by 1.2%.

Our balance sheet is in great shape, with minimal commitments, and all but $6 million of our developments are complete and funded. We have no further debt maturities in 2008, and just $39 million of debt maturities in 2009, which we'll pre-fund with new Freddie Mac debt during the fourth quarter. We're putting this pre-funding in place four or five months ahead of a more normal schedule; we figure this will cost us 2 cents a share, including ½ cent a share in the fourth quarter, but we're willing to pay this just to be doubly sure we have the financing we'll need. In 2010 our only debt maturity is our $50 million line of credit, that we anticipate renewing in the ordinary course of business. And our major debt funding, which is through Agency credit facilities begins maturing in traunches between 2011 and 2018. We use swaps on our credit facilities to reduce interest rate risk, and these are laddered to mature over the next seven years. At the end of the quarter we had $174 million of combined capacity available in excess cash, pre-committed Agency credit facilities, and our bank line of credit.

We have continued to strengthen the balance sheet using our continuous equity program. We raised $99 million of new common equity through the end of the third quarter, plus a further $5 million in October, and we've averaged a net price of $52.98 before we closed down the program when Reit stock prices dropped. Our debt stands at 51% of gross assets, down from 52% in September last year, and this compares to a second quarter sector median of 55%.

At the midpoint of our 2008 guidance, our dividends are 66% of FFO and 83% of AFFO, both in the best 1/3 of the sector. Our fixed charge coverage ratio of 2.5 is also in the top 1/3 of the sector. Our cash flow and FFO are high quality, almost entirely derived from income related to apartment rentals, not from transactions or asset sales.

Our swaps and floating rate debt are either directly or indirectly tied to Libor, and increased volatility impacts our cost of funds. In six weeks following the Lehman bankruptcy Libor spiked, rising from 2.80 to 4.82, before dropping back down again; it seems that Libor volatility is declining and returning to a more reasonable level. We estimate that this spike will cost us around 1 ½ cents per share of FFO in the fourth quarter.

During the quarter, we acquired three high quality properties which represent the kind of opportunities we increasingly are seeing as sellers become more anxious and the acquisition environment improves. We expect a blended NOI yield of approximately 6.3% from these properties in their first year of operation.

We'd targeted four properties for disposition totaling 990 units, representing a cross-section of older properties that no longer fit our objectives. As mentioned in the release, at the present time we anticipate that three will sell for about $28 million, a 6.8% cap rate, around the end of this year. We're reviewing purchase proposals on the fourth, with a possible delay of the sale until the markets settle. For the same reason that acquisition opportunities are improving, disposition pricing is becoming a little less attractive, but we're in the fortunate position of not needing to sell assets to raise cash to fund our business, and are entirely focused on the smart recycling of our capital.

Our redevelopment program continues to generate attractive returns, with interior renovations on 3,100 apartments completed through the end of September. We plan to redevelop a total of 3,800 units this year, at an average cost of $4,900 per apartment. So far, we've seen the renovated units generate average incremental revenue per lease of $95 per month, and a 10% unleveraged IRR. In addition, we have five exterior repositioning projects scheduled to begin this year totaling $2 million. We underwrite these exterior projects to generate the same kind of returns (through additional rental rates) as for our interior renovation. We're carefully monitoring our redevelopment program as some markets soften; it is likely that due to the tougher economy, we'll tend to focus more on some of the 'renovate-lite' projects – lower investment per unit – where we don't need to achieve such a large revenue increase, and we may moderate the number of apartments selected.

The two new development projects, Copper Ridge in Dallas, and St Augustine Phase II in Jacksonville are on schedule for completion in the fourth quarter, with total remaining investment of $6 million. Copper Ridge has started lease up, which is proceeding well, and at the end of October, 90 of 141 available apartments were leased. The first building at St Augustine is just coming on line, and we have 19 apartments leased. Due to the rapid lease-up of Copper Ridge, we are exploring bringing forward the construction of 45 additional units, and will likely commence construction early in 2009, with a probable additional investment of around $4 million, partly built on 12 acres of adjacent land that we purchased in the quarter.

We've dialed back our expectations for the economy, and for the balance of this year we project slower revenue growth, partly offset by reduced G&A costs. In the fourth quarter we expect increased interest costs due to the Libor spike that I mentioned and the early funding of our $39 million 2009 debt maturity. We've taken the mid-point of our FFO forecast for the fourth quarter and for 2008 down by 3 cents from our prior guidance.

- We're now projecting same-store NOI growth for 2008 in the range of 1% - 1½%. This is based on revenues growth of 2% – 2 ½% and expense growth in a range of 3¼% - 3¾%. We previously pointed out that we have tough comparisons in the back-half of 2008 due to the very favorable insurance renewal and real estate tax adjustments that benefited us in 2007.
- The reduction in forecast same-store NOI is partially offset by increased NOI from acquisitions and by less G&A expense than we anticipated.
- We have a few more shares outstanding than we planned last quarter, which is modestly dilutive to FFO/share. Year to date we've raised $104 million more equity than we originally forecast, costing us 4 cents per share of FFO dilution for all of 2008.
- We expect about 16 cents of FFO dilution for the full year from recent acquisitions of properties in lease-up, including Talus Ranch in Phoenix, and from development properties

Eric

Thanks Simon. We hope that the key points you take away from this morning's call are the following:

First, the fundamentals driving revenue growth, while moderating in the third quarter, are holding up. We expect to carry our current trends in occupancy and pricing into the fourth quarter and 2009 at which point prior year comparisons should turn more favorable towards the back half of the year. We believe Mid-America's market profile, quality of product and strength of operating platform will drive stable performance over the next few quarters.

Second, a significant aspect of the operating expense pressure in the third quarter and expected in the fourth quarter is attributable to very tough prior year comparisons, one time events and trends that we expect to moderate.

And lastly, Mid-America's balance sheet is in good shape. We are fortunate to have raised $104 million of additional equity earlier this year and we have the capacity and coverage to be patient and disciplined with capital decisions during a time of significant volatility and opportunity.

And a final point I want to make. With only a couple of months left to go this year, our revised FFO expectations for the year are within 3 cents per share, at the mid-point, of where we started the year. When you consider that our original expectations did not assume that we would raise any new equity this year, or that the economy would be this weak for this long, or that the capital and debt markets would be this volatile, and yet, overall FFO expectations are this close to where we stated the year, says something very positive about the stability of our strategy, the high quality of our earnings, and the strength of our operations. We believe we are well positioned for this part of the cycle and we look forward to executing on the opportunities before us.