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Transcript of
Elme Communities
Fourth Quarter 2022 Earnings Conference Call
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Participants

Paul McDermott - Chairman, President & Chief Executive Officer
Stephen Riffee - Executive Vice President & Chief Financial Officer
Amy Hopkins – Vice President, Investor Relations
Steve Freishtat – Vice President, Finance
Grant Montgomery - Vice President, Head of Research

Analysts

Young Ku – Wells Fargo
Michael Lewis – Truist Securities
Anthony Paolone – JP Morgan
Alan Peterson – Green Street

Presentation

Operator
Welcome to the Elme Communities Fourth Quarter and year-end Earnings Conference Call. As a reminder, today's call is being recorded. At this time, I would like to turn the call over to Amy Hopkins, Vice President, Investor Relations. Amy, please go ahead.

Amy Hopkins – Vice President, Investor Relations
Good morning, everyone and thank you for joining us for our fourth quarter earnings call. On the call with me today are Paul McDermott, President and Chief Executive Officer; Steve Riffee, Executive Vice President and Chief Financial Officer; Steven Freishtat, Vice President, Finance; Grant Montgomery, Vice President and Head of Research; and Drew Hammond, Vice President, Chief Accounting Officer and Treasurer.

Today's event is being webcast through the Investors section of our website at elmecommunities.com, and a replay will be available this afternoon. We will have a slide presentation in conjunction with our prepared remarks, and those slides will also be available on our webcast replay.

Before we begin our prepared remarks, I would like to remind everyone that this conference call contains forward-looking statements that involve known and unknown risks and uncertainties, which may cause actual results to differ materially, and we undertake no duty to update them as actual events unfold. We refer to certain of these risks in our SEC filings.

Reconciliations of the GAAP and non-GAAP financial measures discussed on this call are available in our most recent earnings press release and financial supplement, which was distributed yesterday and can be found on the Investors page of our website.

And with that, I'd like to turn the call over to Paul.

Paul McDermott – President & Chief Executive Officer
Thank you, Amy. Good morning, everyone, and thanks for joining us today. We ended the year with strong fourth quarter performance and 2023 is off to a good start, with solid operating fundamentals and favorable demand indicators. We are reiterating our 2023 guidance, which reflects double-digit same store NOI and Core FFO growth. Our investment-grade balance sheet is in great shape, with low leverage and ample liquidity, and we have no debt maturities until 2025. We feel very good about our AFFO growth outlook, and we are increasing our quarterly dividend by approximately 6%.

The economic outlook continues to evolve, and we will likely face a slowing economy this year. While we are not immune, our mid-market strategy is designed to outperform across cycles, and to provide relative insulation during downturns, when residents are more likely to trade down to a lower rent level instead of trading up. Over the past five and 10-year periods, our target vintages have outperformed newer vintages in our respective markets.

Toward the end of last year, we began to see headlines surrounding job cuts for high-wage technology positions due to the intentional cooling of the economy by the Fed. However, in the Washington Metro, the tech heavy, Information and Professional, Scientific and Technical sectors continue to grow, up 2.7% and 2%, respectively year-over-year. As recently highlighted in the *Wall Street Journal*, a study of software engineering job postings at year-end found that the Washington region has more job openings in this field than the San Francisco Bay area.

The strength in these jobs is particularly evident in Northern Virginia, where most of our portfolio is located, and where the Information sector, which includes software engineering jobs, grew at a brisk rate 5.6% in 2022. The Washington Metro is known to have the most stable employment of all the gateway markets. This stability supported very strong credit performance throughout the pandemic, as we sustained 99% collection rates, and we expect to continue to experience solid collection trends. Furthermore, multifamily rent growth for the Washington Metro is expected to outperform the US average this year, and nearly all the major gateway markets. In Atlanta, the regional economy is projected to fare well in the face of increased macroeconomic headwinds in 2023, maintaining job growth of over 1% according to Oxford Economics. Over the long term we continue to believe that Atlanta's industrial mix will drive outsized job creation, wage growth, and net migration, supporting sustained demand for apartments that are affordable to the largest segments of the renter market.

In terms of the potential impact from new supply in a slowing economy, our price points are well below the rent levels for new deliveries. In the Washington Metro, our monthly rents are over $600 below nearby Class A communities. In Atlanta, our monthly rents are over $500 below nearby Class A communities.

Furthermore, our communities are not located in areas that are receiving high supply. Almost 88% of the new supply in the Atlanta Metro is delivering outside of Elme submarkets in 2023 and 2024. And in Washington, development is highly concentrated in the region's core vs. our suburban focus, with 84% of units under construction inside the Capital Beltway. Again, in both markets the new supply is priced above our price points for different renter cohorts.
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In terms of the impact of a slowing economy on the cost of homeownership, the national cost of owning a home compared to renting a single-family starter home is the highest it's been in over 20 years. The cost of owning a home in our markets has grown more than renting an apartment over the past few years and now stands at nearly

$600 per month, or 28% above our rents in Atlanta, and over $1,200 dollars per month, or 43% above our rents in the Washington Metro. Even after factoring the potential for home price declines, homeownership will remain unaffordable for median-income renters in our markets.

To summarize, our portfolio offers downside protection in a slowing economy for the following reasons. First, our resident base is less exposed to job losses. Second, our price points serve as a buffer during periods of supply pressure. Third, we do not have exposure to high supply submarkets, lastly, housing remains undersupplied in our markets driving up the cost of homeownership which is particularly impactful for median-income households. Our rent levels are affordable for the largest and most underserved renter cohorts and our communities should benefit from sustained demand for affordable rental options over the near and longer-term.

We are now in the final phase of our infrastructure transformation, which includes transitioning community-level operations to Elme management. The process has been seamless thus far, and we will have nearly 40% of our homes under management by next week, over 50% by the end of the quarter, and all communities under management by the end of the summer. The full spectrum of operational benefits is extensive, and we continue to identify opportunities to deliver operational upside once our community onboarding process is complete.

We built an operating platform that is highly scalable, and we continue to see the opportunity to deliver positive operating leverage by growing our portfolio and expanding into the Sunbelt markets. We are confident in our investment strategy and our ability to create value through thoughtful capital allocation. The markets that we are targeting have industries with the best long-term growth prospects and a growing need for affordable rental options for median incomes. While deal volumes remain muted, we are actively underwriting opportunities. We will be ready to act when the time is right and will only pursue opportunities that we expect will create value for our shareholders and align with our strategy and mission.

This year we plan to extend the rollout of smart home technology to all our communities. We designed our smart home initiative to improve our residents' day-to-day experience at investment levels that makes sense for mid-market price points. Our initial program includes smart locks, smart thermostats, smart lights, and water leak sensors. Overall, these technologies will provide ease of living for our residents, reduce our operating expenses, advance our environmental goals, and enable a better digital experience in the form of self-guided tours for potential residents.

I am pleased to share that we made substantial progress on our ESG initiatives during 2022. Delivering industry-leading ESG performance for value-oriented communities is core to our goal of elevating the standard for value living. To quickly summarize our achievements, we achieved our highest GRESB score to date, achieved our greenhouse gas and water goals, aligned our reporting with GRI standards, joined the Better Climate Initiative, increased our multifamily sustainability certifications, and expanded the number of EV chargers at our communities.

As we transition our communities to Elme management, we are advancing financial inclusion by providing our residents the ability to boost their credit scores by submitting on time rent payments to all three credit bureaus at no cost. ESG is core to our mission of delivering a superior living experience for mid-market rents and we are pleased with the progress we made in 2022 and look forward to keeping you updated on our ESG goals.

Before I turn it over to Steve Riffee to provide an update on our operating trends and to cover full year and fourth quarter performance, I'd like to say a few words of gratitude. This is Steve's last earnings call with us ahead of his retirement on February 28th. I cannot thank Steve enough for the dedication that he has shown this company over the past eight years. His leadership and vision were instrumental to our transformation, and he is leaving us with a team that is well prepared to drive our company forward. He will be greatly missed by everyone who worked with him, and we wish him the best in his retirement.

Steve Riffee – Executive Vice President & Chief Financial Officer
Thank you, Paul. I am grateful to you and to our team for all we were able to do together, and I am looking forward to the growth ahead for our Company going forward.

Now, starting with our operating trends. The year is off to a strong start and demand indicators continue to look good through the winter months. Year-to-date traffic and application volumes are up on a year-over-year basis, extending the trend that we experienced during the second half of last year.

Effective-new-lease-rate growth was 1.1% and effective-renewal-lease-rate growth was 10.1%, which blends to 5.7%, for same store move-ins so far that took place during the fourth quarter.

Thus far this year, demand trends remain solid, and lease rates have increased since December. Effective-blended-lease-rate growth averaged 4.5% for January move-ins, comprised of renewal lease rate growth of 8.8% and new lease rate growth of 1.3%. For February move-ins so far, effective blended lease rate growth increased to 5.8% for our same store communities, comprised of renewal lease rate growth of 9.1% and new lease rate growth of 3.7%. Our revenue maximization strategy prioritizes occupancy over lease rate growth during the winter months, and as such, we adjusted pricing to sustain occupancy during our lightest volume months.

New lease rates are on an upward trend, and we are currently signing new leases with effective rate increases of over 4%, on average. Looking forward, we expect new lease rates to continue to increase to the mid-single digits in the spring and summer leasing seasons followed by a decline to the low single digits toward next winter.

Renewal lease rates remain very strong, and we are currently sending out renewal offers for April lease expirations with effective rate increases of over 7%, on average, and so far, we are experiencing high renewal acceptance rates. We expect renewal rates to trend down from the current high-single-digit level, eventually converging to a more normalized level in the low single digits by the end of the year.

All in all, we feel good about the lease rate growth we captured during the fourth quarter and the trends that we are seeing now heading into the spring leasing season. Lease rates tend to be weaker during the winter, and while new lease rates moderated through January, renewal rates remained very strong all through the winter. The combined new and renewals that we are quoting for March and April are providing the upward trending rent levels just as we expected heading into the spring leasing season. These are positive winter months adding to historically high embedded growth as we head into the spring months.

Occupancy averaged 95% during the quarter for our same store portfolio and has increased 30 basis points on a year-to-date basis. As of the second week of February, same store occupancy was 95.6%, positioning us to continue to drive rent growth and capture more of our loss to lease. Retention was 62% during the quarter, which is a slight sequential increase as we continue to experience high renewal demand supporting very strong renewal rate growth of approximately 9% year-to-date.

Average effective monthly rent per home grew 9.7% in the fourth quarter compared to the prior year, and 7.6% for the full year, reflecting the impact of the very strong lease rate growth we captured during 2022. For our portfolio, average monthly rent grew significantly more in the second half of 2022 to provide historically high embedded growth at the end of the year.

Our current rent levels in February plus the March move-ins we've signed represent rental rate growth of approximately 5%, which is nearly 70% of the rental rate growth that we expect for the full year. Our current loss to lease, which represents the difference between current asking rents and our in-place leases, is approximately 4.4%, and we expect our loss to lease to increase into the spring given the solid demand trends that we are seeing today.

We are where we expected to be heading into the spring and summer leasing seasons and our line of sight on the busiest leasing months will significantly increase over the next two to three months. By June, we expect to have locked in 90% of our total rental rate growth for the year. We feel good about the visibility that we have today and where rent growth is tracking compared to our expectations.

Moving onto renovations. We completed more than 300 full renovations during 2022 at an ROI of over 13% excluding the rent growth that we achieved on comparable unrenovated units. We expect to be closer to our historical renovation run rate of approximately 600 units per year in 2023, and for renovation-led value creation to drive higher rent and NOI growth over the next few years. Executing value-add renovations at low-teen cash-on-cash returns, on average, remains a key part of our growth strategy.

Now turning to our full year and fourth quarter financial results.

Core FFO for the fourth quarter was $0.24 per diluted share, representing year-over-year growth of over 40% driven by strong growth in rental income and the full deployment of our commercial portfolio sale proceeds. Core FFO for 2022 was $0.88 per share, in line with the midpoint of our guidance range.

Multifamily same-store revenue grew by 8.9% for the quarter and 7.3% for the full year due to growth in rental rates, lower concessions, higher occupancy, and an 11% year-over-year decrease in bad debt for the full year.

Operating expenses grew 4% for the fourth quarter and 4.6% for the full year driven by non-controllable expenses such as real estate taxes and utilities.

Multifamily same-store NOI grew 11.6% for the fourth quarter and 8.8% for the full year. This represents the end of a strong year, even while executing our transformation, and now we have excellent momentum carrying into 2023.

Now, it is my privilege to turn it over to Steve Freishtat, who I have great confidence in. Steve will cover financing updates and our 2023 outlook. As we announced in November, Steve is succeeding me as Chief Financial Officer following my retirement at the end of this month. Steve brings extensive knowledge of capital markets, strategic transactions, capital allocation, public company operations and financial planning. He's been instrumental in the execution of our multifamily transformation, and I know he is going to be an excellent CFO. He also has an excellent team that has been through all of this with us and are ready for new opportunities to create value.

Steve Freishtat – Vice President, Finance
Thanks, Steve. You're leaving me with a great team, and we are very excited for the opportunity to continue to build on everything you helped create over the last eight years. Now, I'll start with our balance sheet.

With an annualized fourth quarter net debt to EBITDA of 4.8x, over $650 million of availability on our line of credit, no secured debt, and no maturities until 2025, our balance sheet is in excellent shape.

In keeping with our proactive approach to managing our debt maturity ladder, on January 10th, we executed a new two-year $125 million term loan with two 1-year extension options. We used the proceeds to pay down our previous $100 million term loan with no prepayment penalty and a portion of the balance on our line of credit. Our new loan has a variable interest rate of adjusted SOFR plus 95 basis points.

At a time when many banks are tightening their lending requirements, we have taken steps to ensure our financial flexibility and increase our liquidity. We feel good about our ability to successfully navigate market volatility while executing on our strategy.

Now, turning to our outlook for 2023.

We are reiterating our 2023 Core FFO guidance range of $0.96 to $1.04 per fully diluted share, which implies double digit year-over-year growth.

Same-store multifamily NOI growth is expected to range from 9% to 11%, which reflects year-over-year growth of 10% at the midpoint, further building on the double-digit NOI growth achieved in the second half of 2022.

Non-same-store multifamily NOI is expected to range from $12.75 to $13.75 million in 2023. While this guidance range does not reflect the impact of potential acquisitions, we had more than $650 million of availability on our line of credit as of year-end, and we are running below our targeted leverage levels. We will continue to evaluate acquisition opportunities in our target markets and will further pursue acquisitions when they create additional value for shareholders.

Other same-store NOI, which consists solely of Watergate 600, is expected to range from $13 to $13.75 million.

We are slightly reducing our guidance for G&A, net of core adjustments, to a range of $25.75 to $27 million. We expect G&A to decline in 2024 as we realize the full year benefits of internalizing multifamily operations and then to remain stable as we scale our portfolio when the time is right to do so. Our G&A guidance excludes the impact of transformation investments for our platform and our full integration, which we now expect to be between $3 and $4 million.

Interest expense is now expected to range between $29 and $30 million, which incorporates a higher anticipated future fed funds rate as the interest rate outlook has shifted since we announced our 2023 guidance last year as well as the impact of our new term loan. The new term loan is subject to our existing swap agreement, which fixes the interest rate on $100 million at 2.16%, through July 21st of this year. We remain very confident in our NOI growth outlook and are currently within our Core FFO guidance range, however, recent Fed actions have put pressure on our midpoint. If expectations were to shift further, we will update our interest expense guidance again and possibly our Core FFO guidance range.

We finished 2022 with a 75% AFFO payout ratio. As Paul mentioned, we are increasing our quarterly dividend by approximately 6% to 18% per share, reflecting confidence in our growth in 2023 and beyond, and the strength of our AFFO growth profile. We expect our Core AFFO payout ratio for this year to be at or below our mid-70s target.

And with that, I will now turn the call back to Paul.

Paul McDermott – President & Chief Executive Officer
Thank you, Steve.

To conclude, we are where we expected to be at this point in the year. We feel good about our ability to deliver double digit Core FFO growth, which will be driven primarily by rent growth, as nearly 70% of that rent growth is already locked in. We are on track to complete the transition of our portfolio to Elme management by this summer, and to begin to see the benefits of that transition and our smart home initiatives in 2024.

Our strategy offers growth as well as relative insulation during downturns, and we expect to benefit from sustained demand for quality, affordable rental options over the near and longer term.

And now operator I'd like to open it up for questions.

Operator
Thank you. Ladies and gentlemen, the floor is now open for questions. Our first question today is coming from Michael Lewis with Truist Securities.

Q: Thank you. Steve, you'll certainly be missed and I wish you all the best in retirement. And congratulations to other Steve taking over the role. My first question, wondering if you could provide some of the components of the same store NOI guidance. Occupancy revenue growth or expense growth or any details you could share?

Steve Freishtat – Vice President, Finance
I'll take a first crack at that. To get to our NOI guidance, we look at our revenue growth expectation of about 8.5% that is primarily driven by rental revenue growth, where we're expecting that to be almost 7%. As we talked about in our prepared remarks. We have captured approximately 5% of that already with our in-place leases and leases signed, but not yet moved in. So, we're at 70%. We're expecting that number to be 90% by June and that leaves about an additional 2% of additional rent growth that is expected to be captured over the remainder of the year.

The difference between the 7% and the 8.5% is smaller contributions from line items like other income and declines in bad debt.

On the expense side, we're expecting expenses to go up about 7% net of reimbursements, and that's primarily driven by three-line items. The first is payroll, which we're seeing pressure on salaries, and we're also ramping up positions ahead of our on-boarding that we're currently going through for our communities.

The second one is taxes. As we're seeing taxes reset, we're seeing pressure on expenses from some from increased taxes. And then the third one is utilities. We're seeing utilities higher in electricity and gas for 2023, but that's mitigated somewhat by reimbursements, where we see reimbursements at about 60% to 70%. So that's really the build up to our 9% to 11% NOI growth.

Q: My second question, how should we think about the upside from getting properties onto your internal property management platform? Is there an operating margin improvement that you're measuring or seeing that you can point to? Or how do you measure and quantify the longer-term benefits from that transition?

Steve Freishtat – Vice President, Finance
As we said, we have on-boarded as of next week, almost 40% of our communities by the end of the quarter we will have 50% and have them all on-board by the end of the summer. And we think we can get there, there are efficiencies that we can take advantage of. Some examples of it are centralization, better revenue management through occupancy initiative, smart buildings and ability to produce R&M maintenance efficiencies and global contract strategy. So, we see a lot of potential upside from being able to take advantage of opportunities of managing our own communities. But in addition to that, we've talked about scalability before, that we're building out a platform that is scalable. So, when we think about being able to double the unit count of this company and keep G&A essentially the same from where it is now, that that's even an additional opportunity and an additional driver for growth.

Q: It seems like there's more investor demand and liquidity in the market for multifamily than for some of the other property types. For all the advantages that you spoke about, but there's still this bid-ask spread that's kind of limiting transactions. I'm wondering what are your target returns for acquisitions today or how are you looking at potential deals given what's happening in the cost of capital and I know you're still looking, but maybe there's a pause here as that bid-ask kind of shakes out. How are you thinking about that and what might be attractive?

Paul McDermott – President & Chief Executive Officer
Well, in terms of our observations on what we're seeing in the marketplace right now, first and foremost, there's not a lot of product in the market on a relative basis. If you look at the year over year numbers of what is in there, a lot of the brokers that we interact with as well as the owners have a large BOV pipeline and we expect, like groups that are in the Odyssey Fund, they're waiting on appraisals from Altus. As you know, appraisals tend to lag the markets anywhere from six to nine months. We think those appraisals are going to hit. We think second quarter will have a lot of mark to market activity. And we believe that we're going to have a more robust second half of the year. As we've said before, these are funds that are still dealing with the denominator effect and have to go through their own process of mark to market. But really, the sellers that we're seeing right now, they are only selling either there's a liquidity requirement, i.e., a queue or they're funding other parts of their operations. As you alluded to, I don't think there's any question that there's enough capital. But we would also say and in talking to

folks that are thinking of taking product to the market, the ask is really coming toward the bid. I think the gap is going to be closing and will be closing as we progress through the year in terms of what we look for right now. A lot of the institutional capital remains on the sidelines. A lot of that private capital is the most active and they're trying to take advantage of some of the in-place leverage, the low leverage that they can utilize. For us, it's going to be maintaining our continued discipline in our underwriting in reference to the top line we are and always have been more realistic about rent growth and about our trade outs. As Steve first alluded to, we are being disciplined in how we look at expenses, labor, insurance, property taxes and utilities, where you have to have discipline around that residual cap rate. Right now risk is being priced appropriately. Our particular focus right now, we're very sensitive to replacement costs. In terms of what we're seeing out there, our cap rates can vary depending on the amount of risk we want to take on. We're seeing Cores in the 4’s to 5’s, Core plus, 4.25% to 5.25% in value add in 5.25% to 5.5% and we've seen that go as high as a 6%. Unlevered IRR are in the 7% range. Levered IRR is in that 10% to 14% range depending on what risk bucket you want to play in.

As Steve alluded to also, we are going to be looking at longer term value creation for our shareholders and we will price our assets appropriately. It's not just about going in cap rates, it's about longer-term growth and value creation for our shareholders.

Operator: Your next question for today is coming from Allen Peterson at Green Street.

Q: I was just hoping you could share the breakout between the legacy mid-Atlantic same store portfolio and the new 2023 additions. Just your expectations on NOI growth between those two groups would be helpful.

Steve Freishtat – Vice President, Finance
Of our 2023 same store pool, there were two Atlanta communities that came into the same store pool this year and we are seeing growth in the Atlanta portfolio, higher than D.C.

Amy Hopkins – Vice President, Investor Relations
Our Atlanta communities are contributing about 60 basis points to our same-store NOI growth for the full year.

Q: In regards to the recent term loan extension, could provide any color, if there's any difficulty right now getting those term loan extensions through, given that some banks may have closed off lending activity for multifamily activity today.

Steve Freishtat – Vice President, Finance
What we've heard from the banks is they are being more selective in this market, they are choosing to do shorter term loans. Our term-loan was a two year, maybe a year or two ago, it would have been a five year. But the banks are selecting based on relationships and based on the sector that companies are in. Being in the multifamily sector, we had an easier time than if we had a portfolio from a year ago with office. But what we saw was the banks are doing shorter term for two years. The pricing has not changed that much, but the upfront fees have gotten a bit more expensive as they're looking for higher returns.

Q: Just one more on the internalization of management for the portfolio. Have you had difficulties in retaining onsite staff or are you having to go out into the marketplace and hire new personnel? Or are you able to transfer the staff at the property smoothly?

Steve Riffee – Executive Vice President & CFO
We've just finished our fourth wave and we've had tremendous success in recruiting and getting people to change jerseys. We're heading into Wave five we got a lot of acceptances there, but we also have beefed up our recruiting and we're supplementing the folks that are coming on board from our third parties with people from the outside. We obviously build our own regional management team. We're making great progress. For the most part, we've been able to retain, we had incentives for people to change jerseys and come to our company.

Operator: Your next question is coming from Young Ku at Wells Fargo.

Q: Wanted to get your thoughts on rent controls, which seems like a hot topic these days. It looks like there have been a couple of rent control motions that are being pushed forward in Maryland. Could you provide some color regarding these and potential impact this may have on your portfolio.

Paul McDermott – President & Chief Executive Officer
Philosophically, we don't believe rent control addresses the main issues which are housing affordability. History would tell you and our research tells us that it really doesn't work and the costs are high and it does not reduce the cost of housing for those who it is intended to serve. I think the best renter protection is an abundant supply of affordable housing. Regarding the near-term risk of rent restrictions, we look at the markets that we operate in right now and I'll get to Montgomery County, where we have three assets. The bulk of our portfolio is Northern Virginia and Atlanta. We don't expect rent control pressure or proposals over the near to medium term. We do have a small amount of exposure in Montgomery County, which represents 6% of our NOI, which had post-pandemic rent restrictions. But we've seen proposals, but we know that nothing is put in place, but the threat is there. Our job is really to work with the local officials and work with the lobbyists here on the Hill to try to find a more palatable solution then rent control. Personally, having been in the affordable business, they should fix what they have in terms of LIHTC voucher systems, etc. It's prevalent, it's a top priority. But right now, it impacts a small part of our portfolio.

Q: You talked about strong job postings in the Metro DC area, I was wondering if you can talk about some in-migration trends within that market, specifically, and in Atlanta?

Grant Montgomery – Vice President, Research
We've seen strong move ins to the Washington region. Greater than 75% of the move ins are actually people coming from the Washington region. We've also seen strong move ins into both Atlanta and Washington, D.C. We looked at an analysis that of forwarding data and move-in versus move-outs outpaced by about 53%. We're still seeing strong movement into the greater Washington, D.C. area. There have been headlines, obviously, about the District being a little softer, but again even within the Washington, D.C. region with the vast majority of our portfolio is suburban, with about 80% being in Northern Virginia. We're seeing good trends on that front and plenty of traffic.

Q: Can you provide some color regarding some of the credit trends within your tenant base in terms of trends you're seeing on average FICO scores, average income or
delinquency rates within your portfolio?

Grant Montgomery – Vice President, Research

The trend that we track most closely is our rent to income ratios. We mentioned in our prepared remarks, that we've actually seen a decline in our rent to income ratio in our Atlanta properties that we own now that are entered the same store pool, we've actually decreased to about 25%
as we've seen, strong growth for new renters moving into our properties and also improving the credit profile versus prior ownership. In the Washington Metro, we've seen the numbers stay steady, which even in the face of strong rent growth we're around 26%, which is in line with our long-term average total rent to income ratios for our assets.

Operator
Your next question for today is coming from Anthony Pallone at JP Morgan.

Q: My first question is in terms of your internalization and when you did the transformation of the company, you talked about going into multiple new markets. You're in Georgia now. If you go to some other places on your target list, will the internalization be able to handle those? Or would you have to still use some third parties before bringing it in.

Paul McDermott – President & Chief Executive Officer
The internalization we will be able to handle those. We've already planned for that. As we alluded to when we rolled out our diversification strategy, we have always planned to both geographically diversify and obviously that will be accompanied by diversified management. We plan on having boots on the ground in the major markets that we expand into.

Q: You mentioned about 600-unit renovations for 2023. Can you just remind us about how much you think you'll spend on those? And also any color on recurring CapEx for this year, either per unit or in total?

Steve Freishtat – Vice President, Finance
For the 600 units, we're expecting about $9 million of spend related to that. We've looked at the recurring CapEx and we see it as 5% of our NOI, which again, is for the multifamily side, which is significantly less than the 20% numbers that we were seeing when we had commercial.

Operator
Thank you. And there are no more questions in queue. I would now like to hand the call back to Paul McDermott for closing remarks.

Paul McDermott – President & Chief Executive Officer
Thank you. Again, I would like to thank everyone for your time and interest today and we look forward to speaking with many of you over the next several weeks.

Operator
This does conclude today's conference. You may disconnect your lines at this time and have a wonderful day. Thank you for your participation.
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