Q3 2024 Earnings Call ***(Corrected version)***

Event Details

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Company: Sonida Senior Living, Inc.
Ticker: SNDA-US

Company Participants

Jason Finkelstein - IGNITION Investor Relation, Founder
Brandon M. Ribar - Sonida Senior Living, Inc., President, Chief Executive Officer & Director
Kevin Detz - Sonida Senior Living, Inc., Chief Financial Officer

MANAGEMENT DISCUSSION SECTION

Operator

Thank you for standing by. My name is Novey, and I will be your conference operator today. At this time, I would like to welcome everyone to the Sonida Senior Living Q3 2024 Earnings Call. Please be aware that all lines have been placed on mute to prevent any background noise. I would now like to turn the call over to Jason Finkelstein, Investor Relations. Please go ahead.

Jason Finkelstein

Thank you, operator. All statements made today, November 13, 2024, which are not historical facts may be deemed to be forward-looking statements within the meaning of federal securities laws. The company expressly disclaims any obligation to update these statements in the future. Actual results or performance may differ materially from forward-looking statements. Certain factors that can cause actual results to differ are detailed in the earnings release that the company issued earlier today as well as in the reports that the company files with the SEC from time to time, including the risk factors contained in the annual report on Form 10-K and quarterly reports on Form 10-Q. Please see today's press release for the full Safe Harbor statement, which may be found in the 8-K filing from this morning at the company's Investor Relations page found at www.sonidaseniorliving.com. Also, please note that during this call the company will present non-GAAP financial measures. For reconciliations of these non-GAAP measures to the most comparable GAAP measure, please also see today's earnings release.

At this time, I'd like to turn the call over to Sonida Senior Living President CEO, Brandon Ribar, for opening remarks.

Brandon M. Ribar

Thank you, Jason. Hello and welcome to our 2024 third quarter earnings call. I'm joined today by Kevin Detz, our Chief Financial Officer. Earlier today, we released our Q3 earnings and investor presentation, which will be referenced throughout this call as we discuss our strategic priorities and operating results, in addition to our view on the year ahead in 2025. You can find our latest presentation at sonidaseniorliving.com in the Investor Relations section if you would like to follow along. In addition, we have included supplemental earnings information within our investor presentation consistent with the prior quarter release.

Q3 remained quite busy for Sonida. I'm extremely grateful to our team who continue providing great care and services for our residents, resulting in ongoing growth in occupancy and margins. I'll touch on these points in detail in a moment, but first I'd like to discuss several key capital allocation events that occurred since the end of Q2. First, we completed acquisitions of 14 new communities with more than $160 million in total asset value. We expect to use Sonida's broad operating platform to drive significant value to these assets and have seen initial positive momentum as part of the Sonida operating system. Second, we've put in place a new $150 million secured line of credit on advantageous terms. In addition, the company successfully accessed public capital in a broad overnight equity offering, resulting in $130 million of new capital at a price of $27 per share. This is an important milestone for the company as the first registered overnight equity offering in more than a decade. Together with our new credit facility, Sonida has the tools in place to access capital and maintain balance sheet flexibility to take advantage of further acquisition opportunities.

Finally, I'm pleased to share that we recently reached agreement with Fannie Mae to extend $220 million of outstanding mortgages covering 18 communities which currently have a maturity date of 12/31/2026 to a new revised maturity date of January 1, 2029. This extension, which is subject to completion of definitive documentation with Fannie Mae, allows us to retain attractive fixed rate debt and move all mature – material debt maturities for the company into 2027 and beyond. These capital allocation successes, coupled with the continued improvement in our same-store portfolio, serve as critical indicators of the progress we are making. Across both operational and capital allocation endeavors, we are committed to delivering results to all of our stakeholders, including residents and their families, our employees and our investors.

On the growth front, we closed our sixth transaction of the year in early November, increasing the total number of communities added this year to 22 of which 19 are owned outright or through strategic joint ventures, and three of which are capital-light management agreements. This growth amounts to nearly 2,000 units added or a 30% increase to our operating portfolio in just the past six months. The transaction environment remains compelling and our growing acquisitions team has line of sight on a robust 2025 pipeline of attractive growth opportunities. I am incredibly proud of our operations team for meeting this challenge of quickly incorporating these new communities into the Sonida family. Given our confidence in the depth of the opportunity set and our ability to find outsized return opportunities, we've chosen to invest in both acquisition and integration resources to strengthen the foundation for long-term value creation.

From an operating performance perspective, our same-store portfolio continues to deliver growth both in occupancy and margin with occupancy, achieving a new weighted average quarterly high at 87%, growing 210 basis points against Q3 of last year and 80 basis points from Q2 this year. On the margin front, the same-store portfolio continues to generate strong operating results on a year-over-year basis, with our community net operating income increasing more than 18% when removing prior year nonrecurring grant income. Kevin will provide further detail on the financial performance in the quarter in his comments.

The occupancy and margin gains reflect continued strength across each of our operating regions, with occupancy growth for the quarter concentrated in our independent living care level. We are seeing continued positive momentum in the second half of the year and are optimistic about the tailwinds supporting continued NOI growth. Achieving portfolio-wide occupancy of 90% is our next significant milestone. In our Q3 investor presentation, we have provided an illustrative view of the potential value creation from both the same-store portfolio as well as the communities purchased this year, the vast majority of which are not in or not meaningful contributors to the third quarter results. Based on our high quality portfolio, industry-wide supply demand dynamics and most importantly, our skilled operating teams, we believe that normalized occupancy can exceed 90% over the next several years.

We are poised to deliver further NOI growth and margin expansion as we push the ongoing improvement in our same-store portfolio and accelerated revenue and margin stabilization in our recently acquired communities. We see an opportunity to further compound our growth by capitalizing on our robust pipeline of additional acquisition opportunities, leveraging our operating capabilities and capital availability. I'll spend a few minutes discussing the fundamentals of our business that support our ongoing confidence in the upside across our 93 communities. We continue to prioritize the strength of our local and regional leadership, as well as the development of activities and programming to deliver a differentiated resident experience. The second half of the year has shown favorable trends in retention at both the community leadership and staff level within our communities. And we continue to develop tools to strengthen employee engagement in both our new and existing communities. On the resident programming front, the advancement of our Joyful Living program in both independent and assisted living settings have contributed to stability in average resident length of stay and enhance our overall reputation score as measured by third party reviews.

Switching to sales and marketing, continued emphasis on development, incubation and implementation of technology to drive down resident acquisition costs and improved conversion metrics has led to a higher percentage of organically generated leads and move-ins. Lead volume in the third quarter increased 7.5% year-over-year and 10% sequentially from Q2 in our same-store owned portfolio. Leads generated through organic channels, including the Sonida website and local referral sources now represent 56% of total lead volume in 2024 versus 52% in 2023 and only 41% in 2022. Prior to our substantial investment in our digital platforms. We are especially pleased that move-ins driven by digital marketing enhancements, including website architecture changes, updated paid search strategy and greater scrutiny over third party listings, have significantly outpaced the change in paid move ins from third party aggregators in 2024. We are excited to further leverage the sales and marketing approach that has delivered 14 consecutive quarters of same-store occupancy growth to drive significant near-term performance improvement and value creation in 2025, particularly in our newly acquired communities.

Through a combination of occupancy growth, ongoing rate improvement and effective expense management, our investments are targeted to stabilize at a double-digit cap rate, delivering significant earnings accretion. We've included a summary of our 2024 year-to-date investments in the investor deck, and each deal reflects a specific approach to finding growth opportunities in the current market. From distressed purchases through banking relationships to strategic joint ventures and recapitalizations, our deep and wide network of relationships continues to deliver accretive investment opportunities. Our investment pipeline remains robust and fluid with clear line of sight to additional opportunities consistent with our targeted transaction profile and propelled by our multifaceted sourcing strategy.

While we are starting to see increased competition and pricing for high-quality and fully stabilized assets, we continue to see a wider bid ask spread for value-add situations and believe the industry still suffers from limited capital availability. Moreover, we are accessing off market transactions by leveraging our industry relationships under the leadership of our CIO, Max Levy, who was appointed earlier this summer. We believe our corporate structure as a pure play senior housing owner, operator and investor, uniquely positions Sonida to access differentiated acquisitions and to deliver significant benefits to shareholders by fully controlling our operations and reinvesting cash flow into high return investments. The combination of availability on our existing credit facility and our ability to access the equity markets when pricing is supportive, allows us to aggressively pursue and complete acquisitions of new communities with significant operational upside at an attractive price per unit.

We see meaningful NOI upside in our same-store portfolio and are focused on acquisitions that we believe will be accretive on a stabilized basis due to even more significant NOI upside from stabilization and/or wide going-in cap rates. From a capital structure perspective, we intend to manage the balance sheet to de-lever through both operational improvement and the funding of our acquisitions with lower leverage.

In summary, Sonida's focus on results-driven operational strategies and capital allocation yielded another quarter of strong performance and meaningful portfolio expansion. Same-store revenue, community net operating income, resident rates and occupancy demonstrated continuing gains year-over-year. The excitement across the entire Sonida team is evident as the company aggressively pursues further growth fueled by operational excellence and a commitment to building strong teams and creating a differentiated resident experience and living environment. As the future unfolds, our goal is to continue delivering strong operating results and measured ongoing improvement in the newly acquired communities, further demonstrating the strength of our people and our platform.

I'll now turn it over to Kevin for a discussion of the financial results.

Kevin Detz

Thanks, Brandon. I will be walking through select pages of today's investor presentation, starting with slide 5. (00:12:36) some of our financial highlights, we achieved a 14th consecutive quarter of occupancy growth for our same-store portfolio. As a reminder, the same-store portfolio excludes the 19 communities acquired over the past six months. On a year-over-year basis, same-store adjusted community net operating income which excludes the non-recurring impact of $500,000 in state grants received in Q3 2023 increased 18.3%. Beyond the increase in occupancy the NOI growth was achieved through blended resident rate increases of 5.5% as well as continued optimization of the portfolio's variable operating expense profile. I will touch upon both rate and operating expenses in more detail later in the presentation.

Earlier, Brandon referenced the company's execution on its strategic growth plans. Beyond our strong operating results, we are very pleased with two significant capital events that are foundational to our growth and the next phase of the company's development. In July and August, the company closed a senior secured credit facility for $150 million and raised $130 million of gross proceeds and a public equity offering. These transactions provided the company with capital for the acquisition closed in the fourth quarter and a discounted debt payoff that I will discuss in a bit, as well as providing additional dry powder for future bolt-on acquisitions. We expect that these transactions will be accretive to the company's equity value as we stabilize the communities acquired. Amidst similar buying opportunities and improving industry outlook and continue improving same-store portfolio performance, we believe further delevering is achievable with a debt to EBITDA ratio goal of below 7X, consistent with public peers.

Rounding out the highlights from this past quarter, in August, the company entered into a loan modification agreement with one of its lenders on two cross communities in Texas. The modification included revised maturities and, more importantly, the ability to make a discounted payoff of $18.5 million on the $28.7 million balance. On November 1, the company made the discounted payoff, which represented a $10 Million or 36% discount on the loan principal balance. These two communities represent the last two communities that required material restructuring for the company's legacy debt stack with the company having addressed 58 of 60 mortgage loans in the past 12 months. The remaining two loans account for approximately 2.5% of the outstanding debt balance.

Moving ahead to slide 15. Resident rates, which exclude onetime community fees and other ancillary revenue streams, increased 5.5% from the same quarter in 2023. Diving deeper into the revenue, level of care fees had similar a year-over-year rate increases, due in large part to the company's recently developed pricing structures on its memory care level. In Q3, the company saw a sequential quarterly rate decline. Beyond the reemergence of seasonality within the industry, the 0.5 percentage decline on rate from Q2 2024 is attributed to occupancy mix. Specifically, our net increase in occupancy quarter-over-quarter had an 84% composition of lower rated independent living occupancy increases with the rest of the modest increases in occupancy driven by our higher rated assisted living and memory care lines. Finally, discounts and concessions both on a percentage of revenue basis and absolute basis continue along a two-year downward trend. The weighting absence of discounts and concessions supports the overall stability of the company's rate profile and service offering and is consistent with Brandon's comments on our direct efforts to internally source more quality leads and conversions over the same period.

Moving to operating expense trends on slide 16. The cost of incremental labor to incremental revenue continues to show stabilization. For purposes of seasonal comparability. note that Q3 is burdened with one more workday and one more holiday as compared to Q2. On a year-over-year basis, Q3's total labor as a percentage of revenue improved by 230 basis points. This is consistent with the 290 basis point increase from Q2 2023 to Q2 2024, using the same metric. The number of same-store fulltime employees in Q3 2024 was down slightly from the previous quarter. The annual increase in average wage rate from Q3 2023 to Q3 2024 was 3.5%, which is at or slightly below inflationary levels over the same period. We believe these trends are sustainable indicators to continued margin expansion as the portfolio's occupancy base grows.

On slide 17, non-labor operating expenses are also showing continued signs of stabilization. On an absolute basis, these costs increased approximately $400,000 from prior quarter. Increases in utility costs comprise nearly the entire amount of the sequential increase from Q2 2024. For seasonal comparability, the sequential increase is relatively consistent with the same increase from Q2 2023 to Q3 2023. As stated above, the company continues to drive lower cost of sales through its digital marketing and local sales programming.

Concluding the remarks on Q3 financial highlights, we will turn our attention to the balance sheet. On the capital investment front, through the third quarter, we have invested more than $18 million year-to-date across both technology and community-based capital expenditures, including both targeted NOI generating capital and recurring maintenance. We expect these targeted NOI projects which feature additional or converted resident units to positively impact performance in 2025. Our debt is comprised of 68% fixed rate notes, meaning variable rate notes nearly fully hedged, yielding a weighted average interest rate just above 5% for the portfolio. As mentioned earlier, the company continues to focus on delevering its balance sheet. As of the date of this release, the company has agreed in principle on terms with Fannie Mae that would extend the maturities of 18 of its individual mortgage communities with a total debt balance of $220 million by two years. This result at a January 1, 2029 maturity date for all 37 communities under Fannie Mae financing. In exchange for the extended loan term, the company will make a series of principal paydowns totaling $10 million over the revised term of the loan, with the first payment expected this quarter. This transaction is subject to definitive documentation by both parties. As always, we appreciate the collaborative nature of our relationship with Fannie Mae over the last two years.

As of today, the company is in compliance with all financial covenants required under its mortgages and revolving credit facility. Prior to turning the presentation back to Brandon, I wanted to spend some time on the path to value creation for the company's shareholders. Starting with our annualized Q3 NOI of $67 million, we selected illustrative data points for both occupancy and NOI margin percentage, which are supported by general industry history as well as our own recent trajectory. Applying 90% occupancy and 30% margins to our same-store portfolio yields an incremental $11 million of NOI contribution. Additionally, layering in similar stabilization achievement of the 19 communities acquired this year with joint ventures being calculated at our respective ownership share would illustratively produce an incremental $22 million of NOI. Under this assumed methodology, the total combined NOI for our owned assets would be approximately $100 million. Note that this chart makes no assumption on future rate growth and is based on current in-place rate levels. To date, the company has already incurred the majority of G&A costs needed to support the additional 19 communities. As a reminder, the company incurs approximately $4.5 million of public company costs annually.

In closing, we continue to be encouraged by the operating trajectory of the portfolio, including our ability to realize performance improvement on the recently acquired communities. Back to you, Brandon.

Brandon M. Ribar

Thanks, Kevin. 2024 continues to present opportunities for Sonida to deliver on our differentiated approach to both internal and external growth. With two months remaining in the year, consistent year-over-year growth in our in-place portfolio remains a primary focus with an expectation to achieve positive recurring cash flow by year end, when including the benefit of our recent acquisitions. Coupled with the ongoing identification and completion of accretive investments within our existing pipeline, it's an exciting time in our business. We firmly believe Sonida is positioned to fulfill our commitment to residents, employees and shareholders to continue building a best-in-class owner, operator and investor in senior living. Thank you all for participating and this concludes today's conference call.

Operator

Ladies and gentlemen, thank you all for joining. You may now disconnect.