MMA Capital Management, LLC [MMAC]
2017 Year End and Business Update Conference Call
Monday, March 19, 2018, 8:30 AM ET

Company Representatives:
Michael Falcone, President and Chief Executive Officer
Dave Bjarnason, Chief Financial Officer

Presentation:

Operator: Good morning, ladies and gentlemen, and welcome to the MMA Capital Management, LLC, 2017 year-end and business update conference call. My name is Anita, and I will be your coordinator for today. At this time, all participants are in a listen-only mode. We will facilitate a question-and-answer session at the end of this conference call.

Some comments today will include forward-looking statements regarding future events and projections of financial performance of MMA Capital Management, which are based on current expectations. These comments are subject to significant risks and uncertainties, which includes those identified in the Company's filings with the Securities and Exchange Commission. These could cause actual results to differ materially from those expressed in these forward-looking statements. The Company undertakes no obligation to update any of this information contained in the forward-looking statements.

Please note this event is being recorded.

I would now like to turn the conference over to Mr. Michael Falcone, CEO of MMA Capital Management. Please go ahead.

Michael Falcone: Thanks, Operator. Good morning, everyone, and welcome.

With me on the call today are Dave Bjarnason, our Chief Financial Officer, and Senior Vice President Megan Sophocles. Gary Mentesana, who usually joins us, is on vacation this week and will not join the meeting this morning. That said, Dave and I will deliver our prepared remarks, after which we will all be available to take questions.

The purpose of our call today is to review our full-year 2017 results and to provide an overall business update, including updates following the recent transaction with Hunt and our transition to an external management arrangement. Although we will necessarily discuss some of the business lines we sold, because they are part of our 2017 results, I will spend more time discussing our continuing operations rather than focusing on the recently sold businesses.

With respect to our financial results, which Dave will review in detail later, we ended the year with $137.5 million of common shareholders' equity, which represents an increase of $12.2 million, or 9.8% for the year. Diluted common shareholders' equity per share came in at $24.48,

an increase of $3.73, or 18%, for the year, which reflects the impact of both performance and our buyback plan on the book value per share.

The net increase in common shareholders' equity in 2017 was driven by $22.7 million of comprehensive income, which was partially offset by $10.5 million of other reduction to common shareholders' equity that was primarily driven by share buybacks. Overall, income that we recognized in 2017 reflects positive returns from realization events in our low-income housing tax credits business line, from real-estate-related investments, from our solar lending joint ventures and from investor capital-raising efforts in South Africa. As a result, we saw year-over-year increases in fee and other income, equity and income from unconsolidated funds and ventures, and net income from consolidated funds and ventures that is allocable to common shareholders.

During the year, we purchased approximately 400,000 shares through our share buyback program at an average price of $24.01 per share, which goes to a $9.6 million reduction in common shareholders' equity. We continue to view share buybacks as a tool in our toolbox for creating shareholder value. But with the Hunt transaction we have added other significant tools that we will use in addition to, and perhaps in lieu of, share buybacks as time goes on.

Chief among these tools is the ability to make accretive investments based on investment opportunities that we expect to see as a result of the origination capabilities of Hunt. In the long term, the Company will seek to invest capital at high-single or low-double digit returns which, combined with our current invested capital, ability to utilize tax losses and relatively inexpensive borrowing costs, could provide significant long-term growth opportunities for the company through the investment of retained capital. Our long-term goal is to issue new shares in order to grow our investment base and to do so at such times as we determine that issuing new shares would be accretive.

In the near term the Board has adopted a 2018 share buyback authorization, currently set at 125,000 shares and with a buyback price limit of $30 per share, roughly a 9% discount to the price at which we issued shares earlier this month, which was $33 per share.

Across our US operations more broadly we saw positive returns from our bond portfolio, experienced continuing growth in our energy lending joint ventures, and saw our LIHTC business line continue to perform as expected, resulting in a very strong year of performance for the US businesses.

Within our leveraged bond business line, our bond portfolio continues to perform at a high level. There were no new defaults, while the weighted average debt service coverage and collection rate of our holdings further increased throughout the year. The leveraged bond portfolio contracted slightly in 2017 due to runoff. At December 31, 2017, this portfolio's UPB and fair value was $231 million and $236 million, respectively, while at December 31, 2016, the [UPB] and fair value was $249 million and $256 million, respectively. Although this portfolio's UPB decreased slightly in 2017, and excluding the effects of subordinated cash flow bonds its weighted average pay rate increased by 13 basis points during the year to 6.21% at December 31, 2017, while the debt service coverage ratio of the leveraged bond portfolio also increased from

1.05x to 1.10x over the same period. The leveraged bond business line was generally not impacted by the sale to Hunt and we expect that our investments in bonds will remain a primary source of revenue in the coming years.

With our renewable energy finance business, the carrying value of our equity investments in our renewable energy joint ventures was $97 million at December 31, up from $75.5 million at the beginning of the year. This net increase was driven in large part by our initial capital investment in Solar Development Lending, LLC, or SDL, which originates solar development loans. It also invested in construction loans during the year. Our investments in these joint ventures continue to be a source of future investment income and the opportunity to put additional capital to work in what we hope will continue to be a growth area.

Our LIHTC business continues to meet or exceed our expectations, with significant year-over-year asset management fee revenue growth. In prior quarters, this is where I would remark that while this year represented a strong performance from this business line, results in the future periods are expected to be lumpy and hard to predict. In light of the Hunt transaction we can actually simplify that statement to say that we enjoyed a very good year of returns from that business line, but we are able to capture the future value from this business line as part of the Hunt transaction, on which I will also provide a brief update shortly.

With respect to the international operations, for the year our operations in South Africa performed well, mainly from our continued capital raising efforts for Fund II. Although we saw performance improvement in our international operations during 2017, it was part of what we sold in the Hunt transaction, including both the investment and property management operations. The only exception is that we retained an 11.85% ownership interest in the South Africa Workforce Housing Fund, the first investment fund that was purchased from an original investor in 2017 pursuant to a put requirement, and that enabled that investor to recycle their investment into Fund II. This retained equity investment is expected to be monetized over the next few years as the South Africa Workforce Housing Fund completes the property exits and wraps up operations.

Lastly, from a corporate operations perspective during 2017 we executed a discounted purchase of approximately $26.4 million of subordinated debt during the year, which resulted in a $4.8 million debt extinguishment gain. At year end, and based on its unpaid principal balance, we had $92 million of relatively inexpensive subordinated debt outstanding.

Additionally, as Dave will further discuss, all material weaknesses in our internal control over financial reporting that were identified in our 2016 Form 10-K have been remediated and in this regard we received a clean opinion from our external auditor related to the effectiveness of our internal controls at December 31, 2017.

Before turning the call over to Dave, I'd also like to provide a quick update on various elements of the Hunt transaction, given the changes to our business model and subsequent transactions.

As we disclosed in both our January announcement and Form 10-K filings, we will recognize an estimated $32 million increase in common shareholders' equity in the first quarter of 2018 in

connection with the sale of our LIHTC business, our international operations and certain assets. And as we previously discussed, we would also recognize an estimated $14 million increase in GAAP common shareholders' equity should Hunt decide to take an assignment of the MGM agreements and, subject to the terms of such agreements, consummate the acquisition of the MGM LIHTC business.

In saying this, I should mention that these estimated increases to common shareholders' equity are expected to differ from amounts that will ultimately be recognized in our financial statements, given that there are various purchase price adjustments that are pending finalization, while various transaction-related expenses are pending recognition in our financial statements. Further, as we just discussed before, we will recognize an estimated $9 million increase to common shareholders' equity on January 1 in connection with the adoption of new revenue recognition rules, the transitional impact of which was primarily attributable to contracts of the company's conveyed LIHTC business.

Separately, Hunt agreed to acquire from us 250,000 common shares in two equal installments, with the first purchase occurring at $33 per share and the second to occur at $34 per share, for an average price of $33.50 per share. We reported a week ago that Hunt successfully closed on the first purchase, acquiring 125,000 shares in exchange for $4,125,000 of cash on March 9, 2018. Pursuant to the transaction terms, the final purchase requirement must be completed by July 9, 2018.

With that, I'll turn the call over to Dave, who will discuss the financial results in greater detail before I revisit the changes to our business from the Hunt transaction. Dave?

Dave Bjarnason: Thank you, Mike, and good morning, everyone.

As I provide an overview of our results, I will refer to various tables in Item 7 of our Form 10-K.

In the fourth quarter we recognized a net increase in common shareholders' equity of $1.8 million while, as Mike mentioned, common shareholders' equity increased on a full-year basis by $12.2 million to $137.5 million. In this regard, diluted common shareholders' equity per share increased to $24.28 per share, which represented a $1.22 per-share increase in the fourth quarter and a $3.73 dollar per-share increase on a full-year basis.

As Mike also indicated, increases in common shareholders' equity and diluted book value per share were driven by $22.7 million of comprehensive income that we recognized in 2017, including $7.7 million in the fourth quarter. In this regard, comprehensive income that we reported, which exceeded what we reported in 2016 by $3.8 million, included $19.4 million of net income and $3.3 million in other comprehensive income. I'll discuss in more detail later the key drivers of comprehensive income that we reported in 2017.

As a partial offset to comprehensive income that we reported in 2017, we recognized $10.5 million of other reductions in common shareholders' equity, including $5.8 million in the fourth quarter, that were primarily due to share repurchases. As Mike mentioned, we purchased

approximately 400,000 shares through our share buyback program at an average price of $24.01 per share, which caused a $9.6 million reduction in common shareholders' equity.

From a liquidity and capital resources perspective, we ended 2017 with $39.3 million of cash and cash equivalents, which decreased $6.2 million on a year-over-year basis. The net cash flows used in financing activities modestly exceeded net cash flows provided by operating and investing activities.

Part of this net decrease in our unrestricted cash position was driven by the deployment of $21.8 million of corporate cash to execute discounted purchases of fixed rate subordinated debt in 2017. And in the process, we recognized $4.8 million of extinguishment gains. More broadly, however, while we used $23.3 million of net cash flows in financing activities in 2017, we generated net cash flows of approximately $17.1 million from operating investment activities.

In taking a closer look at drivers of comprehensive income that we reported and that I previously mentioned, we reported $19.4 million of net income allocable to common shareholders in 2017, including $5.5 million in the fourth quarter.

As you can see on Table 9 of our filing, net income allocable to common shareholders that we reported in 2017 was $23 million less than we reported in 2016. However, it should be noted, as you can also see in Tables 7 and 9 of our filing, $33.1 million of gains and $3.6 million of losses that we recognized in net income in 2016 and 2017, respectively, represent equity-neutral adjustments that were counterbalanced in full by offsetting adjustments that we recognized in other comprehensive income during those reported periods. In other words, the year-over-year decline in net income allocable to common shareholders is similarly masked by year-over-year increases in other comprehensive income.

This said, I'll now touch on in a little more detail key performance drivers and results associated with each of our primary business and financing activities that affected common shareholders' equity, starting with a look at our bond portfolio.

Excluding equity-neutral adjustments that I mentioned earlier, we reported approximately $3.1 million of net fair value gains in 2017 related to both bond investments that are recognized on our balance sheet and total return swaps, or TRS, that we accounted for as derivatives, with net fair value gains on these instruments being relatively flat in the fourth quarter. By comparison, we recognized $12.7 million of net fair value gains associated with our leveraged bond portfolio in 2016. In this regard, net gains that we reported in 2017 on our leveraged bond portfolio were primarily attributable to fair value increases associated with underlying properties to secure certain of our subordinated cash flow and nonperforming bond investments.

From a yield perspective, we recognized $9.2 million of interest income in 2017 related to our bond investments, including $2.1 million in the fourth quarter. As you can see from Table 11 in our filing, this represents a $2.3 million decrease compared to interest income to be recognized in 2016 on our bond investments. This decrease was driven primarily by portfolio runoff, or the paydown of the investments in this portfolio, coupled with the elimination of certain bond

investments for reporting purposes due to the consolidation of certain property partnerships in 2016.

With respect to other investments in the leveraged bond business line at December 31, 2017, we directly owned one parcel of land and are an equity partner in the Spanish Fort venture, whose incremental tax revenues secure our infrastructure bond investments. Net returns in 2017 for investments in this sub portfolio that we owned at December 31 were relatively negligible although, as discussed in the third quarter, the Savannah River Landing development was sold and, as a result, we recognized $3.8 million of equity in income from the partnership that held such real estate.

With respect to interest rate hedges, we recognized $1.3 million of net fair value losses in 2017, including approximately $500,000 of net fair value gains in the fourth quarter. This compares to approximately $4.1 million of net fair value gains that we recognized on these hedge positions in 2016. This year-over-year decline in net fair value gains and losses was driven by the flattening of the yield curve.

With respect to cash loans and other short-term investments of the Company, we recognized approximately $1.1 million of interest income in 2017, including $180,000 in the fourth quarter. As you can see from Table 10 of our filing, we reported $2.4 million less in interest income in 2017 associated with these investments compared to the interest income that we recognized on these investments in 2016, the decrease of which was in large part due by the sale in 2016 of solar loans to solar ventures that we managed.

With respect to our Energy Capital business, we continued to see positive returns in 2017 in the solar ventures that we managed. At December 31, 2017, the unpaid principal balance loans that were funded through the solar ventures was $278.4 million, while loans outstanding had a weighted average remaining maturity and coupon of 9 months and 8.7%, respectively. In this regard, our related equity investments in these ventures [had a total] value of $97 million at December 31, 2017.

This said, in 2017 we recognized $9.2 million of equity income from these ventures, including $2.2 million in the fourth quarter. As you'll see in Table 15 of our filing, we recognized in 2017 $2.9 million more of equity in income from our solar ventures relative to what we recognized in 2016, an increase of which was driven primarily by annual increases in the amount of loan origination and related fees earned by the solar ventures. We also recognized approximately $2.3 million of income in 2017 associated with reimbursements from the ventures for our direct costs associated with management-related activities.

With respect to returns from our LIHTC business, we further discuss in our filing the various interests and obligations that pertain to this business line. In connection with our interests and obligations associated with TC Fund I we recognized $9 million of asset management fees in 2017, including $1.1 million in the fourth quarter. We did not recognize any asset management fees from TC Fund 1 in 2016.

We also recognized in 2017 approximately $1 million of other guarantee-related income due to the amortization of deferred guarantee fees and the repayment of a mandatory loan that we made to TC Fund 1 in connection with our guarantee.

With respect to our interest and obligations associated with Morrison Grove Management, or MGM, we collected about $1.9 million in interest in 2017 associated with a $13 million subordinated loan that we made to MGM, including $900,000 in the fourth quarter. However, because this loan was not recognized for financial statement purposes at December 31, 2017, interest that we collected on this loan was deferred on our balance sheet and therefore is not recognized in earnings. As of December 31, 2017, we recognized $10.3 million of deferred revenue in connection with principal and interest payments received from MGM.

In 2017 we reported $1.7 million of income from direct real estate investments of the LIHTC business line, which is primarily attributable to the disposition of two investments acquired during the fourth quarter of 2015. Additionally, as detailed in Table 17, which is located on Page 32 of our filing, in 2017 we recognized $4 million of net income from consolidated (inaudible) that was allocable to common shareholders. These allocations, which amounted to a net loss in 2016 of $3.3 million, primarily relate to guaranteed fees, equity losses from lower-tier property partnerships and interest income on bond investments that are eliminated for reporting purposes.

The year-over-year increase in net income from CFVs allocable to common shareholders is primarily due to the sale of the underlying real estate of one of the company's consolidated partnerships during the fourth quarter of 2017 that resulted in the recognition of approximately $5.7 million of net income from consolidated funds and ventures that was allocable to common shareholders.

With respect to funds that we managed through International Housing Solutions, or IHS, we recognized $12.6 million in fee and other income in 2017, recording $3.6 million in the fourth quarter. This represents a $5.9 million increase compared to what we reported in 2016. And it was primarily driven by catch-up management fees that we recognized in connection with additional invested capital that was closed in IHS Fund II SA and IHS Fund II SSA in 2017.

In connection with our equity co-investments in funds managed by IHS, which we account for using the equity method, the carrying value of these investments in our consolidated balance sheet was $17.2 million at December 31, 2017, while we recognized equity in income with the corresponding funds that we manage of approximately $300,000 in 2017, which compares favorably to $500,000 of equity in losses in funds that we managed in 2016. The improvement in portfolio valuations, coupled with the upsides of our equity co-investment in the South Africa Workforce Housing Fund in the third quarter, drove this year-over-year increase.

As far as interest and other operating expenses, I'll start with a quick look at our cost of funding. You can see from our filing that our financing arrangements are divided into two groups, based on their purpose -- debt obligations that finance bonds and other interest-bearing assets, which we refer to as asset-related debt; and debt obligations that finance other assets and activities of the company, which we refer to as other debt.

With respect to asset-related debt, the total UPB of this debt was $83.9 million at December 31, 2017. While only modest amortization occurred in 2017, we recognized approximately $1.8 million of interest expense associated with asset-related debt in 2017, including approximately $500,000 in the fourth quarter.

As you can also see from Table 10 of our filing, this represented a year-over-year increase of $400,000 in the cost of funding associated with this debt, an increase of which, in large part, was driven by both an increase in the reference rates on the variable rate debt obligations and the execution of additional TRS on certain bond investments (inaudible).

Our reported cost of funding associated with other debt was $4.5 million in 2017, including $1 million in the fourth quarter. As you can see from Table 12 in our filing, our cost of funding associated with other debt was steady in the aggregate on a year-over-year basis. This is because year-over-year decreases in our cost of funding associated with our subordinated debt, which was driven by discounted purchases of $26.4 million to company subordinated debt in 2017, largely offset increases in the cost of funding associated with notes payable and other debt, an increase of which was driven by both an increase in reference rates associated with TRS that were used to finance certain of the company's bond investments, and the issuance of debt in the third quarter of 2017 to finance the purchase of an equity investment in the South Africa Workforce Housing Fund.

Lastly, with respect to our core operating expenses, which includes salaries and benefits, payroll and administrative expenses, professional fees and other expenses, we recognized $33.9 million in such expenses in 2017, including $8.9 million in the fourth quarter. As you can see from Table 13 in our filings, this represents a year-over-year increase of approximately $7.1 million compared to what we reported in 2016.

This increase was tied to several factors. Salaries and benefits increased on a year-over-year basis by $2.3 million, in part due to an increase in the price of our common shares, which caused the amount of stock compensation expense to increase, as well as was due to an increase in incremental costs associated with additional headcount and incentive compensation. Secondly, professional fees increased by $3.4 million on a year-over-year basis in large part due the cost of various legal, valuation, advisory services that we incurred in connection with the Hunt transaction and the amendment of operating agreements that governed Fund II SSA. And lastly, other expenses increased by $1.3 million on a year-over-year basis primarily as a result of the cost of fee-related concessions that were made to certain investors in Fund II SSA in the fourth quarter of 2017.

In considering our 2017 results and the various drivers that I touched on, it is important to bear in mind that as a result of the Hunt transaction the company will no longer recognize in 2018 various revenues and expenses, including but not limited to, asset management fees and expense reimbursement revenues from IHS, LIHTC and renewable energy funds that we previously managed, and employee salaries and benefits other than stock compensation expenses associated with unexercised options that were not conveyed.

In place of these and other revenues and expenses, that are further discussed in Page 22 of our filing, that will no longer be recognized by us in future reporting periods, and not withstanding revenues and expenses associated with the assets and liabilities of the company that were excluded from the Hunt transaction, the company will recognize in future reporting periods both interest income associated with the (inaudible) receivable from Hunt, but various costs set forth in the management agreement with Hunt, including base management fees, incentive management fees and reimbursements to the external manager for certain allocable overhead costs. We further discuss these and other reporting changes, including the deconsolidation of nearly all of our consolidated funds and ventures resulting from the Hunt transaction on Pages 22 and 23 of our filing.

Before handing the call back over to Mike, I also briefly wanted to mention that, as Mike noted earlier, we successfully remediated material weaknesses in our internal control and financial reporting as disclosed in our 2016 Form 10-K. As a result, we concluded that the company's internal control over financial reporting was effective as of December 31, 2017. And in this regard we received from our external auditor a clean audit opinion on the effectiveness of our internal control and financial reporting as of year end.

With that, I will turn the call back over to Mike.

Michael Falcone: Thanks, Dave.

As we talked about at the closing of the Hunt transaction, for some time we have heard from shareholders that our business is too small and too complicated to understand. With this transaction we've started a process to change that. When all elements of the transaction are complete and assuming that Hunt elects to exercise its options to acquire the MGM LIHTC business, we will have achieved significant value realization from our tax credit in international businesses, simplified our balance sheet, reduced our overhead and increased transparency, while preserving our net operating losses and our attractive low-priced, long-term subordinate debt.

Going forward we will continue to invest primarily in debt related to affordable housing and clean energy. We expect to have other income-producing investment opportunities as well, with the additional reach provided by the Hunt organization. Over the long term we plan to continue to execute on our strategy to invest both new and recycled capital, primarily in debt backed by real assets to generate attractive, risk-adjusted returns. We expect to employ modest leverage. We will target total returns of approximately 8% to 12% and we will focus on real assets with positive social and environmental impacts.

Before we take questions from our callers, I just wanted to reiterate that we remain focused on improving the per-share value of the company and maximizing returns for shareholders. We believe that the Hunt transaction was a significant advancement towards those goals. In addition, it's important to note that the management team and staff that have served the company will continue to support it and will now have the added resources and expertise of the Hunt team to draw upon as we move forward.

I'd like to take this opportunity to personally thank our team for the extraordinary efforts that they have put in during the last six to nine months. Their efforts on behalf of all shareholders went above and beyond in all respects what can be considered expected. Those efforts were and are much appreciated. Thank you.

We are excited about the future, remain committed to our shareholders and we thank you for your support.

We'll now open the call to questions. Operator?

Questions and Answers:

Operator: We will now begin the question-and-answer session. (Operator Instructions)

As there appears to be no questions, I would like to turn the conference back over to Michael Falcone for any closing remarks.

Michael Falcone: Great. Thanks, Operator.

Well, I'm glad this transactipm that we sort of did in the first quarter was so clear that everybody completely understood it. But I suspect that it's the case that people are still scratching their heads a little bit perhaps. So to the extent that people do have questions, please feel free to call our investor relations line. As I've said, we're very excited about our future, and we're deeply grateful to our employees for the efforts that they put forward over the last six or nine months. And we're equally grateful to our shareholders, who have sort of stuck with us through a long ride here. And we're excited about the opportunities that we're going to be able to deliver to shareholders in the future.

So thank you all very much and have a great week.

Operator: This conference has now concluded. Thank you for attending today's presentation. You may now disconnect.