May 9, 2023

Armada Hoffler Properties, Inc. (AHH)

Q1 2023 Earnings Call

Operator

Good morning, ladies and gentlemen, and welcome to the Armada Hoffler First Quarter 2023 Earnings Conference Call.

(Operator Instructions)

This call is being recorded on Tuesday, May 9, 2023. I would now like to turn the conference over to Chelsea Forrest, Director of Corporate Communications and Investor Relations. Please go ahead.

Chelsea Forrest

Good morning and thank you for joining Armada Hoffler's First Quarter 2023 Earnings Conference Call and Webcast.

On the call with me this morning, in addition to myself, is Lou Haddad, CEO; Matthew Barnes-Smith, CFO; and Shawn Tibbetts, COO. The press release announcing our first quarter earnings, along with our supplemental package, were distributed this morning. A replay of the call will be available shortly after the conclusion of the call through June 9, 2023. The numbers to access the replay are provided in the earnings press release.

For those who listen to the rebroadcast of this presentation, we remind you that the remarks made herein are as of today, May 9, 2023, and will not be updated subsequent to the initial earnings call.

During this call, we may make forward-looking statements, including statements related to the future performance of our portfolio, our development pipeline, the impact of acquisitions and dispositions, our mezzanine program, our construction business, our liquidity position, our portfolio performance, and financing activities as well as comments on our outlook.

Listeners are cautioned that any forward-looking statements are based upon management's beliefs, assumptions, and expectations, taking into account information that is currently available. These beliefs, assumptions and expectations may change as a result of possible events or factors, not all of which are known and many of which are difficult to predict and generally beyond our control.

These risks and uncertainties can cause actual results to differ materially from our current expectations, and we advise listeners to review the forward-looking statement disclosure in our press release that we distributed this morning, and the risk factors disclosed in documents we have filed with or furnished to the SEC.

We will also discuss certain non-GAAP financial measures, including, but not limited to, FFO and normalized FFO. Definitions of these non-GAAP measures as well as reconciliations to the most comparable GAAP measures are included in the quarterly supplemental package, which is available on our website at armadahoffler.com.

I'll now turn the call over to Lou.

Lou Haddad

Thanks, Chelsea. Good morning, everyone, and thank you for joining us today.

This morning, we reported earnings for the first quarter of $0.30 per share, in line with our expectations and consistent with our full year guidance.

As you can see from our press release, the portfolio continues to deliver substantial growth in same-store sales and re-leasing spreads while maintaining occupancy of 97% portfolio-wide.

As pointed out on numerous occasions, best-in-market properties yield impressive results in most any economic climate. Later in the call, Shawn and Matt will give you the details on the quarter as well as the current state of operations and financial metrics. I will use my time to describe two very important post-quarter events.

Last week's announcement of our planned acquisition and recapitalization of the Interlock mixed-use asset in West Midtown, Atlanta, is a game-changing success on several levels. We anticipate funding the acquisition with $100 million of unsecured fixed rate financing, the issuance of a relatively small amount of OP units priced at $13, and the conversion of our existing mezzanine loan on the property into equity. At a 6.5% going-in cash cap rate, the property is immediately accretive to earnings.

Although a significant majority of the NOI is achieved through retail and entertainment operations, Georgia Tech's Georgia Advanced Technology Ventures anchors the 200,000 square feet of state-of-the-art office space. This 50,000 square foot lease serves as an incubator for technology developed at Georgia Tech. Several other tenants, both retail and office, have noted the proximity, stability, and involvement of the university as an important advantage afforded by the building. We expect to quickly lease-up remaining vacancy which will bring the stabilized GAAP cap rate on this trophy asset to well over 8%.

With this single transaction, we will accomplish several objectives. Adding yet another trophy quality mixed-use asset to the portfolio, along with the other assets in the area, creating a concentration of investment in some of Atlanta's premier growth markets, thus complementing our existing dominant market position in Baltimore's Harbor Point and Virginia Beach’s Town Center. We also substantially increased property NOI while rightsizing our mezzanine investment program – one that has proven to be a reliable source of investment opportunities. The retirement of this loan removes the last impediment to our long-stated goal of reducing the size of that program to more moderate levels that will focus on partnering on infill multifamily projects.

That said, as the Interlock is the fourth major acquisition we've achieved at significant discounts through our construction activities and mezzanine lending, we will continue to strategically deploy these mechanisms where our underwriting indicates the opportunity for eventual acquisition of top quality properties.

Perhaps most importantly, the Interlock, combined with the Gainesville apartment complex and the mixed-use Southern Post gives us a platform for further growth in the dynamic Greater Atlanta market.

The concentration of trophy-quality mixed-use assets in Virginia Beach, the Baltimore Harbor, and now Atlanta, combined with a steadily growing presence in the Carolinas, gives us solid positions in some of the most desirable markets in the Southeast.

Before I mention the second major post-quarter development, I'll give it the context of some near-term headwinds, which are actually long-term opportunities that make up the announcement all the more impressive.

The Interlock acquisition, while significantly accretive, resulted in a material reduction in our previously projected guidance for mezzanine income for the year. Add to that, the long hope for recapture of the Bed Bath & Beyond stores, which now appears to be likely, will result in less rental revenue in those two locations. Shawn will give you some detail on the various options we are considering for those sites. However, in the short term, this is another drag on 2023 NOI. All that said, despite these near-term challenges, due to the continued robust increases in portfolio income, the strength of third-party construction fee income, strong liquidity, and interest expense consistency, we are maintaining our previous guidance as we anticipate momentum to continue throughout the year.

Therefore, in keeping with our policy of dividend payouts in the 80% of AFFO range, the Board has acted to raise the quarterly dividend to $0.195 a 2.6% increase. With this change, the dividend will now eclipse its pre-pandemic level on an annual basis. The primary differences between then and now, aside from a stock price nearing $20 and are a much stronger balance sheet and a far greater percentage of income coming from trophy rental income properties.

I'll now turn the call over to Shawn.

Shawn Tibbetts

Thank you, Lou. As Lou indicated, the company continues to perform well, consistent with our guidance and with momentum following our record-breaking 2022 results. Our teams remain focused on value creation while working against the backdrop of a tough economic cycle.

To reiterate, we believe that the best-in-class performance throughout the portfolio, safe and reliable construction services, combined with seamless execution of high-quality development projects, will continue to create sustained shareholder value for years to come. Please refer to the supplemental package to review our operating portfolio highlights. I would like to call out a few of the noteworthy operational metrics that are contributing to our continued growth and sustained high occupancy across the portfolio.

2023 quarter one year-over-year same-store NOI for the portfolio was positive in all segments; was 4.3% on a GAAP basis, 5.3% on a cash basis, with retail coming in at 7.3% on a cash basis.

2023 quarter one year-over-year re-leasing spread on the commercial portfolio were positive 10.1% on a GAAP basis and 6.6% on a cash basis. We've been producing double-digit GAAP re-leasing spreads in the retail space for three quarters in a row.

Our asset management team continues to produce superior results as their agile approach enables us to keep our buildings full with high-quality tenants and residents. We previously discussed the post-COVID era commercial tenant watch list and the process continues to serve as a useful indicator for tenants who are, or who may be, potentially at risk due to various economic factors in the market.

There are a couple of high-profile tenants currently in focus. As a result of recent press surrounding bankruptcy proceedings, the tenant that is top of mind is Bed Bath & Beyond. As stated last quarter, we are in discussions with a popular high credit tenant who would like to fill the Durham, North Carolina space as soon as possible. Since the announcement, we've also fielded six unsolicited costs from retail tenants who would like to take immediate possession of our six-acre Virginia Beach location. As you may recall, we have long-awaited multifamily development plans for this site. However, given the level of interest, we will use this opportunity to determine which option results in the greatest long-term value creation.

In terms of office performance, we remain well leased at 96.8% with a high-quality roster of tenants. The retail segment is also experiencing sustained elevated levels of lease-up at 97.1% across the portfolio. I had previously cited a comment made by DBRS Morningstar and our recent BBB-rated credit report that referred to high occupancy rates across our portfolio and issues we are facing with accommodating tenant expansion, specifically relating to office space. To that end, I'm happy to report that we capitalized on one such opportunity during the first quarter.

Our team developed a plan to relocate and consolidate a portion of our own employee base to create greater opportunities for revenue-generating space. We were able to execute a long-term lease with KPMG here in our headquarters building at Town Center, Virginia Beach. This new lease is yet another example of high credit tenants taking the flight to quality, demonstrating the strength and attractiveness of our mixed-use ecosystems. This brings the 800,000 square feet of Town Center office space to 99% leased.

The theme for our multifamily portfolio is consistent growth. As we predicted, growth has settled in at the mid-single-digit range for the quarter, and we see this trend continuing in the months ahead, especially given our assets are in well located, walkable and mixed-use environments. Our portfolio continues to stand strong against macroeconomic headwinds. State-of-the-art properties, combined with superior locations, create trophy assets that are virtually the best in their respective submarkets. The complementary property types outperform, especially during times of economic uncertainty and increased pressures.

Earlier in the call, Lou mentioned acquisition as a means for growth and the Interlock is demonstrative of that thesis. As you know, we also create high-value real estate through our internal development and construction processes. To that end, our construction and development teams are currently hard at work manufacturing high-quality assets located within mixed-use settings that will soon be added to our growing and robust portfolio. The team is also highly focused on delivery of the largest third-party backlog in our company's history, further contributing to the earnings of the firm.

Our Southern Post mixed-use project in Roswell, Georgia, continues to progress nicely and is scheduled for initial delivery early next year. The retail space has seen quite a bit of activity and is 56% leased with another 31% under LOI. The office has also experienced significant leasing activity as of late. We are currently negotiating with a high credit tenant relocating from the West Coast for a 37,000 square foot strategic corporate relocation. This tenant will anchor roughly 40% of the office space and we believe execution of this lease will aid an acceleration of the leasing activity within the asset. We are also excited about the lease-up opportunities in the apartment space especially given the barriers to entry in the high-end submarket.

At our Harbor Point site, the T. Rowe Price Global headquarters project continues to progress. We look forward to updating you with more details as we get closer to delivery. Across the street, we are well underway with the 312-unit allied apartment building. Success at our 1405 Point and Dock Street multifamily assets continues to bolster our outlook as we develop this complementary high-quality asset in the best location within the submarket. We remain on target for initial occupancy in both buildings during the third quarter of 2024.

Finally, we believe that amongst all of our assets, our people are the most valuable. Our talented teams continue to manufacture and manage the high-quality assets that are our value proposition. We appreciate all you do on behalf of the company and its shareholders.

I will now turn the call over to Matt.

Matthew Barnes-Smith

Good morning, and thank you, Shawn. Another set of strong results by our operating team demonstrating consistency in performance and the quality of our assets.

For the first quarter of 2023, we reported FFO of $0.23 per diluted share and normalized FFO of $0.30 per diluted share, in-line with both our guidance estimates and coverage analyst consensus. Therefore, we have maintained our guidance range accordingly at $1.23 to $1.27 per diluted share of normalized FFO, and the Board have responsibly increased our dividend to $0.195 per quarter. This modest dividend increase of just under 3% maintains our AFFO coverage ratio in the 80% range and cannot only be attributed to our portfolio's performance, but also our strong balance sheet.

As we continue to transition our balance sheet towards long-term fixed rate unsecured debt, we will maintain our liquidity and respectable financial metrics.

For the first quarter of 2023, and our stabilized portfolio debt to stabilize portfolio EBITDA is at 5.4x in line with our stated target. Our debt service coverage ratio and fixed charge coverage ratio reported 2.8x and 2.3x, respectively, once again demonstrating the team's ability to manage and execute this transition in adverse market conditions.

Our liquidity position continues to be strong at roughly $180 million more than able to cover the 2023 cash requirements for our development pipeline and any potential preferred equity deals. This, combined with our well-structured debt maturity letter means that we continue to grow earnings without the need to enter the equity markets until we feel that we are receiving appropriate value. For reference, we have no debt maturities in 2023, and the small amount of debt maturing in 2024 and 2025 will be paid off at maturity adding these assets to our unencumbered borrowing base.

You will have noticed from our supplemental financial package that we are currently over-hedged. This is due to several timing factors and will self-correct over the coming year as these derivatives expire.

As interest rates continue to fluctuate, we will constantly monitor the environment to ensure we either convert the variable rate debt to long-term fixed-rate debt in the private placement market or layer in new hedge positions when our current set of positions mature. One of the key themes over the last 12 months is the rebalancing of our portfolio with the reduction of our mezzanine book, strategically selecting projects that we would look to.

The announcement of acquiring the mixed-use in stock asset in West Midtown Atlanta replaces the mezzanine interest income with stable property NOI, increasing the value of these earnings. We will take this opportunity to continue our balance sheet transition and place a two-year, $75 million unsecured term loan paying off its current construction debt. This SOFR plus 140 basis point loan has been swapped at 4.7% for the entire term, including extensions, providing us with predictability in our cash flows. The unsecured term loan has a 1-year extension option, the capacity to be increased to $150 million and is a prime candidate for a debt private placement in the future when the economic conditions return to more favorable levels.

I will now pass back over to Lou for his closing comments.

Lou Haddad

Thank you, Matt.

Our shareholder-focused mindset anchors our actions as a result of the natural alignment created by management's significant ownership stake in the firm. Our team remains committed to the continued focus on consistent performance while meeting and exceeding expectations, especially in uncertain times like these.

I'll now turn the call back over to the operator for questions and answers.

Q&A Session

Operator

Thank you, ladies and gentlemen, we will now begin the question-and-answer session.

(Operator Instructions)

First question comes from the line of Rob Stevenson with Janney.

Rob Stevenson

Looking at the revised guidance assumes roughly $900,000 less in interest income for the year, what does the mezz pipeline look today given that you're going to be losing biggest source of income out of that portfolio when you close the Interlock transaction?

Lou Haddad

Rob, I'm going to let Shawn answer that specifically. But as you know, we've long awaited this opportunity to right size that program, and it's going to level off in the $80 million range. We have a number of new opportunities we're looking at focused primarily on the Charlotte and Atlanta markets. So, our expectation is that mid-income for 2024 is going to be roughly where it is today.

Shawn Tibbetts

Yes. Thanks, Lou. Rob, I think the high-level answer to your question is we want to continue, as Lou said, to look for the opportunities where we can jump in and own. And obviously, that's more of an art at times than a science.

As you know, in the supplemental, we kind of outlined the projects outstanding. You see the Interlock still there. With that, that kind of $55 million principal will come back in as well as the accrued. So about $90 million will come back in the door. We do have two deals out with our partners at Terwilliger Pappas that are mixed-used to lose point in the Southeast, one in Charlotte and one in a suburb or a satellite of Atlanta.

So, what we intend to do is look for those opportunities that are attractive for us to check the boxes for our portfolio and potentially put out for another one of those when it makes sense. But I think to Lou's point, we're going to remain pretty consistent kind of steady hand on the wheel. And if something comes across the transom, we're willing to pull the trigger.

Rob Stevenson

How much on Solis City Park II in Gainesville to is left to put out? It looks like on the supplemental, you the balance between those two is, call it, just under $34 million. Is there a substantial amount left or to get to $80 million-ish or whatever you're really talking about doing somewhere in the neighborhood of $45 million of new loans.

Shawn Tibbetts

There's 30 left. So I think, to your point, we won't get to the $80 million with just these two, so we'll have to have to look for opportunities there if in fact, we want to hit that cap. But again, our kind of loose cap there is for guidance, not in terms of financial guidance, but guidance internally on how we're going to conduct business in the mezzanine platform. So, I think to answer your question, you could potentially see us take another one if it fits and if the timing works well for us.

Rob Stevenson

So just to be clear, sort of $34 million -- so the two Solis transactions that are on Page 18 of the supplemental, those are more or less fully funded at this point. And then there's another, call it, $30 million coming from Charlotte in the Atlanta with Terwilliger Pappas. And then so to get to 80, you'd be looking at doing something in the neighborhood of another $15-ish million on top of that?

Shawn Tibbetts

I think close. We're going to put out a combination of 30 more between these 2, Solis City Park and Solis Gainesville that you see. And subsequent to that, to get up to 80, we will have to agree to do another project with Terwilliger Pappas.

And again, that will -- timing will be a major factor there. Location, kind of our underwriting and appetite to own that asset potentially will also go into the mix. So, I think a lot has to do with underwriting, obviously, and a heck of a lot has to do with timing. But again, we'll have to put down another project on the sheet here to get to the $80 million to answer the question.

Rob Stevenson

And then Bed Bath & Beyond a Town Center, is that an either/or? Or is there a scenario where you do ground floor retail with somebody with the apartments above it?

Lou Haddad

Yes. That's – you just hit the third option. And so, we're going to be looking at all three over the next month or so and try and pick a direction. Hopefully, it's going to be compatible with bringing some new-to-market retailers into the area, which is our mandate from the city when we pull the trigger on retail. But at the same time, as we said, we've long waited for this opportunity to do some multifamily there as well.

Rob Stevenson

And I guess the question there sort of begs, how are you guys thinking about demand for apartment units at Town Center? You already have roughly 760 units there. How much could you add there without sort of weakening pricing for your existing units with adding another whatever it's going to wind up being 150, 200, 300 units, whatever that you're thinking about. How do you think about that as going from maybe 760 to 1,000 units at Town Center. Is that too much right now?

Lou Haddad

That's a really good question, Rob. It's something that we're considering as we speak. And it's actually even broader than that. Not only are we not willing to dilute ourselves as we get the highest rents in the region here at Town Center, but also, there is competition for these dollars. So, a new project here in Virginia Beach, we know we'll be successful, but is that the best use of our dollars when they could be deployed in Charlotte or

Atlanta or Charleston or Raleigh -- and we have all those opportunities. So not only do we need to see that it would be very accretive to add here. but we also have to be convinced that it's going to be better than a competing project that we can do in another region.

Rob Stevenson

And if you choose to just basically take the Bed Bath and re-tenant them, as is, what type -- how material is the TIs that you need to do on a per square foot basis in order for it to be ready for another tenant to move in?

Lou Haddad

Well, a lot depends on who those tenants are. Like I said, we really would gravitate towards new-to-market tenants. And while that can be an expensive proposition, we effectively have a feeding frenzy right now with people that are wanting us to deal with them in terms of getting first position on the new space. So, it remains to be seen where that ends up. In any event, I can assure you it will be accretive versus the Bed Bath that was sitting there. We just want to make the best use of the dollars as well as add to the mix here at Town Center.

Rob Stevenson

And does that hold true for the Durham location as well?

Lou Haddad

There's a little bit of a different story. That's a traditional strip center, and it has an awful lot of restrictions on it in terms of what you can and cannot put in there. Fortunately, the tenant that is desperate to get in there, fits all the restrictions. So that will probably be a one and done more type of deal.

Rob Stevenson

And then last one for me. Any known move-outs at this point in the office or retail portfolio for the '23 or '24 expirations or on the office side, any known material downsizings?

Shawn Tibbetts

So Harrisonburg, I would say in the Regal space is the kind of top of list, but as you know, we have and they're not known move out to be clear, but the term’s ending. We have a 10-acre site there that we are also looking at with a similar eye, how do we best utilize that real estate. They are still paying rent. They are still performing up in Harrisonburg, but that's one, that's kind of top of mind there, 49,000 feet. But again, there are 10 acres sitting there that we want to get our hands on.

A couple of other retails, Rob, but other than that, we're in pretty good shape here. We expect most of these folks to renew and renew in place. So, we feel good about that.

Lou Haddad

On the office side, we're looking at potentially one move out, and we're already negotiating a letter of intent to refill that. I really don't expect anything to happen materially on the office. Like I said here at Town Center, as Sean mentioned, it's 99% full. We actually could stand to have somebody move out so we can just create a little breathing room for some of these other tenants.

Rob Stevenson

And that move out is it down set? Or is that elsewhere in the office portfolio?

Lou Haddad

It's at town center. We'll have an announcement and a replacement tenant here in the not-too-distant future.

Operator

Your next question comes from Wes Golladay with Baird.

Wes Golladay

Can you talk about how peak leasing season is shaping up for multifamily – where you send out your renewals?

Shawn Tibbetts

Sure. So, you said peak season for multifamily is shaping up well. We are, I would say, performing better than the cyclical historical kind of cyclical curve that we watch. We are seeing, as I mentioned, mid-single digits in terms of renewals, if you will. And we think that's where kind of where we predicted last year, the norm would hit this year. So we feel good about that. All of our properties are performing strong and continuing to ramp up into the second and third quarter – kind of first quarter, obviously, is a little damp across the board. So second and third quarter look good, mid-single digits.

Wes Golladay

And when you look out to next year, do you see any supply pressure coming in?

Shawn Tibbetts

Not necessarily in our kind of submarkets and our ecosystems. Again, we're kind of protected in certain cases by these mixed-use facilities, not only protected, but also kind of supplemented or turbocharged, if you will, by our ecosystem arrangements. We feel good about submarkets. There are certainly more supply coming online. But again, we don't see -- we haven't been underwriting double digits as folks were last year. We're in the mid-single digits and intend to remain there to be conservative.

Wes Golladay

And then maybe just switching over to retail. It seems like the demand is pretty strong. Can you confirm the Durham box for Bed Bath? It doesn't look like it will be a box split there? And then maybe overall, can you talk about the TIs in retail that seem to be ticking up on renewals?

Lou Haddad

So, on the Bed Bath, like I said, it's -- the most likely candidate is we'll take the entire space. We've had inquiries from a couple of others to divide it up and we'll see that doesn't hold as much appeal for us. But again, never say never and we'll see what rents are.

As far as Tis, we're pretty happy with the re-leasing spreads that we're getting and the double-digit same-store growth. We're happy to invest TIs for credit tenants that are going to be with us for a long time.

Wes Golladay

And then maybe on the acquisition front, you mentioned that you want to wait for a better cost of capital. But could you do more OP unit deals above the stock price to get some acquisitions done?

Lou Haddad

We could. Again, we're not -- as you know us, we're far and away the largest shareholder in the company. And so, we don't take the deployment of OP units lightly. Even at the premium that we can charge now, we think they're well undervalued. So, we're going to be very selective about that happening.

At the same time, we're going to continue to be opportunistic. I mean, the market has obviously mispriced, high-quality real estate in general. -- in our equity in particular, but that's not going to dissuade us from adding trophy properties when possible.

Operator

Next question comes from Peter Abramowitz with Jefferies.

Peter Abramowitz

Yes, I just wanted to follow up. I know there were some questions here about the TIs on the Bed Bath and Beyond the two spaces. Are you able to quantify what do you think the mark-to-market is on those spaces today?

Lou Haddad

Peter, it's hard to say right now. The last Bed Bath that we refilled, we refilled on an as is, where is basis. And so strictly by the metrics that people follow of re-leasing spreads that look bad, I'll tell you that we'll do that deal every time for the right tenant. So, it's – it's too early to say right now. I can say that if we deploy new capital, it's going to be a substantially higher cap rate than what we were looking at with Bed Bath as a value.

Peter Abramowitz

And then also on the TI front, I guess, could you just talk about the tenant you're talking to for the office space at Southern Post, I know it's probably not easy for them to necessarily find new development in a suburban submarket like that. But overall, it is a tough office environment. So, could you talk about TIs for that and just kind of the rent levels that you're looking at relative to your underwriting, how that's kind of shaping up?

Lou Haddad

Yes. We're actually a bit above pro forma rents. Shawn, do you have the stats there?

Shawn Tibbetts

Yes, I was going to say the same thing. I think we're performing at least specifically in that lease, like I said, at least to be 40% kind of anchor in 40% of the office space, and we are above where we thought we would be from a pro forma rent standpoint. As you know, TIs continue to increase, but to Lou's comment on the last question, when we baked this all in, we are happy to see a higher yield and with a high credit tenant happy to lock that in, in the office space on a long-term lease. So, I think, all in all, we are better than we pro forma-ed at least thus far, and we'll continue to look for those types of opportunities.

Lou Haddad

Peter, I know you you're talking to an awful lot of companies. We're just not seeing what most people are seeing, what I guess is what most people are seeing, we're demanding higher rents -- and when someone is demanding higher TI, then they pay rent fully for it.

And as you – at 97% or whatever it is leased, we can be awfully selective with who we want to bring in. The KPMG deal is a great example that Shawn mentioned earlier. We really wanted that tenant and there was no space here. So, we – we actually spent some extra money to move folks around, so we can create 15,000 feet for those folks. But that's a tenant that's going to be here forever.

So, you've got to -- we have just a different paradigm than I think is happening or at least what you read in the headlines, what's happening in the market.

Peter Abramowitz

And then one last one. So, you have the Interlock lined up here. So, I know that kind of taken a lot of your attention here and is the big use of capital this year. I guess, generally, could you talk about -- I think maybe there was some discussion before in the guidance of some kind of more traditional like grocery anchor shopping center deals, whether off-market or marketed.

Could you talk about that space? Are you seeing any kind of distress from sellers and potential opportunity. And if you do see that, how would you be able to address that. Obviously, that would be attractive, but then you have to balance that against capital needs.

Lou Haddad

Sure. Again, I'm not sure what's happening nationwide and what the headlines are. But I can tell you, in our markets, high-quality neighborhood retail is not being offered at any kind of discount. So, it's – we're still in a position where the kind of things that we want to own, we're probably going to have to create because they're still trading at the ones that are trading or trading at various cap rates.

So that – those the horror stories that you're hearing and seeing just aren't happening in the belt from Maryland, down to Virginia and the Carolinas and Georgia.

Operator

(Operator Instructions)

Next question, we have Chris Sakai with Singular Research.

Chris Sakai

Can you talk about pricing on the construction side of things. Has it moderated still? And what are you seeing as far as commodity pricing is concerned?

Lou Haddad

Sure. I guess the best way to characterize it is that we're no longer seeing double-digit increases across the board in construction prices. Commodities have moderated a bit. Labor has not, and there's still a shortage of highly qualified contractors to go around.

So, what we're seeing year-over-year is that prices have stabilized, but they've stabilized at a very high level. I think that's going to continue to choke some new development off. With regard to our construction company, they're doing -- aside from the T-Rowe Price building, it's almost exclusively in the multifamily space that our third-party clients are remaining very active. -- partially because wood prices have come down substantially over the last six months or so.

Chris Sakai

And then as far as your guidance is concerned, can you talk about expectations for occupancy in that guidance?

Lou Haddad

Yes. We're – obviously, we're at a very high level right now, nearly 98% portfolio-wide. And as Shawn mentioned, 99% leased here at Town Center. Our expectation has always been that our properties stabilized in the mid-90s. We don't get overly excited when they get to the high 90s. Our historic lows are in the low 90s. So it's going to fluctuate in that area.

When you have a portfolio that is not overly large, one substantial tenant can move that needle a bit. So that's why we just want to be in that range. It's great to be at 97, 98, 99. But I can't -- we wouldn't say that that's going to continue indefinitely. What I say -- what I can say, we believe will continue indefinitely is that we'll continue to move rents northward.

Operator

And there are no further questions at this time. I'll turn the call to Louis for closing remarks.

Lou Haddad

Thanks, everyone, for your attention this morning. We appreciate your interest in the company. We look forward to more announcements over the next couple of months, and stay tuned. Thank you. Bye-bye.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines.