

**PRO Real Estate Investment Trust**

**2022 Second Quarter Results Conference Call**

August 11, 2022 — 12:00 p.m. E.T.

Length: 31 minutes

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## **CORPORATE PARTICIPANTS**

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## **CONFERENCE CALL PARTICIPANTS**

**Nicholas Telega**

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**Lorne Kalmar**

*TD Securities — Analyst*

**Mark Rothschild**

*Canaccord Genuity — Analyst*

**Brad Sturges**

*Raymond James — Analyst*

**Himanshu Gupta**

*Scotiabank — Analyst*

**Sumayya Syed**

*CIBC Capital Markets — Analyst*

## PRESENTATION

### Operator

Good morning and welcome to the PROREIT's Second Quarter Results Conference Call. At this time, all lines have been placed on mute to prevent background noise. Management will make a short presentation, which will be followed by a question-and-answer period, open exclusively to financial analysts. In order to ask a question, simply press star then the number one on your telephone keypad. If you would like to withdraw your question, please press star then the number two.

For your convenience, the press release, along with the second quarter financial statements and management's discussion and analysis, are available at [proreit.com](http://proreit.com) in the investor section and on SEDAR.

Before we start, I have been asked by PROREIT to read the following message regarding forward-looking statements and non-IFRS measures:

PROREIT's remarks today may contain forward-looking statements about its current and future plans, expectations, intentions, results, levels of activity, performance, goals or achievements, or other future events or developments. Forward-looking statements are based on information currently available to management and on estimates and assumptions made based on factors that management believes are appropriate and reasonable in the circumstances; however, there can be no assurance that such estimates and assumptions will prove to be correct. Many factors could cause actual results, levels of activity, performance, achievements, future events, or developments to differ materially from those expressed or implied by the forward-looking statements. As a result, PROREIT cannot guarantee that any forward-looking statement will materialize and you are cautioned not to place undue reliance on these forward-

looking statements. For additional information on the assumptions and risks, please consult the cautionary statement regarding forward-looking statements contained in PROREIT's MD&A dated August 10, 2022, available at [www.sedar.com](http://www.sedar.com).

Forward-looking statements represent management's expectation as of August 10, 2022 and, except as may be required by law, PROREIT has no intention and undertakes no obligation to update or revise any forward-looking statement, whether as a result of new information, future events, or otherwise.

The discussion today will include non-IFRS financial measures. These non-IFRS measures should be considered in addition to and not as a substitute for or in isolation from the REIT's IFRS results. For a description of these non-IFRS financial measures, please see the 2022 second quarter earnings release and the MD&A. A reconciliation of non-IFRS to IFRS results, as applicable, may be found in the earnings release and MD&A for the 2023 second quarter. Please refer to the non-IFRS measures section in the MD&A for the second quarter for additional information.

I will now turn the call over to Mr. James Beckerleg, President and Chief Executive Officer.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Thank you, operator, for the introduction. Good morning, everyone, and welcome to our second quarter call. Joining me today in my remarks is Gordon Lawlor, as most of you know, our Executive Vice President and Chief Financial Officer. Also on the call today for questions is Alison Schafer, our SVP of Finance, and Mark O'Brien, our Senior Vice President, Leasing Operations and Sustainability.

Yesterday we released strong Q2 results, both from an operational and a financial standpoint. Our performance largely results for our increasing presence in the industrial sector as well as the meaningful operational and leasing synergies we continue to achieve.

Last week, subsequent to quarter end, we completed our joint venture agreement with Crestpoint Real Estate Investments, a high-profile institutional real estate investor. Many of you already know we now own an industrial portfolio of 42 properties with them totalling nearly 3.1 million square feet of gross leasable area. Save for one property in Moncton, the joint venture portfolio is located in Halifax's Burnside Industrial Park, one of Canada's strongest industrial nodes. I, for one, am very proud of this partnership, which actually involved two transactions.

First, PROREIT and Crestpoint each acquired a 50% interest in 21 properties owned by a third-party. The cost to PROREIT was approximately \$114 million before closing costs, mainly financed with the proceeds of the 50% interest and approximately \$148 million of new fixed-rate mortgages. The balance was satisfied with cash on hand, and that includes cash from the sale of Crestpoint of a 50% interest in 21 of PROREIT's previously owned properties. That sale to Crestpoint represents the second part of the partnership transaction. In detail, PROREIT sold a 50% interest in 21 properties to Crestpoint for approximately \$113.5 million before closing costs. And proceeds, including \$49 million in cash, proceeds included approximately \$49 million in cash, I'm sorry, with Crestpoint, also assuming a 50% interest and approximately \$129 million of PROREIT's in-place fixed rate are.

On a net basis, the cash flow resulting from the acquisition and the sale allowed for a modest reduction in PROREIT's overall debt level and a profit above our carrying value. The overall transaction has

many other benefits for PROREIT and, fortunately, it is immediately accretive to our earnings. There is a significant market leasing upside embedded in this desirable portfolio. Given its scale, it is a unique opportunity to further increase our footprint in Eastern Canada. And then, finally, it allows us to leverage our operational platform as the sole property manager of the entire portfolio.

Subsequent to quarter end we also announced an agreement to sell a portfolio of nine non-strategic retail properties to a third party for just under \$19 million prior to closing costs. These properties were all located in Western Canada and totalled approximately 94,000 square feet of GLA. The closing of that transaction is scheduled for later in September. Conclusion of that deal will further weight our portfolio towards the industrial sector and, again, provide us some net cash for debt reduction.

Let me now turn briefly to our operational results for the second quarter. Our industrial sector now accounts for 80% of our gross leasable area on a pro forma basis, reflecting the two transactions I just spoke to. It generated a solid 4.7% increase in same property NOI in the quarter compared to the same period last year. Our small retail portfolio also continued to perform well, recording a 3.2% increase in their same property net operating income. We actually believe this reflects our focus on necessity-based retail properties with strong anchor tenants in place. Our office segment, which now represents just 7% of our GLA on a pro forma basis, did record a decrease in same property NOI resulting from a one-time adjustment of \$137,000 related to a prior period and a small uptick in vacancy in two of our eight-property portfolio. Part of that vacancy has now been released for a six-year term successfully commencing on November 1<sup>st</sup> of this year at rates above the matured lease. It might also be noted by the analyst listening that, when excluding the \$137,000 non-recurring adjustment, our overall same property NOI increased by 2.2% in Q2 2022 compared to the same prior year period.

Rental rates continue to be a growth driver across our portfolio. Mark-to-market net rent spreads at the end of the second quarter was 24% of our total portfolio and 35% for our important industrial segment specifically. Our occupancies remained firm at 98.3% at quarter end and I can also report that we have successfully renewed or replaced 82% of the 853,000 square feet of leases maturing in 2022, achieving an average increase of 12.9% over the maturing rent for those leases.

So, at this point I'll turn the remarks over to Gordie, who will provide some details on our Q2 financial results.

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Thank you, Jim, and good afternoon, everyone.

We recorded a solid financial performance in the second quarter. Property revenue grew to \$23.7 million, a 33.6% increase compared to the same period in 2021. Net operating income reached \$14.3 million, up 33% year over year. AFFO totalled \$7.9 million, a 36.9% increase compared to the same prior period. These increases were mainly driven by the net transaction activity during the last 12-month period, notably the acquisition of 16 properties and the sale of three non-core strategic buildings, sorry, non-strategic buildings. Basic AFFO continues to steadily improve with 86.5% in the second quarter of 2022 compared to 92.3% for the same period last year.

During the quarter we kept focus on maintaining our strong financial discipline and liquidity position. Debt to gross book value was 51.2% at June 30<sup>th</sup>, down from 58.2% at the same date last year.

We remain committed to reducing our debt to gross book value ratio below 50% over the next few quarters.

We have approximately \$10 million in mortgage renewals maturing in the next 12 months after you take into account the sale agreement of nine non-core retail properties that Jim spoke to. The proceeds from the sale will be used to repay approximately \$14.1 million of related mortgages maturing in 2023, or January actually, with the balance to pay down a term loan.

Our liquidity position remains healthy. At June 30<sup>th</sup> we had \$28 million available under our credit facility compared to \$38 million at the end of March. This is mainly a result of some negative working capital in the quarter due to annual property taxes as well as a payout of a small mortgage when it came due. Distributions of \$0.0375 per unit were declared monthly throughout the second quarter of 2022. Finally, our weighted average cap rate for the portfolio was approximately 5.7% at the end of the quarter, or \$155 per square foot, down from 6.3% at the end of the second quarter of 2021.

I'll now turn the call back to Jim for closing remarks.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Thanks, Gordie.

To conclude, our management team does remain mindful of the current environment with the macroeconomic uncertainty, high inflation, and rising interest rates that we all face each day; however, we do believe our management team, and your board, continue to focus with discipline on opportunities that meet our laid out objectives. We believe PROREIT is advantageously positioned to further drive both



performance and growth as we go forward. We remain a robust tenant-based REIT with a strategically located portfolio and I am very confident the talent and team can generate value for all of our stakeholders again as we move forward.

So, that wraps up for formal remarks this morning with respect to the second quarter and I'll turn it back now to the operator to take any questions that there are from participating financial analysts. Thanks very much.

## Q & A

### Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press star followed by the one on your touchtone phone. You will hear a three-tone prompt acknowledging your request and your questions will be polled in the order they are received. Should you wish to decline from the polling process, please press star followed by the two. If you are using a speakerphone, please lift the handset before pressing any keys. One moment please for your first question.

The first question comes from Nicholas Telega of BMO. Please go ahead.

**Nicholas Telega** — Analyst, BMO

Thanks and good afternoon. So, with the recent transactions, the portfolio is seeing an increase in industrial weighting. I was just wondering your thoughts about the target weightings by asset class moving forward, maybe particularly for retail and office.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

It's Jim speaking. Our strategies from a board perspective haven't really changed from what we chatted about last quarter and that is we see a natural evolution going forward of increased weighting in the industrial sector. That will come from, currently unidentified, but acquisitions when we enter that market, and to some extent judicial sales of retail and/or office portfolio, although the office portfolio is now really small. We don't have a specific target date to move out of those two sectors. Our retail portfolio especially is managed much like the small bay industrial portfolio. It's strongly anchored by grocery anchors or drug stores and national chains of that nature and, as you'll see from the numbers, is performing well. So we don't see any inherent important strategy to move away from that sector.

**Nicholas Telega** — Analyst, BMO

Okay, great. And— Please go ahead.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Sorry, we're waiting for an inbound question.

**Nicholas Telega** — Analyst, BMO

Oh, okay. Can you just comment on what you've seen in the transaction market lately and maybe any implications for pricing?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

It's Gordie Lawlor here. We haven't seen many transactions, especially in our markets, in the last, give or take, six months. We've seen some GTA industrial deals and track them, but lower airport-related Mississauga. We were the Atlantic Canada deal, if you will, so there was that, and then we haven't too much in Winnipeg or Ottawa.

So there hasn't been a lot in the last six months. It's the time of year, too, as well besides noise in the market and whatnot, it's July and August, so we expect some pick up here September, October, but it's been quite quiet in the last six months. So, not a lot of markers on deals or cap rates at this point in time, which I think is reflective of most of the REITs that have come out at this point in on their under valuations.

**Nicholas Telega** — Analyst, BMO

Perfect. Thanks for the colour and I'll turn it back.

**Operator**

Thank you. The next question comes from Lorne Kalmar of TD Securities. Please go ahead.

**Lorne Kalmar** — Analyst, TD Securities

Thanks. Good afternoon, guys. Maybe just flipping back to the dispositions quickly, was that a marketed deal?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

Yes. Mark O'Brien here. We did market it with a broker, Avison Young. We had it in the marketplace and we did have some inbounds that we looked at closely. We circled back with one of them. It took some time. And certainly, with the uncertainties and the rising interest rate environment, it did drag on, but we did have a marketed deal and we do have it under contract for sale with a known entity in Western Canada.

**Lorne Kalmar** — Analyst, TD Securities

Okay. And can you guys give a little bit of guidance on the cap rate?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

Yeah. So, on a stabilized basis, it's kind of pencilling out to a mid-seven cap, and that's a function of low (inaudible). These nine properties were in a five-year pool with RBC lender and they were sort of the weakest of the 19 that we bought in this Rexall portfolio, and actually only two out of the nine are Rexall anchored. And these are secondary, smaller markets in Western Canada. So we sort of see it as the weaker grouping of the original 19, so reflected in that 7.5 cap.

**Lorne Kalmar** — Analyst, TD Securities

Okay. So you're (inaudible) be stronger for it. Maybe just flipping quickly to the JV, what do you expect in incremental management fees from managing the 42 properties?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

It's Gordie. Management fees will pencil about \$800,000 and then incremental fees, including leasing fees, would be another \$500,000 to \$700,000 depending so, give or take, \$1.3 million to \$1.5 million.

**Lorne Kalmar** — Analyst, TD Securities

And net of costs as well or are there other costs associated?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

No, net of costs.

**Lorne Kalmar** — Analyst, TD Securities

Net of costs? Okay, great. And then was there a difference in cap rate between the portfolio you guys disposed of, the 50% interest I guess, and the one that you acquired?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Yes.

**Lorne Kalmar** — Analyst, TD Securities

Could you give a little colour on that?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Yes. So, give or take a 6% on the buy and 5.2% on the sale. And largely driven by the assets that we sold, the weighted average rental rate we had in the portfolio we had was a little bit lower than what we were buying at, so that was part of the reflection of the difference in pricing.

**Lorne Kalmar** — Analyst, TD Securities

That's great. Then did I see you guys have an additional office vacancy this quarter?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Yeah, there was a 2,500 square feet that came due in May that they didn't renew, but that's, actually, we're looking at this yesterday. I mean we think that sits for a bit, if you will. We've had some moving parts in a couple of our buildings, but the exposure here in the next year we don't think is any more than another \$70,000. That's an annual number. And then we've got 12,000 feet coming on stream at the end of Q4. So, hopefully we're in a bit of the upside of this number when we go forward.

**Lorne Kalmar** — Analyst, TD Securities

Okay. You answered my follow-up question. Okay, great. Thank you, guys, so much for the colour.

## **Operator**

Thank you. The next question comes from Mark Rothschild of Canaccord. Please go ahead.

**Mark Rothschild** — Analyst, Canaccord Genuity

Thanks. Good afternoon, guys. You already addressed a lot of what I had. Just maybe if you could expand a little bit on how you're thinking about dealing with your capital now with different objectives such as reducing leverage but also wanting to continue to grow.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Mark, it's Jim. Gordie can expand on the comments if he wishes. I mean our stated objectives out there right now with the incremental cash that's flowing from a couple of these transactions we've spoken of is to apply toward debt reduction. I think we have chatted with the broader community about liking to see our debt to equity ratio gets below 50% as we move forward and so that's where we're focused on right now. We have the liquidity in place for opportunistic small deployments of capital if, as, and when we see those, but before we do something significant that would involve capital raising, I mean we want to see stability in the markets, of course, like everybody else, and hopefully a decline in our cost of capital. Gordie, do you want to add to that?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

No, I think that's right. I mean, as far as options and debt reduction, we still have a little bit of expensive debt there, about \$6 million, so our goal is to have gone by the end of the year and that's really

been our focus. And then we'll see what September brings with people back at the desks and whatnot and then we'll go from there.

**Mark Rothschild** — Analyst, Canaccord Genuity

Okay, thanks.

**Operator**

Thank you. The next question comes from Brad Sturges, Raymond James. Please go ahead.

**Brad Sturges** — Analyst, Raymond James

Hi, guys. Just on the back of the asset sales out west, is there anything else that would be earmarked for sale at this point or is that kind of, for now, the last kind of, ah, the only thing which we should see from a transaction point of view at the moment?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Hey, Brad. It's Gordie. I think we indicated a few quarters ago that we had about \$30 million circled for the year. So we've got two-thirds of that done. It's some smaller properties, some one-offs that may take a bit of time, but that's probably it unless something comes up during the year.

**Brad Sturges** — Analyst, Raymond James



Okay. And then in terms of the, ah, you know, congrats with the new JV with Crestpoint there, obviously it's Halifax-Dartmouth focused. It's early days in the new JV, but do you see room to expand that JV further or is this kind of, for now, the potential size of that JV?

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Sorry, either one of us could answer that. I mean we've got a good relationship with Crestpoint, we've transacted with them before, but I mean there's no specific plans on the table. I think if we were looking at other opportunities in the Burnside industrial park, we would look at them jointly. I mean we would be happy to expand here further, although, at the present time we have, I guess—

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

40% of the market, yeah.

**James Beckerleg** — President & Chief Executive Officer, PRO Real Estate Investment Trust

Not an owner-occupied market. So we have a dominant position there.

**Brad Sturges** — Analyst, Raymond James

Yeah, that makes sense. Last question, just to go back to the cap rate discussion there and, obviously, in terms of your book value, you held steady on the cap rate. I guess would you be waiting to see more transactional data before you make adjustments to your book value? Or how should we think about that in the next couple of quarters?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

It's Gordie. So, yeah, I mean especially in our markets we haven't seen any movement at this time, Winnipeg for sure and Halifax was (inaudible) with where we were on our last deals and that. Moncton, there's really be no transactions either, just a little bit of industrial in Ottawa as well, so we haven't seen anything as of late.

But, not dissimilar to other REITs, I mean we'll review that in the next two quarters. I mean our cash flow is growing in this real estate as well, so it's really looking at, ah, cap rates are one thing, discount rates, and then incremental cash flow. So we'll have to look at our portfolio over the next six months to see, but we're not seeing anything drastic in our valuations at this point. But it's our responsibility to review it quarterly, right?

**Brad Sturges** — Analyst, Raymond James

Okay. Thanks a lot. I'll turn it back.

**Operator**

Thank you. The next question comes from Himanshu Gupta of Scotiabank. Please go ahead.

**Himanshu Gupta** — Analyst, Scotiabank

Thank you and good afternoon. Just on 2023 lease expiries, can you remind us how much is coming due for next year and what are your expectations in terms of (inaudible) in terms of upside in base rents?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

Mark O'Brien here. So, for 2023 lease expiries, we have about 825,000 square feet, and about 85% of that is industrial, call it, 9% retail, and 6% office, which is a higher proportion of industrial than to our 2022 expiries, so that's a net positive, absolutely. Again, we talked to market, mark to market on industrial just seems to keep widening in terms of where we are and where the market is so, again, we're going to be benefitting from all that mark-to-market leasing spread.

**Himanshu Gupta** — Analyst, Scotiabank

And is there (inaudible) you have on the industrial, what kind of leasing spread you can achieve for the next year? I mean any early discussion there?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

So we're trending right now, I'm talking about industrial leasing spreads, we're about 22% across Canada. We see the strongest market, again, in our Burnside market, where we're trending 35%. But if we look at the mark to market for that specific geography, it's actually closer to 50%. And now with the JV where we own 40% of the inventory, we think we can really push that further.

**Himanshu Gupta** — Analyst, Scotiabank

Got it. Thank you. And maybe a follow up to that, Burnside market you dominate now, almost 40% market share there. What is the lease term on that portfolio, on the Dartmouth portfolio? I remember it's a shorter lease term, right?

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

It's Gordie. It's about three years.

**Himanshu Gupta** — Analyst, Scotiabank

It's about three years, okay. And clearly I can see, I mean based on your comment, you can see much more rental upside as some of these leases coming due into that one market.

**Gordon Lawlor** — Executive Vice President & Chief Financial Officer, PRO Real Estate Investment Trust

Yes, indeed. I mean Mark can comment but, as of August 4<sup>th</sup> there, we picked up another 400 tenants, so he's got a busy time here in the next little while. But again, we're seeing \$7 rents moving to \$9.50 and \$10 basically across the board is what we're seeing.

Is that correct, Mark?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

Yeah. I mean we're targeting 35% to 45% renewal spreads for that market.

**Himanshu Gupta** — Analyst, Scotiabank

Awesome. Thank you and congratulations again on the Crestpoint JV. I'll turn it back.

**Operator**

Thank you. Once again, ladies and gentlemen, if you do have a question, please press star one at this time.

The next question comes from Sumayya Syed from CIBC. Please go ahead.

**Sumayya Syed** — Analyst, CIBC Capital Markets

Thanks. I just have the one question now. Just on the renewal spreads year to date you've gotten about a 13% lift. Would you have the approximate breakdown by segment?

**Mark O'Brien** — Senior Vice President, Leasing Operations & Sustainability, PRO Real Estate Investment Trust

Yes, we do. So, again, the 22% I mentioned for the industrial, 22.4% to be exact. Office was about 2%, sort of in line with what we were expecting. Retail, we had a little bit of a negative just with a couple of tenants, outside tenants where we had to do a bit of a rental reduction. But again, if we just pulled those two retail tenants out of that criteria, we would have been 5% increase on renewal spreads for retail. So I would say, just generally, 22.5% and 2%.

**Sumayya Syed** — Analyst, CIBC Capital Markets

Okay, great. That's all I had. Thank you.

**Operator**

Thank you. There are no further questions at this time. Ladies and gentlemen, this does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your lines.