FINAL TRANSCRIPT

# Q1 2016 Retail REIT Investor Call

May 12 2016, 2016 – 9:00a ET

SPEAKERS

Conor McBroom
*Vice President, Investor Relations, Slate Asset Management*

Greg Stevenson
*Chief Executive Officer*

Blair Welch
***Partner & Co-Founder***

Brady Welch
***Partner & Co-Founder***

ANALYSTS

Jimmy Shan
*GMP Securities LP*

Dean Wilkinson
*CIBC World Markets Inc.*

Pier Nasso
*BMO Capital Markets*

## Operator

Good morning, ladies and gentlemen, and welcome to the Slate Retail REIT first quarter 2016 financial results conference call. As a reminder, this call is being recorded today, Thursday, May 12, 2016, at 9:00 a.m. Eastern Standard Time. Your host for today's call is Conor McBroom. You may begin.

## Conor McBroom, Vice President, Investor Relations

Thank you, operator, and good morning, everyone. Welcome to the first quarter 2016 conference call for Slate Retail REIT. I'm joined today by Greg Stevenson.

Before getting started, I'd like to remind participants that our discussion today may contain forward-looking statements and therefore ask you to familiarize yourself with the disclaimers regarding forward-looking statements as well as non-IFRS financial statements, both of which can be found in management's discussion and analysis. You can visit Slate's website to access all of the REIT's financial disclosure, including our May 2016 investor update, which will be available shortly after today's call.

We'll devote most of our time today to answering your questions but prior to this I'll provide a brief overview of our first quarter results and summarize what we observe to be three meaningful opportunities to continue growing our business throughout the balance of 2016 and beyond.

We remind you that all dollar amounts in this presentation are expressed in U.S. dollars unless otherwise noted.

Funds from operations for the first quarter was $10.7 million or 42 percent higher than the same quarter one year ago. This translated into FFO per unit of $0.34, a $0.01 increase over the previous quarter and a slight $0.02 decrease from Q1 2015.

Net operating income increased 5.1 percent compared to Q4 2015 while same-property NOI decreased 1 percent over the same quarter for the previous year. We attribute this to a slight decline in occupancy, which included the departure of a grocery tenant Food Basics at County Line Plaza in Philadelphia that was discussed back in March. We view this as an opportunity to re-tenant with a stronger grocer at better rents. Notwithstanding this, our overall portfolio occupancy continues to be incredibly strong, at or around 95 percent. Since first quarter 2015 we've added 23 investment properties to the portfolio, which have largely contributed to an additional $6 million in NOI.

Subsequent to the first quarter we also completed the previously announced unit holder rights offering, which was 46 percent oversubscribed. In total, the REIT raised new equity proceeds of $36.6 million that we'll be putting to work in the form of new property acquisitions and existing property development opportunities over the course of the next 12 months. We appreciate the ongoing support of our unitholders, many of whom got behind the rights offering increasing their ownership in SRT. Importantly, Slate Asset Management exercised not only its full basic subscription privilege but oversubscribed for an additional $1.7 million worth of units, increasing its position as the REIT's largest investor by over 50 basis points to 6.7 percent.

Before answering your questions this morning we'll leave you with three themes that continue to develop in our business and we believe will be key drivers of performance moving forwards. First, in the United States grocery retail segment occupancy and rents are rising as tenant demand exceeds available supply. As proof of this, our leasing program had a tremendous first quarter in which we completed nearly 284,000 square feet of transactions, including over 102,000 square feet of new shop space deals at nearly 35 percent above portfolio-wide in-place shop space rent. We also completed nearly 182,000 square feet of lease renewals at 5.8 percent over expiring rents. We view the remainder of 2016 as an excellent opportunity to continue delivering organic growth for our unitholders through our leasing program.

A second observation is that anchor tenants are overwhelmingly choosing to redevelop existing properties versus building new ones due to the more attractive returns that the former option currently presents. Indeed, new grocery store development in the United States remains at 30-year lows. We continue to cultivate relationships with our anchor tenants and will focus considerable resources throughout the remainder of this year on property redevelopment initiatives that are focused on expanding grocers and reinvesting in properties that present opportunities to add value and execute long-term leases. In increasing the credit profiles and overall quality of our centers, we'll drive foot traffic and attract other national tenants that want to do business in close proximity to our grocers. With no anchor expiries remaining in 2016 and only 3.7 percent of gross leasable area remaining for renewal, we've also turned our attention to renewing major leases in 2017 and beyond.

Lastly, our third observation is that other investors are still heavily focused on the top five to six U.S. MSAs where they're typically completing for stabilized trophy-quality assets on an income basis as opposed to value add. This trend is leaving other large secondary markets void of institutional capital and operational proficiency and it continues to provide SRT with the opportunity to buy attractively and increasingly originate opportunities where we can operationally re-imagine great real estate. From the point of view of external growth, in the first quarter we also sold our first property since the REIT's inception, Madison Center in the Huntsville metropolitan area of Alabama. The property was sold for $9.1 million, which was nicely on top of the IFRS carrying value and represented a capitalization rate of approximately 140 basis points inside what we purchased the property for less than three years ago. In the process we also pocketed over $1.5 million of NOI. Proceeds of the sale went towards the purchase of Charles Town Plaza, a Walmart anchored shopping center in the Washington Baltimore metropolitan area where Slate Retail has an existing presence of high-quality assets. This asset sale demonstrates the considerable embedded upside within our U.S. shopping center portfolio and the acquisition is consistent with our strategy moving forwards to identify opportunities to acquire in large often overlooked markets where, in our opinion, we can develop operational scale. We will continue to seek to invest in markets where capital is scarce and we can buy below replacement cost, creating an attractive margin of safety in the process.

We thank you for your continued support of our strategy. With that, operator, please open the line for questions.

## Q&A

## QUESTION AND ANSWER SESSION

**Operator**

Certainly. At this time, if you would like to ask a question, please press star followed by the number one on your telephone keypad. Again, that was star followed by the number one on your telephone keypad. We'll pause for just a moment to compile the Q&A roster.

Your first question comes from the line of Jimmy Shan from GMP Securities. Your line is open.

**Jimmy Shan, GMP Securities**

Thanks. Good morning, guys. So just on the North Augusta leasing that you did in the quarter, I was just trying to reconcile some numbers here. It looks like your new lease rental spread is about 35 percent but you make reference to rent increasing by 114 percent as it relates to North Augusta. So was that done after the quarter? Like I'm just trying to determine how those two numbers match up.

**Greg Stevenson, Chief Executive Officer**

So the 35 percent is all new leasing, the rental rate relative to comparable space across our entire portfolio. So North Augusta is very specific. It is the rental rate for those tenants weighted average relative to just the Kmart. So you're comparing to very different things. Does that make sense?

**Jimmy Shan, GMP Securities**

Okay, so out of the 60, well, there was 100,000 of new lease done in the new quarter; how much of those would relate to North Augusta?

**Greg Stevenson, Chief Executive Officer**

About 70,000.

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**Jimmy Shan, GMP Securities**

Okay. So the 114 percent is in reference to the Kmart lease as opposed to comparable space.

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**Greg Stevenson, Chief Executive Officer**

That's exactly right.

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**Jimmy Shan, GMP Securities**

Okay. Got it. Then the, so the TI in CapEx, $2.7 million in the quarter, was that also mostly relating to North Augusta?

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**Greg Stevenson, Chief Executive Officer**

No, a lot of that spend hasn't happened yet. Some of it has, probably 30 percent of it. The $2.7 million is an increase relative to leasing cost across the entire portfolio. If we were to provide some guidance around that, we think it will be $2.5 million to $3 million a quarter on average. You know, it's going to be lumpy but $10 million to $12 million annually. Half of that has to do with the fact that our portfolio has doubled in size in the last 12 months and the other half will be things like North August and some of the redevelopment opportunities that we've spoken about. And, to give you an idea, we spent about $7 a foot in TIs and leasing costs. And if you then take the new leases and then add in the spread, so just the incremental income on the revenue from renewals it's just shy of $5. So we're talking about a 68 percent return on invested capital. And then you account for the fact that that's just one year. So the average lease term for all of those leases is over eight years. So then you say by year two that's 130 percent return on invested capital and that grows every year over eight years. So what we're really excited about, while AFFO may be slightly lower this quarter the opportunity to invest this capital at such returns is something that we're really excited about.

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**Jimmy Shan, GMP Securities**

And then you made mention of the strategic acquisition loans in the MD&A. I wondered if you could talk about how many of those do you plan to do over the next little while and whether or not the REIT itself would consider doing some of the conversion itself and sort of the pricing mechanism upon which the assets will be transferred.

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**Greg Stevenson, Chief Executive Officer**

Sure. So we talked a bit about this quarter. It continues to be something we're really excited about. And, as I said, this is grocers bringing us development opportunities or acquisition opportunities and not the other way around. And then as it relates to that loan, there's one right now at $7.7 million on an asset base of $1 billion so it's not super meaningful yet and it's not moving super quickly either, because we're trying to be very thoughtful about this, and so are our partners in the grocers, but we've got a very large list of opportunities that we've been brought. It's really hard to say how big at this point. It continues to grow with every passing week.

The relevant thing for us is how much of this will be outstanding at any given time, and that's the harder thing to understand, but while there may be $100 million worth of these opportunities it could be half of that given outstanding as we move this stuff over to Slate Retail. And really it comes down to the fact that Slate Retail REIT in a lot of these cases, or all of these cases, Slate Retail REIT has the option to buy them. We have no interest in owning non-grocery anchored real estate. We believe that the downside to not being able to convert these into grocery-anchored boxes far outweighs any upside of taking them on. I think, most importantly, Slate Retail REIT pays no acquisition fee when we get these and we then get a huge pipeline of opportunities that would never otherwise get and we can buy these things for above market cap rates and valuations. So we're really excited about.

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**Brady Welch, Partner & Co-Founder**

Jimmy, it's Brady. Just to be clear, to add on what Greg says, we're excited about it but, to be abundantly clear, every opportunity is shown to Slate Retail REIT's board before anything is done and it's discussed how the REIT would like to capitalize on the opportunity. They get the first look at the deal and how it gets structured. So it's a pretty good deal for the REIT.

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**Jimmy Shan, GMP Securities**

Okay. And so… I know it's hard to figure out how much of those you're going to do but are you, you know, do you think you're going to be making a couple more loans in the near term or is this still going to be something where it might be… Or is it one of those things where it'll come sort of onesies and twosies?

**Greg Stevenson, Chief Executive Officer**

No, there'll be a couple more. And I'm not shying away from guessing because I'm trying to be sneaky, I'm doing that because I'll say something and it will be wrong, because that's how the nature of these things work. But the opportunity is big and there's a lot that we are looking at right now. And the other thing is for some of these grocers, they're anywhere between 5-6 percent of base rent and we've got, you know, 10 to 15 stores with some of these grocers, Slate Retail REIT does, and so we're really, Slate Retail REIT is really benefiting from SLAM being able to take on these opportunities. And it helps, when we're doing these developments with the grocers and then we've got, Slate Retail REIT has an existing store where renewals are coming up, those discussions are going far better than they used to because this relationship is growing stronger. So there's a lot of different benefits but, you know, at any given time we're not exactly sure but there's more coming down the pipe.

**Jimmy Shan, GMP Securities**

And these would be assets that would be 100 percent owned by the REIT to the extent that you do buy them after the repositioning. Or would it be joint venture with the grocer?

**Greg Stevenson, Chief Executive Officer**

It would be JV with the grocer. So the good thing is they'd be investing a lot of their money alongside us, which gives us further comfort in the deal and obviously the attractiveness and their commitment to the store long term.

**Jimmy Shan, GMP Securities**

Okay. Okay, thanks.

**Greg Stevenson, Chief Executive Officer**

No sweat.

**Operator**

Your next question comes from the line of Dean Wilkinson from CIBC. Please go ahead.

**Dean Wilkinson, CIBC World Markets**

Thanks. Good morning, guys. On the Charlottetown Plaza, can you give us a cap rate or will that be sort of after you close it?

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**Greg Stevenson, Chief Executive Officer**

Yeah, it was about a 7.6, 7.7 cap rate.

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**Dean Wilkinson, CIBC World Markets**

7.6, 7.7, okay. And I'm assuming that acquisition satisfied the rollover requirement on Madison Center?

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**Greg Stevenson, Chief Executive Officer**

That's exactly right.

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**Dean Wilkinson, CIBC World Markets**

Perfect. So you're done on that. Okay. In terms of the $10 million to $12 million guidance on the capital leasing costs, would that be roughly split 75 percent towards leasing, 25 percent to capital?

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**Greg Stevenson, Chief Executive Officer**

That's probably a fair assumption, yeah.

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**Dean Wilkinson, CIBC World Markets**

Okay. And, as you said, that's going to be somewhat lumpy over the quarters but that's what you expect the annual kind of run rate to be on that.

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**Greg Stevenson, Chief Executive Officer**

Yeah.

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**Dean Wilkinson, CIBC World Markets**

Now that's, I mean it looks like a high number but I understand that there's a lot of leasing costs that you have. Once you go beyond sort of a 12-month window would that number come down? Or do you think that it's going to naturally run that high.

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**Greg Stevenson, Chief Executive Officer**

I think it's growing as our portfolio grows, and that's just part of it. So if you look at it as a percentage of assets it's not growing as much as it is on, you know, an absolute basis. But it will be... If we were to stay at 66 properties, which we won't, it would come down from $10 million to $12 million. But, you know, we're going to continue to grow. With the rights offering and the debt recast, both of which we think are fantastic, we can grow the REIT by 10 percent. So part of this guidance I think partial, you know, is built in to account for the fact—

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**Dean Wilkinson, CIBC World Markets**

It's built in to account for that, yeah. So I'm just trying to think of it on a normalized per square foot basis, right? So to sort of back into a future assumption around, you know, you grow the GLA by so much, we apply sort of a normalized reserve for TIs, LCs, and CapEx to get me to a number.

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**Greg Stevenson, Chief Executive Officer**

Yeah. I haven't looked at it that way but, you know what? I will. I'll run a number and then I'll get back to you on that so you can plug something in that so it changes as we grow.

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**Dean Wilkinson, CIBC World Markets**

Perfect. That works. And then just on the $7.7 million loan outstanding, have you said where that property is?

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**Greg Stevenson, Chief Executive Officer**

We can't yet, and only because this program for us is one where the grocer says this is a property where there's no grocery anchor and we want to be there. And the reason they're coming to us is because if they go and try and buy the center the seller is going to know what they want to do. So they've tapped us for two reasons. One, because we can go and buy it opportunistically without the seller necessarily knowing we've got the grocer in our back pocket. So we don't have to pay for that growth.

And I think the second part is, you know, we've done a very great job, the guys here have done a very great job in building the relationship with these folks, so we're a preferred counterparty, and it really comes back to the secondary market story. If we were in markets with Kimco and Equity One, all these large cap REITs, you know, I'm not going to sit here and say that they'd be coming to Slate Retail REIT. But we're going where other people aren't and we're far more capitalized, far more sophisticated, and I think that's why we're the preferred counterparty, because we are the top dog in the markets that we're in and we've built that relationship.

So we're just not saying because we don't really want to give that away, because it's a huge benefit to Slate Retail REIT.

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**Brady Welch, Partner & Co-Founder**

Hey, Dean. It's Brady. The other reason is that in order to do the grocery store we need to get control of space and so we don't want to be telling the market that we're going to be cutting the deal. So that's part of the reason. We're not trying to be coy by not saying where but part of the risk in the deal is getting that space to be able to do a grocery.

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**Dean Wilkinson, CIBC World Markets**

Right. So then when you've got control and then it's in your hands then we'll know kind of where it is and what the plan is.

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**Blair Welch, Partner & Co-Founder**

Exactly. We'll be able to cut the deal with the grocery store then.

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**Dean Wilkinson, CIBC World Markets**

Okay. That sounds fair enough. And then in terms of the loan package, has the REIT, like is there a security against the asset or is it just sort of like a GSA of the Slate sub in the U.S. that secures the loan.

**Greg Stevenson, Chief Executive Officer**

Yeah, there's a security against the property. And we earn 8% percent so it's accretive to the REIT.

**Dean Wilkinson, CIBC World Markets**

Okay. And that's a current pay or does that accrue?

**Greg Stevenson, Chief Executive Officer**

That accrues.

**Dean Wilkinson, CIBC World Markets**

That accrues to the back end and just falls into the proceeds on sale I assume then?

**Greg Stevenson, Chief Executive Officer**

That's right. Whether it's us buying it or someone else.

**Dean Wilkinson, CIBC World Markets**

Perfect. Okay, that's all I had. Thanks, guys.

**Operator**

If there are any additional questions at this time, please press star followed by the number one on your telephone keypad.

Your next question comes from the line of Pier Nasso from BMO Capital. Please go ahead.

**Pier Nasso, BMO Capital Markets**

Hi. Good morning. Most of my questions got answered just on that strategic acquisition loan, the $7.7 million. Is there any idea on timing, like when the trigger would get pulled on something like that?

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**Greg Stevenson, Chief Executive Officer**

Well, there's not, and that's a lot of the reason why Slate Retail REIT isn't going in day one is because of that uncertainty. As a lender our downside is that the tenant that we need out of the space wants to stay because they're doing well, so it's not bad downside as a lender, which is why we like that position. You know, if we were an owner that's bad downside for us, because then we own a non-grocery anchored strip center with, you know, it's tough to say there's going to be growth in rent. So there's no timing and it largely depends on how successful we are in getting that tenant out of there and, you know, that's the risk to us.

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**Blair Welch, Partner & Co-Founder**

I think as soon as the deal is baked, that's when the REIT has the opportunity to take control of it. So as soon as that deal is done with the grocer and everything can be announced and it's public, that's when the REIT can exercise. So it's right away. It's just the REIT won't, we won't talk about it until it's all fully tied up neatly with a bow.

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**Greg Stevenson, Chief Executive Officer**

Yeah. We don't know when that, how long that might be.

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**Pier Nasso, BMO Capital Markets**

Okay. Thanks. I'll turn it back.

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**Operator**

There are no further questions at this time. I turn the call back over to the presenters.

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**Conor McBroom, Vice President, Investor Relations**

Thanks for joining us this morning. As always, we welcome any additional follow-up questions after the call and we look forward to providing our next update.

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**Operator**

This concludes today's conference call. You may now disconnect.

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