Retail REIT
SLATE

FINAL TRANSCRIPT

Q2 2015 Investor Call

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SPEAKERS

Conor McBroom
Vice President, Investor Relations

Greg Stevenson
Chief Executive Officer, Slate Retail REIT

Brady Welch
Chief Financial Officer, Slate Retail REIT | Partner & Co Founder, Slate Asset Management L.P.

Blair Welch
Partner & Co Founder, Slate Asset Management L.P.

ANALYSTS

Heather Kirk
BMO Capital Markets

Jimmy Shan
GMP Securities

Sumayya Hussain
CIBC

Endri Leno
National Bank Financial

Michael Smith
RBC Capital Markets

Operator

Good morning, and welcome to Slate Retail REIT's second quarter 2015 investor conference call. At this time, participants are in a listen-only mode. However, at the conclusion of today's presentation, management will conduct a question-and-answer period.

Participants are reminded that today's conference is being recorded for the benefit of unitholders and other interested parties who may want to review the call at a later time.

I will now turn the call over to Mr. Conor McBroom, Vice President of Investor Relations. Please go ahead, Mr. Conor McBroom.

Conor McBroom — Vice President of Investor Relations, Slate Retail REIT

Thanks, Operator. Hello, everyone. We appreciate you taking the time to participate this morning, including those joining via our webcast. I'm here today with Greg Stevenson, Blair Welch, and Brady Welch.

Before getting started, I'll remind listeners that our discussion today main contain forward-looking statements. We, therefore, ask that you familiarize yourself with the disclaimers regarding forward-looking statements, as well as non-IFRS financial measures, both of which can be found in management's discussion and analysis for the quarter.

You may access all of Slate Retail REIT's financial disclosure, including the August 2015 Investor Update, on slateam.com/SRT.

Moving on and setting aside financial results for a moment, our big announcement this week is the appointment of Greg Stevenson to Chief Executive Officer of Slate Retail, which takes effect immediately. This is very exciting news for the REIT's ongoing growth and development, and to that Blair will say a few words.

Blair Welch — Partner and Co-Founder, Slate Asset Management, Slate Retail REIT

Thanks, Conor. I'd like to congratulate Greg on his appointment to Chief Executive Officer. Since being at Slate, Greg is a leader. He came to Slate as a CFA and with very good experience, including working at a leading worldwide real estate company.

In his time at Slate he has been the head of U.S. operations, leading our accounting group, our asset managers, our leasing, and construction team. Many of the people on the phone have dealt with Greg personally. Whether it's the analysts, investment bankers, or financing sources, Greg's been leading the charge and doing a great job.

Greg also has extremely strong tenant relationships, has worked with our leasing brokers, and has effectively earned this responsibility. We couldn't be happier for Greg. That's the first thing.

The second thing is I think this shows the bench strength of Slate Asset Management, how we can grow great people from within and have great people on our team to support what we have. We have dedicated focus on Slate Retail REIT.

And then third, I'm not going anywhere. We are the largest investor in Slate Retail REIT, and I will still be a Trustee. We are focused on this investment every day. It's important to us. And again, I just want to congratulate Greg. We're excited for the future.

Conor McBroom

Thanks, Blair. So our plan today is to devote most of the time we have to answering your questions, but we also want to briefly outline some key highlights from the quarter as we continue to expand the Slate Retail platform.

Net operating income for the quarter was $12.9 million, or 87 percent higher than a year ago. Funds from operations was $8.5 million, or $0.31 per unit, representing 15 percent growth on a per unit basis over the same period a year ago. And last, adjusted funds from operations for the quarter was $7.7 million, or $0.28 per unit, a 12 percent increase over last year.

Q2 was another very active quarter for our leasing program. We completed nearly 200,000 square feet of transactions, and in the process achieved 6.6 percent renewal spreads for tenants below 10,000 square feet. Meanwhile, for tenants over 10,000 square feet the renewal spread was nearly 3 percent.

So as we carry out our business plan we continue to witness the meaningful impact that our below-market in-place rents, which on average are below $10.00 per square foot still, is having on our ability to grow revenue.

When you couple this with the fact new shopping centre supply remains at 30-year lows in the United States, and the direct impact of this supply shortage on occupancy, we foresee considerable runway in the months and years ahead for continued growth.

Slate Retail also made a number of strategic acquisitions in Q2, not the least of which being the vend-in of Slate US Opportunity (No. 3) Realty Trust and its 13 strong performing grocery shopping centres, each of them highly complementary to SRT's portfolio.

During and subsequent to the quarter, the REIT also acquired or committed to acquire eight additional properties, raising the portfolio total to 63 properties that comprise more than 7 million square feet.

All of this is to say we have more than doubled the size of the 29-asset portfolio that was listed on the Toronto Stock Exchange in April of last year, and in the process we've increased the number of distinct tenants in our portfolio to over 600 from around 360 originally.

We also continue to strengthen the geographical diversification, as the REIT now has assets in 20 states. The REIT also continues to provide more exposure to larger markets relative to most of our peers in Canada and the United States, with the vast majority of portfolio revenue derived from cities with over 1 million population.

We continue to be proactive managers of debt capital. Most recently in June, we completed nearly $60 million of fixed rate financing, which further reduced the REIT's proportion of floating rate debt to 68 percent versus over 86 percent on June 30th of last year.

In the last 12 months, our fixed rate financing initiatives, which are targeted at properties that management has stabilized, has resulted in the repatriation of nearly $17 million of equity. In the process we've also lowered the REIT's interest rate by 30 basis points.

As Greg describes in his letter to unitholders that prefaces management's discussion analysis for the second quarter, we believe that considerable organic growth opportunities persist across our portfolio.

Firstly, as I touched upon earlier, the reality is that the vast majority of our properties have below-market in-place rents – 25 percent below market on average. Second, we continue to purchase properties from undercapitalized investors and owners to which shopping centres are not a core holding. From here, the Slate Retail management team can add value by applying its expertise in real estate operations.

Lastly, we continue to purchase properties where we have a previously established relationship with the anchor tenant. Opportunities exist at many of these properties to partner strategically with the anchor to enhance and/or redevelop the property, which creates enormous value for both investors and tenants in the process.

Turning to alignment, Slate Asset Management, as Blair mentioned, continues to be the REIT's largest unitholder with an approximate $30 million equity stake in Slate Retail REIT in US dollars. More than anything else, we are motivated to grow our investment alongside fellow unitholders. We're passionate about our business plan and the value-add opportunities we continue to uncover.

Although at Slate we see ourselves as real estate operators first, we also have a duty to be effective allocators of capital. In May, the REIT renewed its normal course issuer bid, and identifying that the market was valuing our real estate at well below replacement cost, we proceeded to repurchase for cancellation nearly 0.5 million trust units, totalling approximately $5.3 million.

Our unit buyback program then carried into the second half of 2015, and moving forwards we'll continue to evaluate unit buyback opportunities to the extent that doing so is a more efficient opportunity to allocate capital than the next best alternative.

So thanks for calling in today, and with that we'll open up the line for questions.

Q&A

Operator

And at this time, I would like to remind everyone in order to ask a question, please press *, then the number 1 on your telephone keypad. We'll pause for just one moment to compile the Q&A roster.

Your first question comes from the line of Heather Kirk from BMO Capital Markets. Your line is open.

Heather Kirk — BMO Capital Markets

Good morning. I'm just trying to reconcile the 25 percent below-market with the 6 percent that you're getting on the mall shop leasing. Do you expect that—on my math I would think if you're 25 percent below market when you roll you'd get more than 25 percent? So do you expect that number to trend up? Or if I'm looking at that the right way?

Greg Stevenson — Chief Executive Officer, Slate Retail REIT

Yeah. I think a lot of it has to do with the leases that expire, so it's subject to that. I think if you also compare the 6 to 9 percent that we've done since inception on renewals with the almost 19 percent that we've done for new deals in the portfolio you start to trend upwards.

Obviously you've got to take both into account, and I think that that number does trend higher as we go forward. I think in the US we're at a 35-year low in supply right now. There's very little new supply coming on, vacancy is ticking downwards, and demand for space is picking up. So all those things, I think, begin to push rental rates higher.

I think the other thing that we've done very well is from a return on an invested capital perspective, or an NER perspective, if you look at our capital, which is actual—I know some other companies report a normalized number—we were $0.07 per square foot. I think the capital that we're investing to get these rental rate increases continues to be a fraction of our peers.

Heather Kirk

And you expect that to sort of be the run rate going forward?

Greg Stevenson

I think it's case by case. I think there will be some opportunities to invest meaningful capital for meaningful return, and I know we talked a bit about it this quarter where we've had opportunities to invest alongside anchors to do some more meaningful redevelopment at our assets.

So run rate, no, because I think there will be some lumpy numbers in there, but I think the benefit of our leases in our asset class is that it does generally not require large amounts of capital.

Heather Kirk

And turning to the other side, can you comment on occupancy being a little bit lower [than the previous quarter – the SUSO 3 acquisitionbrought down some of the (unintelligible) it looks like?

Greg Stevenson

I think you nailed it. SUSO 3 was lower, and that dragged the weighted average down. Same-store occupancy was flat, SUSO 3, and then I think a lot of the recent acquisitions we've picked up some assets with a bit more vacancy where we think that there's a leasing opportunity.

And to your point, I think we recognize that at some of these assets they've been under managed, and we think we can lease them up and we think we can bring rents to market.

Heather Kirk

Great. Thanks very much.

Operator

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

Jimmy Shan — GMP Securities

Thanks. First of all, congratulations, Greg.

Greg Stevenson

Thank you.

Jimmy Shan

My first question is just on the capital allocation. So you've been active obviously on the NCIB. I'm just kind of curious as to how you think about allocating capital now in terms of unit buyback versus acquisition at this point?

Greg Stevenson

Yeah. I think it's NAV per share growth, or NAV per unit growth, I should say, at the end of the day, and it's not necessarily point in time. I mean I think if we see a real estate asset where we think that the growth in the future is meaningful, while it may not be as accretive as purchasing shares today it may be even more so in the future. And effectively we just weigh the two against each other.

Obviously we believe that our portfolio at the size and quality it is today and our stock price in June and July, we thought it reflected a mispricing relative to some of the opportunities we saw in the real estate assets that we could purchase. So our job is to allocate capital appropriately, and if our units continue to look attractive to us you will continue to see us buying back units in the open market.

And if we find great real estate deals, which Adam and Darrell continue to do, we're going to do that as well because we're real estate operators, and we think that we're at a point in time in the US where capital continues to flow to core markets. And some of the assets that we are looking at have been ignored, and it's great real estate with under-market rents, and we've been able to pick up some vacancy. And we think that there is an opportunity to lease it up and bring rents to market and there'll be income growth as a result of that.

Jimmy Shan

Okay. And the last two acquisitions you guys made, the Birmingham and the Locust Grove, it looked like you're buying it with some vacancy. Can you maybe talk a little bit about those two properties? And kind of step them back, kind of bigger picture on the acquisition strategy, is that what you're looking to do more of?

Greg Stevenson

Yeah. I think it's case by case. This was a unique example. So the prior owner was a utility company that was sitting on excess cash in 2006, and thought they'd try their hand at developing real estate assets. And they developed two very nice assets, Publix-anchored shopping centres. Publix is a private grocer, one of the top in the United States with next to no debt, very strong covenant. Both of these assets are in great markets.

And when we went to visit the assets we had tenants coming out asking us if we were the owners of the shopping centre because they wanted to lease more space and that they hadn't seen the owner in two or three years, and they couldn't find anyone to get a hold of to lease more space.

We know the markets very well. We're active in Atlanta already. We've got very strong leasing teams there, and we've already got some leases signed at these centres already very shortly after purchasing this centre.

So I think it's what we talked about in the letter, which is we think that there's an opportunity to purchase assets where the prior landlord isn't a real estate operator, whether that's a utility company building a real estate asset to find a home for their money, or if it's a large institutional REIT that this is asset 430 of 862 type of thing.

So I think it's case by case. We're not out there searching for vacancies trying to hit a home run. I think we take calculated risks. And where we see an opportunity that we think with a high probability that we can lease up the space and grow income we're going to do that.

Jimmy Shan

Okay. So what would the going-in cap look like on these two? And what do you think once you do the leases? And how would that stabilize—what would it stabilize to?

Greg Stevenson

It would go from what we bought it at, which is about a 7 cap, to slightly over an 8 cap.

Blair Welch

It's a pretty typical story, or it sounds for most Canadians. When some companies have a big pile of money and all of a sudden they become developers sometimes that doesn't end well for those people.

Jimmy Shan

Right, right.

Greg Stevenson

Yeah. I think it's the same sort of thing, right? On a price per square foot basis it's very attractive, and price per square foot comes down to us being able to lease competitively and offer rental rates that our competitors who pay more can't. And we win that fight.

Jimmy Shan

Okay. Last question is just on the Ahold and Delhaize merger. Do you have a sense of how that may impact your stores?

Greg Stevenson

I don't think it will have any impact. Consolidations with other grocers haven't. I mean it really all comes down to the location and the store. We pay very, very close attention to size and format. We want to make sure it's a format that works for the grocer. Whether it's Ahold and Delhaize or any of our other grocers, we look at GROC ratios. We've got a sub-3 percent GROC ratio across the portfolio.

We talk to the grocers; we make sure that it's a profitable store; we make sure that they've invested recently in the store, i.e. if Delhaize, Ahold, or someone else decided that they didn't want to be in any typical market anymore someone else would be there to take those sales because the sales and the profitability are strong enough.

But initial indications are that this will have no impact on any of the stores that we have. We think it's a good thing. We think it strengthens the credit, so we're happy about it.

Jimmy Shan

Okay. Thank you.

Operator

Your next question comes from the line of Michael Smith from RBC Capital Markets. Your line is open.

Michael Smith — RBC Capital Markets

Thank you. I have two questions. First, with the 10-year treasury below 2.2 percent do you see yourself fixing more debt? And secondly, you're now in 20 states. Where do you see that eventually getting to? Or capping out at?

Greg Stevenson

I think the first question is our goal is to fix more debt over time just in general. We're not going to do it in advance of our leasing and management program, i.e. when we have reset rents, increased occupancy, increased anchor term, and added the value we think we can add to the assets, we will take them out to the market for refinance.

And the six assets that we financed in Q2 at 10-year fixed rate debt at 4.14 percent were comprised of those types of fixed assets. And I think the game plan will be no different going forward. And I think we'll continue to look to do that and maybe do another one in 2015 as we continue to add value to the existing portfolio.

The second question, we're in 20 different states mainly east of the Mississippi. We look across the country for deals. I think that there are benefits to adding capacity in the existing markets that we're in. So we'll continue to do that.

I also think that there's 37,000 grocery stores in the Unites States and there are plenty of opportunities to add capacity in the markets we're in, and we're going to continue to look to do that. So there's no goal to say we need to be on the West Coast. What we want to do is pay the right price for great real estate, and if we can do it in the existing markets that's great.

Blair Welch

Just to add to that, Michael, I don't think it's a fair thing to say there's 50 states in the US and 10 provinces. It's not the same. The US is regional; the grocers are regional. It's not like they're in one state. For example, we break the US into six regions: the Southeast, the Mid-Atlantic, Northeast, Midwest, Great Lakes, Central Corridor for Energy, and West Coast.

So it's not like there's a lot of states in the Southeast and there's regional grocers throughout those states, it's not like it's widely spread apart. We really follow the grocers; we want to be with the best grocers in the region.

Michael Smith

Okay. Good. That makes sense. Thank you.

Operator

Your next question comes from the line of Sumayya Hussain. Your line is open.

Sumayya Hussain — CIBC

Thank you. I just have a question on the G&A. It ticked up a little bit higher in Q2 than it has been historically, so what would be a good run rate to use going forward?

Greg Stevenson

I think that the guidance we've given before for total G&A, which includes asset management fees, is 1.1 million a quarter. This quarter we had a few onetime items that won't be there in Q3 or Q4, so I think G&A, including asset management fees, is going to be about 1.1 million a quarter is our run rate.

Sumayya Hussain

Okay. So Q3 would also see some onetime personnel transition expenses?

Greg Stevenson

No. They won't be in—Q2 was higher due to onetime items, and you won't see those in Q3.

Sumayya Hussain

Okay. Thanks. Just a question for Blair. Going forward, where do you see yourself focusing your efforts? Do you see yourself going back to the private side? Compiling a pool of assets? Just what's the focus of Slate going forward?

Blair Welch

Yeah. I think that waking up today and not having the CEO job it was the same as I got up yesterday. My focus is the exact same and it's to grow Slate Asset Management and work with a great team of people, which I do.

And Slate Retail REIT's a great business. We're the largest investor, and I'm going to be helping Greg and his team grow it. And for Slate Office REIT we're the largest investor, and I feel the same way. And whether it's working with our pension fund partners, it's about building a great real estate team. And that's what we have been doing since we started Slate, and I'll just continue to do that.

Sumayya Hussain

Great. Thank you. And last question for Greg. What do you see as one or two main opportunities to do things maybe a little bit differently going forward? Or what's going to be your priority?

Greg Stevenson

I don't think so—I may have to change desks because I've got the two largest shareholders sitting next to me, but other than that I think it's business as usual. To Blair's point, nothing has really changed in how the REIT will be operated.

Our goal is to buy great real estate, grow income per unit and net asset value per unit for our shareholders, of which management and insiders are the largest. So that's what we're going to continue to get out of bed every day to do.

Sumayya Hussain

Okay. Thank you.

Operator

There are no further questions at this time. I will turn the call back to Mr. McBroom for closing remarks.

Conor McBroom

Really quickly, thanks, everyone, for participating today, and for your ongoing support of Slate Retail. We're available any time to answer any additional questions you have, and we look forward to providing another update later on this fall.

Thanks very much.

Operator

Ladies and gentlemen, thank you for your participation. This concludes today's conference call. You may now disconnect.

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