FINAL TRANSCRIPT

Q3 2015 Investor Call

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20 minutes

SPEAKERS

Greg Stevenson
Chief Executive Officer, Slate Retail REIT

Conor McBroom
Vice President, Investor Relations

ANALYSTS

Heather Kirk
BMO Capital Markets

Jimmy Shan
GMP Securities

Dean Wilkinson
CIBC World Markets

Endri Leno
National Bank Financial

Michael Smith
RBC Capital Markets

Operator

Good morning ladies and gentlemen, and welcome to the Slate Retail REIT Q3 2015 financial results conference call. As a reminder, this call is being recorded today, Monday, November 16th, 2015 at 9:30am Eastern Standard Time.

Your host for today's call is Conor McBroom. You may begin.

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

Thank you operator and good morning everyone. Joining me on the line today is Greg Stevenson. Before getting started I'm going to remind you that our discussion today may contain forward looking statements, and therefore ask that you please familiarize yourself with disclaimers regarding forward looking statements as well as non-IFRS financial statements, both of which can be found in management's discussion and analysis for the quarter.

You can visit Slate's website to access all of Slate Retail REIT's financial disclosure including our November 2015 investor update, which will be available shortly after the conference call. We'll devote most of our time today to answering any questions, but we'll briefly summarize some of the achievements of our US platform.

Slate Retail has had another exceptional quarter, highlighted by net operating income which increased by over 7% compared with the same quarter for the previous year. This translated into funds from operations, which grew by nearly 14% year over year.

During the quarter, the REIT acquired five additional investment properties in South Carolina, Colorado, Georgia and Florida. Not only are these states that we already have an established presence, but we acquired these properties for approximately $139 per square foot representing a significant discount to replacement cost. This coupled with low in-place rents, which now average just over ten dollars per square foot portfolio wide, means that we're able to compete aggressively for tenants via our leasing program.

Because our rents are nearly 25% below market we're also able to grow rental revenue appreciably over time. In this regard, lease renewal spreads for shop space in the quarter was 9.6% above expiring rent. On the other hand, nearly 23,000 square feet of new leasing was completed at a 47.1% premium to portfolio wide shop space rent.

This is very positive activity and it's really the continuation of a robust leasing program throughout 2015, which year-to-date has seen well over half a million square feet of completed transactions. Year over year we've also increased same store occupancy and NOI margin by 50 and 100 basis points respectively. So in conclusion we're very excited with how the business is performing to this point in the year. We firmly believe there is ample runway for continued growth. As Greg pointed out in his letter to unitholders for the quarter, supply for grocery anchored real estate is at multi-decade lows in the United States. Tenant demand to rent space is only increasing as the US economy strengthens along with household income and job growth.

We're pleased to once again have been able to increase distributions to unitholders, the second time in the last twelve months. At the same time we're maintaining among the lowest payout ratios of all Canadian REITs, which is consistently below 70%. Recognizing considerable value in the price of our units, we continued repurchasing units for cancelation during the third quarter under the REIT's Normal-Course Issuer Bid (NCIB).

In fact, we amended the NCIB in the third quarter to allow for the repurchase of up to 2.6 million units from 1.1 million units – the new allocation representing approximately 10% of the REIT's public float. Year to date we've bought back units totaling nearly US$12 million. With increased capacity under the NCIB we'll continue to evaluate the opportunity to buy back units to the extent we feel this investment decision will provide the best long term results for fellow investors.

So with that we'll turn the call over to answer any questions, thank you.

Q&A

Operator

At this time I'll inform participants that in order to ask a question please press star then the number 1 on your telephone key pad. Again, that's star then 1. We'll pause for a moment and compile the Q&A roster. Again, if there are any questions, star then 1 on your telephone keypad.

And your first question comes from the line of Jimmy Shan from GMP Securities, your line is now open.

Jimmy Shan — GMP Securities

Thanks, good morning guys. Just on the Buckeye Plaza situation, can you provide a bit of context as to what happened there and then how should we think about anchor tenant renewals coming up? I know you've got nothing coming up in 2016 but as we look at beyond that, how should we think about that?

Greg Stevenson — Chief Executive Officer, Slate Retail REIT

Sure, Buckeye Plaza was a GAR asset, so it was one of the first properties that we purchased back in 2011, so it was a double digit cap rate at the time. I think the new rent reflects more of a market rent. I think this an anomaly obviously being one of the earlier assets that we purchased, I think it speaks to our strategy of purchasing centres with very strong sales which this plaza certainly has.

We kept our anchor, which is obviously part of our strategy and the asset remains almost 100% occupied. What we never like to see is a decrease – I think this is a one-off situation and we kept our anchor at no cost either, so I think that's another important part of this.

Jimmy Shan

And so, are there – if I were to look at the top ten or top fifteen anchor tenants – would they, in general, be at about market? Would you say? Or overall?

Greg Stevenson

Yes, I think over time it's very lease dependent. Some anchors have preset options, some are flat, some have growth and some don't, some it becomes a negotiation. I think we believe that most all of our anchor leases and our shop space leases have under market rents.

Jimmy Shan

On the insurance premium that you talked about in a letter and the property management savings, would those actually directly flow to the bottom line, or is that really more of a savings to the tenant?

Greg Stevenson

Well, it's going to be both. I think it'll be a gross rents savings which means that we're more competitive than our property sets in our markets (i.e. it'll help us on our gross rent number), and then for leases that we don't recover all of our expenses (which we have obviously), that would flow directly to NOI, as would it would for our vacant space, so that's 6% of total GLA.

Jimmy Shan

And is that effective this quarter or is that already built into the numbers in the last few quarters?

Greg Stevenson

No, it just – both are two recent transactions that you'll see going forward.

Jimmy Shan

And then on the property management, I know CBRE was really the main provider there, has there been any change as a result of getting it out or?

Greg Stevenson

No change, I think we just have more people and more support at a lowered cost, so I think it's been a net benefit just like Retail REIT.

Jimmy Shan

OK, thank you.

Operator

Your next question comes from the line of Dean Wilkinson from CIBC, your line is now open.

Dean Wilkinson – CIBC World Markets

Thanks, morning guys. Just further to Jimmy's question there on the insurance premiums and the property management, what kind of margin impact do you think we could reasonably expect there or to put it another way, do you have any guidance in terms of the NOI margins? Would they still be running somewhere around 75% on an annualized basis?

Greg Stevenson

We model between 68 and 70. I don't think there'll be a material change, I think we keep it as is and I think that one thing that we've started to look at – and it's not going to be every acquisition but – you'll note that three of our acquisitions within the quarter were below 90% occupancy which would obviously have some effect on our margins in the short term.

So I think long term it's an opportunity; we can lease these assets up and we've been successful with the existing assets in our portfolio. I think because of some of these new acquisitions that I would continue to model 68% to 70% in NOI margins with the 68% and 70% range being seasonal, the winter months you had asked in Q1, Dean, snow removal largely affects those numbers, but then as you see, as we go later throughout the year we're back up today to just shy of 73%.

So I think 70% is a good number.

Dean Wilkinson

70% and then the potential to increase that a little on some lease up.

Greg Stevenson

Correct.

Dean Wilkinson

And would the G&A at $1.9 million be reflective of where you think you are now?

Greg Stevenson

Yes, I think that's right on top of what we expected.

Dean Wilkinson

And the other question I had was just on the – and this may be a little more detail than you have handy – on the aging receivables, it looks like you've made some progress there, particularly on the longer dated stuff – did you collect all of that or did you have to write some of that off?

Greg Stevenson

No, there was bad debt this quarter: $321,000 which is – it's quite lumpy, it's obviously nonrecurring costs. Largest quarter to date – yes, there was bad debt this quarter, $321,000.

Dean Wilkinson

$321,000 and then the other about $700,000 would've just been collected then. Perfect, that's all I got then, thanks guys.

Greg Stevenson

Thanks.

Operator

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

Michael Smith — RBC Capital Markets

Thank you and good morning. Just on your same property NOI growth, at 7.2 a very healthy number, what are you thinking for the next twelve months?

Greg Stevenson

No real foresight into that. I think what we continue to try to do is come in every day and move up occupancy, increase rents, keep an eye on our costs, stay competitive on a leasing perspective and spend capital wisely.

I think our NOI quarter to quarter will vary. I think the strategy is with under market rents and the ability to purchase assets below replacement cost which allows us to win a leasing fight, should serve for same property NOI growth going forward, but no real insight as to what it's going to do quarter over quarter.

Michael Smith

Okay, and on capital, what are you thinking in terms of leverage, buybacks and acquisitions? How do you think about that now?

Greg Stevenson

All three strategies remain the same. If our units continue to provide a good value proposition, we'll continue to buy back units.

On acquisitions, if we can find a great piece of real estate that we think will provide future growth and strengthens the portfolio, well same thing, I think we'll continue to do that.

And then leverage, the plan is to continue to stabilize assets and move them into fixed rate debt pools as we've done in the past.

Michael Smith

That's it for me, thank you.

Operator

Your next question comes from the line of Shez Samji from Aston Hill, your line is now open.

Shez Samji – Aston Hill Financial

Hello guys, thanks for taking my call. Your Birmingham acquisition, it kind of stands out from an occupancy perspective, can you just explain the thesis on that one?

Greg Stevenson

Yeah sure. We talked a bit about this last quarter, that we had the opportunity to buy two Publix anchored shopping centres. Publix is one of the best operators in the United States. And it was the same sort of

thing: it was below replacement costs, under market rents, strong anchor with strong sales and a low GROC ratio which is effectively gross rent as a percentage of sales and speaks to the profitability of the grocer.

And it was a non-real estate operator who we were buying the centre from. And we've had some success in the past, taking over these undermanaged centres, spending some modest capital, being proactive on the asset management side. And we've been leasing up space, increasing occupancy, increasing rent and this is the exact same story here. It was a non-real estate operator and we've already had success on the leasing side of both assets with new leases and occupancies already starting to tick upwards.

So that's the plan and we bought these at a cap rate that was still slightly north of 7%, so if you stabilize these there we're getting 8 to north 8 of a cap rate on something that we think has a reasonably high probability of happening, so that's how we were thinking about that. I think in the markets that we like and we have experience in I think we'll look to do more of these. It's not going to become our whole portfolio but where opportunities present themselves, we'll definitely jump at them.

Shez Samji

And have you guys considered a recycling program on your portfolio or is it too early for that?

Greg Stevenson

Say that one more time?

Shez Samji

A recycling program? Like, selling some properties and recycling that capital into more properties like these? Like the Birmingham?

Greg Stevenson

Nothing as of yet. We buy every asset and we bought every asset one by one and we go around the room and say, would you own this asset forever and the answer is always yes if it's an asset that we end up buying. So no intention to sell yet.

If there's a too-good-to-be-true offer on the table it's obviously something that we would consider because there's more, we think, great deals out there on a real estate perspective and we think our units are cheap as well.

Shez Samji

Great, perfect, thanks guys.

Operator

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

Heather Kirk – BMO Capital Markets

Good morning. In terms of the acquisition market, can you just comment a little bit on what you're seeing from a cap rate perspective and also, I'd just be curious to get your thoughts on how far you'd be willing to push leverage given the choppier state of the new equities market.

Greg Stevenson

Yes, cap rates have come in across the United States in certain markets more than others, and the markets that we're in we've seen a slight down-tick across the board. I think we've underwritten now seven billion dollars of just grocery-anchored real estate since inception. There is more product coming to market, we think the role of 2006-2007 ten-year CMBS will provide another opportunity for us.

I think we'd have to roll up our sleeves a little more than the past but we're the third or fourth most active buyer of grocery stores in the United States. So people know who we are and we see a lot of deals, so I don't think we'll have a hard time finding more real estate.

I think we've been partnering with grocers which has become a new source of acquisitions for us, where they're an operator in some of our markets whether it's ten or fifteen miles away or nearby and they're with a struggling landlord. So we're starting to see that too and we've proven that we can close. We've done now 65 separate transactions, which I think will be our benefit.

So I don't think anything changes, I think that we might see some more portfolios come to market as pricing gets a little bit better. Folks are going to start to look to monetize – that is my guess – and then I think as it relates to debt, I don't think anything changes there, I think we're going to maintain a relatively conservative leverage ratio. Our target is 55% – we may come up a bit if we find some great real estate but I don't think the plan is to take leverage up much higher than it is today.

Heather Kirk

But you'd be willing in the short term to maybe push it a little bit further if you saw the right kind of portfolio?

Greg Stevenson

We're not looking at any portfolios. I think, we're going to continue to buy one-off assets one by one because that's where we think the opportunity is because portfolios are trading for much tighter cap rates, but yes, if there's an opportunity to buy a great piece of real estate and I mean taking our leverage from 55 to 57 then yes, that's something we would definitely do.

Heather Kirk

And just following up on the lower occupancy acquisitions, what's your target timeline when you buy an asset like that that's in the 70% to 80% occupancy range? Are you looking to get that to stabilize within a 24 month period or how should we be looking at the growth component of those acquisitions?

Greg Stevenson

Our returns work at the occupancy levels they're at today because we've been able to buy advantageously so we've been pretty conservative on the leasing side. I think that our guys have been doing an excellent job of being proactive asset managers and I think by the 24 to 36 month period is probably quite realistic. We're certainly not underwriting it in six to twelve months, because we don't need to.

Heather Kirk

You said that you didn't really have foresight into the same property NOI number… do you have a target you'd be happy to achieve?

Greg Stevenson

I think we want to outpace inflation over the long term. We manage our business looking out a few years, not a few quarters because that's how we think about it. So really, no quarter over quarter target. It's more of a long term three to five year plan that we hope to outpace inflation by a meaningful number.

Heather Kirk

Great, thanks very much.

Operator

There are no further questions at this time, Mr. McBroom, I turn the conference back to you sir.

Conor McBroom

Thanks everyone for taking the time to be with us this morning, if you have any follow up questions feel free to reach out directly to me or Greg, otherwise, we look forward to providing our next update in the early bit of next year. Thanks again.

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