FINAL TRANSCRIPT

Choice Properties Real Estate Investment Trust
Second Quarter Results Conference Call
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Same Damiani
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Sumayya Hussain
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Pammi Bir
Scotia Capital — Analyst

PRESENTATION

Operator

Good morning. My name is Chris, and I will be your conference Operator today. At this time, I would like to welcome everyone to the Choice Properties Real Estate Investment Trust Second Quarter Results Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press *, then the number 1 on your telephone keypad. If you would like to withdraw your question, press the # key. Thank you.

Kim Lee, VP of Investor Relations, you may begin your conference.

Kim Lee — **Vice President, Investor Relations, Choice Properties Real Estate Investment Trust**

Thank you, Chris. Good morning, and welcome to the Choice Properties REIT Second Quarter 2017 Conference Call.

This call is also being webcast simultaneously on our website at choicereit.ca, where you will also find a copy of our Q2 summary information package that we will be referring to on this call.

I'm joined here this morning by John Morrison, President and Chief Executive Officer, and Bart Munn, Chief Financial Officer.

Before we begin today's call, I want to remind you that by discussing our financial and operating performance, and in responding to your questions, we may make forward-looking statements, including statements concerning Choice Properties' objectives, its strategies to achieve those objectives, as well as statements with respect to management's beliefs; plans; estimates; intentions; outlook; and similar statements concerning anticipated future events; results; circumstances; performance; or expectations that are not historical facts.

These statements are based on our current estimates and assumptions and are subject to risks and uncertainties that could cause our actual results to differ materially from the conclusions in these forward-looking statements.

Additional information on the material risks that could impact our actual results, and the estimates and assumptions we applied in making these statements, can be found in our 2016 annual report in Management's Discussion and Analysis related thereto, together with Choice Properties' Annual Information Form that are all available on our website and on SEDAR.

And now I'll turn it over to John.

John Morrison —
President & Chief Executive Officer, Choice Properties Real Estate Investment Trust

Thank you, Kim, and good morning, everyone. Thank you for joining our conference call this morning.

The second quarter of 2017 was another successful quarter for Choice Properties. We remain focused on adding value and delivering results. We continued to invest in our portfolio, constructed new retail space, and maintained our high occupancy rate.

Our business performed well, achieving year-over-year growth in key performance metrics, including a 5.2 percent increase in funds from operations per unit.

Now let me provide you with some of the highlights. Our investments in our portfolio during the second quarter resulted in the construction of 114,000 square feet of new retail space for 24 tenants on our sites in British Columbia, Alberta, Ontario, Quebec, and Prince Edward Island. This new GLA contributed to the completion of eight projects that delivered a weighted average yield of approximately 9 percent.

In addition, a third-party acquisition for 8.4 million was completed in Brooks, Alberta, which is our second Loblaw-anchored multi-tenant property acquired from a third party. Including this acquisition, we have acquired nearly 0.5 million square feet of gross leasable area for a total purchase price of approximately $100,000 million from third-party vendors.

For the remainder of the year, as we progress with ongoing projects and launch new projects, we expect to complete an incremental 66,000 square feet of new GLA to meet our 2017 projected completion target of 347,000 square feet of new GLA.

Projects expected to be complete in 2017 are expected to deliver yields ranging from 7 to 8 percent.

At the same time, we remain active in the market looking to acquire retail real estate that is well suited to our portfolio, and expect to complete acquisitions from our dedicated pipeline of Loblaw properties and from third-party vendors.

In addition to our large number of retail-intensification projects, we continue to make headway with predevelopment activity for our mixed-use redevelopment opportunities. This quarter we held our first public open house to connect with neighbouring communities and to understand local needs and aspirations for our 2280 Dundas Street West property located in Toronto's Bloor-Dundas mobility hub.

The open house was a success with attendance exceeding our expectations. The community feedback and input we gained at the event will serve to inform our concepts, plans, and programs for this site.

Turning to leasing activity, during the second quarter resulted in binding commitments for approximately 162,000 square feet of GLA. This includes approximately 33,000 square feet of renewals and 94,000 square feet of GLA we completed within our development program.

The average rent increase on renewals was 1.6 percent, including 21,000 square feet renewed at the same rent. Leases executed this quarter resulted in an average base rent of $23.90 per square foot on a same-store basis and $24.76 per square foot, including the higher rent from newly developed GLA.

With a stable portfolio primarily focused on non-discretionary and service-oriented retailers, we continued to maintain our total portfolio's high occupancy rate at 98.9 percent for the quarter.

And with that, I will turn the call over to Bart to provide you with a review of the financials for the quarter.

Bart Munn —
Chief Financial Officer, Choice Properties Real Estate Investment Trust

Thanks, John, and good morning, everyone. I refer you to Slide 8 of our presentation material, where you'll find selected financial results for the second quarter.

As of June 30, 2017, Choice Properties' portfolio comprised 537 properties with a total gross leasable area of 43.8 million square feet. Under IFRS, our investment properties were valued at approximately 9.2 billion based on a weighted average cap rate of 6.1 percent.

For the quarter, rental revenue was 208.6 million and net operating income was 144 million, 5.7 percent and 5.3 percent higher than in Q2 2016, respectively.

On a same-stores basis, NOI increased to 136.4 million, or by 1.2 percent from Q2 2016. This increase was primarily a result of revenue from capital recoveries, rent steps in Loblaw leases, and higher average rents on new ancillary leases.

Adjusted general and administrative expenses for the quarter were 5.2 million compared to 5.8 million for the comparative period in 2016. Adjusted G&A excludes mark-to-market of unit-based compensation, related party property management fees, and internal expenses for leasing. The ratio of G&A expense to total revenue was 2.5 percent. For the balance of the year, we expect our G&A run rate to be within this range.

Funds from operations for the quarter were 108.4 million, or $0.262 per diluted unit compared to $102.3 million, or $0.249 per diluted unit in Q2 2016. The 5.9 percent year-over-year growth in FFO per unit was largely due to higher net property income and lower G&A expenses, partially offset by increases in interest and other financing charges.

With respect to cash flows, our adjusted cash flow from operations, ACFO, was 87.8 million compared to 80.1 million last year. With total distributions declared of 75.3 million for Q2, our payout ratio for the quarter was 85.4 percent. This compares to 85.5 percent for Q2 2016.

While ACFO can vary across quarters due to timing of operational cash flows, we expect our annual ACFO payout ratio to be in the 85 percent range.

Our debt service coverage ratio of 3.6 times remains unchanged, and our weighted average term to maturity on our senior unsecured debentures is five years. We currently have approximately 242 million of available liquidity, including undrawn operating lines of 234 million.

Let me now turn it over to John to provide his closing remarks.

John Morrison

Thanks, Bart. Q2 results reflect the stability and consistency of our business, as well as its potential for incremental growth. With the benefit of a strong core business, we remain focused on execution to our key growth drivers to continue to build momentum and create value for all our stakeholders.

Looking ahead, we expect to continue to capitalize on our pipeline of growth opportunities, particularly with respect to development and mixed-use redevelopment. The entire Choice team is fully engaged and committed to delivering results, and I'd like to take this opportunity to thank them for their efforts and congratulate them on another successful quarter.

And now, Operator, we would be pleased to take questions.

Q&A

Operator

At this time, I would like to remind everyone in order to ask a question, press *, then the number

1 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 Sam Damiani of TD Securities. Your line is open.

Sam Damiani — TD Securities

Thank you, and good morning.

John Morrison

Morning.

Sam Damiani

John, just on the acquisitions from Loblaw, we've seen the pace of those slow a bit over the last year or two, and the last sort of material acquisition over $100 million was over a year ago. Just wondering if we should sort of take this as a new kind of level of frequency? Or if you see something large happening in the near or medium term?

John Morrison

It’s a good question, Sam. So we have not completed an acquisition with Loblaw yet, but we are working on one. We expect them to be—and I think we’ve communicated this in the past—we expect them to be smaller in nature in terms of the dollar investment. So you should be thinking about a range of 100 to 150.

And it really is a result of the fact that we’ve taken down quite a bit of the portfolio. There’s still obviously properties left, but we are getting into what I describe as the back half of the program.

Sam Damiani

Okay. Thank you for that. And just switching over to the development side, you mentioned 2280 Dundas. I wonder if you could just give us—I know it’s very, very preliminary—but how you think this site might be developed, either in a similar or different way than the Golden Mile plan that’s largely been finalized?

John Morrison

I think the one similarity, Sam, would be it’s what we call—and it’s a common real estate term—it’s a transit-oriented development site. So it’s what we call a TOD. And this one is a heavier transit-oriented site, given that there’s the GO Transit station, the Union Pearson Express, the Dundas Subway, and of course there’s buses as well, so. And then you look at Golden Mile and it will have—it has buses, but it’ll have the LRT with two stops at that site. So from a transit point of view it’s different. And the Golden Mile site is much larger, and the demographics in that area are different as well in terms of the type of retail and the type of housing.

So for example, Golden Mile will have a No Frills as an anchor whereas Dundas and Bloor will have a full-line Loblaws as an anchor. So you can see the difference in terms of the merchandising strategy. And I expect that the—or we expect that the rental rates for residential units will be different as well.

Sam Damiani

So you’re envisioning more rental versus condo at this site as you do at the Golden Mile?

John Morrison

Well, we haven't landed on the combination of rental versus condo for either site. Our preference is rental for both sites, but we haven't sort of determined how much of each for either of the sites at this point.

Sam Damiani

Okay. And what's the next step on the 2280 site in terms of another public—

John Morrison

Well, the next step is—yeah. We held a community event back in the middle of June which was very successful. We determined that there was an opportunity to reach out to the community to get their input in terms of what they'd like to see in terms of us building this new area within their neighbourhood.

And so we're taking their feedback, and we're virtually in the design stage right now in terms of mapping it all out and positioning the various components of it. So we're looking to have that available this fall where we'd actually go back to the community and share our thoughts with them.

At the same time, we work with the city. We're working with the city with our plans and thinking at the same time.

Sam Damiani

Okay. Great. Thank you very much.

John Morrison

You're welcome.

Operator

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

Sumayya Hussain — CIBC

Thank you. Morning.

John Morrison

Good morning.

Bart Munn

Good morning.

Sumayya Hussain

So last quarter you guys mentioned a mixed-use development upcoming in Ottawa. Any updates since that? Have you brought in partners? Or just any other update on that or other preliminary developments?

John Morrison

Yeah. We have progressed quite well on that particular project. We have settled with a partner. We're not in a position to announce it yet because we haven't finalized the documentation, but we're pretty confident that there's going to be something that we're going to be announcing very soon.

Sumayya Hussain

And it'll be a combination of retail and rental?

John Morrison

This'll be a residential building because the retail already exists.

Sumayya Hussain

Okay. But no quantification on the number of units at this point?

John Morrison

It'll be part of our announcement.

Sumayya Hussain

Okay. Thanks. And it was just a really small piece, but on the 21,000 that you renewed at in-place rents, any more colour on what happened there?

John Morrison

Not really. It was just the tenant was at a market rent, and we just renewed the tenant at the existing rent because they were currently at a market rent. So there was no opportunity to increase the rent.

Sumayya Hussain

Okay. And which market was this?

John Morrison

I don't recall. Sorry.

Sumayya Hussain

Okay. That's fine. That's it for me. Thanks.

John Morrison

Sorry, let me just add some comment on that. It wasn't one tenant. It was four tenants, and they were in smaller markets; Truro, Nova Scotia, for example. One was in Kingston.

Operator

Your next question comes from the line of Pammi Bir of Scotia Capital. Your line is open.

Pammi Bir — Scotia Capital

Thanks. Good morning. You've done a few third-party deals now, so just curious as to whether there's additional opportunities from that perspective as, I guess, the pipeline from Loblaw starts to slow down a bit? And then if you could comment on whether you've seen any shift in cap rates yet in the grocery-anchored space?

John Morrison

So from the very beginning, Pammi, we've been looking outside the internal acquisition opportunities that we have with Loblaw. We've been doing that since day one. I think one of the distinct advantages that we have—I don't think—we do have and we've communicated this is when we see a property coming to the market that we think that we can add value to and there is, for example, a Loblaw-tenanted—or Loblaw-owned tenant on the site, be it Loblaws or Shoppers Drug Mart, then we have the ability to obviously speak to the tenant in terms of their future plans or performance and what have you, and make some assumptions in terms of where rental rates can be adjusted going forward. And that's really because of the relationship that we have.

So that gives us an advantage. And so we're able to look at more of these types of sites in additional to other opportunities that we might see.

So to answer your question, we will continue to look for these opportunities because we view them as both strategic and value-add for us.

Pammi Bir

And then I guess from a cap rate standpoint this last year—

John Morrison

Oh, yeah, sorry.

Pammi Bir

Yeah. Just—

John Morrison

No, we haven't really seen any change in cap rate for grocery-anchored. They're an asset class that is still in very high demand from both investors such as ourselves, I would say some smaller institutional investors, and private investors for sure.

Pammi Bir

Okay. Maybe just turning to developments for a second, the 110 million that you expect to, I guess, complete this year in terms of costs or the capital spend for the 2017 projects. How much of that has been completed to date in terms of you've given the square footage number? I just wanted to confirm, I think I saw in the supplemental something close to 20 million. Is that about right, or?

John Morrison

We're just going to check, if you don't mind. Yeah. That's about right, Pammi.

Pammi Bir

Okay. So call it another 80 million, 90 million left to go for the balance of the year?

John Morrison

Rough, rough. Yeah.

Pammi Bir

Yeah. Okay. And then just lastly turning to, I guess, Golden Mile. Any update here with respect to the potential size of that investment? There's I guess certainly some information available on the potential density. But can you provide maybe an update on that process and what—

John Morrison

Not at this point, Pammi. We're not finalized on the total investment yet.

Pammi Bir

Okay. And then just maybe looking, I guess, going back to the Dundas Street project. What sort of time line here are we looking at in terms of when you think—and I know it's early and you're working on the plans—but is this perhaps something that is at least probably five years down the road, or?

John Morrison

I would—yeah, three plus. I mean these projects that we're doing—and I think the thing that everybody needs to understand is these will be phased projects. They have to be phased projects because we have to build new before we can demolish old. And so depending on the number of components that we need to build new for and then demolish old it's going to take a little bit longer, but we're trying to move them obviously as quickly as we can. And we're expecting that Golden Mile we'll be into the ground on that project before we're into the ground on Dundas and Bloor.

Pammi Bir

Okay. That's helpful. Maybe just one last sort of high-level one; any thoughts with respect to the Amazon–Whole Foods transaction and just curious what your views are here with respect to the grocery-anchored space and perhaps, I guess, some implications for Loblaw?

John Morrison

Well, obviously it was big news when it came out. It's certainly on everyone's mind. My personal reaction was it's another online retailer buying bricks-and-mortar, which we've seen a lot of that happening in terms of these virtual retailers realizing they need a brick-and-mortar strategy.

I think when you look at the Whole Foods footprint, 400 stores, rough, rough, 13 in Canada, we don't expect that there's going to be a tremendous effect in the near term on the grocery business in Canada.

But at the same time, I would offer that—and I can only speak for Loblaw—but they're very advanced in terms of their thinking around technology. Click & Collect continues to grow in terms of the number of locations and other technological advances that they're working on as a retailer.

So it's not—nobody knows what Amazon's plan is. And so we'll—but I think we feel comfortable that our main tenant is in a very good position for the future.

Pammi Bir

I guess just as an extension, do you view I guess the Canadian grocery-anchored landscape as perhaps more insulated relative to the US or not?

John Morrison

Well, I think it's—yeah. I think I would say that because there's more competition in the United States, more price competition in the United States than there is in Canada. I mean, not to say that Canada isn't competitive, but it's definitely a different—I mean there's a lot more Walmarts down there. There's a lot—Kroger is a big player, and there's a lot more regional players in the United States than you see in Canada.

Pammi Bir

Great. Thanks very much.

Operator

And there are no further questions at this time. I now turn the call back to John Morrison, President and CEO.

John Morrison

Thank you, Chris. And thank you all for joining our conference call today, and we look forward to speaking with you next quarter.

Have a great day.

Operator

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