**FINAL TRANSCRIPT**

# Choice Properties Real Estate Investment Trust
## First Quarter Results Conference Call

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## CONFERENCE CALL PARTICIPANTS

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**Troy MacLean**
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**Alex Avery**
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**Matt Logan**
*RBC Capital Markets — Analyst*

**Michael Markidis**
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## PRESENTATION

**Operator**

Good morning. My name is Anastasia, 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 First 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 of Investor Relations, Choice Properties Real Estate Investment Trust

Thank you, Anastasia. Good morning, and welcome to the Choice Properties REIT First Quarter 2015 Conference Call. This call is also being webcast simultaneously on our website at choicereit.ca where you will also find a copy of our Q1 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, and intentions, 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 risk and uncertainty that could 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 apply in making these statements can be found in our 2015 first quarter report to unitholders and management's discussion and analysis related thereto together with our Annual Information Form that are all available on our website and on SEDAR.

I will now turn it over to John.

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

Thank you, Kim, and good morning, everyone, and thank you for joining our conference call. I'm going to start with an overview of the quarter and Bart Munn will follow with a presentation of the financials, and then after that we'll open it up for questions.
Our business performed well in the first quarter of 2015 as we further invested in our portfolio and enhanced our management reporting systems and our leasing, property accounting, and property management teams.

In the first quarter of 2015, we acquired additional land for development, completed the acquisition of a warehouse and a small shopping centre, and raised $250 million through the issuance of secured—sorry, senior unsecured debentures. Our financial results for the quarter reflect the continued strong performance of our REIT, with year-over-year growth in net operating income and funds from operations driven principally by acquisitions and improvements in ancillary leasing. Let me now provide you with more details of our investment and leasing activities for the first quarter of 2015. As we discussed on our last call, we acquired two parcels of land. The first site is a 16-acre parcel in Barrie, Ontario that we purchased from Loblaw for $9.6 million. We intend to co-develop the Barrie site with Penequity, who own the adjacent 21-acre site, whereby together we will construct an integrated retail centre spanning approximately 350,000 square feet. We have commenced construction on our portion for a new 60,000 square foot Zehrs grocery store and a 20,000 square foot Shoppers Drug Mart, which are expected to open by the end of this year with the additional ancillary GLA to be completed in 2016.

The second parcel we acquired this quarter is a 9-acre site in Kanata, Ontario, which we acquired as part of a 50/50 co-ownership agreement with Penequity for approximately $3.9 million, and our intention is to develop a grocery-anchored retail centre on this site.
As for income-producing properties, we completed the acquisition of a 921,000 square foot warehouse in Pickering, Ontario from Loblaw for a purchase price of $81.2 million, representing an accretive capitalization rate of 6.5 percent. We also closed on the acquisition of a small shopping centre totalling 55,000 square feet in Porters Lake, Nova Scotia from a third party for a purchase price of $5.2 million, representing an accretive capitalization rate of 9.5 percent based on in-place NOI of about $0.5 million. The shopping centre is anchored by a 47,000 square foot Loblaw grocery store on an adjacent Choice Properties-owned site. Upon closing on the purchase of this shopping centre, we combined the two adjacent properties into one for business and reporting purposes.
Our total property count to date stands at 475 spanning 39.9 million square feet and includes five parcels of land for development.

During the quarter, our development program continued to make progress. This year our plan is to invest approximately $160 million in development capital, and we expect to complete about 225,000 square feet of additional GLA with expected returns ranging from 7.5 to 9.5 percent.

Of these projects, we completed two of the smaller projects in Q1, the construction of an 11,000 square foot of new GLA for a retail tenant in Saint John, New Brunswick, and the construction of a new gas bar in Toronto at a property on Black Creek Drive. Together, these two projects yield 7.4 percent.

Other projects which we initiated during the quarter include Barrie, Ontario, which I mentioned earlier, where we have initiated the construction of the 60,000 square foot Zehrs and 20,000 square foot Shoppers Drug Mart that we expect to complete before year-end and the ancillary space will follow thereafter.

In Burlington, Ontario we continued ongoing predevelopment activity during the quarter and are on track to commence construction of a new retail GLA for ancillary tenants in the coming months. We expect to complete construction of approximately 30,000 square feet of new GLA by the second half of next year.

In Regina, Saskatchewan we have commenced construction for a Shoppers Drug Mart, which is scheduled to open this year, followed by additional retail GLA in the second half of next year. In total this project is expected to deliver approximately 60,000 square feet of new GLA.

In Edmonton, Alberta we have commenced site servicing in advance of construction of a Shoppers Drug Mart store, as well as retail GLA for ancillary tenants which are targeted for completion before year-end. This project is expected to deliver approximately 20,000 square feet of new GLA. And we have a second project in Edmonton, Alberta, where we have started construction of approximately 40,000 square feet of new GLA for ancillary tenants, and we expect the first tenant to take possession before year-end and the entire project to be complete in the first half of 2016.

At the same time, we continue to make progress with our ongoing development projects, including the construction of a new 125,000 square foot Real Canadian Superstore. This store, along with a Shoppers Drug Mart, will anchor our 250,000 square foot shopping centre development called Grandview Central in Surrey, British Columbia.

In addition, we have advanced construction for a 200,000 square foot expansion of our warehouse in Boucherville, Quebec, which is scheduled to be completed by the second half of 2016.

Leasing activity during the quarter resulted in almost 235,000 square feet of committed GLA, including approximately 34,000 square feet of renewals. We maintained our high occupancy rate during the quarter at 98.3 percent compared to 98.1 percent at the end of the fourth quarter of 2014.
And with that, I will turn the call over to Bart to provide you a review of the financials for the quarter.

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

Thanks, John, and good morning. I'd like to refer you to Slide 9 of our presentation material where you'll find selected financial results for the first quarter.

So as of March 31st, Choice Properties' portfolio comprised 475 properties with a total gross leasable area of 39.9 million square feet. Under IFRS, the REIT's investment properties were valued at 8 billion based on a weighted average cap rate of 6.19 percent, which is essentially unchanged from the year-end 2014.

For the quarter, rental revenue was 181.7 million and net operating income was 125.3 million, 8.8 percent and 8.6 percent higher than in Q1 2014, respectively. The increases were primarily due to acquisitions, which contributed 11.6 million in incremental revenue and 7.7 million in incremental NOI. Same property NOI increased 2.2 percent compared to the same period in 2014, driven by higher base rent and net recoveries as a result of improved leasing activity related to ancillary GLA and rental revenue from new GLA as a result of development.

General and administrative expenses for the quarter, excluding internal expenses for leasing, were 5.5 million, an increase of 2.9 percent compared to Q1 2014. This increase was largely due to higher internal expenses driven by the internalization of the property management functions, partially offset by recoverable operating expenses allocated to properties and a decrease in service agreement expenses as a result of functions that Choice Properties has assumed directly. While general and administrative expenses were higher year over year on an absolute basis, as a percentage of revenue G&A expenses were 3 percent for Q1 2015 compared to 3.2 in Q1 2014.

FFO for the quarter was 94.3 million, or $0.238 per unit, compared to the comparative period of 83.4 million, or $0.224, which excludes a noncash finance gain of 3.3 million. The improvement of FFO over the comparative period was largely due to NOI from acquisitions and improvement in ancillary leasing. AFFO for Q1 was 75.5 million, an increase of 6.8 million over the comparative period. AFFO per unit was $0.191 compared to $0.185 in Q1 2014.

As at March 31st, our debt metrics are stable with a debt to total assets ratio of 45.8 percent, which is well within our maximum threshold, a debt service coverage ratio of 3.5 times, and a debt to EBITDA ratio of 7.4 times. Our issuance of 250 million in senior unsecured debentures in February has improved our financial flexibility, lowered the weighted average coupon rate of our debt, and effectively mitigated refinancing risk in the near term. Combined with strong cash flow from operations and access to a $500 million senior unsecured credit facility, we have the financial capacity and flexibility to meet all ongoing obligations and successfully finance future growth.

So let me turn this back over to John for his closing remarks.

## John Morrison

Thanks, Bart. Choice Properties delivered a successful first quarter 2015. The quarter has set the stage for our 2015 initiatives, which includes additional acquisitions, new and progressing development projects, and enhanced leasing and property management activity.

For the balance of this year we will remain our focus on growth and continue to execute on enhancing the strength of our business to deliver solid operation and financial performance.

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

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# Q&A

## Operator

As a reminder, if you would like to ask a question, please press *, then the number 1 on your telephone keypad.

Your first question comes from Sam Damiani with TD Securities. Your line is open.

## Sam Damiani — TD Securities

Thanks. Good morning, everyone. Just on the—first of all, good quarter; nice to see the impact of the internalization flow through nicely into the financials. I guess just on that, do you see the impact on G&A continuing in a similar way throughout the balance of the year?

## Bart Munn

That's our projections right now, so we are basing it sort of on a 3 percent of revenue should be a good run rate for you.

## Sam Damiani

Okay. Great. And just looking at the acquisition pipeline with Loblaw, I mean what do you see kind of coming down the pike in the next little while?

## Bart Munn

On the acquisition side, Sam, we're continuing to move forward on our program. I would expect probably two vend-ins this year again similar to past pattern, one in sort of the first half and a second in the second half of 2015.

## Sam Damiani

Okay. And maybe just finally on the development pipeline. Is all of that 1.35 million square feet through 2017, is all that commercial space? Or is there any residential built into that?

**John Morrison**
It's primarily commercial, Sam. In fact, it's all commercial. We are looking at residential opportunities, but that square footage has not been factored into these numbers.

**Sam Damiani**
And apart from the projects that you've identified in detail over the next couple years, I mean are there any other large projects that are worth highlighting at this time built into those 2016 and 2017 completion targets?

**John Morrison**
Well, there are a number of projects that we haven't highlighted that we're obviously working on, but it's too early in the predevelopment stages to disclose which ones they are.

**Sam Damiani**
Okay. Thank you very much.

**Operator**
Your next question comes from Troy MacLean with BMO. Your line is open.

**Troy MacLean** — BMO
Good morning.

**Bart Munn**
Good morning.

**John Morrison**
Good morning.

**Troy MacLean**
How much of the ancillary GLA is pre-leased for the 2015 and 2016 developments?

**John Morrison**
Well, we don't actually—for the predevelopment or the development projects? Because there's a difference. We won't start construction or commit capital beyond predevelopment until we're roughly 70 or 75 percent pre-leased, so you can assume that if we're starting construction on a certain aspect of a project that it's been pre-leased, and our target is as I described.

**Troy MacLean**
The REIT has four Shoppers under construction with three expected to be completed this year. Is that kind of a good run rate for Shoppers Drug Mart development within the portfolio over the next couple years? Or could that grow over time?

**John Morrison**
I wouldn't say it would be a run rate, Troy. These are what we all would describe as near-term opportunities that we're taking advantage of I think both from Shoppers' perspective and ours. And we'll see how this program continues to unfold, but I wouldn't exactly call it an annual run rate.

**Troy MacLean**
Yeah. And then just on the 90,000 square feet of retail space that got converted to Loblaw storage in Q1…

**John Morrison**
Yeah.

**Troy MacLean**
Was that formerly Loblaw space? Or did it belong to another retailer?

**John Morrison**
It belonged to another retailer. It was space that we actually took off the market for future re-development purposes, and we were able to lease it to Loblaw on a short-term basis.

**Troy MacLean**
And then what are the development plans for that space?

**John Morrison**
This would be an urban mixed use site, which again as I was just mentioning earlier we're in preplanning, predevelopment conceptual stages on. So it's too early to give further details because likely the concept will continue to evolve as we work through it, so in the meantime Loblaws will occupy this space.

**Troy MacLean**
Perfect. Thank you. I'll turn it back.

**Operator**
Your next question comes from Alex Avery with CIBC. Your line is open.

**Alex Avery** — CIBC
Thank you. I was just wondering if there were going any opportunities for Choice related to any of the Target leases or any of the activity that's going on there.

**John Morrison**
We've taken a look at the Target portfolio, Alex, and for us it's not something that's a fit in terms of our portfolio where we want to hold real estate. So it's not something that we're going to pursue.

**Alex Avery**
And then I guess along the same lines, the existing Shoppers portfolio largely not owned. Safe to assume that you guys have looked through that and there's nothing of interest for the REIT at this point?

**John Morrison**
That's true.

**Alex Avery**
Okay. That's great. Thank you.

**Operator**
Your next question comes from Pammi Bir with Scotia Capital. Your line is open.

**Pammi Bir** — Scotia Capital
Thanks. Just going back to the expected vend-ins, I guess, from Loblaw over the course of the rest of the year. What are your thoughts with respect to the mix between debt and equity in terms of funding those, just given you've used—or the Class B units, sorry, have been used a bit more heavily in the past couple of transactions?

**Bart Munn**
Yeah. Pammi, I think for the transactions that are coming down the pipe this year, obviously we don't have a solid number yet because it's going to depend on sort of fair values of the individual properties, but I think we'd probably be on sort of the lower side. So I would say if you use a 50 percent debt to equity you would probably have a pretty good estimate.

**Pammi Bir**
Okay. And then just on the—just looking at the distribution for a moment. The payout ratio certainly looks like it's in fairly good shape. Can you give us an update in terms of where perhaps the Board's thoughts are with respect to a possible increase in the distribution? Can you also remind us just what your target payout ratio is?

**Bart Munn**
Yeah. So yeah, it certainly has moved down. As you recall, a year and a half ago we started—we had just around 90 percent. We're now sitting at sort of 85, 86. The one thing that we always should have been focused on is the debt renewal in 2016 because that can have a big impact on our sustainability of distributions. So as we work through that we will certainly be looking very closely at where our payout ratio sits and where we want it to sort of range between.

I would say right now at 85 percent it's probably sort of on a bit on the low side, so I could see once we nail down the '16 financing that there could be opportunity to increase the distribution.

**Pammi Bir**
And then sorry, where are you in terms of looking at that 2016 maturity in terms of what sort of duration would you put on that? Any thoughts there?

**Bart Munn**
Yeah. My thinking would be to refinance that. Most likely it would be 10-year money. If we changed from that it wouldn't be much less than—it'd probably range between 8 and 10 years. And that's just because we're looking at our debt maturity profile, and that's where that piece of paper would most appropriately fall. And we'd like to capitalize on the rates in the marketplace right now.

**Pammi Bir**
And in terms of the timing on that, when you might have a better sense of…

**Bart Munn**
Well, we know we've got to do it within the next twelve months.

**Pammi Bir**
Yeah.

**Bart Munn**
As far as the exact timing, we'll just be opportunistic based on what's happening in the marketplace.

**Pammi Bir**
Okay. All right. Thank you.

**Bart Munn**
Okay

**Operator**
Your next question comes from Matt Logan with RBC Capital Markets. Your line is open.

**Matt Logan** — RBC Capital Markets
Good morning. Just wondering if I could as you a couple quick questions here?

**Bart Munn**
Sure.

**Matt Logan**
Looking at your capitalized borrowing costs and interest income, just noticed that that ticked up during the quarter, and wondering if you could provide some additional colour?

**Bart Munn**
Yeah. It's just as our development program is stepping up.

**Matt Logan**
Mm-hmm.

**Bart Munn**
Where then we've got a bigger base and we're able to capitalize a greater portion of our unsecured debt to the projects.

**Matt Logan**
Okay. And your interest income is likely to be recurring?

**Bart Munn**
Yes. We've done a couple of mezzanine loans that are now on our books, so that interest income will continue.

**Matt Logan**
Excellent. Thank you.

**Operator**
Your next question comes from Sam Damiani with TD Securities. Your line is open.

**Sam Damiani**
Thanks. Just on the development completions through 2017. You've provided the cost to complete; you've provided the sort of total annual development spend. Would you also be able to tell us the total cost of the completions in each year?

**John Morrison**
Yeah. Just bear with us here, Sam. Yeah. It's actually outlined in the MD&A. So if you look at 2016, we're talking about 785,000 square feet of GLA that the total cost to complete is 228 million, '17 is 120 million, and then that totals just over 400 million for this year and the next two years.

**Sam Damiani**
Okay. I just wasn't sure how much money had already been spent on those projects certainly for 2015.

**John Morrison**
Yeah...

**Sam Damiani**
Just looking at the sort of total cost all in start to finish.

**John Morrison**
Right. We've highlighted certainly how much we spent in Q1, but we don't have that information in front of us in terms of…

**Bart Munn**
Well, yeah, Sam, if you go—if you're looking at that section just go down into the note just below it. You'll see we've got a commitment of the current year of 18 million at this point.

**Sam Damiani**
Okay.

**Bart Munn**
So those are binding commitments and obligations to the REIT. And the other ones are so far out in the future that we've yet to have commitments on those.

**Sam Damiani**
Okay.

**Bart Munn**
If you're talking about commitments of capital dollars versus commitments of leasing or anything.

**Sam Damiani**
Right. I mean maybe perhaps just as an example what would be the total all-in cost for Surrey and maybe Boucherville, what would those two larger projects represent?

**Bart Munn**
Well, we haven't disclosed them on individual. But I think what you need to do is so in '15 you take your 62 million and then you can determine the return on that 62 million based on the range we show you below. We haven't disclosed individual costs and returns by project at this point because we are continuing to—they continually evolve, there continues to be leasing, and the numbers will change.

**Sam Damiani**
But the returns of 7.5 to 9.5 percent that's on the total cost, not just the cost to complete?

**Bart Munn**
It's on the 62 million that will be completed in the current year.

**Sam Damiani**
Sorry. The 62 is just the portion remaining?

**Bart Munn**
No. The 62 is what's being spent on projects that are going to be completed in the current year.

**Sam Damiani**
Okay. That's fine.

**Bart Munn**
If you want to give me a call, Sam, we can go into it in more detail, but the way we're showing it here is the 62 million is the cost, the total cost, not within the year, but the total cost of projects that are going to come on stream in 2015. And then the spread there, the 7.5 to 9.5, is the range of the returns for those projects that are going to come on stream and then the 158, which we show there, is the total development dollars that will be spent during 2015, but will be on these, plus other projects that are ramping up.

**Sam Damiani**
Understood, understood. And just curious about those Shoppers Drug Mart leases; were those relocations for Shoppers in those markets? Or where they increased store count in those markets?

**John Morrison**
One is a relocate; the others are new locations.

**Sam Damiani**
Which city was the relocate, if you don't mind my asking?

**John Morrison**
Barrie.

**Sam Damiani**
Barrie. Thank you.

**Operator**
Your next question comes from Michael Markidis with Desjardins. Your line is open.

**Michael Markidis** — Desjardins
Thanks, and good morning. Just two quick ones for me, first with respect to potential vend-ins from LCL. You've given some good colour on expected timing and quantum, but how should we be thinking of the mix of property and perhaps the unlevered yield going in on the—given the geographies of the assets that are being contemplated?

**Michael Markidis**
Would it be similar or lower?

**Bart Munn**
I would think the mix is similar to what we've moved into the portfolio previously. We may be seeing a little more smaller market.
And as far as the cap rate goes, I would say in the past we've been kind of doing it in the 6.5 range, sort of give or take a dime there. I think it's going to be north of that, but I can't really say how high—how far off of that until I know the exact properties that are actually coming in because each market will dictate the individual cap rate for that property.

**Michael Markidis**
Sure.

**Bart Munn**
But I would say it's fair to assume it's 6.5 to—north of 6.5. I just can't say how much differently.

**Michael Markidis**
Okay. And can you remind me, are fair value appraisals done on these vend-ins when they're done? Or are they relied on from the time of the IPO prospectus?

**Bart Munn**
No. There are fair value appraisals done on all vend-ins at the time that we are negotiating with Loblaw.

**Michael Markidis**
Okay. That's what I thought. And then just moving over, some question was asked about the distribution. You mentioned the 2016 maturity, which carries a pretty low rate. Does the 2017 development maturity factor into that analysis as well, given that it's a similar interest rate? Or is it not really a factor for you in determining what the recommendation for distribution might be?

**Bart Munn**
We consider it, but I would say that by the time we get to '17 you've see our ramp-up on our development side.

**Michael Markidis**
Yeah.

**Bart Munn**
And sort of we now have two things happening that are picking up. We have the increase of same store rents as a result of just how our increases flow over the five-year period up to 1.5 percent on same store. So we're into then our third/fourth year.
And then also the development, the contributions from the development program will offset any sort of downside of higher interest costs. So it is considered, but I would say less of an issue than say the '16.

**Michael Markidis**
Okay. And I don't know if you gave this piece before, but I think the question was asked what the target payout ratio was and I think I missed it if you gave it, or if you didn't mention it.

**Bart Munn**
Well, the target ratio is sort of—we've sort of said it's in sort of 85 to 90. We are reviewing that to see if maybe we should move it down. The industry as a whole seems to be looking to sort of have lower payout ratios, but that being said, we would still see potential for dividend increases, even if we were moving our payout ratios down slightly.

**Michael Markidis**
Okay. And granted that the market's been fairly choppy on the rate side and the unsecured markets—maybe I don't want to say closed—but pricing seems to be moving in the opposite direction of where people would like. Can you give us a sense where 8 to 10 money might be for you guys with the recent quotes you've gotten?

**Bart Munn**
I would say let's say 10 just because it's an easier comparative. The 10s have probably ranged in the last six weeks because, as you say, it's been very volatile between somewheres around 330 to 350.

**Michael Markidis**
Okay. That's great. Thanks very much.

**Bart Munn**
Okay.

**Operator**
As a reminder, if you would like to ask a question, please press *, then the number 1 on your telephone keypad.
There are no further questions at this time. I turn the call back over to the presenters.

## John Morrison

Thank you, Operator, and thank all of you for joining us on our conference call today. Our Annual Meeting of Unitholders is being held actually today at St. Andrew's Club & Conference Centre here in Toronto, and it scheduled to start shortly at 11:00 a.m.
We hope to see you there, and if we don't we look forward to speaking with you at our next conference call for Q2.

## Operator

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