



**EDGEFRONT REAL ESTATE INVESTMENT TRUST**

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**For the three and six months ended June 30, 2014**

**August 20, 2014**

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management's discussion and analysis ("MD&A") of Edgefront Real Estate Investment Trust ("the REIT") for the three and six months ended June 30, 2014 should be read in conjunction with the REIT's audited financial statements for the year ended December 31, 2013 and the unaudited condensed consolidated interim financial statements for the three and six months ended June 30, 2014. The information contained in this MD&A reflects events up to August 20, 2014, the date on which this MD&A was approved by the REIT's Board of Trustees. Financial data included in this MD&A is presented in Canadian dollars, which is the functional currency of the REIT, and has been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Additional information about the REIT can be accessed at [www.sedar.com](http://www.sedar.com).

## FORWARD LOOKING STATEMENTS

Certain statements contained in this MD&A constitute forward-looking statements which reflect the REIT's current expectations and projections about future results. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "expects" or "does not expect", "is expected", "estimates", "intends", "anticipates" or "does not anticipate", or "believes", or variations of such words and phrases or state that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the REIT to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements contained in this MD&A. Such forward-looking statements are based on a number of assumptions that may prove to be incorrect.

While the REIT anticipates that subsequent events and developments may cause its views to change, the REIT specifically disclaims any obligation to update these forward-looking statements except as required by applicable law. These forward-looking statements should not be relied upon as representing the REIT's views as of any date subsequent to the date of this MD&A. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. The factors identified above are not intended to represent a complete list of the factors that could affect the REIT.

## NON-IFRS FINANCIAL MEASURES

Net operating income ("NOI") is a measure of operating performance based on income generated from the properties of the REIT. Management considers this non-IFRS measure to be an important measure of the REIT's operating performance. Funds from operations ("FFO") is a measure of operating performance based on the funds generated from the business of the REIT before reinvestment or provision for other capital needs. Management considers this non-IFRS measure to be an important measure of the REIT's operating performance. Management considers adjusted funds from operations ("AFFO"), a non-IFRS measure, to be an important performance measure to determine the sustainability of future distributions paid to holders of Units after provision for maintenance capital expenditures. Gross Book Value is defined in the Declaration of Trust and is a measure of the value of the REIT's assets. Management considers this non-IFRS measure to be an important measure of the REIT's asset base and financial position. Indebtedness to Gross Book Value is a compliance measure in the Declaration of Trust and establishes the limit for financial leverage of the REIT. Total Debt to Gross Book Value Ratio is considered to be an important measure of the REIT's financial position.

NOI, FFO and AFFO are not measures defined by IFRS, do not have standardized meanings prescribed by IFRS and should not be construed as alternatives to net income/loss, cash flow from operating activities or other measures of financial performance calculated in accordance with IFRS. NOI, FFO and AFFO as computed by the REIT may differ from similar measures as reported by other trusts or companies in similar or different industries.

NOI is used by industry analysts, investors and management to measure operating performance of Canadian real estate investment trusts. NOI represents rental revenue from properties less property operating expenses as presented in the statements of income prepared in accordance with IFRS. Accordingly, NOI excludes certain expenses included in the determination of net income such as general and administrative expense, unit-based compensation expense, fair value adjustments, interest income and expense and distributions on Class B LP Units.

The REIT calculates FFO in accordance with the whitepaper issued by the Real Property Association of Canada. FFO is defined as net earnings in accordance with IFRS, excluding fair value adjustments on investment properties and fair value adjustments and other effects of redeemable units classified as liabilities and the Class B LP Units, if any.

AFFO is defined as FFO subject to certain adjustments, including: amortization of deferred financing and leasing costs, compensation expense related to deferred unit incentive plans, trustee and asset management fees contractually settled in units, differences resulting from recognizing ground lease payments on a straight-line basis, and reserves for normalized maintenance capital expenditures, tenant incentives and leasing costs, as determined by the Trustees. Other adjustments may be made to AFFO as determined by the Trustees in their discretion.

The diluted weighted average number of units used to calculate diluted AFO per unit and diluted AFFO per unit reflects conversion of all dilutive potential units, represented by unit options, assuming that unit options are exercised with the assumed proceeds (comprised of exercise price and any related unrecognized compensation cost) used to purchase units at the average market price during the period.

AFFO payout ratio is calculated as total distributions declared during the period (including distributions declared on Class B LP Units) divided by AFFO.

## **BUSINESS OVERVIEW AND STRATEGY**

Edgefront Real Estate Investment Trust (the “REIT”) is the successor to Edgefront Realty Corp. (the “Corporation”) following the conversion of the Corporation to a real estate investment trust. The Corporation was incorporated under the Business Corporation Act (Ontario) on July 30, 2012. On January 6, 2014, shareholders of the Corporation voted to approve a plan of arrangement (the “Arrangement”) providing for the conversion of the Corporation into the REIT. The Arrangement became effective January 13, 2014. Further details of the Arrangement are contained in the information circular dated December 5, 2013 which can be found at [www.sedar.com](http://www.sedar.com).

On January 14, 2014, the REIT acquired RW Real Estate Holdings Limited Partnership (“RW LP”), 17367366 Alberta Limited, which is the general partner of RW LP, and 1781339 Alberta Limited, which was the sole limited partner of RW LP immediately preceding the purchase of these entities by the REIT. Following the acquisition of these entities by the REIT, the REIT is the sole limited partner of RW LP.

The REIT was established under the laws of Ontario pursuant to its declaration of trust, as amended and restated effective April 28, 2014.

The REIT owns and operates commercial real estate properties in Western Canada and Atlantic Canada, with a primary focus on industrial properties.

The strategy of the REIT is to grow by acquiring industrial commercial real estate assets in Western Canada, and other jurisdictions, potentially including the United States, where opportunities exist to purchase assets on terms such that the acquisitions are expected to be accretive, on a per unit basis, to the earnings of the REIT. The REIT will seek to identify potential acquisitions using investment criteria that focus on the security of cash flow, potential for capital appreciation, and potential for increasing value through more efficient management of the assets being acquired.

The REIT has formed a strategic partnership with TriWest Capital Partners (“TriWest”), one of Canada’s leading private equity firms. Through its relationship with TriWest the REIT has access to a pipeline of properties owned by TriWest’s current and former portfolio companies as well as the properties of many of the companies that TriWest meets with. The REIT may have the opportunity to acquire these properties through sale-and-leaseback transactions with strong tenants and long-term leases. The REIT views this non-marketed pipeline of potential acquisition properties as a key differentiator for the REIT, particularly as the REIT plans to gain considerable scale in its current phase of growth.

## **ACQUISITIONS**

On January 14, 2014, the REIT acquired 10 industrial properties located in Western Canada (the “RTL Westcan Properties”). The purchase price for the RTL Westcan Properties was \$68,000,000, of which \$34,000,000 was satisfied through the issuance of 17,000,000 REIT units to the vendor, with the remainder settled primarily in cash generated through new financing secured against the RTL Westcan Properties.

The acquisition is considered a reverse take-over under securities regulations due to the vendors receiving units totaling more than 50 percent of the outstanding units of the REIT as consideration for the acquisition of the properties. For accounting purposes, the acquisition has been accounted for as an asset acquisition, and IFRS 2 has been applied in accounting for the units issued in connection with the acquisition.

In the context of a reverse takeover, the REIT concluded that it is the accounting acquirer, as it is the entity whose former management dominates the combined entity. Furthermore, the composition of the REIT's board, in conjunction with the REIT's nominating agreement, allow the REIT to nominate the majority of the members of the governing body of the combined entity, and the vendor is required to support the REIT's nominees.

On March 8, 2013, the Corporation acquired the rights in a 66 year ground lease to a property located at 695 University Avenue, Charlottetown, Prince Edward Island (the "QT Property"). The purchase was approved by the TSX Venture Exchange as the Corporation's qualifying transaction as defined in Policy 2.4 "Capital Pool Companies" of the TSX Venture Exchange Policies. The ground lease commenced May 1, 2006, and has two ten year options to renew. The property contains a building with approximately 4,500 square feet of gross leasable area, and is leased to a schedule I Canadian chartered bank. Prior to the acquisition of this property, the REIT did not have any commercial operations.

On May 1, 2013, the Corporation acquired an office property located in Miramichi, New Brunswick (the "Miramichi Property"), for a purchase price of \$5,465,000. New mortgage financing with a ten year term, a 12 year amortization period, and bearing interest at a rate of 3.74% was arranged for the property by the Corporation. The property is comprised of a two-story office building constructed in 2012 with approximately 29,000 square feet of leasable area.

### REIT PROPERTIES AS AT JUNE 30, 2014

Property Address	Property Use	Year Built and/or Renovated	Rentable Area (Square Feet)	Occupancy	Lease Expiry Year
<i>Western Canada</i>					
12104 & 12110 - 17 <sup>th</sup> Street, NE, Edmonton, AB	Truck Maintenance Facility and Headquarters	1973, 1980, 1991 & 2011	116,582	100%	Nov. 15, 2025
3780 & 4020 - 76 <sup>th</sup> Avenue, SE, Calgary, AB	Truck Maintenance Facility	1973, 1975 & 1990	58,937	100%	Nov. 15, 2025
14801 - 97 <sup>th</sup> Street, Grande Prairie, AB	Truck Loading and Warehouse Facility	1988	42,120	100%	Nov. 15, 2025
5406 - 59 <sup>th</sup> Avenue, Lloydminster, AB	Truck Maintenance Facility	1972, 1980 & 1995	12,425	100%	Nov. 15, 2025
110 - 71 <sup>st</sup> Street, Saskatoon, SK	Truck Maintenance Facility and Warehouse	1984	74,796	100%	Nov. 15, 2025
15 Peters Avenue, Saskatoon, SK	Warehouse Facility	1985	38,160	100%	Nov. 15, 2025
850 Manitoba Street E & 15 - 9 <sup>th</sup> Avenue, NE, Moose Jaw, SK	Truck Maintenance and Storage Facility	1983	18,800	100%	Nov. 15, 2025
965 McMaster Way, Kamloops, BC	Truck Maintenance Facility	2007	13,706	100%	Nov. 15, 2025
49 Kam Lake Road, Yellowknife, NWT	Cement Facility	1978	7,674	100%	Nov. 15, 2025
348-352 Old Airport Road, Yellowknife, NWT	Truck Maintenance Facility	Office: 1997 Other: 1977-1990	53,212	100%	Nov. 15, 2025
<i>Eastern Canada</i>					
695 University Avenue, Charlottetown, PEI	Retail	2006	4,500	100%	June 30, 2016
139 Douglastown Boulevard, Miramichi, NB	Office	2012	<u>28,950</u>	100%	Oct. 1, 2022
<b>Total</b>			<b><u>469,862</u></b>		

## SUMMARY OF RESULTS

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
<b>Financial Highlights</b>	\$	\$	\$	\$
Funds from operations (FFO) (1)	839,761	(557,710)	1,477,455	(570,214)
Adjusted funds from operations (AFFO) (1)	1,007,831	(585,574)	1,793,471	(569,593)
Distributions declared (2)	792,763	-	1,465,846	-
Weighted average units outstanding – basic (3)	19,810,711	2,750,000	18,559,549	2,750,000
Weighted average units outstanding – diluted (3)	19,827,219	2,750,000	18,559,549	2,750,000
Distributions per unit (2) (3) (4)	0.040	N/A	0.079	N/A
FFO per unit (1) (3)				
Basic	0.042	(0.203)	0.080	(0.207)
Diluted	0.042	(0.203)	0.080	(0.207)
AFFO per unit (1) (3)				
Basic	0.051	(0.213)	0.097	(0.207)
Diluted	0.051	(0.213)	0.097	(0.207)
AFFO payout ratio (1) (2)	78.7%	N/A	81.7%	N/A
Debt to total assets ratio	46.6%	38.7%	46.6%	38.7%

(1) See Non-IFRS Measures

(2) Includes distributions payable to holders of Class B LP Units which are accounted for as interest expense in the unaudited condensed consolidated interim financial statements.

(3) Weighted average number of units includes the Class B LP Units and for June 30, 2013 has been adjusted to reflect the 20 for 1 exchange of shares of the Corporation for units of the REIT in connection with the plan of arrangement completed January 13, 2014.

(4) On February 4, 2014, the REIT announced its initial distribution relating to the period from January 14, 2014 to January 31, 2014, which was paid on February 28, 2014.

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
<b>Financial Results</b>	\$	\$	\$	\$
Rental income	1,771,095	164,223	3,299,566	174,721
Operating expenses	<u>(310,371)</u>	<u>(89,464)</u>	<u>(574,403)</u>	<u>(94,105)</u>
Net operating income	1,460,724	74,759	2,725,163	80,616
General and administrative expenses	(246,770)	(391,167)	(508,868)	(419,098)
Transaction costs	-	(221,667)	-	(221,667)
Fair value adjustment of investment properties	-	468,463	(915,346)	438,900
Fair value adjustment of class B LP units	(93,600)	-	(93,600)	-
Fair value adjustment of unit options	<u>(32,000)</u>	<u>-</u>	<u>(31,000)</u>	<u>-</u>
Income (loss) before Finance income (expense)	1,088,354	(69,612)	1,176,349	(121,249)
Net interest expense	(374,193)	(19,635)	(738,840)	(10,065)
Distributions on Class B LP Units	<u>(14,396)</u>	<u>-</u>	<u>(26,665)</u>	<u>-</u>
Net income	<u>699,765</u>	<u>(89,247)</u>	<u>410,844</u>	<u>(131,314)</u>

Net income for the six months ended June 30, 2014 was reduced by a fair value adjustment of investment properties in Q1, equal to the acquisition costs incurred in relation to the acquisition completed in that quarter of \$915,346.

Excluding this item, net income for the six months ended June 30, 2014 would have been \$1,326,190.

Net operating income of \$1,460,724 for the three months ended June 30, 2014 was \$1,385,965 higher than net operating income of \$74,759 for the three months ended June 30, 2013, due to the fact that the REIT only owned the Miramichi property for 61 of 91 days during the three months ended June 30, 2013. During the three months ended June 30, 2014, the REIT generated net operating income from the Miramichi Property for the entire three month period. Additionally, the REIT acquired 10 industrial investment properties on January 14, 2014, which generated net operating income of \$1,341,000 during the quarter. For the six months ended June 30, 2014, operating income of \$2,725,163 was higher than net operating income in the same period of 2013 of \$80,616 due to the REIT owning the QT Property, the Miramichi Property and the RTL Westcan Properties for 181 days, 181 days, and 168 days, respectively, during the six months ended June 30, 2014 as compared to 115 days, 61 days, and 0 days, respectively during the same six month period of 2013. Approximately \$2,495,000 of net operating income was generated from the RTL Westcan Properties during the six months ended June 30, 2014.

Net interest expense of \$374,193 for the three months ended June 30, 2014 is related to debt financing secured to acquire the QT Property, the Miramichi Property and the RTL Westcan Properties. In the three months ended June 30, 2013, the REIT only paid interest on the mortgage secured against the Miramichi property for 61 of 91 days, and for the QT property for the full quarter. Net interest expense of \$374,193 for the three months ended June 30, 2014 is comparable to net interest expense for the three months ended March 31, 2014 of \$364,647. On March 5, 2014, \$30,000,000 drawn against the Credit Facility was converted to fixed rate borrowings at an interest rate of 3.9%. Interest on this amount was based on the fixed rate for the entire three month period ending June 30, 2014. For the six month period ended June 30, 2014, net interest expense of \$738,840 was \$728,775 higher than net interest expense of \$10,065 during the six months ended June 30, 2013 due to higher borrowings in the period relating to debt incurred to acquire the RTL Westcan Properties, and more days interest relating to the QT Property and Miramichi Property during the period. In the six three months ended June 30, 2013, the REIT had excess cash invested in guaranteed investment certificates which generated net interest income of \$17,771 (for the six months ended June 30, 2014 - \$1,176).

For the three months ended June 30, 2014, general and administrative expense of \$246,770 was primarily related to accrued asset management fees payable to the REIT's external manager (see the section below titled "related party transactions") in the amount of \$150,900, accrued trustees fees and expenses of \$30,125, other professional fees of \$25,844, costs in relation to the filing of the REIT's annual information form and financial statements of approximately \$15,000, and other costs. General and administrative expense of \$391,167 for the three months ended June 30, 2013 was primarily comprised of professional and other fees of approximately \$370,000 related to a contemplated plan of arrangement and acquisitions, as further detailed in the information circular dated May 17, 2013. Costs related to the plan of arrangement included legal, tax, audit and other costs. The remainder of general and administrative expenses for the three months ended June 30, 2013 related to professional fees of \$6,000, communications costs of approximately \$6,000, and other costs of approximately \$9,000.

For the six months ended June 30, 2014, general and administrative expense of \$508,868 was primarily related to asset management fees payable to the REIT's external manager (see the section below titled "related party transactions") in the amount of \$276,635, other professional fees of \$63,721, accrued trustees fees and expenses of \$55,250, costs related to the plan of arrangement of \$53,208, costs in relation to the filing of the REIT's annual information form and financial statements of approximately \$15,000, directors and officers insurance expense of approximately \$10,000, and other costs. For the six months ended June 30, 2013, general and administrative expense of \$419,098 was primarily comprised of professional and other fees of approximately \$375,000 related to the contemplated plan of arrangement and acquisitions and the remainder of expenses related to listing fees of approximately \$14,000, professional fees of approximately \$13,000, communication expenses of approximately \$10,000 and other costs of approximately \$7,000.

Transaction costs of \$221,667 in the three and six months ended June 30, 2013 related to due diligence costs associated with properties the Corporation had intended to purchase, but ultimately abandoned which were expensed. The costs related to audited financial statements, environmental assessments, building condition reports, appraisals and other information about the properties during the due diligence period.

Fair value adjustment of investment properties for the six months ended June 30, 2014 is equal to the acquisition costs incurred in relation to the RTL Westcan acquisition. Fair value adjustment of investment properties for the three and six months ended June 30, 2013 of \$468,463 and \$438,900, respectively, related primarily to the fair value adjustment recorded with respect to the Miramichi Property in the second quarter of 2013. A third party appraisal dated February 7, 2013, using the discounted cash flow method and applying a discount rate of 7.5% and a terminal capitalization rate of 7.0% arrived at an appraised value of \$6,170,000 for the Miramichi property. Based on the direct capitalization approach, applying a capitalization rate of 6.75%, the appraisal valued the property at \$5,990,000. As at June 30, 2013, the fair value of the investment property was determined internally by management through the application of the direct capitalization method using a capitalization rate of 6.75%.

<b>Select Balance Sheet Data</b>	<b>As at June 30, 2014</b>	<b>As at December 31, 2013</b>
	<b>\$</b>	<b>\$</b>
Income properties	78,380,000	7,140,000
Cash and cash equivalents	142,923	681,636
Total Assets	79,883,355	8,631,984
Current liabilities	1,770,147	939,089
Non- current portion of mortgages payable	2,977,056	3,087,154
Revolving credit facility	34,046,082	-
Unit options	63,000	-
Class B LP Units	<u>777,600</u>	<u>-</u>
Total non-current liabilities	37,863,738	3,087,154
Unitholders' equity	40,249,470	4,605,741
Debt to total assets	46.6%	38.4%

#### **Debt to Total Assets**

The REIT's debt to total assets at June 30, 2014 was 46.6%, as compared to 38.4% at December 31, 2013 and 46.8% at March 31, 2014. The REIT's targeted debt to total assets ratio is between 45% and 55%. The REIT's calculation of debt for the quarter includes mortgages payable and revolving credit facility balances at the amounts carried on the REIT's statement of financial position.

#### **SUMMARY OF QUARTERLY RESULTS<sup>(1)</sup>**

	<b>Q2 2014</b>	<b>Q1 2014</b>	<b>Q4 2013</b>	<b>Q3 2013</b>
Property income	\$ 1,771,095	\$ 1,528,471	\$ 226,698	\$ 225,889
Property expenses	\$ <u>(310,371)</u>	\$ <u>(264,032)</u>	\$ <u>(100,021)</u>	\$ <u>(91,599)</u>
Net operating income (NOI)	\$ 1,460,724	\$ 1,264,439	\$ 126,677	\$ 134,290
Net income (loss)	\$ 699,765	\$ (288,921)	\$ (231,435)	\$ 39,814
Weighted average number of units, basic*	19,810,711	17,134,655	2,750,000	2,750,000
Weighted average number of units, diluted*	19,827,129	17,134,655	2,750,000	2,750,000
	<b>Q2 2013</b>	<b>Q1 2013</b>	<b>Q4 2012</b>	<b>Q3 2012**</b>
Property income	\$ 164,223	\$ 10,498	\$ -	\$ -
Property expenses	\$ <u>(89,464)</u>	\$ <u>(4,641)</u>	\$ -	\$ -
Net operating income (NOI)	\$ 74,759	\$ 5,857	\$ -	\$ -
Net income (loss)	\$ (89,247)	\$ (42,067)	\$ (276,988)	\$ (12,787)
Weighted average number of units, basic and diluted*	2,750,000	2,750,000	2,636,957	1,066,272

(1) The quarterly results fluctuate based on timing related to pursuing and completing acquisitions and corporate activities.

\* Weighted average number of units has been adjusted to reflect the 20 for 1 exchange of shares of the Corporation for units of the REIT in connection with the plan of arrangement completed January 13, 2014.

\*\* Period from July 30, 2012 (date of incorporation) to September 30, 2012.

## FUNDS FROM OPERATIONS AND ADJUSTED FUNDS FROM OPERATIONS

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	\$	\$	\$	\$
<b><u>FFO</u></b>				
Net income (loss)	699,765	(89,247)	410,844	(131,314)
Adjustments:				
Fair value adjustment of investment properties	-	(468,463)	915,346	(438,900)
Fair value adjustment of Class B LP Units	93,600	-	93,600	-
Fair value adjustment of unit options	32,000	-	31,000	-
Distributions on Class B LP Units expensed	<u>14,396</u>	<u>-</u>	<u>26,665</u>	<u>-</u>
Funds from operations (FFO)	839,761	(557,710)	1,477,455	(570,214)
<b><u>AFFO</u></b>				
FFO	839,761	(557,710)	1,477,455	(570,214)
Adjustments:				
Non-cash asset management fees to be settled in units	150,900	-	276,635	-
Non-cash trustee fees to be settled in units	20,625	-	41,250	-
Amortization of deferred financing fees	27,511	2,136	55,063	2,421
Straight-line ground lease	4,034	-	8,068	-
Capital reserve (1)	<u>(35,000)</u>	<u>(30,000)</u>	<u>(65,000)</u>	<u>(1,800)</u>
Adjusted funds from operations (AFFO)	1,007,831	(585,574)	1,793,471	(569,593)

(1) Based on an estimate of \$0.30 per square foot of gross leasable area per year. Capital reserve includes capital expenditures, tenant inducements and leasing costs.

## FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

The REIT's principal source of liquidity is cash and cash equivalents on hand and the undrawn borrowing capacity on its revolving credit facility. As at June 30, 2014, the REIT had cash and cash equivalents of \$142,923 (December 31, 2013 - \$681,636) and working capital deficit of \$280,792 (December 31, 2013 - \$538,895 of working capital). Management of the REIT believes that sufficient cash from operations will be generated to meet the working capital deficit, and the REIT has the ability to draw funds on the revolving credit facility if required. The REIT has sufficient liquidity to maintain and expand its business.

The following table details the changes in cash and cash equivalents for the three and six months ended June 30, 2014 and June 30, 2014.

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2014
	\$	\$	\$	\$
<b>Cash provided by (used in):</b>				
Operating activities	394,739	(27,811)	684,293	(354,265)
Investing activities	-	(5,521,537)	(34,076,127)	(6,211,146)
Financing activities	<u>(388,641)</u>	<u>2,927,498</u>	<u>32,853,121</u>	<u>2,915,831</u>
Change in cash and cash equivalents	6,098	(2,621,850)	(538,713)	(3,649,580)
Cash and cash equivalents – beginning of period	<u>136,825</u>	<u>3,911,988</u>	<u>681,636</u>	<u>4,939,718</u>
Cash and cash equivalents – end of period	<u>142,923</u>	<u>1,290,138</u>	<u>142,923</u>	<u>1,290,138</u>

Cash generated from operating activities for the three months ended June 30, 2014 of \$394,739 includes cash used from changes in working capital of \$462,171, relating primarily to \$325,000 of deposits paid in the quarter in respect of acquisitions which were completed on July 15, 2014, the payment of annual property taxes for the Miramichi property in the amount of approximately \$213,000, and the payment of annual property tax and ground lease expenses relating to the PEI property in the amount of \$68,000, net of items accrued in payables at June 30, 2014.

Cash used in financing activities for the three months ended June 30, 2014 includes distributions paid of \$755,400 and principal repayment of mortgages of \$55,846, net of proceeds from borrowings on the credit facility of \$422,605. Borrowings against the credit facility were primarily used to fund \$325,000 of deposits, as well as approximately \$97,000 of costs relating to the prospectus offering which was completed July 15, 2014.

The REIT believes that it has sufficient financial resources to operate its investment properties and to identify, investigate and complete potential acquisitions, and to fund further expenditures as required.

### **Mortgages Payable**

On March 8, 2013, when the REIT acquired the QT Property, as partial consideration for the purchase, it assumed a mortgage secured by a charge against the QT Property, bearing interest at 4.0% and maturing September 1, 2017. On May 1, 2013, when the REIT acquired the Miramichi Property, new mortgage financing with a ten year term, a 12 year amortization period, and bearing interest at a rate of 3.74% was arranged by the REIT.

The mortgages payable are secured by charges against the investment properties. At June 30, 2014, the weighted average interest rate, including deferred financing costs, on the mortgages payable is 4.07% and the weighted average term to maturity is 8.01 years. As at June 30, 2014, unamortized deferred financing costs of \$50,516 are netted against mortgages payable. Interest expense recorded in the period includes the amortization of deferred financing costs relating to mortgages payable in the amount of \$2,628 for the three months ended June 30, 2014 and \$5,297 for the six month period then ended.

The breakdown of future principal repayments, including mortgage maturity, is presented in the following table:

	<b>Scheduled Repayments</b>	<b>Principal Maturities</b>	<b>Total</b>
	\$	\$	\$
Remainder of 2014	113,265	-	113,265
2015	232,957	-	232,957
2016	241,800	-	241,800
2017	245,901	414,040	659,941
2018	239,685	-	239,685
Thereafter	1,171,601	596,981	1,768,582
Total	<u>2,245,209</u>	<u>1,011,021</u>	<u>3,256,230</u>

### **Revolving Credit Facility**

On January 14, 2014, through the acquisition of a limited partnership the REIT assumed the rights and obligations of a revolving credit facility (the "Credit Facility"). The Credit Facility is secured against the 10 RTL Westcan Properties, and allows the REIT to draw against the facility in the form of prime advances, bankers' acceptance advances, or fixed rate and term advances. Prime rate advances bear interest at 125 basis points per annum over the Canadian prime borrowing rate. Banker's acceptance advances bear interest at 225 basis points per annum over the floating bankers' acceptance rate. Total financing costs in the amount of \$497,666 were incurred in connection with the establishment of the Credit Facility.

At June 30, 2014, \$30,000,000 was drawn against the Credit Facility in the form of fixed rate and term borrowings, bearing interest at a rate of 3.90% and maturing on January 10, 2019. \$3,600,000 was drawn in the form of bankers' acceptance borrowings, at an interest rate, including the applicable stamping fee, of 3.49%, and maturing July 4, 2014, and \$893,981 was in the form of prime rate borrowings. At June 30, 2014 deferred financing costs of \$447,899 are netted against the Credit Facility. Interest expense recorded in the period includes the amortization of deferred financing costs relating to the Credit Facility in the amount of \$24,883 for the three months ended June 30, 2014, and \$49,766 for the six month period then ended.

The Credit Facility includes, inter alia, covenants that RW LP, the subsidiary of the REIT which is party to the credit facility, (i) will not allow the Total Funded Debt to Real Property Ratio to exceed 60% at any time; and (ii) the Interest Coverage Ratio shall not be less than 2.25:1.00. The Credit Facility also contains restrictions on, inter alia, change of business, sale of assets, and mergers and acquisitions without the consent of the lender and includes events of default such as failure to pay the principal loan, failure to observe covenants and involuntary insolvency. As at June 30, 2014, RW LP was in compliance with both of these covenants.

Total Funded Debt to Real Property Ratio is a defined term contained in the Credit Facility. Total Funded Debt to Real Property Ratio is calculated as the total amount drawn against the Credit Facility divided by the fair market value of the investment properties of RW LP.

Interest Coverage Ratio is a defined term contained in the Credit Facility. Interest Coverage Ratio is calculated by the dividing the interest expense of RW LP by the result of the following as contained in the RW LP Statement of Income: net income plus interest expense, plus loss on fair value adjustment of investment properties, less gain on fair value adjustment of investment properties, plus depreciation and amortization.

Total Funded Debt to Real Property Ratio and Interest Coverage Ratio are not measures defined by IFRS, do not have standardized meanings prescribed by IFRS and should not be construed as alternatives to net income/loss, financial position, cash flow from operating activities or other measures of financial performance calculated in accordance with IFRS. These covenant calculations are not used by the REIT as a measure of the REIT's future or historical financial performance, financial position or cash flow, but are used solely to determine RW Real Estate LP's compliance with its covenants set out in the Credit Facility Agreement.

## **SIGNIFICANT ACCOUNTING POLICIES AND ACCOUNTING ESTIMATES**

A summary of significant accounting policies and accounting estimates can be found in note 2 to the REIT's condensed consolidated interim financial statements.

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities and contingent liabilities at the date of the financial statements and the reported amount of expenses during the period. Actual results may differ materially from these estimates.

The estimates and judgements used in determining the recorded amount for asset, liabilities and equity in the financial statements include the following:

### **Investment Properties**

The critical assumptions and estimates used when determining the fair value of investment properties are stabilized income and capitalization rates. Management determines fair value internally utilizing financial information, external market data and capitalization rates determined by reference to third party appraisals and reports published by industry experts including commercial real estate brokerages. The REIT also applies judgement in determining whether the properties it acquires are considered to be asset acquisitions or business combinations. The REIT considers all the properties it has acquired to date to be asset acquisitions.

### **Unit options**

The estimates used when determining the fair value of unit-based compensation are the average expected share option holding period, the average expected volatility rate, and the average risk-free interest rate. The average expected unit option holding period used is estimated to be half of the life of the option. The average expected volatility rate is estimated based on the historical volatility of comparable companies over a period of time approximating the average expected unit option holding period. The average risk-free interest rate is based on government of Canada bonds with terms consistent with the average expected share option holding period.

## **CHANGES IN ACCOUNTING POLICIES**

The REIT has adopted the following new and revised standards, along with consequential amendments, effective January 1, 2014. These changes were required due to changes in IFRS, and were made in accordance with the applicable transitional provisions and are summarized as follows:

IFRS Interpretation Committee (IFRIC) 21, “Levies” (IFRIC 21) provides an interpretation on the accounting for levies imposed by governments. IFRIC 21 clarifies that the obligating event that gives rise to liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. The adoption of IFRIC 21 did not have any impact on the condensed consolidated interim financial statements of the REIT.

IAS 32, “Financial Instruments: Presentation” (IAS 32) clarifies requirements for offsetting of financial assets and financial liabilities. The adoption of IAS 32 did not have any impact on the condensed consolidated interim financial statements of the REIT.

IAS 36, “Impairment of Assets” addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The adoption of IAS 36 did not have any impact on the condensed consolidated interim financial statements of the REIT.

## **FINANCIAL INSTRUMENTS AND RISKS AND UNCERTAINTIES**

### *Real property ownership and tenant risk*

All real property investments are subject to elements of risk. The value of real property and any improvements thereto depends on the credit and financial stability of tenants and upon the vacancy rates of the property. The properties generate revenue through rental payments made by the tenants thereof. The ability to rent vacant property will be affected by many factors, including changes in general economic conditions (such as the availability and cost of mortgage funds), local conditions (such as an oversupply of space or a reduction in demand for real estate in the area), government regulations, changing demographics, competition from other available properties, and various other factors.

Upon the expiry of any lease, there can be no assurance that the lease will be renewed or the tenant will be replaced. The terms of any subsequent lease may be less favourable to the REIT than those of an existing lease. In the event of default by a tenant, the REIT may experience delays or limitations in enforcing its rights as landlord and incur substantial costs in protecting its investment. Furthermore, at any time, a tenant may seek the protection of bankruptcy, insolvency or similar laws which could result in the rejection and termination of the lease of the tenant and, thereby, cause a reduction in the cash flows available to the REIT.

### *Competition*

The real estate business is competitive. Numerous developers, managers and owners of properties compete with the REIT when seeking tenants. Some of the competing properties may be better located than the REIT’s properties. The existence of competition could have an impact on the REIT’s ability to lease its properties and could have an impact on the rents that can be charged. The REIT is subject to competition for suitable real property investments and a number of these competitors have greater financial resources than those of the REIT. There is a risk that continuing increased competition for real property acquisitions may increase purchase prices to levels that are not accretive.

### *Fixed costs and increased expenses*

The REIT incurs a number of fixed costs which must be paid throughout its ownership of real property, regardless of whether its properties are producing income. Fixed costs include utilities, property taxes, maintenance costs, mortgage payments, insurance costs, and related costs.

### *General uninsured risks*

The REIT carries comprehensive general liability, fire, flood, extended coverage and rental loss insurance with customary policy specifications, limits and deductibles. There can be no assurance, however, that claims in excess of the insurance coverage or claims not covered by the insurance coverage will not arise or that the liability coverage will continue to be available on acceptable terms.

### *Environmental and litigation risk*

The REIT is subject to federal, provincial and local environmental regulations that apply generally to the ownership of real property and the operation of commercial properties. If it fails to comply with those laws, the REIT could be subject to significant fines or other governmental sanctions. Under various federal, provincial and local laws, ordinances and regulations, an owner or operator of real estate may be required to investigate and clean up hazardous or toxic substances or petroleum product releases at a facility and may be held liable to a governmental entity or to third parties for property damage and for investigation and clean-up costs incurred by such parties in connection with contamination. Such liability may be imposed whether or not the owner or operator knew of, or was responsible for, the presence of these hazardous or toxic substances. The cost of investigation, remediation or removal of such substances may be substantial, and the presence of such substances, or the failure to properly remediate such substances, may adversely affect the REIT's ability to sell or rent such facility or to borrow using such facility as collateral. In order to assess the potential for liabilities arising from the environmental condition at the REIT's properties, the REIT may obtain or examine environmental assessments prepared by environmental consulting firms. The environmental assessments received in respect of the investment properties have not revealed, nor is the REIT aware of, any environmental liability that the company believes will have a material adverse effect on it.

In addition, in connection with the ownership, operation and management of real properties, the REIT could potentially be liable for property damage or injuries to persons and property. In the normal course of the REIT's operations, it may become involved in, named as a party to or the subject of, various legal proceedings, including regulatory proceedings, tax proceedings and legal actions relating to personal injuries, property damage, property taxes, land rights, the environment and contract disputes.

### *Liquidity risk*

Liquidity risk is the risk that the REIT will not have the financial resources required to meet its financial obligations as they become due. The REIT manages this risk by ensuring it has sufficient cash and cash equivalents on hand to meet obligations as they become due by forecasting cash flows from operations, cash required for investing activities and cash from financing activities. As at June 30, 2014, the REIT had cash and cash equivalents of \$142,923 (December 31, 2013 - \$681,636), mortgages payable of \$3,205,714 (December 31, 2013 - \$3,311,591), a revolving credit facility balance of \$34,046,082 (December 31, 2013 - \$nil) and accounts payable and accrued liabilities of \$1,281,989 (December 31, 2013 - \$714,652). The REIT's working capital was negative at June 30, 2014, however, the REIT has access to undrawn amounts under its revolving credit and expects to generate sufficient cash from operations to satisfy its financial liabilities. The REIT is not subject to significant liquidity risk.

The contractual maturities and repayment obligations of the REIT's financial liabilities are as follows:

	<b>Accounts payable and accrued liabilities</b>	<b>Credit facility principal repayment</b>	<b>Interest on fixed portion of credit facility</b>	<b>Mortgage payable</b>	<b>Mortgage interest</b>	<b>Total</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Remainder of						
2014	1,281,989	-	589,808	113,265	60,153	2,045,215
2015	-	-	1,170,000	232,957	113,878	1,516,835
2016	-	-	1,170,000	241,800	105,035	1,516,835
2017	-	-	1,170,000	659,941	91,767	1,921,708
2018	-	-	1,170,000	239,685	70,481	1,480,166
Thereafter	-	34,493,981	28,849	1,768,582	198,299	36,489,711
<b>Total</b>	<b>1,281,989</b>	<b>34,493,981</b>	<b>5,298,657</b>	<b>3,256,230</b>	<b>639,613</b>	<b>44,970,470</b>

### *Interest rate risk*

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. There is a risk that the REIT may not be able to renegotiate its mortgages at maturity on terms as favourable as the existing mortgages payable. At June 30, 2014, there was a total of \$893,981 drawn against the REIT's revolving credit facility which bears interest at floating bankers' acceptance and Canadian prime rates plus a fixed spread. There is a risk that prevailing interest rates could increase, and those increases could be significant. The

REIT mitigates interest rate risk by maintaining reasonable levels of debt to gross book value and aims to structure new debt to stagger the maturities to ensure that the majority of debt does not become due for repayment in any one particular year. The REIT may also convert borrowings under the revolving credit facility from floating rate to fixed rate borrowings as part of its interest rate risk management strategy.

#### *Credit risk*

Credit risk is the risk that one party to a financial instrument will cause a loss to another party by failing to pay for its obligations. The REIT is subject to credit risk with respect to its cash and cash equivalents. The REIT mitigates credit risk by depositing cash with and investing in guaranteed investment certificates of a Canadian schedule I chartered bank and monitoring the bank's credit ratings.

As at June 30, 2014, the REIT had four tenants, with one tenant accounting for approximately 83 percent of the REIT's rental income, resulting in concentration of credit risk, however, the major tenant is an established business with a history of profitable operations. The REIT will continue to monitor the credit worthiness of the tenants on an ongoing basis.

#### **COMMITMENTS**

On March 8, 2013, the REIT acquired the income property located at 695 University Avenue, Charlottetown, Prince Edward Island. The property is subject to a 66 year land lease which commenced May 1, 2006, and has two ten year options to renew. The land lease provides for annual base rent and additional rent comprised of the property's proportionate share of common area maintenance and property tax expense. The full annual ground lease payment is due in advance each May 1st. As at June 30, 2014, annual future minimum ground lease payments on account of base rent are as follows:

	<b>Remainder of 2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>Thereafter</b>
	\$	\$	\$	\$	\$	\$
Minimum annual rent	-	48,000	52,800	52,800	52,800	3,528,914

#### **OUTSTANDING UNIT / SHARE DATA**

	<b>Shares</b>	<b>Units</b>	<b>Amount</b>
			\$
Share Capital of the Corporation, December 31, 2013	55,000,000	-	4,947,451
Common Shares exchanged for REIT Units (One REIT unit for every 20 common shares)	(47,800,000)	2,390,000	-
Common Shares exchanged for Class B LP Units (One Class B LP unit for every 20 common shares)	(7,200,000)	-	(580,000)
Units issued as consideration, purchase of Acquisition Properties	-	17,000,000	37,240,000
Units issued as consideration for management services	-	66,176	125,734
Units issued under distribution reinvestment plan	-	11,186	22,332
Unitholders' equity, June 30, 2014	-	19,467,362	41,755,517

On January 14, 2014, the REIT issued 17,000,000 REIT units to the vendor of the RTL Westcan Properties as partial satisfaction of the purchase price for the properties acquired, with the remainder of the purchase price settled with \$34,000,000 in cash. The fair values of the RTL Westcan Properties were determined by reference to appraisal reports prepared by qualified third party appraisers. The aggregate appraised value of the RTL Westcan Properties is \$71,240,000. The carrying amount of the REIT Units issued as partial consideration for the acquisition was determined in accordance with IFRS 2 by reference to the fair value of the assets acquired in exchange for the units.

As at August 20, 2014, a total of 28,293,775 REIT units and 360,000 Class B LP Units were issued and outstanding.

## DISTRIBUTIONS

On February 4, 2014, the REIT declared its initial distribution of \$0.00742 per unit, for the period from January 14, 2014 to January 31, 2014, payable on February 28, 2014 to unitholders of record on February 14, 2014. At the same time the REIT declared a regular monthly distribution for the period from February 1, 2014 to February 28, 2014 in the amount of \$0.01333 per unit, representing \$0.16 per unit on an annualized basis. The REIT currently continues to pay a monthly distribution of \$0.01333 per unit. Total distributions declared with respect to REIT units in the three months ended June 30, 2014 amounted \$778,367, and \$1,439,181 for the six month period then ended. No distributions were declared or paid during the three or six months ended June 30, 2013.

In accordance with National Policy 41-201, "Income Trusts and Other Offerings", the REIT is required to provide the following information:

	<b>Three Months Ended June 30, 2014</b>	<b>Year ended December 31, 2013</b>	<b>Period from July 30, 2012 to December 31, 2012</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>
Cash flows from operating activities	394,739	(853,645)	(15,233)
Net income (loss)	699,765	(322,935)	(289,775)
Actual cash distributions paid or payable during the period	755,400	-	52,800
Excess (shortfall) of cash flows from operating activities over cash distributions paid	(360,661)	N/A	N/A
Excess (shortfall) of net income (loss) over cash distributions paid	(55,635)	N/A	N/A

Cash flow from operating activities for the three months ended June 30, 2014 includes \$325,000 of deposits paid and approximately \$97,000 paid in respect of fees for the prospectus offering and acquisitions completed on July 15, 2015. These items were funded through borrowings against the REIT's revolving credit facility. Net of these two items, cash flows from operations exceeds distributions paid or payable during the period.

Net income for the three months ended June 30, 2014 includes non-cash fair value adjustments amounting to \$125,600. Net of these items, net income exceeds distributions paid or payable during the period.

## DISTRIBUTION REINVESTMENT PLAN

The REIT adopted a distribution reinvestment plan (DRIP) on February 20, 2014, pursuant to which resident Canadian holders of not less than 1,000 units are entitled to elect to have all or some of the cash distributions of the REIT automatically reinvested in additional units at a price per unit calculated by reference to the weighted average of the trading price for the units on the relevant stock exchange or marketplace for the five trading days immediately preceding the relevant distribution date. Eligible unitholders who so elect will receive a bonus distribution of units equal to 3% of each distribution that was reinvested by them under the DRIP. For the three month period ended June 30, 2014, 10,973 units were issued under the DRIP for a stated value of \$21,937. For the six month period ended June 30, 2014, 11,186 units for a stated value of \$22,332 were issued under the drip.

## **ACCOUNTING STANDARDS ISSUED BUT NOT YET EFFECTIVE**

There are pending changes to IFRS which are not yet effective for the period ended June 30, 2014 which have not been applied in the preparation of the REIT's financial statements. The REIT is currently considering the impact that these standards changes will have on the financial statements. The standards issued or amended but not yet effective at June 30, 2014 include the following:

IFRS 9, Financial Instruments, is a new standard which will replace IAS 39, Financial Instruments: Recognition and Measurement, and addresses classification and measurement of financial assets, as well as providing guidance on financial liabilities and derecognition of financial instruments. IFRS 9 provides a single approach, based on how an entity manages its financial instruments and the contractual cash flow characteristics of the financial assets to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple classification options in IAS 39. In November 2013, amendments were made to IFRS 9 which include new hedge accounting guidelines. In July 2014, further amendments were made to include an effective date of annual periods beginning on or after January 1, 2018.

IFRS 15, Revenue from Contracts with Customers, is a new standard providing accounting guidance on the recognition, measurement and disclosure of revenue from contracts with customers. IFRS 15 does not apply to contracts within the scope of the standard on leases. IFRS 15 is effective for annual periods beginning on or after January 1, 2017 and must be applied retrospectively.

## **RELATED PARTY TRANSACTIONS**

On January 14, 2014, pursuant to an asset management agreement (the Management Agreement) entered into between the REIT and Edgefront Realty Advisors (the Manager), the REIT engaged the Manager to provide management services to the REIT, including providing the services of a chief executive officer and a chief financial officer to the REIT. The Manager is owned by a group including the chief executive officer and chief financial officer of the REIT, who collectively own 50 percent of the Manager, as well as a group which owns or controls a majority of Units of the REIT. In performing its obligations under the Management Agreement, the Manager will be entitled to receive the following fees from the REIT or its subsidiaries:

i) An annual asset management fee in the amount of:

0.75% of the gross book value, as defined in the Management Agreement, up to \$150 million, to be paid in Units;

0.65% of the gross book value, as defined in the Management Agreement, between \$150 million and \$300 million, to be paid 50% in Units and 50% in cash; and

0.50% of the gross book value, as defined in the Management Agreement, over \$300 million, to be paid 50% in Units and 50% in cash.

ii) An acquisition fee in the amount of 0.50% of the purchase price of any property acquired by the REIT payable in cash on completion of each acquisition.

iii) A construction management fee payable on capital projects in an amount equal to 5% of all hard construction costs incurred on a project, excluding any maintenance capital expenditures. The construction management fee will be paid in cash upon substantial completion of each capital project.

iv) A property management fee, being the fee payable in respect of such services provided by the Manager that is deemed recoverable and recovered from the tenants, payable in cash on a cost recovery basis.

In the six month period ended June 30, 2014, acquisition fees in the amount of \$340,000 were paid to the manager. No acquisition fees were accrued or paid in the three months ended June 30, 2014.

The portion of the annual asset management fee relating to the period from January 14, 2014 to March 31, 2014 of \$125,735 was settled by issuing 66,176 units of the REIT to the Manager in the three month period ended June 30, 2014. The portion of the annual asset management fee relating to the period from April 1, 2014 to June 30, 2014 of \$150,900 was expensed in the three month period ended June 30, 2014 and is accrued in the condensed consolidated interim statement of financial position at June 30, 2014.

Trustee fees in respect of annual retainers and meeting fees in the amount of \$50,250 have been accrued at June 30, 2014.

During the year ended December 31, 2013, cash bonuses totalling \$190,000 were paid to the REIT's CEO and CFO. No director or trustee compensation was paid during the year ended December 31, 2013.

#### **SUBSEQUENT EVENTS**

On July 15, 2014, the REIT completed a public offering of units. 8,750,000 units were issued from treasury under the offering, generating gross proceeds of \$17,500,000 to the REIT. On the same date, the REIT acquired three investment properties located in Alberta and controlled by TriWest Capital Partners, for an aggregate purchase price of \$36,744,000. The purchase price was satisfied with funds raised through the offering as well as funds drawn against the Credit Facility. The limit of the Credit Facility was increased from \$45,000,000 to \$60,000,000 to allow for financing of these acquisitions. The term of the Credit Facility was also extended to July 15, 2020.