CORPORATE PARTICIPANTS

Steve Hodgson
Chief Executive Officer

Charles Peach
Chief Financial Officer

Lindsay Stiles
Chief Operating Officer

Braden Lyons
Associate

CONFERENCE CALL PARTICIPANTS

Lorne Kalmar
TD Securities

Sairam Srinivas
Cormark Securities

Jenny Ma
BMO Capital Markets

Matt Kornack
National Bank Financial

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Slate Office REIT Fourth Quarter 2021 Financial Results Conference Call.

At this time, all participants are in a listen-only mode. After the speaker presentation, there will be a question-and-answer session. To ask a question during the session, please press star-one on your telephone. Please be advised today's call is being recorded. If you require further assistance, please press star-zero.

I would now like to hand the conference call over to Braden Lyons, Slate Office REIT. You may begin, sir.

Braden Lyons, Associate

Thank you, operator, and good morning, everyone. Welcome to the Q4 2021 conference call for Slate Office REIT. I'm joined this morning by Steve Hodgson, Chief Executive Officer; Lindsay Stiles, Chief Operating Officer; and Charles Peach, Chief Financial Officer.

Before getting started, I would like to remind participants that our discussion today may contain forward-looking statements, and therefore we ask you to review the disclaimers regarding forward-looking statements as well as non-IFRS measures, both of which can be found in management's discussion and analysis. You can visit Slate Office REIT's website to access all of the REIT's financial disclosure, including our Q4 2021 investor update, which is available now.

I will now hand over the call to Steve for opening remarks.

Steve Hodgson, Chief Executive Officer

Thank you, Braden. Before I pass it to Charles, I'd first like to comment on our recent acquisition of Yew Grove REIT in Ireland and why that transaction aligns with our strategic direction.

We have a strong conviction in the office sector and believe that physical workspace is an essential enabler of collaboration, culture, and innovation. We also believe there's an opportunity to align our portfolio with tenants and industries that continue to drive demand for office space.

The Yew Grove acquisition exemplifies this. We have purchased a portfolio of high-quality, well-located assets with government, technology, and life science tenants. This portfolio increases our exposure to credit quality income, enhances our occupancy and weighted average lease term, and is overall additive to the durability of our cash flow.

We have also onboarded a team in Ireland with a strong track record and a pipeline of additional acquisition opportunities, which positions the REIT well for continued growth in the region.

I will now hand it over to Charles for his comments on our year-end results.

Charles Peach, Chief Financial Officer

Thank you, Steve. In 2021, the REIT had an industry-leading distribution yield of 8%, which is well-covered with an AFFO payout ratio of 76%. From a balance sheet perspective, we extended our revolving credit facility and refinanced certain mortgage debt to increase liquidity and reduce interest costs, while raising acquisition capital through the issuance of subscription receipts and convertible debentures.

The REIT delivered a total unitholder return of approximately 31% in 2021, which is higher than our Canadian office REIT peer group. Going forward, the

Irish portfolio is expected to be accretive to AFFO per unit and contribute to stable organic income growth.

In 2021, our leasing volumes were approximately 12.2% and 7.4% higher than 2020 and 2019 respectively, and our rental rate spreads were positive at 6.5%. When you include the Irish portfolio, the weighted average lease term in our portfolio is 5.7 years, and 66.3% of our tenants are government or high-quality credit tenants.

Stable and growing cash flow is a key focus for the REIT, and the recent acquisition is an example of both of these. Slate Office REIT continues to offer investors a durable cash flow and distribution, a trading discount to a well-supported net asset value, and a scalable platform that is positioned for growth.

I'll now hand over for questions.

Operator

At this time, I would like to remind everyone, in order to ask a question, to please press star-one on your telephone. And again, that is star-one for questions at this time.

And our first question will come from the line of Lorne Kalmar of TD Securities. Please hold one moment.

Lorne Kalmar, TD Securities

Thank you. Good morning, everyone, and welcome, Charles.

Steve Hodgson, Chief Executive Officer

Morning.

Lorne Kalmar, TD Securities

On the dispositions, I think you guys said you're targeting about $100 million. How is that progressing? What sort of geographies are you targeting, and what do you expect the cadence of the dispositions to be?

Steve Hodgson, Chief Executive Officer

It's progressing well. It's still about $100 million of asset dispositions that we've earmarked for the next quarter or two in, primarily, the greater Toronto area.

Lorne Kalmar, TD Securities

And is that the focus on the GTA a function of what the pricing is in that market versus other markets, or how did you kind of hone in on that geography?

Steve Hodgson, Chief Executive Officer

No, it's more specific. In one case, there's some expected rollover in a building where the buyer has a solution for that. In another case, it's a building we don't think fits the strategic direction of higher-quality core plus, credit quality tenants, the types of tenants and industries that we're targeting that we think will continue to grow in a post-pandemic environment.

It's a repositioning of the portfolio that, again, as we mentioned in the opening remarks, is really exemplified by the type of product that we're buying in Ireland.

Lorne Kalmar, TD Securities

So, sort of an addition by subtraction?

Steve Hodgson, Chief Executive Officer

Yes.

Lorne Kalmar, TD Securities

Fair enough.

Steve Hodgson, Chief Executive Officer

The dynamic in Toronto creates an environment where we can sell at a very compelling valuation and lower cap rate than we can buy elsewhere where we think we can buy assets to better fit our long-term strategy.

Lorne Kalmar, TD Securities

Okay. And then, maybe just the last one from me, I believe you mentioned you guys have pretty decent pipeline of European acquisitions now with the acquisition of Yew Gove. Would you guys look to dispose of additional assets to fund that? And how do you see the geographic breakdown of the portfolio evolving over the next couple years?

Steve Hodgson, Chief Executive Officer

We've been vocal that there is a significant pipeline of opportunities in Ireland and in other markets. We're still looking in Canada and the U.S., to be very clear, but there is an immediate pipeline in Ireland that's actionable. We could probably do $200 to $300 million of transactions there in the near-term, and we have the team and the relationships to do that on the ground. So, that's very exciting.

To fund that, I think it'll be a mix of some balance sheet cash. It'd be a mix of recycling capital from asset dispositions. And then for larger sort of portfolio transactions, we'd look to do something more creative and hope that the continued strength in our AFFO growth per unit will help us close that gap on NAV where we can continue to raise equity and grow our business.

Lorne Kalmar, TD Securities

Okay. And then just back to the last part of the question, how do you guys see the portfolio geography evolving over the next couple years?

Steve Hodgson, Chief Executive Officer

I would shy away from that question just because we've always been somewhat market agnostic. I think we'll invest where we have presence or where Slate Asset Management has presence. But beyond that, it's really been more opportunity driven.

I will say, could I see the portfolio being a third Europe, a third U.S., and a third Canada? That's certainly a scenario that could play out, but I wouldn't want to be held to that because it'll be opportunity driven.

Lorne Kalmar, TD Securities

Well, in that case, I will not hold you to that. Thanks very much.

Steve Hodgson, Chief Executive Officer

Thank you.

Lorne Kalmar, TD Securities

I'll turn it back.

Operator

Thank you. And the next question will come from the line of Sairam Srinivas from Cormark Securities.

Sairam Srinivas, Cormark Securities

Good morning, everybody. Just a couple of questions, and probably starting with some of Lorne's questions. I want to piggyback on that. Steve, in lieu of the dispositions you mentioned in the GTA, pro forma these dispositions and just broadly speaking and not per your numbers, how does the NOI contribution look like on that market? Because right now, as I see it, it's much more of a stabilized market that's kind of cash flow positive. How do you see that evolving?

Steve Hodgson, Chief Executive Officer

Is the question, how do we feel about removing the NOI contribution from the greater Toronto area and redeploying elsewhere?

Sairam Srinivas, Cormark Securities

Yes.

Steve Hodgson, Chief Executive Officer

To be clear, we will continue to grow in the GTA as well, and it's identified as a target market for us. We're here. We like it. We know it extremely well. This is more about the tenants and the quality of the buildings.

What we're seeing is that, out of the pandemic, there is going to be certain tenants and industries that are going to be bigger utilizers of office space than others. And the demands of those tenants are shifting, and one of the key things is a flight to quality.

Where we have older stock or product that is still in high demand because of the liquidity available in Toronto for commercial real estate, then we can go buy something in what we feel is a market like Ireland, with tailwinds behind it from a macroeconomic perspective, really great tenants, really long-term weighted average lease term, upside on rents, and at a significant discount to replacement cost, we would make that trade all day.

And I think, notwithstanding Toronto, is known as a very stable and strong fundamentals, when you get down to the asset level, you have to make the next level of decision.

Sairam Srinivas, Cormark Securities

That makes sense, Steve. Thanks for the color. My second question's essentially on the rent abatement we saw this quarter. Can you give some color on that, and do we expect more of that coming into '22?

Steve Hodgson, Chief Executive Officer

I can cover that. I think the rent abatement, we'll try not to use that language again in our disclosure, because this really was a positive thing. We renewed a tenant in Chicago for 26,000 square feet. And as part of that deal, which is custom in that market, they're entitled to a free rent portion at the beginning of their term.

That's what that is. It's not rebating any rents that we were already contractually owed. This is a new term, an extension of existing tenant with a free rent package that's built up front in their lease.

Sairam Srinivas, Cormark Securities

That makes sense. And finally, Steve, my last questions on leasing so far in Q1. Can you give some color on what you're seeing in the market? And are you seeing some life in the market in terms of back to office plans and are you seeing tenants coming?

Lindsay Stiles, Chief Operating Officer

Hi, Sai. We've seen positive activity, as we mentioned at the beginning of the call, over 770,000 square feet of leasing completed last year, 12% higher than 2020 and 7% higher than 2019 and that activity and momentum has certainly carried into Q1.

Specifically, on the return to the office, certainly some of the larger companies who were planning to be back by now delayed things slightly due to Omicron. That's really coming to a close. There are all kinds of announcements coming out now. I would say the general sentiment at a high-level is that people will be back, anywhere between after March break and the end of Q2.

Things have been pushed, perhaps, by a month, but the general sentiment is that people are coming back and excited to do so. Utilization for us across the portfolio, I'd say now as compared to the end of last year, we've probably seen an uptick of anywhere from 10% to 20% depending on the market. And we think, outside of the GTA, which obviously is a little bit slower in recovery just due to restrictions being in place longer, we're going to be in much better shape. By the end of this year, we'll be getting closer to pre-pandemic utilization rates.

We're really encouraged by the conversations we're having with existing tenants and then new potential tenants who want to tour our assets and talk about doing deals. It's positive all around.

Sairam Srinivas, Cormark Securities

Thanks for the color, Lindsay. I'll turn it back.

Operator

Thank you, sir. And again, ladies and gentlemen, at this time, to ask additional questions, please press star-one on your telephone.

And the next question will come from the line of Jenny Ma of BMO Capital Markets.

Jenny Ma, BMO Capital Markets

Thanks, and good morning.

Steve Hodgson, Chief Executive Officer

Morning.

Jenny Ma, BMO Capital Markets

Congratulations on the close of the Yew Grove deal, and welcome to Charles. I want to circle back to the discussion about potential dispositions. I'm sure you can't specify which GTA assets you're looking at, but I know there's a portfolio that is partially held by your partner, Wafra. Could you just remind us what the terms are there, whether or not you comment, if they would be a potential buyer and, if there was a sale, are there typical ropers going both ways? How does that all play out?

Steve Hodgson, Chief Executive Officer

I'll answer your question to say, first of all, that the planned dispositions or the dispositions that are underway already do not have anything to do with that portfolio that we co-own with Wafra.

Jenny Ma, BMO Capital Markets

Okay.

Steve Hodgson, Chief Executive Officer

And then, within the Wafra JV agreement, just for interest, they bought it through somewhat of a closed end fund. Their investment horizon is probably to sell in the next few years but they're open to extending that longer if needed. Their ultimate objective is to maximize the value of the assets.

I don't think they'll be the buyer of our interest. We could potentially be the buyer of theirs but we're still working through that.

Jenny Ma, BMO Capital Markets

Okay. So, if the time comes for them to liquidate then, is it put to you first? And if you refuse, does it have to go to market? Like, how does that play out?

Steve Hodgson, Chief Executive Officer

That's correct, yes.

Jenny Ma, BMO Capital Markets

Okay. And turning to the Yew Grove portfolio, is there anything within that portfolio that you might deem as non-core and potentially for sale?

Charles Peach, Chief Financial Officer

It’s Charles here. I think within that portfolio there is one asset that has a retail component to it. It's one of the smaller assets that's been in the portfolio ever since IPO 3.5 years ago. And we're in the process of selling that, and that is the one thing that I would see in there as a non-core asset which we're looking to sell at the moment.

If I look at the rest of the portfolio, the rest of the portfolio has many of the key characteristics that Slate's portfolio has. It has assets which are below market rents. They are below replacement cost. And we’ve shown the ability, in the team that’s come over, to be able to source further assets at the same rates and levels over the last three years and we look forward to continuing to do that to provide Slate Office REIT the opportunity to deploy capital where it believes best, be it in Ireland or elsewhere.

Jenny Ma, BMO Capital Markets

Okay, great. Thank you for that. And then maybe as a bit of a lesson for all of us sitting in Canada, could you do a compare and contrast of the office experience and the outlook post-Omicron in Canada versus Ireland? I think we're well-versed in terms of what's happening in Canada, particularly in Toronto. But how would Ireland compare as far as where they are in terms of occupancy, reopening, and a return to normal or return to office?

Charles Peach, Chief Financial Officer

I think it's fairly similar. If I look across the Irish experience and do a comparison within Europe itself, Ireland had a relatively harsh lockdown, and it is coming out of that at the moment.

If I look at our portfolio, we have to be specific to the sort of assets we see within that. And the portfolio has not only office assets but also it has some life science tenants as well, which have been a focus for us for the last three years and it's an area which we've grown and which we continue to grow, and an example of that being a development that we have in the Midlands for a life science tenant.

The benefit particularly of having those tenants in the portfolio and having advanced manufacturing is they continued to have very high occupancy throughout the pandemic and at the same time, that showed that, while occupancy fell elsewhere, there were certain types of assets which became increasingly attractive, both from a use perspective and also in the mind of investors too when they look at those type of assets as well.

I think that's an example of the ability that we have in Ireland, and in other places as well, to look across a broad universe of assets specifically for those that fit the sort of credit quality tenants, occupancy, and returns we're looking to achieve.

Jenny Ma, BMO Capital Markets

Okay. So, if we look at the path to the return to office--well, for the office specific assets anyway, it would be more or less similar to Canada based on what we know now? Is that a fair comment?

Charles Peach, Chief Financial Officer

Relatively.

Jenny Ma, BMO Capital Markets

Okay. Okay. Well, I look forward to a property tour for the Irish portfolio down the road. Thank you, and I'll turn it back.

Steve Hodgson, Chief Executive Officer

Absolutely, yes.

Operator

Thank you. Once again, ladies and gentlemen, to ask questions, please press star-one on your keypad at this time.

The next question will come from the line of Matt Kornack of National Bank.

Matt Kornack, National Bank Financial

Just wanted to pick up on that theme of life sciences and lab space and you did mention you're looking for more of that type of product in Ireland. But do you see kind of a refocusing of maybe the Canadian and U.S. portfolios in that vein as well, or is that going to be particularly Irish in nature?

Steve Hodgson, Chief Executive Officer

There's an opportunity that we're looking at in the U.S. right now, actually, that is in that space and seems like a very compelling deal. Aside from that, we'll continue to look at these opportunities in the U.S. and Canada.

There's not a lot, as you may know, of life science. I think, Toronto in particular is trying to figure that out right now. I do see that as a growing emerging industry but there's a lot of pension fund capital in Canada chasing that as well, so I'm not sure if we'll be there from a pricing perspective. But again, these sort of one-off opportunities in the U.S., we're seeing them. Then in Ireland, of course, there's a significant pipeline that we've identified.

Matt Kornack, National Bank Financial

And then I guess in Canada, you have some SNC exposure. Some of that is related to space that I think needs to be used in training, etc. But has that generally been a focus of your portfolio composition, or is that just something that has come out of particular opportunities in particular markets?

Steve Hodgson, Chief Executive Officer

Yes, I think there's two reasons you'd be attracted to life sciences. One is it's been highlighted through the pandemic that it's a growing emerging industry and an essential business and then the other is, from a landlord's perspective, generally the tenants are investing a lot into their space. And when they do that, they become very sticky tenants, right?

There’s a parallel there to the SNC deal that you're mentioning, which I think you're talking about their nuclear division that we have with them in the Sheridan Business Park, where they've made a significant investment in that space, and they also own a research and development facility immediately adjacent to the buildings they lease from us.

Yes, it's always been a focus in that sense. Identifying a sticky tenant is a great way to create value in real estate.

Matt Kornack, National Bank Financial

Okay, fair enough. And then on the free rent front, what's the term of the free rent period, and when would we expect cash rent to start at that lease?

Lindsay Stiles, Chief Operating Officer

It would kick in Q2.

Matt Kornack, National Bank Financial

Okay. And then on spreads, it sounds like, and not surprisingly, that in filling some of the vacancy in St. John's, you're seeing a bit lower rents. But can you kind of bifurcate that and then speak to the opportunity maybe this year on spreads and then kind of jive that with thoughts on occupancy and the trajectory on occupancy for this year, and maybe if you want to go into next, for sure?

Lindsay Stiles, Chief Operating Officer

Sure. Matt, our rental rate spreads, as we noted, were 6.5% last year overall. Our rates are currently at a discount to market of about 8.5%. We see continued opportunity to adjust to market and drive income growth. We're confident, based on volume and the ability to adjust upward, and that would include the Ireland portfolio as well. From that side of things, we continue to feel really good.

On an occupancy side of things, adding the Ireland portfolio, we're at 85% today, and with the volume we saw last year being higher than the two years prior with markets reopening and having all these conversations about tenants wanting to be back in the market and, as Steve noted, really aligning ourselves with those larger utilizers of office space, we think we have a really great opportunity to get closer to that 90% stabilization if things continue as they've been going.

Matt Kornack, National Bank Financial

Okay. And I guess with office, things take a while in terms of fixturing it, etc. So, for this year, if we were to model, should we assume just a modest pick up? And then, for that 8.5%, is there some lumpiness in terms of the lease maturity profile there, or is it fairly safe to kind of take an 8.5% and apply it to maturity, adjusting for some retention ratio?

Steve Hodgson, Chief Executive Officer

Let me address the maturity profile. We do expect some vacancy this year. The SNC Lavalin, the tenant you brought up, Matt, they have two locations with us. One was the Sheridan Business Park, where it's their nuclear division, and they've made all that investment. It's a very profitable division. Those buildings are highly utilized even through the pandemic. And then they had their location at the West Mall, which is along the 427, where they have 190,000 square feet.

We'll see a significant downsize from them. We're looking and trying to finalize a deal to retain them for 10 years, but it'll be at a significant downsize. 195, The West Mall, is the building they primarily occupy. That building's very strategically situated. It's a very nice buildout. It's a very nice building. It'll be in high demand by both tenants and potential users. We've been in discussions with a number of groups and hope to have some updates the next time we speak.

That's primarily, from Lindsay and the team's perspective, one of the bigger challenges we have coming into the year. But even in a worst-case scenario with that, we anticipate maintaining or slightly growing our overall occupancy by the end of the year.

Matt Kornack, National Bank Financial

And on the in-place rents for SNC there, would they be consistent with that sort of 8.5% below market, or is it more meaningful or less meaningful?

Steve Hodgson, Chief Executive Officer

Yes. Market rents are about 19, and they're paying about 16.50.

Matt Kornack, National Bank Financial

Okay, perfect. Thanks, guys.

Operator

And at this time, there are no further questions in the queue, and I will turn the call over Mr. Lyons. Sir, please go ahead.

Braden Lyons, Associate

Thank you, everyone, for joining the Q4 2021 conference call for Slate Office REIT. Have a great day.

Operator

Thank you for participating in today's conference call. You may now disconnect.