CORPORATE PARTICIPANTS

Steve Hodgson
Chief Executive Officer

Charles Peach
Chief Financial Officer

Lindsay Stiles
Chief Operating Officer

CONFERENCE CALL PARTICIPANTS

Sairam Srinivas, Cormark Securities

Scott Fromson, CIBC

Jenny Ma, BMO Capital Markets

Jas Cumberbatch, TD Securities

George Huang, Raymond James

Anthony Bogdan, National Bank

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Slate Office REIT second quarter 2022 financial results conference call. At this time, all lines are in a listen-only mode. Following the presentation, we will conduct a question-and-answer session. If at any time during the call you require immediate assistance, please press star zero for the operator.

This call is being recorded on Thursday, August 4, 2022.

I would now like to turn the conference over to Paul Wolanski, Senior Vice President, National Sales and Investor Relations. Please go ahead.

Paul Wolanski, Senior Vice President, National Sales and Investor Relations

Thank you, operator, and good morning, everyone. Welcome to the Q2 2022 conference call for Slate Office REIT. I am 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 Q2 2022 investor update, which is available now.

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

Steve Hodgson, Chief Executive Officer

Thank you, Paul, and good morning, everyone. Recent global macroeconomic pressures have challenged the performance of public equity markets, with real estate securities being no exception. Across the board, REIT trading prices have significantly diverged from their underlying real estate values. However, even against this backdrop, Slate Office REIT's operational performance continues to trend positively. Our core operations remain stable, and we've seen positive leasing momentum and AFFO growth.

Our conviction in the office sector remains strong. We know that physical workspaces enable collaboration, culture, and innovation. The tenants we are focused on recognize this as well.

This quarter, we completed approximately 240,000 square feet of leasing at a rental rate spread of 25.2 percent. This positive rental rate spread demonstrates that well operated, well located, and high-quality real estate remains in demand, and tenants who recognize the value of the office are willing to pay for it.

We are well positioned to capitalize on mispriced investment opportunities arising from this market and we will continue to position the portfolio to provide stable income and value creation to our unitholders.

I will now hand it over to Charles for some additional highlights.

Charles Peach, Chief Financial Officer

Thank you, Steve. In the second quarter of 2022, the REIT paid a distribution yield of 8.6 percent, and over the first six months of the year, has provided an AFFO payout ratio of 78.9 percent.

Loan-to-value was reduced to 59 percent while FFO, Core-FFO, and AFFO per unit all increased from the first quarter.

The REIT had a full three months of income from the 23 asset Irish portfolio that was acquired in the first quarter of this year. The acquisition was enhanced by the completion and letting of the life sciences development facility in Athlone, an extension of the Irish portfolio's financing facility, to five years.

There are further investment opportunities being evaluated for addition to this portfolio.

I will now hand over for questions.

QUESTION AND ANSWER SESSION

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the star followed by the one on your touchtone phone. You will hear a three-tone prompt acknowledging your request, and your questions will be polled in the order they are received.

Should you wish to decline from polling process, please press star followed by two. If you are using a speakerphone, please lift the handset before pressing any keys. One moment, please, for your first question.

First question comes from Sairam Srinivas from Cormark Securities. Please go ahead.

Sairam Srinivas, Cormark Securities

Thank you, operator. Good morning, guys, and Lindsay. Congratulations on a good quarter. These are some fascinating numbers, and looking through that, from modeling point of view, when can we expect this to actually reflect on earnings?

Steve Hodgson, Chief Executive Officer

I think in 2023, we'll start to see some of that traction. A lot of the leasing that we do at this stage in the year, it's in advance of when the rent starts commencing because there's fixturing periods for the balance of the year. In addition, as we disclosed, SNC-Lavalin vacating 195 The West Mall offsets some of the gains that we've made.

When you look at the quarter, although we declined slightly in occupancy, if you remove the one-time event of SNC-Lavalin vacating, we're actually ahead in occupancy everywhere else in the portfolio. We've been quite pleased with the gains that we've made in Atlantic Canada, and the strength of the oil and gas sector there, driving demand in Newfoundland, and soon to be New Brunswick as well.

Sairam Srinivas, Cormark Securities

Thanks for the color, Steve. That’s a great segue to my next question. I know you mentioned the SNC during the last quarter's call, but were there any other tenants that dropped out as well? I think there's some volatility there as well.

Steve Hodgson, Chief Executive Officer

Nothing of note over the last quarter, Sai. There's an airline industry tenant, Air Transat, at 191 The West Mall, that we had collected a termination fee from about six months ago, and they still have some term, but we're actively trying to lease that space as well.

Sairam Srinivas, Cormark Securities

That makes sense. Thanks, Steve. Finally, my last question is on the financing plan-- can you give some color on the refinancing activity for the upcoming maturities?

Charles Peach, Chief Financial Officer

We keep a close eye on the upcoming maturities. One of the keys that we look for is to ensure that we have a spread that's appropriate over time and over lenders of what we face in front of us. So, Sai, this year, we've already had a refinancing of 11 percent of the portfolio, which was the extension of the Irish facility, which was done over the past quarter. For the remainder of this year, we have 13 percent, I believe, of our debt to refinance.

Though that's on two separate facilities, it gives us the opportunity to take one of those facilities, which is on a floating rate, and potentially convert that to a fixed rate, which helps us from an interest rate risk perspective, too. As we are in discussions with lenders on both of those, I won't go into any further commercial details on those.

For 2023, we have maturities as well within the portfolio. Of those maturities on the mortgage side, we have five, which are spread throughout the year from April to December. At the same time, they're spread between a number of lenders. I mentioned beforehand we look to have a spread of maturities in lenders as well. We have three separate lenders on those.

The revolver is due for maturity next year, and we obviously keep a close eye on where we stand with that, and with the syndicate, to provide that at the same time too. We're in negotiations on our two debt facilities that are due to mature this year at the moment, and we are well aware of maturities that we have coming up next year.

Throughout this, our aim is to ensure we have an appropriate mix of lenders, and at the same time, timings of maturities going forward.

Sairam Srinivas, Cormark Securities

Thanks for that color, Charles. The ECB raising rates just hit morning, are you seeing activity or any impact of that on the transaction activity in Ireland?

Charles Peach, Chief Financial Officer

Not from where we have seen, no. ECB has raised rates from a pretty low level to a slightly higher level at the moment. There is an expectation of future raising of rates. We're not susceptible to the Bank of England changing their rates, which they did about 50 basis points earlier today, as we don't currently borrow in Sterling.

The Euro facility we have at the moment is a three-month floater of Euribor. That's historically been negative since 2015. That recently went slightly positive as well. That's one of the exposures that we might look to hedge.

Sairam Srinivas, Cormark Securities

Thanks for that, Charles, and thanks, Steve. I'll turn it back.

Operator

Thank you. The next question comes from Scott Fromson of CIBC. Please go ahead.

Scott Fromson, CIBC

Thanks. Good morning, folks. Most of my questions were answered in Sai's suite of questions. But can you provide a little bit more color on the leasing spreads, particularly on the new leases?

Steve Hodgson, Chief Executive Officer

The extension of the building in Athlone, Ireland with the life science tenant was a big driver of the increase in rental spreads on new leasing. If you remove the impact of that, we're still overall, from a leasing spreads perspective, in the high single digits. That did have a pretty big impact, but at the same time, it'll have an immediate impact to our earnings as well, and we're quite pleased that it's a long-term lease with a life science tenant.

Scott Fromson, CIBC

Thanks, Steve. On capital recycling, do you have any planned dispositions to augment your capital position?

Steve Hodgson, Chief Executive Officer

As we messaged at the time of the Ireland acquisition, we have been working on about 100 million of dispositions in Canada. We've made great progress on that, and I expect that to occur in the third quarter.

Scott Fromson, CIBC

Great. Thanks, Steve. I'll turn it over.

Operator

Thank you. The next question comes from Jenny Ma of BMO Capital Markets. Please go ahead.

Jenny Ma, BMO Capital Markets

Thanks, and good morning. Steve, you mentioned the potential disposition in Canada for Q3. I'm wondering from a vantage point, you had talked about some opportunities to acquire assets at pretty good values, but how do you think about those opportunities, where they might be, and whether or not buying back stock is in the mix in terms of capital allocation?

Steve Hodgson, Chief Executive Officer

That's the question we discuss with our Board quite often. On the acquisition front—in the markets in which we operate—we don't expect a lot of transaction volume for the balance of the year. I think groups are still in price discovery mode and there's some volatility.

Where we see some opportunities is in some smaller bolt-on acquisitions that are complementary to our existing portfolio, whether that be an asset that might be in one of the business parks that we hold assets in in Ireland, or something in the life science space elsewhere. That's what we're focused on, and it would be a recycling of capital.

What we're working through with our board is the pros and cons of those small, strategic acquisitions versus buying back our own stock, which we agree is cheap right now.

We don't view that as a strategy. We view that as a tactic. Our ultimate strategy is growth because it has many benefits in terms of diversification and getting to a lower cost of capital, but we do see the value when the stock's trading at such a discount.

Jenny Ma, BMO Capital Markets

Great. I just want to run back to the debt stack. What kind of indicative rates are you seeing for some of the near-term mortgage maturities? And could you comment on what the loan-to-values would be for the 2022 and 2023 maturities on the mortgages?

Charles Peach, Chief Financial Officer

Thanks, Jenny. I think what we've been looking to do is keep the loan-to-value broadly similar on those particular loans to where it stands at the moment. They are different assets, but I think one of the keys to remember is that the assets that we are looking to refinance over the next couple of years are assets which are backed by the solid cash flows from the solid tenants who have continued to support those throughout the pandemic, and so on as well, so, they are supportive.

As to the absolute rate, I'd rather not answer that question given we are in negotiations on some of our facilities at the moment. I think post-that, I'll be happy to talk more on number.

Steve Hodgson, Chief Executive Officer

A bit of color on the two mortgages that are refinancing this year—one is in Chicago on our building that's anchored on a long-term lease with CIBC. The other is anchored by a 10-year lease with the federal government in Toronto. So, we feel confident.

We've demonstrated throughout the pandemic where we've done a considerable amount of refinancing, that the banks are very supportive of us as a sponsor, not only as SOT, but also as Slate Asset Management. We do, quite frankly, expect that there'll be some rate impacts given the current environment and the benchmark rates moving, but we think we'll be on a relatively good stand.

Jenny Ma, BMO Capital Markets

So, would you say the LTVs would be similar to that 60 percent level where the portfolio leverage metric is?

Steve Hodgson, Chief Executive Officer

Correct.

Jenny Ma, BMO Capital Markets

Great. How are you thinking about the floating rate debt exposure? I think at this point, perhaps fixing it today is not necessarily worthwhile. With the kind of floating exposure you have, is it just something you're going to navigate through until we get to a more favorable environment? Or is it something you're still considering taking down given the interest rate uncertainty going forward?

Charles Peach, Chief Financial Officer

We always have to consider whether we would take it down at any point. It's whether we actually execute on that. If I look at our unhedged floating rates at the moment, it's split broadly 50/50 between exposure to Canadian floating rates and to Euro floating rates.

If I look at the exposure that we have on Canadian floating rates, it's essentially up across a number of different assets, so, part of that might be driven by what our plan is for those particular assets from a refinancing perspective for the work we might have to do there.

On the European side of things, considering we have a single facility there which we've recently extended out to five years, and that's backed by a solid group of income producing assets, if we were to look to hedge out some of our interest rate risk, that would be the more favorable direction for us to go.

It's something we look at frequently from a pricing perspective and to see how it fits in with the REIT strategy as well. For example, however, if you were to take the European facility and were to hedge that in its entirety, that would change it from being 79.9 percent fixed, or hedged-to-fix, to 90 percent.

Jenny Ma, BMO Capital Market

Great. Last question from me. It says in the MD&A that the parking revenue was up about $200,000 year over year, which is nice to see. I'm wondering how parking revenue is tracking below full potential-- meaning, if we get back to pre-pandemic levels, how much room would there be on the parking revenue front?

Steve Hodgson, Chief Executive Officer

Good question, Jenny. We don't know the answer off the top of our heads. We will get back to you on a subsequent call.

Jenny Ma, BMO Capital Markets

Sure. I'd appreciate that. That's all for me. Thank you.

Operator

Thank you. Once again, ladies and gentlemen, if you do have a question, please press star one at this time. The next question comes from Jas Cumberbatch of TD. Please go ahead.

Jas Cumberbatch, TD Securities

Good morning. I'm on for Jonathan Kelcher. Most of my questions have been answered, but I just have a couple here.

Firstly, the asset that you have for sale in Toronto, do you have any color on the timing and the cap rate for the asset that you have for sale?

Steve Hodgson, Chief Executive Officer

As we said in the last quarter call, it's just shy of 100 million of assets, in the mid-six cap rate range. When we're buying in Ireland at north of a seven-cap rate, assets that have longer term leases, with better credit, with less capital required in the buildings, and overall less tenant risk, that's the kind of trade we're making.

Jas Cumberbatch, TD Securities

Ok. What do you expect occupancy to be by the end of the year?

Steve Hodgson, Chief Executive Officer

I would say pretty flat at this point. Any new leasing that we do would not materialize until the following year.

Jas Cumberbatch, TD Securities

Okay. Lastly, I know you said transactions in the market are obviously very limited right now, but of the transactions that you've seen, have you seen any movement in cap rates? What's the general sentiment out there?

Steve Hodgson, Chief Executive Officer

That's the thing, there's not a lot of data points. We made decisions to keep our IFRS value essentially where they were last quarter. In conjunction with our audit team and our Board. We felt that was prudent. We just haven't seen data points.

I think it's an interesting market now. Everyone's waiting to see what happens in terms of trading. Of course, we always have the view that IFRS value should be a willing-seller, willing-buyer. We're not going to focus on distressed situations, and we just haven't seen a lot of willing-seller, willing-buyer situations to point to.

Jas Cumberbatch, TD Securities

Okay. Thanks. That's it for me. I'll turn it back.

Operator

Thank you. The next question comes from George Huang of Raymond James. Please go ahead.

George Huang, Raymond James

Good morning, team, and thank you for taking my question. What drove the lease termination income in the Chicago portfolio? Any color there you could provide would be very helpful.

Steve Hodgson, Chief Executive Officer

That was a tenant that elected to terminate their space, in which we had notice. We've already got an adjacent tenant that is looking to take that space over. We collect the termination income in advance when they give notice, which is typically six to 12 months out, and then we have time to lease the space to someone else. In this case, it was a change in ownership for that tenant. They decided to consolidate, and it just so happened the adjacent tenant wanted to take over that space, so, it's a good situation.

George Huang, Raymond James

Thanks for that. My follow up would be a question on net effective rent growth and your expectations for the rest of the year. What's your expectation in terms of being able to capture the 7 percent gap between your current in-place rents and the market rents?

Steve Hodgson, Chief Executive Officer

That gap is for the entire portfolio over the next 12 months. I believe the expiries are about 6 percent below market. That would be our expectation. We have opportunities to overachieve that in certain areas. For those of the analysts that attended our property tours in Ireland, you would've seen where we got space back on roll over of tenants and were able to reposition those suites into a higher category of energy ratings. This is a market where there's a direct quantifiable benefit to ESG initiatives because there's an energy rating in which, if you can get to a higher level, it directly garners a higher rent. We're doing that in two instances in our gateway assets in Ireland on the East Wall as well as our City West Business Park buildings.

That's where we'll outperform that number by a considerable amount.

George Huang, Raymond James

Thanks for that. One final question from me. You touched on Atlantic Canada and the recovery that the economy is seeing there. Is there any more granularity you can provide on occupancy recovery from the current 75 percent level, absent any plan dispositions?

Steve Hodgson, Chief Executive Officer

We did 38,000 square feet of new leasing in Atlantic Canada. The bulk of that was in Newfoundland, and one fairly large deal in Saint John, New Brunswick. That's nice to see because those have, quite frankly, been somewhat stagnant with the way the oil and gas sector was performing.

But there's projects kicking off, offshore drilling projects. Obviously, the commodity price is helpful to support those projects. It's a clean way of producing energy. It's priced off a different index. Things are really picking up there, and it's not like we have hundreds of thousands of square feet. We can do small deals every quarter and make quite a bit of ground.

I'm optimistic that by the end of next year, we'll be getting above 80 percent in that Atlantic portfolio and start to see the recovery in rents, as well, as a result.

George Huang, Raymond James

Fantastic. That's all from me today. I'll turn it back.

Operator

Thank you. The next question comes from Anthony Bogdan of National Bank.

Anthony Bogdan, National Bank

Hey, guys. To get back to the leasing spreads in Ireland, are you expecting future leasing deals to continue to yield higher spreads? Or will they be closer to the rest of the portfolio?

Steve Hodgson, Chief Executive Officer

I think that the expiries that we have over the next 12 months we've calculated to be about 6 percent below market. But that's on a current state basis. What I was saying is that there are opportunities—for those that were on the tour in Ireland, they would've directly seen some of these opportunities—where we're repositing buildings or units to a higher standard of energy rating and a higher quality.

As we know, tenants are looking for quality right now and are willing to pay for it. That's where we can outperform that rental growth projection in Ireland.

Anthony Bogdan, National Bank

Got it. Thanks. One more question from me. Have you seen any change in office utilization or foot traffic in Q2?

Lindsay Stiles, Chief Operating Officer

Specific to the GTA, we saw tenants like TD and CIBC formally implement their back to the office strategy. That certainly increased occupancy just generally. For our portfolio specifically, minus summer vacations, certainly utilization was up consistent to the increases we've seen in prior quarters - Q1 versus Q2. As we've messaged previously, we expect a more significant increase in September. A lot of companies are holding off on their official back to the office launch until September when kids are back in school.

Anthony Bogdan, National Bank

Great. Thanks.

Steve Hodgson, Chief Executive Officer

Thank you.

Operator

Thank you. There are no further questions at this time. Please continue.

Paul Wolanski, Senior Vice President, National Sales and Investor Relations

Thank you, everyone, for joining the Q2 2022 conference call for Slate Office REIT. Have a great day.

Operator

Thank you. Ladies and gentlemen, this does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your lines.
