



Crombie

Final Transcript

Crombie Real Estate Investment Trust

First Quarter 2021 Earnings Call

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This transcript contains forward-looking statements about expected future events and the financial and operating performance of Crombie. These statements include, but are not limited to, statements concerning management's beliefs, plans, estimates, intentions, and similar statements concerning anticipated future events, results, circumstances, performance or expectations that are not historical fact. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may", "will", "estimate", "anticipate", "believe", "expect", "intend" or similar expressions suggesting future outcomes or events. Such forward-looking statements reflect management's current beliefs and are based on information currently available to management. Forward-looking information in this transcript includes statements regarding:

- (I) The disposition of properties, including properties under contract, and the anticipated reinvestment of net proceeds, which could be impacted by the availability of purchasers, the availability of accretive property acquisitions, requirements and timing for Sobeys investments, the timing of property development activities or other uses for net proceeds and real estate market conditions;
- (II) Our development pipeline and diversification to mixed-use and residential developments, including statements regarding the locations identified, timing, cost, development size and nature, anticipated yield on cost, and impact on net asset value and net asset value per unit, cash flow growth, unitholder value or other financial measures, all of which may be impacted by real estate market cycles, the availability of financing opportunities and labour, actual development costs, continuance of current market and capitalization rate conditions and general economic conditions and factors described under the "property development/redevelopment" section of our most recent management's discussion and analysis, and which assumes obtaining required municipal zoning and development approvals and successful agreements with existing tenants, and where applicable, successful execution of development activities undertaken by related parties not under the direct control of Crombie;
- (III) Set growth and reinvesting to develop or otherwise make improvements to existing properties, which could be impacted by the availability of labour, capital resource availability and allocation decisions as well as actual development costs;
- (IV) The accretive acquisition of properties, including the cost and timing of new properties under right of first offer agreements, and the anticipated extent of the accretion of any acquisitions, which could be impacted by demand for properties and the effect that demand has on acquisition capitalization rates and changes in interest rates;
- (V) Overall indebtedness levels and terms and expectations relating to refinancing, which could be impacted by the level of acquisition and disposition activity that Crombie is able to achieve, levels of indebtedness, Crombie's ability to maintain and strengthen its investment grade credit rating, future financing opportunities, future interest rates, creditworthiness of major tenants, and market conditions;

- (VI) Generating improved rental income and occupancy levels, which could be impacted by changes in demand for Crombie's properties, tenant bankruptcies, the effects of general economic conditions and supply of competitive locations in proximity to Crombie locations;
- (VII) Expected increase in revenue in 2021 and 2022, which could be impacted by timing of completion of development projects underway, ability to secure tenants and the effects of general economic conditions;
- (VIII) Anticipated replacement of expiring tenancies, which could be impacted by the effects of general economic conditions and the supply of competitive locations;
- (IX) The anticipated rate of general and administrative expenses as a percentage of property revenue, which could be impacted by changes in property revenue and/or changes in general and administrative expenses; and
- (X) Anticipated distributions, distribution growth and payout ratios, which could be impacted by results of operations and capital resource allocation decisions. These forward-looking statements are presented for the purpose of assisting Crombie's unitholders and financial analysts in understanding Crombie's operating environment and may or may not be appropriate for other purposes. These forward-looking statements are not guarantees of future events or performance and, by their nature, are based on Crombie's current estimates and assumptions. Crombie can give no assurance that actual results will be consistent with these forward-looking statements. A number of factors, including those discussed under "risk management" in Crombie's management's discussion and analysis for the year and quarter ended December 31, 2020 and those discussed under "risk factors" in Crombie's most recent annual information form (available at www.sedar.com) could cause actual results, performance, achievements, prospects or opportunities to differ materially from the results discussed or implied in the forward-looking statements. These factors should be considered carefully, and a reader should not place undue reliance on the forward-looking statements.

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Crombie REIT's Q1 Earnings Conference Call. At this time, all lines are in listen-only mode. Following the presentation, we'll conduct a question-and-answer session. This call is being recorded on May 6, 2021.

I would now like to turn the conference over to Ruth Martin. Please go ahead.

Ruth Martin – Crombie REIT, Director, Investor Relations and Financial Analysis

Thank you. Good day everyone, and welcome to Crombie REIT's First Quarter Conference Call and Webcast. Thank you for joining us. This call is being recorded in live audio and is available on our website at www.crombiereit.com. Slides to accompany today's call are available on the Investor section of our website under Presentations and Events.

On the call today are Don Clow, President and Chief Executive Officer, Clinton Keay, Chief Financial Officer and Secretary, and Glenn Hynes, Executive Vice President and Chief Operating Officer.

Today's discussion includes forward-looking statements. As always, we want to caution you that such statements are based on management's assumptions and beliefs. These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially from such statements. Please see our public filings, including our Annual Information Form for a discussion of these risk factors.

I will now turn the call over to Don who will begin our discussion with comments on Crombie's overall strategy and outlook. Glenn will follow with a development update and a review of Crombie's operating fundamentals and results. Clinton will then discuss our financial results, capital allocation, and approach to funding, and Don will conclude with a few final remarks. Over to you, Don.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Thank you, Ruth and good day, everyone. Thanks for joining us for our first quarter conference call.

Despite the continued disruption caused by COVID-19, Crombie continues to pursue our long-term strategy with strong, short-term results. Our long-term strategy has not changed as we remain committed to delivering stability, sustainability, and growth for the benefit of all of our stakeholders. The Crombie team continues to grow and optimize the quality of our grocery-anchored real estate portfolio and execute our development pipeline delivering major developments in Canada's largest cities, while at the same time improving our balance sheet and overall financial condition. In other words, “playing good defense and offense at the same time.” As the capital markets turn their focus from balance sheets and liquidity to growth, Crombie is positioned to continue to perform well.

We have built a very solid foundation for our business. Grocery-anchored retail, retail-related industrial, and for the first time in Crombie's history, residential rental units, continue to be the best classes of real estate in Canada. We have executed our strategy well to deliver solid

fundamentals, driven by high committed occupancy of 96.3 percent and strong leasing performance in the first quarter. Covenant and term are highly coveted especially during times of crisis. Crombie benefits from both the strong and improving covenant of Empire and an overall lengthy weighted average lease term of 9.9 years, which is influenced by Empire's remaining lease term of 13.1 years.

We have significantly de-risked our business by materially increasing liquidity and the weighted average turned to maturity of our debt by leveraging multiple sources of capital, as well as taking advantage of the low interest rate environment.

Over 55 percent of Crombie's annual minimum rent comes from Empire, Canada's second largest grocery retailer. We have aligned our strategies to collectively drive high-quality, risk adjusted growth with Crombie planning to invest approximately \$100 million to \$200 million annually in Empire related initiatives. This alignment includes strategic and accretive investments in the modernization, acquisition, and expansion of grocery stores, including the FreshCo discount format in Western Canada and the Farm Boy banner in Ontario; accelerating Empire's build-out of their online grocery home delivery service, Voilà; land-use intensifications, and the unlocking of major developments.

Voilà operates under a hub-and-spoke network. Orders are filled through large state-of-the-art automated customer fulfilment centres (or CFCs), the hubs of the system. To increase efficiency and expand a CFCs coverage area, a number of smaller cross dock facilities, the spokes of the system, are placed to support each CFC.

Crombie has the opportunity to participate in ownership and development of both hub and spoke locations. The 300,000 square foot Voilà par IGA CFC in Montreal developed by Crombie reached substantial completion of the base building in the fourth quarter of 2020 and is expected to start delivering to customers in early 2022. We are delighted to also be developing their Calgary CFC. Crombie also has multiple opportunities to support Empire with their spoke locations. We purchase land and develop greenfield spoke facilities, or repurpose existing space within our portfolio into a spoke facility. We are capitalizing on these opportunities with the first 31,000 square foot spoke location opening at our Queensway Commons property in Etobicoke, Ontario. As our portfolio continues to evolve, these hub and spoke locations will augment our growing base of retail-related industrial assets and further diversify our income stream.

Crombie is fortunate to have a strong and strategic partner that will not only continue to be a Canadian grocery industry leader for years to come, but will also drive significant value creation in both food retail and real estate over the long-term.

In addition to this work with Empire, we have become a significant developer of major mixed-use real estate in some of the best urban markets in Canada with a target investment of \$150 million to \$250 million annually. These major development projects play a key role in our long-term strategy of accelerating NAV and AFFO growth. Our major development pipeline consists of 29 sites, including five near-term projects. Many of these sites are conveniently located within walking distance of existing and future transit corridors within Canada's largest cities.

Our team and our current partners, Westbank and Prince Developments, have worked diligently and safely to ensure our development projects remained on track and on budget over the last few years, including throughout the pandemic. The quality and diversification of our developments and their economic returns remains of utmost importance. So this is truly a transformational time for Crombie. In 2020, we saw our first four major developments reach substantial completion, making it a landmark year. Tenant move-ins began in November 2020 and our first residential development, Davie Street in Vancouver, officially reached substantial completion in the first quarter. We are very pleased to achieve these key milestones, and with progress continuing on our Le Duke and Bronte Village projects, we expect revenue will continue to ramp up into 2022.

Lastly, and most importantly, as we are in the midst of the third wave of COVID-19, we remain focused on the health and safety of our employees, tenants, and communities. I am incredibly proud of our capable, passionate, and empathetic team and the work they do. Our team has been exceptionally resilient while we have been and continue to be on “defense” but interestingly they are also steadfastly focused on “offense” or achieving high AFFO and NAV growth over the short and medium-term.

With that, I'll now turn the call over to Glenn who will provide an update on our developments and our operational highlights.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thank you, Don, and good day everyone.

Crombie's strong fundamentals on our 287-property portfolio were driven by high committed occupancy of 96.3 percent and strong economic occupancy of 95.5 percent. New leases increased occupancy by 432,000 square feet, while we experienced just 101,000 square feet of net lease expires, vacancies, terminations, and space adjustments. The largest contributor to the new leasing activity in the quarter was a 300,000 square foot Voilà par IGA CFC in Montreal, which commenced paying rent in January. In the quarter, 86 percent, or 373,000 square feet, of new leases were completed in VECTOM or Major Markets, aligned with Crombie's strategy of increasing its presence in these markets.

At the end of the quarter, 147,000 square feet was committed at an average first year rate of \$19.05 per square foot, which will boost future NOI growth throughout 2021. 49,000 square feet of committed space is at our completed major development projects, Avalon Mall, Belmont Market, and Davie Street retail. Another 49,000 square feet is leased to one office tenant at our Scotia Square complex in Halifax, Nova Scotia.

During the quarter, 387,000 square feet of renewals were completed at a 3 percent increase over expiring rental rates. Approximately 60 percent of renewal activity occurred in VECTOM and Major Markets at an increase of 3.1 percent over expiring rental rates.

We are happy to say that 98 percent of our portfolio was open and operating as of March 31. Our team is dedicated to ensuring our underlying business fundamentals remain strong and are able to support areas of the business that are still feeling the impacts of COVID-19.

Since the onset of the pandemic there have been numerous declarations of store closures, CCAA applications, and/or bankruptcies, in the broader market. Our defensive grocery-anchored portfolio is well positioned with minimal exposure to these announced closures with only 25 leases potentially impacted, representing approximately 1.1 percent of annual minimum rent. To date, only three of these leases have been disclaimed or vacated, representing approximately 0.1 percent of annual minimum rent, which indicates the strength and resilience of our properties.

Property development is a strategic priority for Crombie as it drives NAV and AFFO growth, while increasing our presence in the country's top urban markets and diversifying our overall portfolio.

We are thrilled that our first major mixed-use development, located in the West End of Vancouver, reached substantial completion earlier this year. Zephyr, the residential component of Davie Street, is owned in partnership with Westbank and contains 330 residential rental units. Surrounded by amenities, Zephyr is built to LEED Gold Equivalent standard and contains a public art feature to enhance the streetscape. Lease up has been strong with initial move-ins beginning in November 2020. As of April 30, 62 percent, or 204 units, have been leased. The skilled team at Westbank continues to work hard despite the ongoing COVID-19 related challenges, with an expectation to reach stabilization by the end of 2021.

Progress is made at our Le Duke and Bronte Village projects as they remain on track and on budget. Substantial completion is expected to be achieved in the third quarter for Le Duke and the fourth quarter for Bronte Village.

We are committed to unlocking significant land value embedded in our major urban market grocery stores as we continue our work to entitle upwards of ten additional projects across Canada, generating opportunities to continue our development program.

As Don noted, Empire recently announced the expansion of their online grocery home delivery service Voilà to Western Canada. Crombie is very pleased to be involved in the upcoming development of Empire's third CFC, located in Calgary. This project is expected to be added to our pipeline in the second quarter of 2021, upon acquisition of the land.

We have also completed property acquisitions and have been active in our capital recycling program. In the first quarter, Crombie acquired six income-producing properties and one development property, for a total aggregate purchase price of \$46 million. Five of the seven acquisitions are located in VECTOM or Major Markets. We concluded the disposition of three income-producing properties for total gross proceeds of \$42 million.

And with that, I will now turn the call over to Clinton who will highlight our first quarter financial results and discuss our capital and development program funding approach.

Clinton Keay – Crombie REIT, Chief Financial Officer and Secretary

Thank you, Glenn, and good day everyone.

Crombie continues to reduce risk and maintain financial strength with a strong and flexible balance sheet, ample liquidity, creatively sourced capital, and prudent capital allocation.

Despite the recent lockdowns and increased restrictions across different areas of the country, strong collection rates continue with 98 percent collected in the first quarter of 2021, and 98 percent for April. This is on par with our fourth quarter collections and a reflection of our stable portfolio.

On a cash basis, same-asset NOI increased by 2.2 percent. Primary drivers of this growth are strong occupancy, modernization income, reduced bad debt expense, and lease termination income. Excluding COVID-19 related adjustments, such as bad debt expense, rent abatements, and a decline in parking revenue, same-asset NOI would have increased by 3.8 percent for the first quarter.

For the quarter, AFFO per unit was \$0.25 and FFO per unit was \$0.29. AFFO and FFO payout ratio were 90.8 percent and 76.4 percent, respectively. FFO in the quarter was impacted by improving net property income, partially offset by higher G&A and finance costs. G&A in the quarter was negatively impacted by the effects of unit-based compensation of approximately \$0.01 per unit.

G&A as a percentage of property revenue for the first quarter was 4.9 percent or \$5 million. G&A excluding the impact of unit-based compensation expense would be 2.9 percent.

Our unencumbered asset pool is approximately \$1.4 billion or 28 percent of Crombie's total assets of \$4.9 billion. Our debt to gross fair value net of cash at the end of Q1 was 48.3

percent. The increased fair value of investment in joint ventures from the completion of Davie Street Residential is a primary driver of the decrease in leverage ratio during the quarter. We ended the quarter with debt to trailing 12-month EBITDA net of cash of 9.58x. This increase is primarily impacted by the spending on development with no income until project completion. Trailing 12 months EBITDA was also disaffected by bad debt provisions taken over the past 12 months.

Looking ahead, we are focused on a continuous improvement of our balance sheet while also retaining flexibility to pursue strategic growth initiatives. During the quarter, we renewed our \$130 million unsecured credit facility now maturing June 30, 2023. \$225 million of our total debt is maturing during the remainder of this year at a weighted average interest rate of 4 percent. Included in this is \$150 million of unsecured notes maturing on June 1, 2021, and \$75 million of mortgages maturing in the fourth quarter.

Crombie is committed to delivering value through NAV and AFFO growth and strategic allocation of capital, while providing support to our employees, tenants, and communities, through an ever-changing environment.

I will now turn the call over to Don for a few closing comments.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Thank you, Clinton.

As we look ahead, the challenge of COVID-19 remains. However, we are committed to our long-term strategy and the safety and well-being of our stakeholders remains a priority. We expect our stable grocery-anchored portfolio and financial strength, together with our resilient team, to continue to work closely with Empire to unlock value, while supporting the business and continuing to grow and develop Crombie.

We are confident in the future we are building at Crombie. Our Q1 results were solid and we're excited by our future opportunities.

That concludes our prepared remarks and we're now happy to answer your questions.

Q & A

Operator

Thank you. Ladies and gentlemen, we'll now begin the question-and-answer session. Your first question comes from Mario Saric from Scotiabank. Mario, please go ahead.

Mario Saric — Analyst, Scotiabank

Hey, good afternoon.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Good afternoon, Mario.

Mario Saric — Analyst, Scotiabank

Just maybe with respect to the substantial completion, can you highlight how much NOI was included in the quarter, if any, at all, and the full impact of transferring to substantial completion during the quarter?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thanks, Mario. It's Glenn. I think in the notes to the financial statements, I think it's around note four or note five, we break out for Davie, now that it's completed. On Page 10 of the financial statements, it shows the revenue with property operating expenses, etc.

We're showing for Davie in the quarter, a net loss, our share of about \$889,000. That reflects the revenue in place based on the initial lease up, and obviously, as the year progresses, that will continue to improve as we continue to lease-up and achieve stabilization by the end of the year.

Mario Saric — Analyst, Scotiabank

Yes. Okay. Thank you for that. I'll take a look. Then maybe shifting gears to the bad debt expense, which is fairly minimal again this quarter, how much of the 0.6 percent would have been attributable to Avalon Mall?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

I would say attributable to Avalon Mall, I can get that easily because it is the portion that is not in same-asset NOI. There's a table in the press release that shows the impact. On Page 3 of

the press release, we show the bad debt expense impact of \$227,000. So of the \$648,000, Mario, of bad debt expense, about \$400,000 of it is in properties that are not in same asset. I would say that's probably almost 100 percent Avalon Mall.

Of the \$648,000, \$400,000 would be Avalon Mall, \$220,000 is properties that are in the same asset category.

Mario Saric — Analyst, Scotiabank

Got it. Okay, and a REIT peer of yours earlier this morning noted improved lease residential rental demand in Newfoundland recently. Maybe, post-quarter, what are you seeing with respect to that collection of bad debt expense at Avalon Mall thus far? Are you seeing any notable trends there?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

We're delighted. Avalon Mall is 99 percent open. Today, 99 percent of tenants, I think as Clinton mentioned, 98 percent collection in the quarter. Our traffic counts at Avalon Mall right now we're at pre-COVID levels essentially. There's still a few tenants that are challenged.

As you know, Newfoundland was shut down for part of February. We did see a bit of a blip in the quarter through February, but sitting today, we're 99 percent plus of our tenants are open. I suspect Avalon Mall is probably one of the top performing malls in the country right now based on Newfoundland's great success with COVID. In St. John's, Newfoundland, we're in very strong position at Avalon Mall.

Mario Saric — Analyst, Scotiabank

Great. Okay. All right. Well, my last question just pertains to the disclosed hub and spoke strategy. I'm assuming that the expected capital deployment there would be included in the \$100 million to \$200 million per year referenced by Don at the start of the call.

How do we compare return potential on that capital spend relative to the more traditional store modernization trends?

Don Clow — Crombie REIT, President and Chief Executive Officer

There'll be—most likely the spokes are in the \$100 million to \$200 million that we're targeting for Sobeys initiatives because they're generally smaller. The major developments are where they're over \$50 million, is the way we characterize them.

The returns, we have had very solid, we call them solid risk adjusted returns where we've seen returns, I'll call it in the 6 to 6.5 percent yield on cost. That's probably a fair target for these types of investments, and they are, I'll call it similar in methodology for the most part to the modernizations and expansions. Yes, that's about all I'll give.

Mario Saric — Analyst, Scotiabank

All right, and the recent Burlington land...

Don Clow — Crombie REIT, President and Chief Executive Officer

We can't comment on it at this stage what that land is for, unfortunately.

Mario Saric — Analyst, Scotiabank

Okay. Sure enough.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Okay. Thank you.

Clinton Keay — Crombie REIT, Chief Financial Officer and Secretary

Mario, are you still on the call? I just wanted to clarify Glenn's comment. He had said that the numbers in note four were our share, they are actually 100 percent of the JV, we would have 50 percent of the numbers in that note.

Operator

Okay. Mario is no longer in the queue, just so you know. Your next question comes from Sumayya Syed from CIBC. Please go ahead.

Sumayya Syed — Analyst, CIBC

Thanks. Good morning, everybody. Just a couple of questions on the hub and spoke model. It looks like the options are to do it either Greenfield or repurpose existing space. What option would you feel is more attractive? Then for repurposing, I guess, as you survey your portfolio for potential space that could work, what do you look for in terms of market and just the physical attributes of the space?

Don Clow — Crombie REIT, President and Chief Executive Officer

The selection of the space is driven by artificial intelligence in terms of maximizing the productivity of the network. We're very fortunate to be working closely with Sobeys in terms of their network intelligence and understanding that AI, and therefore being able to source sites. Clearly, if we have a site that the AI would say it's an area where it's good and we have a site ourselves, and then we start looking. We've announced that the site in Etobicoke will be converted and it was a former CRU tenant of ours and not a Sobeys store. That one fit very nicely for us and the returns and costs, etc., worked for us and so we are converting that. There will be others that are Greenfield. Essentially, again, we're looking for returns in that 6 to 6.5 percent yield on cost in terms of the overall program and each individual site, depending on where it is. As you get into the centers of the major cities in the country, that's going to be more and more challenging to deliver, but also potentially more and more impactful in terms of returns. We're still working very closely, as I said, with Sobeys to try to figure out the economics on those, but we're excited about it because they think it's one of the most strategic parts of their business and we're excited to be a part of it and providing solutions.

Sumayya Syed — Analyst, CIBC

Absolutely. Thanks for that, and then you spoke a bit about just the strength at Avalon Mall and it looks like same store sales were up about 10 percent. Just any more colour there. Were there a couple of significant drivers or you just saw more broad-based improvement from all the tenants there?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

I would say, Sumayya, it's a broad base, but what's really cool at Avalon now is the opening of the tenants. We've had a Sport Chek open recently, Tommy Hilfiger, GAP/Banana Republic. It was a really great halo effect now that the racetrack phase II expansion area of the mall is open. We're having the influx of these first two Newfoundland and Labrador tenants. That's causing a great buzz in the mall.

Of course, we had the other retailer, the European retailer, that's escaping me right now, that opened last November, that is doing great business. I think we're seeing a broad-based strength in the mall and that's how I would describe it.

Sumayya Syed — Analyst, CIBC

Okay. Just lastly...

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

H&M was the tenant I was thinking of. Sorry, H&M is the tenant opened late last year.

Sumayya Syed — Analyst, CIBC

Okay, great, and just lastly, as sort of a minor detail point, but there was about some lease termination income of around \$1.5 million in the quarter. Just wondering what that pertained to.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Sure. Interestingly, it's not COVID-related, first of all. I think we indicated in our script that we had about 25 leases across the country that had been subject to disclaim or CCAA. Of those 25, only three have resulted in a tenant departure, which is 0.1 percent. Those were in my early remarks. There was about half a dozen lease terminations in the quarter and I will characterize a few of them. A few were at Avalon; tenants that had made plans to depart the mall and departed and we get compensated in the quarter. One in Halifax for about \$400,000 was an office tenant where an M&A transaction of another tenant that we had, bought the tenant in another one of our buildings and decided to consolidate and paid us out.

There was another, a small call centre tenant in Atlantic Canada. It was a bit of a mixed bag, but nothing specific that was, I'll call it COVID directly related. These were plans that were put in place before, but it did add up to about \$1.5 million in the quarter.

Sumayya Syed — Analyst, CIBC

Okay. That's very helpful. Thank you.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Thank you.

Operator

Your next question comes from Tal Woolley from National Bank Financial. Please go ahead.

Tal Wolley — Analyst, National Bank Financial

Hi, good morning, gentlemen.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Hi, Tal.

Tal Wolley — Analyst, National Bank Financial

Just as a refresher for me, I don't cover any of the other apartment REITs, the rent control laws for BC, how should we be thinking about rental growth there over time as that asset develops?

Don Clow — Crombie REIT, President and Chief Executive Officer

The long-term rental growth in Vancouver has been low single digits, about 3 to 5 percent. That's one of the main reasons in the long-term that we felt this investment was extremely important for us. We continue to try to grow our AFFO and, ultimately, through growing our rents. The rental growth there, there's been a pause. There is rent control effectively this year, announced a while ago. I think it was last fall. It was one of the reasons we've gone out to market at higher rents than maybe we would originally anticipate because that was in place and we weren't certain how long it would last. We're still not quite certain, but I think on a long-term basis with tremendous macro-economic factors, demographic factors with immigration, and I think Vancouver will be a fantastic place to invest on a long-term basis. We're continuing to look

at it. For Davie Street in particular, starting with a higher than proforma number that we're quite pleased with, and our partner Westbank has done an outstanding job delivering a product that had been very well received in the market. I think on a long-term basis, rental growth will I think revert to significant levels on a national basis I think in that 3 to 5 percent level. I don't know if I can tell you more. I can't really predict the future, Tal, but my gut sense.

Tal Wolley — Analyst, National Bank Financial

That's helpful. Thank you. For the spoke facilities, so I just understand what's going on there. This is a case where you have one large carrier coming in, dropping off. Is it effectively a cross dock facility between one carrier into a bunch of local carriers, or is there actual activity like packing and stuff like that going on in these spoke facilities?

Donald Clow — Crombie REIT, President and Chief Executive Officer

No, it's a cross dock. I mean, if you think about it, let's take an example, our new Montreal CFC, there's an order from Quebec City, and because it's in a, whatever, a couple hours away or whatever, it's loaded on an 18 wheeler, shipped to Quebec City, and there's a cross dock facility there that's a spoke where it's broken down, put into a cube van and then delivered to the home.

In and around the major centers in the country, Empire has not disclosed to date how many spokes that they'll have, but I think there'll be a fairly significant number given the dispersion of the population.

Again, it's driven by artificial intelligence, which will tell them the optimization of how to deliver profitably, which I think is the big issue in delivering low margin products like groceries, is that even the largest players in the world can't do that profitably at the moment and have to—I think Ocado is really doing it profitably in the U.K. and bringing that methodology to Canada through Sobeys. We have great hope that this whole network ultimately will drive some very significant profitability for Empire and be very successful.

Tal Wolley — Analyst, National Bank Financial

If you were to use some of your existing shopping centers to locate some of these, it's not seen as like a different use? Like it all fits within zoning, it's not a big deal to do, or if it might take a little bit of work, you're not that worried about it?

Donald Clow — Crombie REIT, President and Chief Executive Officer

We're not worried about it at all. Generally, it fits within the use. We are smart enough to figure it out in terms of figuring out the traffic flow, and the civil engineering and the parking, which is really, you've got parking of cube vans, etc., and putting those in place, placing those in areas where it doesn't affect foot traffic for the adjacent retail which is what we're doing in the current location, the first one that we're doing.

Tal Wolley — Analyst, National Bank Financial

Okay, and then just maybe right now, I know in the Maritimes there's been some restricted activity that's happened, unfortunately. Can you just give us a rundown for how things

are kind of evolving right now and whether we should have any real concerns about just lockdown activity and stuff like that for the next quarters?

Donald Clow — Crombie REIT, President and Chief Executive Officer

I'll speak generally to it. We're in lockdown in Nova Scotia, but the other three provinces are doing pretty well. We've got on it early here in Nova Scotia. The government and departments of health have done, I believe a very good job of managing the pandemic for the last 14 months and getting on it early has proven successful in the past I think not only for Nova Scotia, but New Brunswick and Newfoundland.

We're hopeful, we're still waiting to see numbers come down. They're still ramping up, but our test positivity rate is very low. I think we're still less than 1 percent. I saw our number was 0.78 percent, which is much lower than some of the provinces in Central and especially Western Canada. We've done a lot of testing and the community has got together and really become, I think the norm now is to be tested on a regular basis in addition to ramping up vaccines to a high level.

We're hopeful, but again, in New Brunswick, PEI, and Newfoundland, we're open as Glenn said earlier, and all of our retail. I think one of my peers had a great joke. He said, the best retail is open retail. We've been fortunate, especially with Avalon to have that, and where we have— in areas of lockdown, we're an essential service, so we've been relatively in good shape.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

I'd like to just add to that, we were running around 98 percent open for the portfolio, and with the recent lockdown activity I think the last stat I saw we're about 93.3 percent. I would say the Halifax lockdown and Nova Scotia lockdown is a factor in that, but we're still pretty satisfied that 93.5 percent of our tenants open and doing business, but that's off a high of about close to 98 percent.

Tal Wolley — Analyst, National Bank Financial

Okay, and then just my last question, prior to the world kind of going into chaos the last 12 plus months, you guys were sort of setting up longer-term financial guidance for the street at sort of that 3 to 5 percent NAV growth, 3 to 5 percent FFO per unit growth.

Obviously, a lot's changed, you've sort of continued to move things forward. Do you still sort of feel comfortable with that, or any sort of changes around how that sort of prior guidance looks a year plus later?

Donald Clow — Crombie REIT, President and Chief Executive Officer

Yes, no, I'm comfortable with it Tal. That's a best in class measure in my mind and I think we've been at the lower end of that. It's really trying to get into the upper end of that range of both NAV growth and AFFO growth.

The nature of the portfolio, which is one of the strongest in the country, we've evolved it over the last decade, really managed the portfolio well to a position of strength as you're seeing with both in a time of defense and a time of offense as we commented in our script.

As we transition to having 10 percent of our portfolio in the next year or two being residential, which has very high occupancy rates and very strong rental growth, we've got 10 percent of our business roughly being retail-related industrial, which is full, we just continue to evolve our portfolio towards essential services and grocery-anchored retail. We think they're the three best asset classes in the country at the moment.

Given the transition, we can achieve those kinds of growth. The spending and work with Sobeys is critical too, to improve their network, which some people, again, don't understand, but it's really trying to improve their competitiveness. Our ability to invest with them also drives growth on a consistent basis if we're able to achieve those spending targets, so yes, we're pretty confident still.

Tal Wolley — Analyst, National Bank Financial

Okay. That's great. Thanks very much, gentlemen.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thanks, Tal.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Thank you.

Operator

Your next question comes from Jenny Ma from BMO Capital Markets. Jenny, please go ahead.

Jenny Ma — Analyst, BMO Capital Markets

Hi, everybody.

Don Clow — Crombie REIT, President and Chief Executive Officer

Hi, Jenny.

Jenny Ma — Analyst, BMO Capital Markets

I wanted to ask about the spoke specifically at Queensway Commons. I'm not sure if I missed it earlier in the call, but how does that align with the store that's currently there? Is it in the same property or is it a couple blocks over?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Yes. There's no grocery store, Jenny, on that site. I think the 31,000-foot space that's at the Queensway was a former golf store or I believe it was, so it was vacant space. There is a Sobeys store in the neighborhood, but this spoke would be serviced by the Vaughan CFC. It is the first spoke facility that Sobeys has opened in GTA and there's obviously more to come.

Jenny Ma — Analyst, BMO Capital Markets

Okay. If I'm understanding it correctly, with the spoke facility, it's part of the Voilà ecosystem, right? There's no back and forth with any stores that might be close by, is that correct?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

That's correct. The second part of the Voilà program, though, is a curbside pickup program that's using some of the same Ocado Voilà technology. They're rolling that out, but no, the hub and spoke program is separate entirely from grocery store in terms of grocery store involvement. It's order is being assembled at the hub, and as Don mentioned, transported to the spoke, which is a cross dock facility put into delivery vans for the last mile delivery.

Jenny Ma — Analyst, BMO Capital Markets

Okay, and I realize, with this being the first one, you might not want to get too specific about the details, but when we think about rents on these spokes, they're classified as an industrial property and I guess it depends on what the use of a former unit would be, but how does that rent sort of fall between that retail to industrial spectrum?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Yes, and basically, it's just that our, as Donnie mentioned, the return that we're getting is a function of 6 to 6.5 percent yield on cost. It's really the rent will fall out of the capital costs that are involved. Obviously, the rents will vary depending on the size of the spoke and the capital costs to get it ready.

They're relatively simple because their cross-dock facilities, that they are to receive orders and then to quickly turn them around through the delivery vehicle. That's all I'll say. I won't give you any dollar specifics, but it's based on a yield on cost, which is very accretive for Crombie.

Jenny Ma — Analyst, BMO Capital Markets

Okay. Got it, and how long does it typically take to get a spoke ready from a box that you already have?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

It varies. The one that we did on the Queensway was probably about a year in the works. It was in that range, and some of the other spokes we'll do will vary. The first one that we have completed is in the range of about 12 months from beginning to end. There was some municipal approval process there as well. That's sort of an order of magnitude.

If we're starting from buying land and developing, then it could be a little bit longer than that, obviously, Jenny, but in this case, a little more efficient because of dealing with a pre-existing structure, as long as approvals are in place on a time efficient basis in and around that 12-month range.

Donald Clow — Crombie REIT, President and Chief Executive Officer

It's one of the key features of our development pipeline. As you know with the major mixed-use developments, they can sometimes take three to five years, whereas some of these

industrial developments are taking us 18 to 24 months, in the case of spokes, as Glenn said, 12 to 18 months, but they allow us to, call it modulate, the spending in our pipeline.

As we've set these targets, as we evolve both the mixed-use pipeline, that's larger commitments, longer periods of time, clearly riskier, but with a higher NAV pickup, but then these are the industrial hubs and spokes are shorter timeframes with, call it better, or call it risk adjusted returns, and short timelines.

It's a really nice balancing act for Crombie to be able to manage our spending levels and manage our commitment levels as we look forward and try to develop a very mature development program. It's a nice feature.

Jenny Ma — Analyst, BMO Capital Markets

Definitely. That's very helpful. Thank you. Moving over to the bad debt, I realize we're talking small numbers here, but it did pick up from Q4 2020. I'm just wondering what the moving parts were and if there were any specific one-off tenants that may have driven that change.

Clinton Keay — Crombie REIT, Chief Financial Officer and Secretary

Jenny, it's Clinton. I think the little, I call it a minor blip, would have been that we had the Avalon Mall closed for a period of time in the quarter. I think that's what you could attribute it to, but nothing...

Jenny Ma — Analyst, BMO Capital Markets

Okay. Great.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

We're all quite happy our expense, as Clinton mentioned, Jenny, 0.6 percent of revenue, I think stacks up pretty well amongst the peers and we're pretty satisfied in collections, in that 98 percent range, we're cautiously optimistic from here.

Jenny Ma — Analyst, BMO Capital Markets

Yes, definitely, and then my final question is, in the MD&A with regards to the disposition, I'm not sure if I'm not reading it correctly, but it said in the footnote that the net property income last year was \$11 million on the \$42 million of disposition. Can you walk me through what the gap is there?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

That sounds—is that in the MD&A or the financial statements?

Jenny Ma — Analyst, BMO Capital Markets

It is in the MD&A.

Clinton Keay — Crombie REIT, Chief Financial Officer and Secretary

Jenny, we'll get back to you on that.

Don Clow — Crombie REIT, President and Chief Executive Officer

Yes, we'll get back to you on that, Jenny.

Jenny Ma — Analyst, BMO Capital Markets

Okay. Sounds good. Thank you very much.

Clinton Keay — Crombie REIT, Chief Financial Officer and Secretary

Okay. Have a good afternoon.

Operator

Your next question comes from Pammi Bir from RBC Capital Markets. Please go ahead.

Pammi Bir — Analyst, RBC Capital Markets

Thanks, and hi, everyone. Sorry, my apologies. I did miss the opening remarks at the start of the call, but maybe just on Zephyr. Can you just comment on the impact it has from a fair value perspective in your debt to gross value calculation relative to maybe the costs that are shown in the notes?

Donald Clow — Crombie REIT, President and Chief Executive Officer

What we'll say, Pammi, is that we're taking—we benefited from a partial recognition of the NAV creation at Zephyr. We're not going to get into specific property by property numbers, but we have provided some ranges, as you know, on our Investor Day back in 2019 when we could all get together.

Those ranges are all holding and we've said, I think in recent IR, \$1.30 to \$1.80 a share, which is what, \$200 million to \$280 million in NAV creation potential in the first six. What we've recognized to date is a portion of Davie Street to date and I think a portion of the Montreal CFC that was completed in Q4 is what's so far been recognized.

You can see it helping us move our debt to GBV on fair value basis down quite nicely, which is what our plan was all along. I apologize, but we're just not prepared to give property specific information on that front, if that's okay.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Pammi, if you look in the financials, you'll find some colour on that. If you want to have a read there, you'll see some details on fair value.

Pammi Bir — Analyst, RBC Capital Markets

Got it. That's helpful, and presumably, as this property gets stabilized over the course of the year, then I presume you would ultimately pick up the full fair value recognitions, right?

Donald Clow — Crombie REIT, President and Chief Executive Officer

Oh, yes. That's right. In fact, Pammi, Westbank's been doing a heck of a job out there in terms of lease-up and the rates were higher than our original proforma. We're hopeful that'll continue. If it does, there may be additional pickup, but it's still too early to tell.

Pammi Bir — Analyst, RBC Capital Markets

Yes, I know the leasing does look pretty well considering, I believe, it only started last fall and I think still with everything that's been happening from the pandemic standpoint, so that's good to see.

Donald Clow — Crombie REIT, President and Chief Executive Officer

Those are cap rates on resi have compressed of Vancouver as you know. CBRE's latest report end up 2.25 to 2.75. It's an improving market, I think for us, improving market circumstances.

Pammi Bir — Analyst, RBC Capital Markets

Got it. Maybe just switching gears, coming back to the lease termination, just to clarify, was any of that related to, I believe, the Walmart, the Topsail, I believe that's one of the closures in your portfolio, but just anything you can share there? Then just prospects on perhaps releasing that space.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Sure. Topsail Road Walmart is our one and only Walmart in the country. Ironically enough, it's got about 12 years left of remaining term so we're not worried at all, but there's no lease termination income in the quarter relating to—that store's still open. I think we have an idea when the closure date will be. It's coming, but as you know from many of those old Walmart leases, Pammi, rents are relatively low. This is an 85,000-foot store. It's in a grocery-anchored center with other great tenants, Sobeys, banks, etc. We will take our time and come up with a

redevelopment play there that'll be, I think, quite accretive to both AFFO and NAV. Until we sort that out, we'll be paid rent in the ordinary course.

Pammi Bir — Analyst, RBC Capital Markets

I see, and have they provided sort of the, I think at what point that store will actually close?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Yes. I believe it's sometime this year. I think they've been public about that in terms of the closure date. From there, they say there's 12 years left in the lease. They don't have a must-operate clause, obviously, but they have to continue paying rent and we will evaluate next steps at the appropriate time.

Pammi Bir — Analyst, RBC Capital Markets

Got it, and then just lastly, just with some of the other terminations that you mentioned, some smaller stuff, just generally speaking, the timing of when perhaps you think you'd be able to get some of that space backfilled?

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Good question. Actually, the office space in Halifax, we've got prospects for. The call center space that's in Atlantic Canada, no current prospects, and we've got avid prospects for Avalon Mall. We've got some tenants there that want to expand. I mentioned earlier about some

of the first two Newfoundland and Labrador tenants that have recently opened, but the spaces at Avalon, we're feeling really strong about and probably the majority of the lease termination income around half of it would have been related to Avalon Mall. We're feeling very good about that.

Pammi Bir — Analyst, RBC Capital Markets

Got it. Thanks very much, Glenn. I will turn it back.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thanks, Pammi.

Operator

Your next question comes from Sam Damiani from TD Securities. Sam, please go ahead.

Sam Damiani — Analyst, TD Securities

Thanks, and good afternoon, everyone.

Don Clow — Crombie REIT, President and Chief Executive Officer

Hi, Sam.

Sam Damiani — Analyst, TD Securities

Just to start off on the developments with the three new projects would have added to the near-term pipeline. How should we think about yields on those relative to the recent Davie Street specifically, and Le Duke which is coming up for completion shortly, where you were kind of in the mid fives, roughly on average for these residential projects historically? How do you think about yield going forward on Broadway and Commercial and the one in Halifax?

Don Clow — Crombie REIT, President and Chief Executive Officer

Sam, we think of the yield still in the fives, depending on the nature of the development. We would typically obviously target, I think it's maybe aggressive, but we do it anyway, it's probably 150 basis points over acquisition cap rates, but we've managed well over that in Vancouver to date.

There is certainly pressure in terms of construction costs at the moment and so we're still working very hard. We haven't committed to the large projects at this stage, but we're working very hard to ensure we're forecasting, I'll call it conservatively. That might compress the yields on cost to some degree, but so far, to date, we've been able to, and we are basically on target and on budget, and we've benefited from rental increases and cap rate compression. In the future, to date, we're still seeing the ability to pass on those cost increases to consumers through rental increases. When we first started looking at some of these projects, a year or two ago, cap rates were higher for these types of projects, like Broadway and Commercial. We think, all in all, we're still in good stead and can make them work and moving forward, having committed but working towards that with our partner, Westbank, on East Broadway, an example, but we are

seeing inflation that's running at a higher rate and it has been volatile. It's something where we're very conservative in our predictions and we'll continue to be, going forward.

Sam Damiani — Analyst, TD Securities

Thank you, and just to be clear, I mean, you've put 1780 East Broadway on the near-term list because your intention is 100 percent to commence construction on that one next year, barring any crazy unforeseen situation, based on your current assessment of the market, on both the revenue and the cost side, that one is a go. Is that right?

Don Clow — Crombie REIT, President and Chief Executive Officer

No, Sam. What I would say is that we're working very closely with Westbank and the City of Vancouver and looking to get the project approved. Until that happens, obviously, it's not. There's no such thing in development as 100 percent certainty.

There's still work to do and before it's finally approved, obviously, Westbank and ourselves will need to have everything up-to-date in terms of cost forecast and revenue forecast. There's a portion of that that's condominium pricing, etc. Still work to do to have the project be 100 percent committed and it won't be committed until we actually sign the contract to commence construction. For us, we have, I'll call it off ramp if the market changes for the negative and that's normal in development, especially with sophisticated developers like Westbank and ourselves, if you're basically trying to make sure you've got that clear picture to profitability.

In our case, we like those mid five returns on assets that have a three-cap handle when it's finished. That's for us, we look at it as a very significant margin of safety when we actually make the commitment. Anyway, we're continuing to work forward on it and we'll be comfortable when we do it and we bring it to our Board for final approval.

Sam Damiani — Analyst, TD Securities

Right, but the market, as it is today, it would be a go if everything was ready to go?

Don Clow — Crombie REIT, President and Chief Executive Officer

We think the market conditions are solid. As I said, we're concerned about cost increases, but we are seeing rental increases and we think the product really fits the market. Westbank had a spectacular design, but we still have work to do with the city. Until we get to the final point with the city, then that that's not determinable. We're getting closer, but we still have work to do.

Sam Damiani — Analyst, TD Securities

Got you, and last one from me, and I'll listen to the replay if this has already been asked, but certainly the lease up at Zephyr has been quite strong, and congratulations to you and your partner there. I guess given the pace of the lease up, did you go out with an asking rent that was perhaps a little lower than you initially hoped to just—in order to get the velocity? How do the rents that you have achieved to date compare to your pre-COVID expectations?

Don Clow — Crombie REIT, President and Chief Executive Officer

Yes, the rents that we'd gone to market with are much higher than our original proforma and so we would have set our proforma four or five years ago and then revisited it last year. Once the province brought in rent control, we actually went to market with higher rents because we knew we wouldn't get growth for a year, maybe, we weren't sure if it would be even more than that. The market's been very receptive. In fact, we're just looking at increasing our rents beyond that number. There is no discounting to get pace. In fact, we're out to market with rents above our proforma and we're still exceeding our expectations in terms of lease-up. Leasing is broad-based in terms of across the unit, so we've got lots of quality in its lap and it's just going very well. Westbank does an outstanding job in terms of the marketing and model suites and we've benefited as a team from that.

Sam Damiani — Analyst, TD Securities

Congratulations. Thank you. I'll turn it back.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thank you.

Operator

Ladies and gentlemen, it appears there are no further at this time. Please proceed.

Ruth Martin — Crombie REIT, Director, Investor Relations and Financial Analysis



Thank you for your time today and we look forward to updating you on our progress on our Q2 call in August. Stay safe and healthy.

Glenn Hynes — Crombie REIT, Executive Vice President and Chief Operating Officer

Thanks everybody.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines.