CORPORATE PARTICIPANTS

Steve Hodgson
Chief Executive Officer

Charles Peach
Chief Financial Officer

Paul Wolanski
Senior Vice President, National Sales, Investor Relations

CONFERENCE CALL PARTICIPANTS

Sairam Srinivas
Cormark Securities

Jonathan Kelcher
TD Securities

Brad Sturges
Raymond James

Jenny Ma
BMO Capital Markets

Matt Kornack
National Bank Financial

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Slate Office REIT Third Quarter 2022 Financial Results Conference Call.

At this time, all lines are in listen-only mode. Following the presentation, we'll conduct a question-and-answer session. At any time during the call, if you require immediate assistance, please press star-zero for the operator. This call is being recorded Wednesday, November 2nd, 2022.

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

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

Thank you, operator, and good morning, everyone. Welcome to the Q3 2022 conference call for Slate Office REIT. I'm joined this morning by Steve Hodgson, Chief Executive 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 Q3 2022 investor update, which is now available.

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

Steve Hodgson, Chief Executive Officer

Thank you, Paul. Good morning, everyone. In the face of sectoral headwinds, including a rapid rise in interest rates not seen in many years, Slate Office REIT continues to demonstrate its resilience, offering unitholders a stable and attractive distribution yield, trading upside to its well-supported net asset value, and a best-in-class management platform.

Our conviction in the office sector remains strong. We know that physical workspace enables collaboration, culture, and innovation. At the same time, we understand that in a post-pandemic era, certain tenants and industries will be more significant users of office space than others.

As such, we will continue to position our portfolio to focus on opportunities that align with tenant demand. We believe well-located, high-quality, and modern office buildings with growing, strong credit tenants will continue to outperform.

The REIT's investment activity during and subsequent to the quarter is a great example of portfolio repositioning. We disposed, at a very attractive price, an older property in Toronto that has tenant and capital risk, and we purchased a higher yielding newer asset in Chicago anchored by a long-term lease with Pfizer, which also has further upside on occupancy. This type of transaction enhances the REIT's ability to provide stable performance.

Notwithstanding the REIT's attractive assets and longer-term upside, our Board of Trustees recognizes that market disruptions related to the pandemic and elevated levels of inflation continue to weigh on the valuations of publicly-traded REITS, creating a divergence between asset values and unit price.

As a board and management team, it is our responsibility to consider every possible opportunity to surface value for our unitholders. To this end, after quarter-end, the board formed a special committee of independent directors to oversee a review of strategic alternatives for the REIT.

As we continue to navigate a highly volatile macroeconomic environment, the strategic review will play a key role in identifying additional ways to maximize value for all unitholders.

All of our routine operations and investment activity will carry on as normal during this period, and we intend to provide an update once the process is completed.

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

Charles Peach, Chief Financial Officer

Thank you, Steve. In the third quarter of 2022, the REIT had a distribution yield of 9.2% and has provided an AFFO payout ratio of 75.9%. Loan-to-value was reduced to 58.4%, while net operating income rose by $500,000.

While disposition costs reduced FFO and core FFO from the prior three months, AFFO for the quarter remained at $0.13 per unit. FFO/core FFO each fell $0.02 to $0.12 and $0.13 respectively on a per unit basis, due to dispositions costs on the mentioned before appraisal value sale of 95 and 105 Moatfield, while AFFO per unit was $0.13, unchanged from the prior quarter.

Both during the quarter and subsequently the REIT has continued to refinance its upcoming debt maturities, having extended its CAD and USD revolving credit facilities while reducing and extending its largest single debt facility at 120 South LaSalle. There is $12 million debt refinancing remaining for 2022, which is progressing well.

I'll now hand over for questions.

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press star followed by one on your touchtone phone. You will hear a three-tone prompt acknowledging your request. If you'd like to withdraw your request, please press star followed by two. If you are using a speakerphone, please lift the handset before pressing any keys. One moment for your first question.

Operator

Sairam Srinivas from Cormark Securities, please go ahead.

Sairam Srinivas, Cormark Securities

Thanks, operator. Hey, Steve. Hey, Paul. And hey, Charles.

Charles Peach, Chief Financial Officer

Hi.

Steve Hodgson, Chief Executive Officer

Hey, Sai.

Sairam Srinivas, Cormark Securities

So, the question I had was around the Chicago acquisition. Could you just take us through the thought process behind the capital allocation there and how you guys see that particular plot of land?

Steve Hodgson, Chief Executive Officer

The Chicago acquisition, as I mentioned in my opening remarks, is really in line with our strategy of repositioning the portfolio. What we've done over the last quarter is effectively reduced our asset base, created some liquidity to pay down debt, but also traded out of an older building that had some tenant and capital risk in Toronto at a 6.4 cap, and bought an office building in Chicago with a long-term lease with an investment grade tenant with upside on occupancy at an 8.4 cap.

And it's a relatively new building with very little capital required in the near-term. So, it's just consistent with our strategy of repositioning the portfolio.

Sairam Srinivas, Cormark Securities

Thanks, Steve. So, the other question I had was on vacancy. And I know this quarter we saw some of that. Is that mainly because of the SNC lease that's expiring at--I mean, the downside in that helping it this month?

Steve Hodgson, Chief Executive Officer

The vacancy that we saw in the quarter, I'm assuming you're referring to, it's a couple of things. It is the phased-out vacancy of SNC-Lavalin at 195, the West Mall. In addition, the disposition of 95-105 Moatfield, being a higher occupied building, had impact on occupancy as well.

But just as a reminder, it was a higher occupied building now, but our view was that there was some tenant risk there. In addition, there was the airline industry tenant on the West Mall property as well that vacated.

So, a few one-off situations, but overall we're seeing some very positive momentum going forward, and particularly in Atlantic Canada, as noted in our results.

Sairam Srinivas, Cormark Securities

Excellent color, Steve. I'll turn it back.

Operator

Your next question comes from the line of Jonathan Kelcher from TD Securities. Please go ahead.

Jonathan Kelcher, TD Securities

Thanks. Good morning. Just staying with the leasing, have you noticed or seen any change in the length of time tenants are taking to make decisions, or any slowdown in touring or anything like that?

Steve Hodgson, Chief Executive Officer

No, I don't think so. I think you see a little bit of that naturally in the summer quarter. But I would say it's actually the opposite of that, Jonathan, in that we've started to see tenants commit to longer-term deals. The new leasing that we did in our portfolio had 9.2 years of average term. That's clearly a sign that tenants are committing long-term to office space.

In terms of tour activity, I think that's where it generally slows down in the summer. With that said, some of the vacancy that we have along the 427, that's recent and transitional, that space had not been vacant for a long time, and we're getting a lot of interest from other users.

Jonathan Kelcher, TD Securities

So, touring activity slowed down in the summer, and you've seen it pick up again in the fall?

Steve Hodgson, Chief Executive Officer

Yes, that's right.

Jonathan Kelcher, TD Securities

Okay. And then you had I think roughly 15 leases that didn't renew in the quarter. You talked about some, but where the rest of those mostly spread all around the portfolio, or was there one geography that was better or worse than others?

Steve Hodgson, Chief Executive Officer

Yes, there were three that were over 5,000 square feet. The rest were spread out amongst the portfolio and small in nature.

Jonathan Kelcher, TD Securities

Okay. And then the lease termination income you had in the quarter, was that one big one or a bunch of little ones?

Steve Hodgson, Chief Executive Officer

That was related to SNC.

Jonathan Kelcher, TD Securities

Okay. Thanks. I'll turn it back.

Operator

Your next question comes from the line of Brad Sturges from Raymond James. Your line is open.

Brad Sturges, Raymond James

Good morning. Just to follow up on the question on the lease termination, the income, would there be any more income you're expecting for the rest of the year, or would that be it for Q3?

Steve Hodgson, Chief Executive Officer

Not anticipating any more lease termination income the balance of the year.

Brad Sturges, Raymond James

And given where you are from an occupancy rate today, where do you kind of see that turning the next two, three quarters?

Steve Hodgson, Chief Executive Officer

We still have the last phase of SNC-Lavalin vacating in Q4, which is just over 40,000 square feet. We do have some new leases coming online in the quarter. But, I would expect occupancy to the end of the year to be relatively flat, because any new leasing we've done even this quarter and next won't be an occupancy until the new year, just given time to retrofit space, etc.

Brad Sturges, Raymond James

And just on the SNC space that you got back, it sounds like you're getting good activity there. Just curious at this point what your timeline might be to re-lease that space.

Steve Hodgson, Chief Executive Officer

Was that the SNC-Lavalin space?

Brad Sturges, Raymond James

Yeah, at the West Mall.

Steve Hodgson, Chief Executive Officer

They're going through a phased exit of that building, but we've been marketing it. There are several larger users that have toured, and there are several full floor users as well. We have some vacancy at 191, in which I think we'll get some traction on putting the full floor tenants there. In 195, our immediate marketing strategy is trying to get the larger users in there, given it is a full building opportunity with naming rights and signage rights.

Brad Sturges, Raymond James

Last question, just going back to the Chicago acquisition. Maybe I missed it, but where within Chicago would that building be located? And then can you just talk through the lease up potential a little bit more in terms of the prospects for leasing up the rest of the building?

Steve Hodgson, Chief Executive Officer

The location of the building is in Lake Forest. It's adjacent to a lab building that Pfizer owns, so it's very strategic for them. A lot of the COVID vaccine lab development R&D was done in that facility.

This is new space to the market. Pfizer previously occupied the entire building. It's a beautiful building, certainly the best in that immediate area, and probably the second best in the region. Lake Forest, as you may know, is a great demographic area. A lot of the tech and life science executives live there.

We've been quite pleased. Even during due diligence, we had a couple of tours for the space. I think our plan of having bought at an 8.4 cap on in-place income, we put in financing as well that Charles can speak to that allows us future funding to fund the lease up. And if we're able to execute on that in short order, it's just an amazing real estate transaction for us.

Brad Sturges, Raymond James

Okay, great. I'll turn it back. Thanks a lot.

Operator

Your next question comes from the line of Jenny Ma from BMO Capital Markets. Please go ahead.

Jenny Ma, BMO Capital Markets

Hi. Thank you and good morning.

Charles Peach, Chief Financial Officer

Hi, Jenny.

Steve Hodgson, Chief Executive Officer

Hi, Jenny.

Jenny Ma, BMO Capital Markets

Just want to follow up on the question about the Chicago asset. For the space that is available for lease right now, is it ready to go or is there any work that you need to put into it or any sort of specialized fit out that a potential tenant might require? Or is it a fairly short timeline to get it going when you've got a new tenant?

Steve Hodgson, Chief Executive Officer

No. The acquisition closed yesterday. Today, we've started work on the retrofit of the lobby. Because it was a single tenant building, we need to retrofit the lobby to make it dual access for multi-tenant. That's really the only change, Jenny.

There are two wings of the building, of which one is where the vacancy is, so, it actually lays out quite well for multi-tenant. And what differentiates this building is the amenities. There's incredible conference space, fitness facilities, and it's adjacent to food and shops.

We expect quite a bit of demand. Pfizer doesn't have any exclusives in their lease preventing us from leasing to any other life science or pharmaceutical company. So, we expect some strong demand.

Jenny Ma, BMO Capital Markets

Okay, great. I just wanted to ask about the Irish portfolio. It looks like there's been an improvement in the overall occupancy, but it would appear there's a couple of assets that have occupancy below 50%. So, could you remind us what the story is there and whether there's an update on when that space could be released?

Steve Hodgson, Chief Executive Officer

We purchased the buildings with that vacancy, so we view that as an opportunity. The new lease that we did was a 20-year deal at about 7,000 square feet. We're quite pleased having executed on that.

The vacancy that you're referring to is at some pretty small buildings, so it's only going to take one tenant at each of those buildings to rectify that. One of those in Cork in particular, we've had some interest and we're working through that.

As you can imagine, having taken over this portfolio, we've made some changes to the teams in place as well as the third party sales teams in place, and we’re relaunching it in a marketing campaign more in line with what Slate is accustomed to elsewhere.

Jenny Ma, BMO Capital Markets

Okay, great. And then moving to the debt stack, could you provide what you're seeing for indicative mortgage rates for--I guess it would be the 2023 renewals that you're looking at and if it's mostly concentrated in Canada or if there's any U.S. or Irish mortgages in that mix as well, and whether or not those rates are different?

Charles Peach, Chief Financial Officer

Over the period so far-- the third quarter and since -- as you notice in the subsequent events, we've done over $500 million CAD equivalent of refinancing, some of which is lengthier, some of which is shorter.

For some, we have rolled at exactly the same rates that had been there before. For others, we have some of the slightly higher rates too. What we do have is the benefit of some of the swaps that we have in place that extend, in some instances, beyond where the refinanced debt was refinanced at. Effectively, we've got the benefit of cheaper past swaps being in place from that point on.

If I look at all-in rates of where things are next year, on the swapped financing, we're down to 3.7% or thereabouts. At the other end of the spectrum, I think at the highest end our projection is around 6.5% which is what we currently see on those maturities coming up next year.

That is based on the projection we see from counterparties, and there could be a fair amount of movement there given the shape of the curve and the movement we've seen in absolute rates, both from a U.S. perspective and Canadian perspective.

I wouldn't underestimate the fact we have European exposure there, too. On the European side of things, we have a floater outstanding. We are significantly progressed in looking at fixing that exposure. If we were to do so, that would reduce our floating rate exposure by over 50%.

Jenny Ma, BMO Capital Markets

Okay. That 6.5% that you mentioned, Charles, is that a result of spread and/or term? And is that on the Canadian or the U.S. side? It sounds a bit high. I know we can't predict rates, but just based on what we know, it still sounds a bit high.

Charles Peach, Chief Financial Officer

That's on the Canadian side of things. What we see there is we have an asset that currently has a swap against it and that swap matures at the maturity date. We have to take into context not only the spread component but also where the underlying rate component is.

Jenny Ma, BMO Capital Markets

Okay, great. And then my last question is--and I'm not sure if you can fulsomely answer this, but I'll try anyway. With regard to the review of strategic alternatives, how long do you expect the process to take?

Steve Hodgson, Chief Executive Officer

Thanks, Jenny. As you mentioned, we're not commenting specifics beyond what we said in the press release, but I can speak more generally and provide some context.

It's very clear that these market disruptions related to the pandemic and elevated inflation continue to weigh on valuations of publicly traded REITs, particularly in the office sector, and that's created a divergence between asset values and unit price. Our board has a responsibility to the REIT and to all of our unitholders to consider every possible opportunity to surface value, and they're taking action to do that.

The review, which is led by the independent trustees and supported by external financial advisor, will provide another layer of analysis and evaluation as we look to surface value creation for the opportunities for the REIT.

They'll be looking at a broad range of options that could include acquisitions, dispositions, corporate transactions, and other partnership opportunities.

Jenny Ma, BMO Capital Markets

Okay. It sounds like a fairly fulsome review then, right? So, we're talking a matter of probably months? Is that fair?

Steve Hodgson, Chief Executive Officer

Yes.

Jenny Ma, BMO Capital Markets

Okay, great. Thank you very much. I'll turn it back.

Operator

Your next question comes from the line of Matt Kornack from National Bank Financial. Please go ahead.

Matt Kornack, National Bank Financial

Hi, guys.

Steve Hodgson, Chief Executive Officer

Hey, Matt.

Matt Kornack, National Bank Financial

Just wanted to quickly follow up on Jenny's line of questioning, and I apologize if you already touched on it. But with regards to the near-term debt maturities, is the expectation that you would get at least the amount that you have outstanding, or are there up-financing opportunities at this point? Just want to get a sense as to liquidity and if you'd even maybe potentially have to reduce the size of some of those.

Charles Peach, Chief Financial Officer

We have liquidity at the moment and we've continued to keep that liquidity which allows an important amount of flexibility when it comes down to debt refinancings.

You will have noted that we gained an additional $8 million CAD in financing since the period end. It's moves like that, on an asset that we own and financed already, which allows us flexibility when we come around to other asset financings in the future. If we see that there's a benefit in taking a lower leverage on an asset in order to pay a lower spread, we'd like to have that flexibility as we go forward into the next period.

An example of our thoughts around what that might be is 120 South LaSalle, where we had 101.75 million outstanding of which we paid down 20 million with the view that, going forward, that should help significantly around spread and the number of counterparties willing to provide financing on that asset. That's an example of how we might use our liquidity and our capital to improve the cost and availability of financing we have over the next year.

Matt Kornack, National Bank Financial

Is it possible to quantify what the benefit would have been on a relative basis?

Charles Peach, Chief Financial Officer

I'd rather not at the moment. We're looking at further financing around those assets coming up within the next four or five months.

Matt Kornack, National Bank Financial

Okay. That's perfectly fair enough. With regards to the West Mall, if someone were to take the large space, what would be your expectations in terms of kind of signing a lease to ultimate cash payment? Does work need to be done in those spaces, or is it in pretty good shape for leasing?

Steve Hodgson, Chief Executive Officer

No, it's in very good shape. You may recall the history of that building. It was overbuilt in the Nortel days. SNC did some incremental work to make it work for them. Most of the walls are demountable wall systems, which provides some flexibility in layout for project space, etc., but also provides flexibility for future tenant use.

The building shows really well, Matt, and yes, there will be some inducements and some time required for tenants to make it their own, but not a significant amount of time.

Just as a reminder too, SNC vacated at a rent of $16.50. The starting rents that we have in the West Mall now are $18.00 to $19.00.

Matt Kornack, National Bank Financial

Okay. And it sounds like, I mean, if you find someone, if someone takes the space, you could potentially have them in and paying cash rent at some point in 2023.

Steve Hodgson, Chief Executive Officer

Yes.

Matt Kornack, National Bank Financial

Okay. And then last one, and maybe you can provide a ballpark if it's competitive disclosure that you don't want to give. But with regards to the recent acquisition in Chicago, what would be your hope in terms of achieving market rents at that property?

Steve Hodgson, Chief Executive Officer

The rent that Pfizer has leased is probably at or slightly below market. Our anticipation, and what we're underwriting for the balance of the space, is very similar.

Matt Kornack, National Bank Financial

And is that sort of midteens, high teens?

Steve Hodgson, Chief Executive Officer

It's an $18.00 rent. Net, fully-net, triple-net with $0.50 escalations per year.

Matt Kornack, National Bank Financial

Okay. So, if you could get to 100% occupancy, that's an 18% cap rate. Am I thinking of that correctly?

Steve Hodgson, Chief Executive Officer

Certainly midteens, yes.

Matt Kornack, National Bank Financial

Okay, fair enough. Okay. Thanks, guys.

Operator

Ladies and gentlemen, as a reminder, should you have a question, please press star followed by one.

There are no further questions at this time. Please proceed.

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

Thank you, everyone, for joining the Q3 2022 conference call for Slate Office REIT. Have a great day.

Operator

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