PARTNERS REIT

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## THREE AND SIX MONTHS ENDED JUNE 30, 2016 AND 2015

# MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL RESULTS

## FORWARD-LOOKING INFORMATION ADVISORY

This Management's Discussion and Analysis ("MD&A") to the unitholders may contain forward-looking statements and information within the meaning of applicable securities legislation. These forward-looking statements reflect management's current beliefs and are based on assumptions and information currently available to management of Partners Real Estate Investment Trust ("Partners", "Partners REIT" or the "REIT"). In some cases, forward-looking statements can be identified by terminology such as "may", "would", "could", "will", "expect", "anticipate", "believe", "intend", "plan", "forecast", "predict", "estimate", "outlook", "potential", "continue", "should", "likely", or the negative of these terms or other comparable terminology, and are not historical fact. Although management believes that the anticipated future results, performance or achievements expressed or implied by the forward-looking statements and information are based upon reasonable assumptions and expectations, the reader should not place undue reliance on forward-looking statements and information because they involve assumptions, known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the REIT to differ materially from anticipated future results, performance or achievements expressed or implied by such forward-looking statements and information.

In making the forward-looking statements in this MD&A, the REIT has applied material assumptions including, but not limited to, the assumption that: (1) commercial real estate markets continue to remain fluid; (2) demand for vacant units at the REIT's properties remains strong enabling the REIT to generate additional rents and enhance recovery ratios; and (3) the REIT is able to refinance maturing debt at favourable interest rates. Other assumptions are discussed throughout this MD&A; in particular under Part V – Risks and Uncertainties.

Forward-looking statements include statements related to acquisitions, development and capital expenditure activities, future maintenance and leasing expenditures, financing, the availability of financing sources and income taxes.

Factors that could cause actual results, performance, or achievements to differ materially from those set forth in the forward-looking statements and information include, but are not limited to: general economic conditions, local real estate conditions, including the development of properties in close proximity to the REIT's properties, timely leasing of newly developed properties and releasing of occupied square footage upon expiration, dependence on tenants' financial condition, changes in operating costs, government regulations and taxation, the uncertainties of real estate development and acquisition activity, the ability to effectively integrate acquisitions, interest rates, availability of equity and debt financing, the ability of the REIT to maintain stable cash flows and distributions and other risks and factors described from time to time in the documents filed by the REIT. The REIT undertakes no obligation to publicly update or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, except as required by law. Additional information about these risks and uncertainties and any corresponding plan to mitigate these risks, where possible, is contained in the REIT's filings with securities regulators, including the REIT's most recently filed Annual Information Form, which is available on www.sedar.com.

These forward-looking statements are made as of August 3, 2016 and disclosure of this material information is current to that date, unless otherwise noted.

# PART I – OVERVIEW & FINANCIAL HIGHLIGHTS

## BASIS OF PRESENTATION

Financial data included in this Management's Discussion and Analysis ("MD&A") for the three and six months ended June 30, 2016, (the "second quarter") includes material information up to August 3, 2016. Financial data has been prepared using accounting policies in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. All dollar references are in Canadian dollars.

This MD&A is intended to provide readers with an assessment of the performance of Partners REIT for the three and six months ended June 30, 2016, as well as its financial position and future prospects. The MD&A should be read in conjunction with the REIT's condensed consolidated financial statements for the three and six months ended June 30, 2016, the audited consolidated financial statements for the year ended December 31, 2015 and the REIT's most recently filed annual information form ("AIF").

In our discussion of operating performance, we define net operating income ("NOI") as gross revenues from income producing properties less operating expenses (which excludes interest expense, general and administrative expenses, amortization, income taxes, corporate transaction costs and fair value gains or losses). We define funds from operations ("FFO") as net income before fair value gains or losses, amortization of leasing fees ("LFs") and tenant allowances ("TAs"), other corporate transactions costs, gains or losses from the sale of properties, net gains from insurance proceeds, and certain other non-cash items and adjusted for any non-controlling interests. Adjusted funds from operations ("AFFO") is defined as FFO net of leasing fees, tenant allowances, tenant improvements and capital expenditures that maintain the current rental operations (ie – sustaining capital expenditures), amortization of deferred financing costs, mortgage penalties from early payout, non-cash interest accretion expense and straight-line rent. NOI is an important measure that we use to assess operating performance, and FFO is a widely-used measure in analyzing real estate. AFFO is typically a measure used to assess an entity's ability to pay distributions. We provide the components of NOI on page 19, and a reconciliation of net income and also cash flow from operations to FFO and AFFO on pages 20-23. NOI, NOI – same property, FFO, and AFFO do not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other issuers.

## BUSINESS OVERVIEW, STRATEGIC DIRECTION AND OUTLOOK

### General Overview

Partners REIT is an unincorporated, open-ended real estate investment trust. The REIT was formed pursuant to a Declaration of Trust initially dated March 27, 2007, and last amended and restated on March 23, 2015. The REIT's units are listed on the Toronto Stock Exchange (the "TSX") and trade under the symbol "PAR.UN". Prior to April 3, 2012, the REIT's units were listed on the TSX Venture Exchange under the same symbol. As at August 3, 2016 the REIT is also listed on the OTC exchange in the United States trading under the symbol PTSRF.

Effective November 3, 2010, the name of Charter Real Estate Investment Trust was changed to Partners Real Estate Investment Trust. All references to "Partners Real Estate Investment Trust", "Partners", "Partners REIT", the "REIT" and similar references in this MD&A refer to Charter Real Estate Investment Trust prior to the name change.

### Business Overview

Partners REIT is focused on the acquisition and management of a geographically diversified portfolio of retail and mixed-use retail community and neighbourhood shopping centres. These properties are located in both primary and secondary markets throughout Canada, and are primarily mid-market assets valued at up to approximately $50 million.

Management is of the view that necessity based retail centres represent attractive investments due to their stable cash flows. The majority of rents at these types of properties are derived from national and regional retailers with multi-year leases. Management's long term plans include pursuing opportunities to acquire assets that are accretive on a per unit basis at attractive capitalization rates. As the portfolio develops and becomes increasingly accretive, the REIT aims to steadily implement sustainable increases to its cash distributions.

Currently, the REIT's portfolio consists of 36 properties located in British Columbia, Alberta, Manitoba, Ontario, and Québec. In total, these properties comprise approximately 2.5 million square feet of gross leasable area ("GLA"). As of June 30, 2016, the REIT had 23 full-time employees.

**Strategy of the REIT**

The REIT's stated mission is to "reward its unitholders with sustainable, long-term returns by developing a retail real estate portfolio that features open-air or standalone properties located in stable primary and secondary markets which are anchored by necessity based retailers. The REIT derives value from this portfolio by prioritizing superior tenant client service, focused leasing activities and active asset management."

Management believes focusing primarily on necessity based retail shopping centres in these markets will provide opportunities for the REIT to obtain high quality, stable retail properties with growth potential through small tenant improvements. These centres are typically up to 250,000 square feet and anchored by discount retailers and/or supermarkets. The REIT intends to maximize the value of its centres by remerchandising, redeveloping, or renewing leases wherever possible. The REIT's goal is to own either "institutional-grade" properties or properties that offer the potential to become "institutional-grade" through redevelopment and lease renewals.

***Accretive opportunities in less competitive markets:*** The REIT applies an acquisition strategy whereby it seeks to acquire high quality properties in less competitive markets. Management believes that focusing upon secondary real estate markets offers the REIT the opportunity to acquire well-tenanted retail properties with strong national and regional retailers at attractive capitalization rates. By combining assets in the secondary market and primary market, management believes that the REIT will generate higher returns with lower risk than if the REIT were to focus exclusively on the secondary market.

***Targeting the mid-market:*** The REIT focuses on acquiring properties or portfolios of properties valued at up to $50 million, which allows it to minimize competition from large real estate investment trusts, corporations, pension funds and institutions. The REIT also considers larger acquisitions that do not fall into the investment parameters of larger real estate investment trusts or institutions, but still provide accretive investment opportunities.

***Stable rents via national and regional tenants:*** The REIT focuses on acquiring retail properties with national and regional retail tenants. These tenants are most likely to fulfill the lease terms to which they have committed and thus offer a stable source of cash flows

***Institutional grade properties:*** The REIT focuses on acquiring properties that are of "institutional grade". These properties tend to generate more interest from national and regional retailers, resulting in more stable cash flows. These properties also tend to be more highly sought after and thus offer greater value should the REIT elect to dispose of a particular asset. Finally, focusing on assets that fit this definition allows the REIT to obtain property financing at cost effective market rates.

**Leasing**

As of June 30, 2016, lease expiries, excluding leases already renewed for 2016 and 2017, represented 1.7% and 10.0%, respectively, of the REIT's total GLA. During the six months ended June 30, 2016 and the year ended December 31, 2015, the REIT has renewed a total of 332,786 square feet or 87% of leasable space that was originally set to expire during 2016.

Since January 2015 a number of retailers have announced closures, restructurings or bankruptcies in Canada, including Aeropostale, Le Chateau, Jones New York, Danier Leather, PJ Pet Store, International Clothiers, Benix, Designer Deport, Sears, Future Shop, Black's, Nine West, Herbal Magic and Target. The REIT's exposure to these retailers is limited. However, any closures from larger retailers will result in increased availability of retail space across Canada over the short-term, and potentially impact both retail rental rates and leasing fundamentals. Despite this changing landscape, the REIT believes there is sufficient demand for the majority of the locations due to become vacant during 2016 and 2017 and that remaining 2016 expiries will be renewed or released at market rates**.** Expiries during 2017 are spread geographically and are generally well located at properties with high demand. The REIT has minimal exposure to Alberta that is limited to three properties representing less than 5% of total GLA.

Barring a further deterioration of the retail leasing environment, management expects that the recent internalization of property management activities at its properties outside of Quebec should contribute to improvements in long term occupancy, through both increased efforts to lease currently vacant space, and increased retention at future expiries.

**Financing**

The REIT has $168.0 million (55.2%) in mortgages maturing over the next two years (July 1, 2016 to June 30, 2018), including $72.9 million in maturing mortgages on eight properties within the next 12 months. These maturing mortgages have a weighted average contractual interest rate of 4.77%. Based on current financing conditions, management expects that refinancing this portion of the REIT's debt should result in a reduction of the REIT's financing costs. Year-to-date in 2016, the REIT has completed a $13.7 million financing at an average contractual rate of 2.94%. During 2015, the REIT completed $51.3 million of new financings at an average contractual interest rate of 4.45%, including second mortgages completed to repay the Series I, 8% debenture in December of 2015.

On August 20, 2015, Partners announced that it would issue to each of the holders of its outstanding units the right to subscribe for additional units of the REIT (a "Right"). The record date for establishing these unitholders was September 14, 2015. A unitholder in Canada was entitled to subscribe for one new unit for every four Rights held upon payment of the subscription price of $3.10 per unit. The Rights Offering expired at 5:00 PM Eastern time on October 21, 2015.

On October 22, 2015, the REIT announced the successful conclusion of the Rights Offering, which benefited from high basic subscription and some over allotment subscription. As a consequence, the REIT issued 100% of the units available under the Rights Offering (6,649,364 units) and raised gross proceeds of approximately $20.6 million.

During the fourth quarter of 2015, the REIT applied the net proceeds from the Rights Offering along with the proceeds generated from the refinancing of mortgages towards the full redemption of the $28.8 million of 8.0% convertible unsecured subordinated debentures (the "Series I Debentures"). The Series I Debentures were scheduled to mature on March 31, 2016.

## FINANCIAL AND OPERATIONAL HIGHLIGHTS

The following is a summary of key financial information and data for the periods indicated (see Part II – Performance Measurement for a description of the key terms).

| | As at and for the three months ended | | As at and for the six months ended | |
|---|---|---|---|---|
| | **Jun 30, 2016** | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Revenues from income producing properties | **$ 13,937,629** | $ 13,856,589 | **$ 28,340,812** | $ 28,380,709 |
| Net income (loss) | **3,344,790** | 789,020 | **5,723,935** | (3,307,301) |
| Net income (loss) per unit - basic | **0.10** | 0.03 | **0.17** | (0.13) |
| NOI - all property [(1)] | **8,315,459** | 8,080,979 | **16,661,408** | 16,573,686 |
| FFO[(1)] | **2,537,933** | 2,175,256 | **5,425,249** | 4,538,505 |
| FFO per unit[(1)] | **0.08** | 0.08 | **0.16** | 0.17 |
| AFFO[(1)] | **2,369,100** | 1,967,313 | **4,876,435** | 4,446,581 |
| AFFO per unit[(1)] | **0.07** | 0.07 | **0.15** | 0.17 |
| Distributions[(2)] | **2,117,373** | 1,672,302 | **4,231,881** | 3,338,386 |
| Distributions per unit[(2)] | **0.06** | 0.06 | **0.13** | 0.13 |
| Distribution payout ratio - FFO/AFFO[(3)] | **83% / 89%** | 77% / 85% | **78% / 87%** | 74% / 75% |
| Cash distributions[(4)] | **1,601,053** | 1,334,969 | **3,194,722** | 2,677,737 |
| Cash distributions per unit - FFO/AFFO[(4)] | **0.05** | 0.05 | **0.10** | 0.10 |
| Cash distribution payout ratio[(5)] | **63% / 68%** | 61% / 68% | **59% / 66%** | 59% / 60% |

| As at | **Jun 30, 2016** | Dec 31, 2015 | Dec 31, 2014 |
|---|---|---|---|
| Total assets | **$ 524,269,414** | $ 520,970,422 | $ 542,551,040 |
| Total debt[(6)] | **363,751,492** | 364,550,117 | 381,967,023 |
| Total equity | **151,405,073** | 148,888,084 | 149,036,368 |
| Weighted average units outstanding - basic | **33,544,654** | 27,831,288 | 26,206,391 |
| Debt-to-gross book value including debentures[(6)] | **69.0%** | 69.5% | 70.0% |
| Debt-to-gross book value excluding debentures[(6)] | **58.1%** | 58.6% | 54.2% |
| Interest coverage ratio[(7)] | **1.59** | 1.59 | 1.80 |
| Debt service coverage ratio[(7)] | **1.06** | 1.07 | 1.22 |
| Mortgages weighted average effective interest rate[(8)] | **4.46%** | 4.57% | 4.43% |
| Portfolio occupancy | **94.2%** | 94.6% | 94.3% |

(1) NOI - all property, FFO and AFFO are non-IFRS financial measures widely used in the real estate industry. See “Part II – Performance Measurement” for further details and advisories.

(2) Represents distributions to unitholders on an accrual basis. Distributions are payable as at the end of the period in which they are declared by the Board of Trustees, and are paid on or around the 15th day of the following month. Distributions per unit exclude the 5% bonus units, or 3% bonus units for distributions with a record date after March 1, 2016, given to participants in the Distribution Reinvestment and Optional Unit Purchase Plan.

(3) Distribution payout ratio is a non-IFRS financial measure widely used in the real estate industry, calculated as total distributions as a percentage of FFO/AFFO. Management considers the distribution payout ratio a valuable metric to determine the sustainability of the REIT’s distribution. Non-IFRS measures do not have standardized meanings and are therefore unlikely to be comparable to similar measures presented by other issuers. There is no directly comparable IFRS measure.

(4) Represents distributions on a cash basis, and as such, excludes the non-cash distributions of units issued under the Distribution Reinvestment and Optional Unit Purchase Plan.

(5) Cash distribution payout ratio is a non-IFRS financial measure widely used in the real estate industry, calculated as cash distributions as a percentage of FFO/AFFO. Management considers the cash distribution payout ratio a valuable metric to determine the sustainability of the REIT’s distribution. Non-IFRS measures do not have standardized meanings and are therefore unlikely to be comparable to similar measures presented by other issuers. There is no directly comparable GAAP measure.

(6) Debt-to-gross book value is a non-IFRS financial measure widely used in the real estate industry. See calculation under “Debt-to-Gross Book Value” in “Part IV – Results of Operations”. Management considers debt-to-gross book value to be a valuable metric in assessing the REIT’s overall leverage. Non-IFRS measures do not have standardized meanings and are therefore unlikely to be comparable to similar measures presented by other issuers. There is no directly comparable IFRS measure.

(7) Interest coverage ratio and debt service coverage ratio are non-IFRS financial measures widely used in the real estate industry, calculated on a rolling four-quarter basis. See definition under “Mortgages and Other Financing” in “Part IV – Results of Operations”. Management considers the interest coverage and debt service coverage ratios to be valuable metrics in assessing the REIT’s ability to make contractual payments on debt. Non-IFRS measures do not have standardized meanings and are therefore unlikely to be comparable to similar measures presented by other issuers. There are no directly comparable IFRS measures.

(8) Represents the weighted average effective interest rate for secured debt excluding debentures and credit facilities.

*Results for the Three Month Period Ending June 30, 2016*

Revenue from income producing properties for the second quarter was $13.9 million, a $0.1 million (1%) increase when compared to the second quarter of 2015. When compared to the first quarter of 2016 ("the prior quarter"), second quarter revenues decreased by $0.5 million mainly as the result of lower property tax recoveries due to lower property tax expense and a reduction in straight-line rents.

Net income for the second quarter was $3.3 million, an improvement of $2.6 million when compared to the second quarter of 2015. This increase to income was primarily due to fair value gains on the REIT's portfolio as compared to losses in the prior year in addition to reduced financing costs. When compared to the prior quarter net income increased by $1.0 million, primarily due to the recognition of fair value gains during the second quarter of 2016.

As there have been no property acquisitions or dispositions in the current or comparative period, same property NOI is equivalent to all property NOI. NOI for the second quarter was $8.3 million, a $0.2 million (3%) increase when compared to $8.1 million for the second quarter of 2015. This increase to NOI was as a result of recoveries of amounts previously allowed for. When compared to the prior quarter, NOI was relatively unchanged.

FFO for the second quarter was $2.5 million, a $0.4 million increase when compared to the same period in the prior year. The increase to FFO was primarily a result of lower interest expense following the repayment of the Series I Debentures. When compared to the prior quarter's FFO of $2.9 million, FFO decreased by $0.4 million, primarily due to higher general and administrative expenses.

AFFO for the second quarter was $2.4 million, an increase of $0.4 million when compared to $2.0 million in the same period in the prior year. This improvement was due to decreased interest expense. AFFO decreased by $0.1 million when compared to the prior quarter due to increased primarily due to higher general and administrative expenses.

In the calculation of AFFO, the REIT recognizes sustaining capital costs on a reserve basis calculated at $1.00 per square foot for fiscal 2016. As such, during the first and second quarters, the REIT's sustaining capex reserve was $0.25 per square foot per quarter for a total of $0.50 per square foot (six months ended June 30, 2015 - $0.40 per square foot). Based on its assessment of the current portfolio, management believes that $1.00 per square foot or $2.5 million closely approximates the ongoing annual sustaining capital expenditures.

Distributions for the second quarter were $2.1 million ($0.06 per unit), an increase of $0.4 million (27%) when compared to $1.7 million ($0.06 per unit) for the second quarter of 2015. This increase in total distributions can be attributed to the increased number of units outstanding as a result of the Rights Offering that closed during the fourth quarter of 2015. The distribution per unit for the second quarter of 2016 was unchanged from the first quarter of 2016.

The AFFO payout ratio for the second quarter was 89% (June 30, 2015 – 85%). Taking into account the REIT's dividend re-investment plan ("DRIP"), the AFFO cash payout ratio for the fourth quarter was 68% (June 30, 2015 – 68%).

*Results for the Six Month Period Ending June 30, 2016*

Revenue from income producing properties for the six months ended June 30, 2016 was $28.3 million, a small decrease when compared to $28.4 million in the second quarter of 2015. This decrease was primarily the result marginally lower occupancy early in 2016.

Net income for the six months ended June 30, 2016 was $5.7 million, an improvement of $9.0 million when compared to a net loss of $3.3 million for the same prior year period. This increase to income was primarily due to fair value gains on the REIT's portfolio as compared to losses in the prior year in addition to reduced financing costs.

NOI for the six months ended June 30, 2016 was $16.7 million, a $0.1 million (1%) increase when compared to $16.6 million for the same prior year period. This increase to NOI was primarily as a result of recoveries of amounts previously allowed for.

FFO for the six months ended June 30, 2016 was $5.4 million, a $0.9 million increase when compared to $4.5 million for the same prior year period. The increase to FFO was primarily as a result of lower interest expense following the repayment of the Series I Debentures ($28.8 million at 8.0% - repaid during the fourth quarter 2015).

AFFO for the six months ended June 30, 2016 was $4.9 million, an improvement of $0.5 million when compared to $4.4 million in the same prior year period due to decreased interest expense partially offset by a higher allowance for sustaining capital expenditures.

Distributions for the six months ended June 30, 2016 were $4.2 million ($0.13 per unit), an increase of $0.9 million (27%) when compared to $3.3 million ($0.13 per unit) for the same prior year period. This increase in total distributions can be attributed to the increased number of units outstanding as a result of the Rights Offering that closed during the fourth quarter of 2015.

The AFFO payout ratio for the six months ended June 30, 2016 was 87% (June 30, 2015 – 75%). Taking into account the REIT's dividend re-investment plan ("DRIP"), the AFFO cash payout ratio for the six months ended June 30, 2016 was 66% (June 30, 2015 – 60%).

*Financial Position*

The REIT's total assets as at June 30, 2016 were $524 million, a $3 million (0.6%) increase when compared to $521 million as at December 31, 2015. This increase was primarily as a result of fair value gains recognized on the REIT's portfolio and increases to the REIT's working capital balances.

The REIT's total debt as at June 30, 2016 was $364 million, a $1 million (0.2%) decrease when compared to $365 million at December 31, 2015. This decrease was the result of regularly scheduled principal payments on the REIT's mortgages outweighing the additional principal borrowed from refinancing activity.

The REIT's debt-to-gross book value at June 30, 2016 was 69.0%, or 58.1% when excluding the impact of convertible debentures. These metrics stood at 69.5% and 58.6%, respectively, as at December 31, 2015.

The REIT's weighted average effective interest rate for mortgages at June 30, 2016 was 4.46%, which is an 0.11% decrease from December 31, 2015's average of 4.57%. This improvement was as a result of the recent refinancing activity.

Partners' interest coverage ratio at June 30, 2016 was 1.59, unchanged from December 31, 2015. The REIT's debt service coverage ratio at June 30, 2016 was 1.06, a slight decrease from December 31, 2015.

Occupancy as at June 30, 2016 was 94.2%, a slight decrease when compared to 94.6% as at December 31, 2015 and unchanged from the prior quarter. Management believes that the REIT's 2016 leasing plans for renewals are progressing well, despite the recent increase in available square footage for the overall market for retail space. As at June 30, 2016, 97.2% of anchor, major and free standing build units were leased.

Net asset value is a measure of the REIT's total assets less its liabilities, and is represented on the balance sheet as unitholders' equity. As at June 30, 2016, the REIT's net asset value was $4.49 per unit, an improvement from $4.46 per unit at December 31, 2015.

# REAL ESTATE PORTFOLIO

## Portfolio Summary

| Property and location | Property type | Date built /redeveloped | Anchor and shadow anchor tenants | Retail (sq.ft.)[1] | Occupancy[2] [3] | % of annualized base rental revenue[3] | Weighted average rent[4] |
|---|---|---|---|---|---|---|---|
| **British Columbia:** | | | | | | | |
| Centuria Urban Village<br>Kelowna, British Columbia | Mixed Use Commercial/ Residential | 2007 | Nesters Market, Shoppers Drug Mart | 32,625 | 100.0% | 2.0% | $22.52 |
| Evergreen Shopping Centre<br>Sooke, British Columbia | Retail Strip Centre | 1978/2010 | Western Foods, Shoppers Drug Mart, BC Liquor | 68,025 | 98.1% | 3.2% | $17.63 |
| Mariner Square Shopping Centre<br>Campbell River, British Columbia | Retail Strip Centre | 2006/2007 | Save-On Foods, Starbucks, London Drugs, BC Liquor | 100,257 | 100.0% | 4.7% | $17.33 |
| Washington Park Shopping Centre<br>Courtenay, British Columbia | Retail Strip Centre | 1992/1993 | Great Canadian Superstore, TD Bank | 32,652 | 87.8% | 1.9% | $25.14 |
| **Alberta:** | | | | | | | |
| 137th Ave.<br>Edmonton, Alberta | Free Standing | 2003 | Shoppers Drug Mart, PartSource | 15,922 | 100.0% | 0.8% | $17.84 |
| Cobblestone Shopping Centre<br>Grand Prairie, Alberta | Retail Strip Centre | 2006/2007 | Shoppers Drug Mart, TD Bank, Starbucks | 42,980 | 100.0% | 3.1% | $26.64 |
| Manning Crossing<br>Edmonton, Alberta | Retail Strip Centre | 1993 - 1996 | Safeway, RBC | 64,544 | 94.9% | 4.0% | $24.15 |
| **Manitoba:** | | | | | | | |
| Shoppers Drug Mart Property<br>Brandon, Manitoba | Free Standing | 2005 | Shoppers Drug Mart | 16,986 | 100.0% | 1.1% | $24.40 |
| Shoppers Drug Mart Property<br>Selkirk, Manitoba | Free Standing | 2005 | Shoppers Drug Mart | 16,685 | 100.0% | 0.9% | $20.00 |
| Shoppers Drug Mart Property<br>Steinbach, Manitoba | Free Standing | 2006 | Shoppers Drug Mart, Medical Practitioners | 20,956 | 100.0% | 1.2% | $21.90 |
| Shoppers Drug Mart Property<br>Winnipeg (Pembina), Manitoba | Free Standing | 2003 | Shoppers Drug Mart | 15,780 | 100.0% | 1.2% | $27.40 |
| Shoppers Drug Mart Property<br>Winnipeg (Sherbrook), Manitoba | Free Standing | 2005 | Shoppers Drug Mart | 16,839 | 100.0% | 1.3% | $28.00 |
| **Ontario:** | | | | | | | |
| Cornwall Square<br>Cornwall, Ontario | Enclosed Mall | 1979/1989 | Sears, Shoppers Drug Mart | 251,192 | 77.4% | 6.4% | $12.17 |
| Crossing Bridge Square<br>Stittsville, Ontario | Retail Strip Centre | 1995 | Farm Boy, McDonalds, IDA | 45,913 | 85.8% | 2.0% | $18.91 |
| Grand Bend Towne Centre,<br>Grand Bend, Ontario | Retail Strip Centre | 2002 | Sobey's, Shoppers Drug Mart | 41,567 | 94.2% | 1.7% | $16.57 |
| King George Square<br>Brantford, Ontario | Retail Strip Centre | 1988 | Shoppers Drug Mart, Dollarama | 66,983 | 100.0% | 3.2% | $18.02 |
| Place Val Est<br>Sudbury, Ontario | Retail Strip Centre | 1983/1987, 1990, 1998 | Metro, LCBO, RBC, Pharmasave | 110,577 | 90.4% | 3.4% | $12.83 |
| Quinte Crossroads,<br>Belleville, Ontario | Power Centre | 2005 - 2007 | The Brick, Home Depot Best Buy, BMO | 85,200 | 100.0% | 4.2% | $18.21 |
| Rona Property<br>Exeter, Ontario | Free Standing | 1996/2000 | Rona | 42,780 | 100.0% | 0.4% | $3.86 |
| Rona Property<br>Seaforth, Ontario | Free Standing | 1962/2000 | Rona | 19,622 | 100.0% | 0.1% | $2.69 |
| Rona Property<br>Zurich, Ontario | Free Standing | 1961/2000 | Rona | 24,400 | 100.0% | 0.1% | $1.63 |

| Property and location | Property type | Date built /redeveloped | Anchor and shadow anchor tenants | Retail (sq.ft.)(1) | Occupancy(2) (3) | % of annualized base rental revenue(3) | Weighted average rent(4) |
|---|---|---|---|---|---|---|---|
| St. Clair Beach Towne Centre<br>Tecumseh, Ontario | Retail Strip Centre | 2004 | Shoppers Drug Mart | 40,088 | 91.2% | 2.2% | $22.70 |
| Thunder Centre<br>Thunder Bay, Ontario | Power Centre | 2004 - 2007 | Home Outfitters, LCBO, Home Depot, Old Navy, Dollarama, Mark's | 168,087 | 98.5% | 7.8% | $17.41 |
| Timmins West Power Centre<br>Timmins, Ontario | Retail Strip Centre | 2007 - 2009 | Michaels, Mark's | 43,774 | 100.0% | 2.0% | $17.29 |
| Wellington Southdale<br>London, Ontario | Retail Strip Centre | 1986, 2000, 2004, 2006 | Landmark Theatres, Dollarama | 86,243 | 98.8% | 4.1% | $17.71 |
| **Québec:** | | | | | | | |
| Centre Village Shopping Centre<br>Nuns Island, Montréal, Québec | Enclosed Mall | 1977, 1991, 2001, 2010, 2012 | Loblaws, SAQ | 96,957 | 94.2% | 3.6% | $14.61 |
| Châteauguay<br>Montréal, Québec | Mixed-use Strip Centre | 1970/1994, 2010 | Shoppers Drug Mart, Staples, Québec Government | 115,295 | 98.4% | 4.0% | $13.15 |
| Elgar Place<br>Nuns Island, Montréal, Québec | Retail Strip Centre | 1969, 1989 | Couche Tard | 10,121 | 100.0% | 0.4% | $14.40 |
| Marcel Laurin<br>Saint Laurent, Québec | Retail Strip Centre | 2011 | Metro, Brunet Pharmacy | 120,222 | 97.1% | 5.8% | $18.60 |
| Méga Centre<br>Montréal, Québec | Power Centre | 1973/1993, 1999, 2000, 2004, 2014 | Walmart, Michaels, Brault & Martineau | 272,034 | 98.6% | 7.8% | $10.88 |
| Place Desormeaux<br>Longueuil, Québec | Enclosed Mall | 1971/1998,2009, 2010 | Walmart, Super C, Québec Government | 249,530 | 93.2% | 7.1% | $11.38 |
| Plaza des Seigneurs<br>Terrebonne, Québec | Retail Strip Centre | 1998 | Uniprix, SAQ, Banque Nationale | 20,833 | 100.0% | 1.2% | $22.16 |
| Repentigny Shopping Centre<br>Repentigny, Québec | Mixed Use Strip Centre | 1988/2009 | Familiprix, Dollarama, Québec Government | 48,557 | 79.7% | 1.7% | $16.48 |
| Saint Remi Shopping Centre<br>Saint Remi, Québec | Retail Strip Centre | 2009 - 2011 | Sobey's, SAQ, IGA Uniprix, Tim Hortons | 62,593 | 92.0% | 2.7% | $17.74 |
| Shoppers Drug Mart Property<br>Gatineau, Québec | Free Standing | 2007 | Shoppers Drug Mart | 17,028 | 100.0% | 1.1% | $24.00 |
| Sorel Shopping Centre,<br>Sorel, Québec | Retail Strip Centre | 2010 - 2012 | Uniprix, SAQ, Tim Hortons | 31,038 | 74.9% | 1.4% | $22.66 |
| **Total** | | | | **2,514,885** | **94.2%** | **100%** | **$15.70** |

Notes:

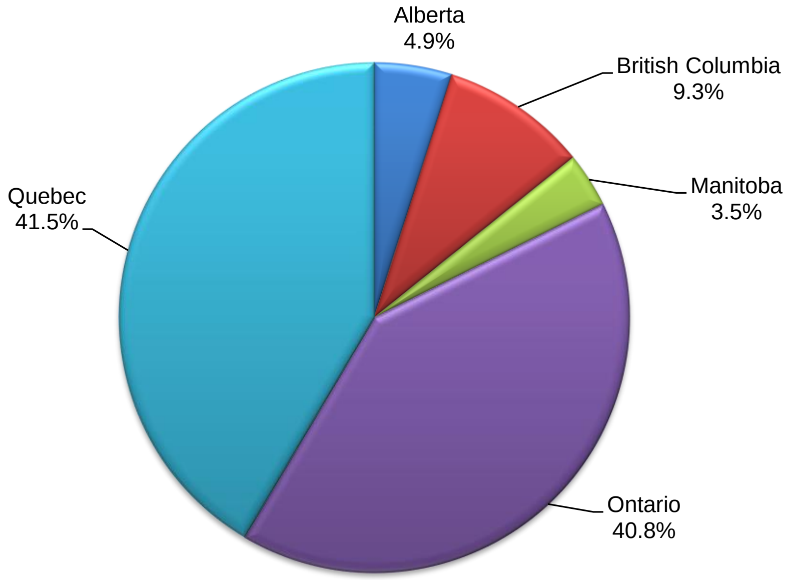
(1) Includes office space in mixed-use retail properties.

(2) Excluding storage space.

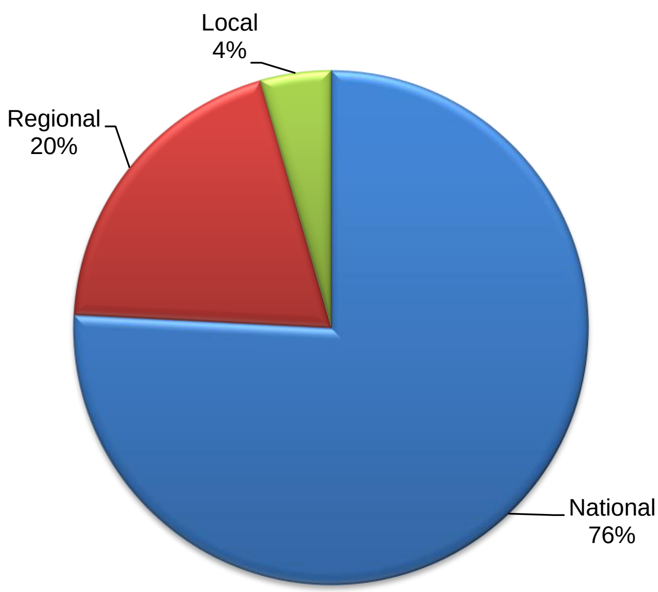
(3) Includes square footage of all material executed leases, regardless of occupancy date, and excludes square footage of all documented material lease terminations updated through June 30, 2016.

(4) Represents the weighted average rent for the portfolio.

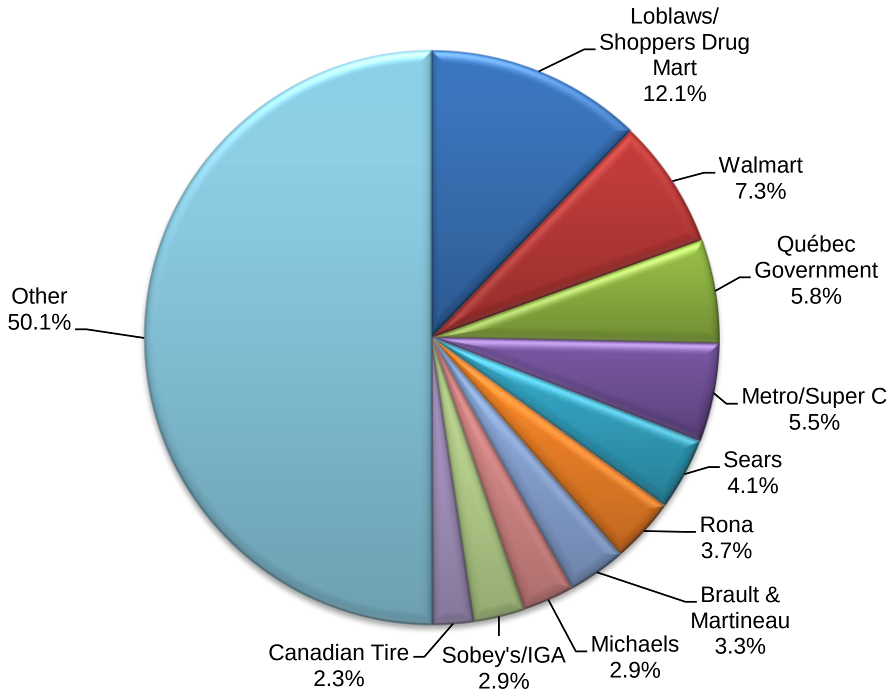
The geographic diversification of the portfolio by GLA is as follows:




The REIT has a strong mix of national and regional tenants by square footage as follows:



The tenant mix of the REIT's portfolio as at June 30, 2016, including the REIT's ten largest tenants by lease square feet excluding storage, is as follows:




**Leasing Activity and Occupancy**

The weighted average term to maturity of existing leases is more than five years. As at June 30, 2016, the REIT had renewed a total of 332,786 square feet of leased space that was originally set to expire during 2016. This represents renewals of over 87% of the GLA originally set to expire during 2016. The table below shows the remaining lease expiries as at June 30, 2016:

| | Expiries (sq.ft.) | Expiries (%) | Rent PSF ($) |
|---|---|---|---|
| 2016 (remaining 6 months) | 42,950 | 1.7% | $ 12.59 |
| 2017 | 250,667 | 10.0% | 15.54 |
| 2018 | 175,022 | 7.0% | 18.68 |
| 2019 | 363,094 | 14.4% | 13.34 |
| 2020 | 361,687 | 14.4% | 13.65 |
| Thereafter | 1,175,115 | 46.7% | 16.76 |
| Vacant | 146,350 | 5.8% | - |
| Total | 2,514,885 | 100.0% | $ 15.70 |
| Weighted average remaining lease term (years) - **5.31 years** | | | |

Lease expiries, new leasing and renewals completed by June 30, 2016 by number of transactions is as follows:

| **Period ended** | **June 30, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| | **# of Transactions** | **(%)** | # of Transactions | (%) |
| Leases renewed | 46 | 59.7% | 34 | 75.6% |
| Leases in progress and not renewed | 31 | 40.3% | 11 | 24.4% |
| Total scheduled expiries 2016 | 77 | 100.0% | 45 | 100.0% |
| Abandonment or early termination | 4 | | 9 | |
| New leases or expansions | 5 | | 19 | |

Lease expiries, new leasing and renewals completed by June 30, 2016 by total square feet is as follows:

| **Period ended** | **June 30, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| | **Sq. Ft.** | **(%)** | Sq. Ft. | (%) |
| Leases renewed | 332,786 | 87.1% | 156,129 | 89.0% |
| Leases in progress and not renewed | 49,211 | 12.9% | 19,324 | 11.0% |
| Total scheduled expiries 2016 | 381,997 | 100.0% | 175,453 | 100.0% |
| Abandonment or early termination | 12,517 | | 11,344 | |
| New leases or expansions | 11,062 | | 32,146 | |

As at June 30, 2016, the REIT had renewed a total of 332,786 square feet, comprising 46 units, in respect of units that had or were set to expire during the year. The balance of 31 units that have or are set to expire during 2016, totaling 59,211 square feet, is either in the process of being renewed or will require new tenant prospects. The success in securing new leases and lease renewals for 2016 expiries reflects the REIT's increased focus and efforts on proactive leasing activities over the past year. These efforts are expected to intensify following the recent internalization of property management activities at the REIT's properties outside of Quebec.

GLA and occupancy of the REIT on a quarter by quarter basis over the last eight quarters was as follows:

| Quarter Ended | Gross Leasable Area (sq. ft.) | Occupied (sq.ft.) | Occupancy (%) |
|---|---|---|---|
| June 30, 2016 | 2,514,885 | 2,368,535 | 94.2% |
| March 31, 2016 | 2,516,483 | 2,369,541 | 94.2% |
| December 31, 2015 | 2,516,483 | 2,379,459 | 94.6% |
| September 30, 2015 | 2,516,360 | 2,390,149 | 95.0% |
| June 30, 2015 | 2,520,364 | 2,385,229 | 94.6% |
| March 31, 2015 | 2,522,745 | 2,385,697 | 94.6% |
| December 31, 2014 | 2,522,974 | 2,380,007 | 94.3% |
| September 30, 2014 | 2,518,523 | 2,418,895 | 96.0% |
| Average | 2,518,602 | 2,384,689 | 94.7% |

The following table summarizes occupancy at June 30, 2016 and December 31, 2015 between anchor / major / free standing building ("FSB") and commercial retail unit ("CRU") tenants:

| | | **30-Jun-16** | | |
|---|---|---|---|---|
| Lease type | Leased sq. ft. | Total sq. ft. | Leased (%) | W.A. rent PSF |
| Anchor / Major / FSB | 1,693,475 | 1,742,216 | 97.2% | $ 14.02 |
| CRU | 675,060 | 772,669 | 87.4% | 19.91 |
| Total | 2,368,535 | 2,514,885 | 94.2% | $ 15.70 |
| | | **31-Dec-15** | | |
| Lease type | Leased sq. ft. | Total sq. ft. | Leased (%) | W.A. rent PSF |
| Anchor / Major / FSB | 1,698,500 | 1,742,921 | 97.5% | $ 14.05 |
| CRU | 680,959 | 773,562 | 88.0% | 19.63 |
| Total | 2,379,459 | 2,516,483 | 94.6% | $ 15.65 |

## PART II – PERFORMANCE MEASUREMENT

The key indicators by which management measures Partners REIT's performance are as follows:

- Net operating income ("NOI");
- Funds from operations ("FFO");
- Adjusted funds from operations ("AFFO");
- Debt service coverage ratio ("DSCR");
- Weighted average interest rate; and
- Occupancy levels.

We have provided the analysis of NOI, FFO, and AFFO under Part IV – Results of Operations.

### Net Operating Income

Net operating income ("NOI") is defined as gross revenues from income producing properties less operating costs from income producing properties. Operating expenses do not include costs associated with financing, general and administration, other corporate transaction costs, amortization, income taxes, realized and unrealized gains and losses, and the equity pick-up of an investment's net earnings. Amortization of tenant costs (an expense) are netted against revenues for IFRS purposes, but are added back in the calculation of NOI. NOI is a non-IFRS financial measure used in the real estate industry. Management considers NOI a meaningful measure of the results from operations that is useful in analyzing the performance of the REIT's property portfolio.

### Funds from Operations

Funds from operations ("FFO") is a non-IFRS financial measure of operating performance widely used by the real estate industry. Partners REIT bases its calculation of FFO on the recommendations of the Real Property Association of Canada ("RealPac"). The definition is meant to standardize the calculation and disclosure of FFO across real estate entities in Canada, and is modeled on the definition adopted by the National Association of Real Estate Investment Trusts ("NAREIT") in the United States. NAREIT's definition of FFO is net income (calculated in accordance with IFRS) excluding gains or losses from the sale of property and fair value increases or decreases in property values; plus depreciation and amortization; adjusted for items that are not indicative of operating performance; and after adjustments for unconsolidated partnerships and joint ventures (which is also calculated to reflect FFO on the same basis). The REIT has reconciled both comprehensive income and cash provided by operations to FFO in a manner equivalent to the RealPac definition (see pages 20-23).

Management considers FFO a meaningful measure of operating performance for financial analysts, investors and unitholders, since it eliminates the assertion that the value of real estate decreases over time and it adjusts for items included in net income (as determined under IFRS) that may not necessarily be the best determinants of operating performance.

### Adjusted Funds from Operations

Adjusted funds from operations ("AFFO") is a non-IFRS financial measure defined as FFO plus the non-cash amortization of deferred financing costs, mortgage penalties from early payout of mortgage financings and interest accretion expense, less any straight line rental revenue that has otherwise been included in income, less sustaining capital expenditures. Sustaining capital expenditures is made up of leasing activities that maintain current rental operations (i.e. - leasing fees, tenant allowances and tenant improvements costs) and property maintenance activities that maintain the physical aspects of the properties (ie – landlord's recoverable and non-recoverable capital costs). Management considers these on-going leasing and properties' maintenance costs to be sustaining capital expenditures as they are fundamental to the operating activities of the REIT and therefore not a discretionary investment.

The calculation of AFFO excludes revenue enhancing capital expenditures that relate to the generation of a new rental stream, as a consequence of leasing existing vacant space to a new tenant or the development or re-development of incremental retail space.

These sustaining capital expenditures are funded from cash generated from operations. Management considers AFFO to be an effective measure of the cash generated from operations and is a measure of the REIT's ability to pay distributions.

NOI, FFO, and AFFO should not be construed as an alternative to net earnings or cash flow from operating activities determined in accordance with IFRS. Management's method of calculating these financial measures may differ from that of other issuers and accordingly, may not be comparable to financial measures with similar captions reported by other issuers.

In the calculation of AFFO, the REIT recognizes sustaining capital costs on a reserve basis calculated at $1.00 per square foot annually. As such, during the second quarter, the REIT's sustaining capex reserve was $0.25 per square foot (June 30, 2015 - $0.25 per square foot). Based on its assessment of the current portfolio, management believes that $1.00 per square foot closely approximates the ongoing annual sustaining capital expenditures. This reserve amount is re-evaluated annually and the 2017 sustaining capital reserve will be determined and reported with the March 31, 2017 reporting period.

**Debt Service Coverage Ratio**

Debt service coverage ratio ("DSCR") is a non-IFRS measure used to determine if the REIT will be able to sustain its debt based on its current cash flow. DSCR is calculated by dividing the REIT's EBITDA by the total annual interest and principal payments made on its debt portfolio. The DSCR is a tool that financial institutions use to evaluate the risk associated with the ability to recover both interest and principal payments and is a common financial covenant contained within lending agreements. As at June 30, 2016, the rolling four-quarter DSCR was 1.06 to 1, a slight decrease from 1.07 to 1 at December 31, 2015.

**Mortgages Weighted Average Effective Interest Rate**

The REIT's weighted average effective interest rate is a non-IFRS financial measure and includes interest on secured debt and excludes interest on debentures and the credit facility. Effective interest rates include the impact of costs paid to secure financing and mark to market interest rate adjustments. This calculation is a useful measure to compare movements in interest rates period over period; and to compare the average rate to the current market rates at that point in time. As at June 30, 2016, the REIT's weighted average effective interest rate for mortgages was 4.46%, improved from 4.57% as at December 31, 2015.

**Occupancy Levels**

Occupancy levels are presented in different manners depending on their context. Occupancy levels could be presented as an average portfolio occupancy rate when analyzing the overall operating performance, or as a point-in-time reference when analyzing future lease expiries, or as an assessment of the period over period performance of each property. Management considers these as useful measures in assessing the overall performance of its portfolio and essential tools to determine which properties require further investigation if performance lags. Refer to Part I – Overview & Financial Highlights under "Leasing Activity and Occupancy" for the REIT's occupancy performance.

## PART III – RECENT DEVELOPMENTS & SUBSEQUENT EVENTS

### Property Management Update

During the second quarter of 2016, the REIT substantially completed the internalization of the property management of its 25 properties in Ontario, Manitoba, Alberta, and British Columbia. Plans to internalize were first announced on March 16, 2016, in a press release titled, *Partners Real Estate Investment Trust Announces Increased Property Management Focus*. With the exception of their finance and accounting functions, these properties had been managed by an external third party that has worked with the REIT in some capacity since September 2014. This internalization of the REIT's property management is expected to generate significant savings with an annual impact of approximately $0.5 million to the REIT's AFFO.

In the same press release the REIT also announced its intention to consolidate the property management of the REIT's 10 properties in Quebec under the oversight of a single external property manager. On June 16, 2016, the REIT announced that the mandate had been awarded to COGIR Real Estate following a formal Request for Proposals and a thorough selection process. The change to a single manager was effective August 1, 2016. The REIT believes this strategy will result in both cost efficiencies and an enhanced tenant experience.

The cost savings associated with these changes should start to materialize in the third quarter of 2016.

### Changes to Senior Management and the Board of Trustees

On January 25, 2016, the REIT announced the appointment of Paul Harrs as Chief Operating Officer. Mr. Harrs will oversee the REIT's leasing, development and property management relationships.

On March 16, 2016, Partners announced the resignation of Marc Charlebois from the REIT's Board of Trustees.

On May 25, 2016, based on voting results at the Annual General Meeting, Jane Domenico was elected to the REIT'S Board of Trustees.

### Debt Financings (Property Mortgages)

On October 1, 2015, the REIT refinanced its Place Val Est asset in the greater Sudbury area of Ontario. The REIT secured a $9.2 million mortgage with a five year term carrying a 3.15% interest rate. The refinancing provided the REIT with approximately $2.8 million in additional liquidity to fund capital investments intended to improve the overall quality of the REIT's portfolio, while $6.3 million of this new mortgage was directed towards the repayment of the property's previous and maturing mortgage, which carried an interest rate of 5.17%. Both the new and previous mortgages originated with the Canadian CMBS division of the Royal Bank of Canada.

On November 12, 2015, the REIT secured a $4.0 million mortgage at the REIT's Shoppers Drug Mart property in Brandon, Manitoba. The $4.0 million mortgage has a five-year term, and an interest rate of 3.32%. $2.0 million of this mortgage was directed towards repayment of the property's previous and maturing mortgage, which carried an interest rate of 5.90%. Remaining net proceeds were deployed towards the reduction of the REIT's debt on other properties. Both the new and previous mortgages originated with Montrose Winnipeg Inc.

Also on November 12, 2015, the REIT announced that it had finalized two new second mortgages with a total value of $15.0 million. These included a second mortgage with a value of $11.0 million and a twenty-month term at Partners' Thunder Centre in Thunder Bay, as well as a second mortgage with a value of $4.0 million and a two-year term at Partners' Mariner Square Shopping Centre in Campbell River, British Columbia. Both mortgages carry an interest rate of 5.50%. A portion of the proceeds from these mortgages was used to complete the redemption of the final 25% of its $28.8 million outstanding in Series I Debentures.

In December 2015, the REIT accepted a one year financing extension for $17.5 million in place of the maturing $22.5 million, 4.90% mortgage. The extended mortgage is secured as a first mortgage on an enclosed mall located in Ontario. The mortgage has a term of one year with interest at the greater of prime plus 2.30% per annum or 5.00% per annum and an amortization period of 20 years.

During all 2015, Partners completed $51.3 million of new debt financings, inclusive of refinancing maturing mortgages, at an average rate of 4.45%.

On June 30, 2016, Partners completed a $13.7 million mortgage financing at the REIT's Wellington Southdale property in London, Ontario. This new mortgage, held by Manulife Financial, is for a five-year term and carries an interest rate of 2.94%. $9.8 million of the proceeds were used for the full repayment of the property's two existing mortgages, which carried an average contractual interest rate of 5.71%. The remaining net proceeds of $3.9 million were deployed partially deployed towards a $3.0 million repayment on Partners' Credit Facility.

**Equity Financings (Rights Offering)**

On October 22, 2015, the REIT announced the successful conclusion of the Rights Offering, which raised proceeds of approximately $20.6 million as a result of high basic subscription and some over allotment subscription. As a result, the REIT issued 6,649,364 units for $3.10 per unit, representing 100% of the units available under the Rights Offering.

The REIT applied the net proceeds towards the redemption of 75% of the $28,750,000 owing on the Series I Debentures which were scheduled to mature on March 31, 2016. These Series I Debentures were redeemed on November 23, 2015, on a pro-rata basis and in accordance with their terms. The REIT completed two second mortgages with a total value of $15.0 million to repay the final 25% of its Series I Debentures, which were redeemed on December 15, 2015.

**Uncertified Class Action Lawsuit**

In April 2014, Partners purchased three retail centres in Ontario from Holyrood Holdings (“Holyrood”) for a purchase price of approximately $83.2 million.

As a result of information obtained subsequently, the REIT’s Trustees initiated a process to reverse the Holyrood Transaction. On October 2, 2014 the REIT and Holyrood obtained an Order from the Ontario Superior Court of Justice that rescinded the April 2014 acquisition.

On December 4, 2014, the REIT announced that it had been notified that a statement of claim dated November 28, 2014 had been issued in the Ontario Superior Court seeking certification of a class action on behalf of persons who held units of the REIT on April 1, 2014 against several parties, including a former officer and Trustees of the REIT. Partners REIT itself has not been named as a defendant in the legal proceedings which allege that the conduct of the defendants in connection with the acquisition by the REIT of three properties from Holyrood in April 2014 caused harm to the plaintiffs.

Partners has certain indemnity obligations to its Trustees and officers (current and former) with respect to this claim, subject to exceptions including where it is determined that there has been a failure to act honestly and in good faith. The REIT has insurance which it expects to be applicable in these circumstances. Given that the REIT has not been named in the litigation, the REIT does not believe it will be material to its business and affairs.

# PART IV – RESULTS OF OPERATIONS

## STATEMENT OF OPERATIONS

The following is financial information from the condensed consolidated statements of comprehensive income for the three and six months ended June 30, 2016:

| Three months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Revenues from income producing properties | $ | **13,937,629** | $ | 13,856,589 | $ | 81,040 | 1% |
| Property operating expenses | | **(2,084,439)** | | (2,043,652) | | (40,787) | (2%) |
| Realty taxes | | **(3,264,136)** | | (3,500,758) | | 236,622 | 7% |
| Property management fees | | **(469,168)** | | (443,318) | | (25,850) | (6%) |
| | | **8,119,886** | | 7,868,861 | | 251,025 | 3% |
| Other expenses: | | | | | | | |
| Financing costs | | **4,642,782** | | 5,058,065 | | (415,283) | (8%) |
| General and administrative expenses | | **1,134,745** | | 847,658 | | 287,087 | 34% |
| Other transaction costs | | **22,233** | | 194,995 | | (172,762) | (89%) |
| | | **5,799,760** | | 6,100,718 | | (300,958) | (5%) |
| Income before FV gains (losses) and insurance | | **2,320,126** | | 1,768,143 | | 551,983 | 31% |
| Insurance proceeds | | **-** | | 1,059,763 | | (1,059,763) | (100%) |
| Fair value gains (losses) | | **1,024,664** | | (2,038,886) | | 3,063,550 | 150% |
| Comprehensive income | $ | **3,344,790** | $ | 789,020 | $ | 2,555,770 | 324% |
| Income per unit, basic | $ | **0.10** | $ | 0.03 | $ | 0.07 | 232% |

| Six months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Revenues from income producing properties | $ | **28,340,812** | $ | 28,380,709 | $ | (39,897) | (0%) |
| Property operating expenses | | **(4,494,074)** | | (4,450,253) | | (43,821) | (1%) |
| Realty taxes | | **(6,763,997)** | | (6,926,684) | | 162,687 | 2% |
| Property management fees | | **(827,398)** | | (815,524) | | (11,874) | (1%) |
| | | **16,255,343** | | 16,188,248 | | 67,095 | 0% |
| Other expenses: | | | | | | | |
| Financing costs | | **9,134,380** | | 10,167,069 | | (1,032,689) | (10%) |
| General and administrative expenses | | **2,101,779** | | 1,868,112 | | 233,667 | 13% |
| Other transaction costs | | **29,533** | | 340,917 | | (311,384) | (91%) |
| | | **11,265,692** | | 12,376,098 | | (1,110,406) | (9%) |
| Income (loss) before FV losses and insurance | | **4,989,651** | | 3,812,150 | | 1,177,501 | 31% |
| Insurance proceeds | | **-** | | 1,059,763 | | (1,059,763) | (100%) |
| Fair value gains (losses) | | **734,284** | | (8,179,214) | | 8,913,498 | 109% |
| Comprehensive income (loss) | $ | **5,723,935** | $ | (3,307,301) | $ | 9,031,236 | 273% |
| Income (loss) per unit, basic | $ | **0.17** | $ | (0.13) | $ | 0.30 | (231%) |

## Comprehensive Income (Loss)

Net income for the second quarter was $3.3 million, an improvement of $2.6 million when compared to the second quarter of 2015. Net income for the six months ended June 30, 2016 was $5.7 million, an improvement of $9.0 million when compared to a net loss of $3.3 million for the same prior year period. These increases to net income were primarily due to fair value gains on the REIT's portfolio as compared to losses in the prior year periods in addition to reduced financing costs.

## Financing Costs

The REIT's financing costs are incurred on debt bearing fixed and variable rates of interest, and consist primarily of interest expense recognized in accordance with the effective interest rate method, which includes not only the REIT's contractual interest expenses, but also financing costs and market interest rate adjustments. Financing costs also include non-cash accretion expense and other incidental interest income and expenses.

Financing costs for the second quarter were $4.6 million, a decrease of $0.5 million (8%) from the second quarter of 2015 amount of $5.1 million. For the six months ended June 30, 2016, financing costs of $9.1 million represented a decrease of $1.1 (10%) million from $10.2 million in the same prior year period. These decreases were due to a reduction in interest and amortization of deferred financings costs that were as a direct result of the Series I Debentures repaid during the fourth quarter of 2015 combined with refinancing maturing mortgages at lower interest rates.

## General and Administrative Expenses

General and administrative expense for the second quarter of 2016 was $1.1 million, an increase of $0.3 million (34%) when compared to $0.8 million during the second quarter of 2015. For the six months ended June 30, 2016 general administrative expense of $2.1 million increased by $0.2 million (13%) from $1.9 million for the same prior year period. These increases from the same prior year periods were due primarily to increased one time adjustments for the relocation of the head office from Barrie to Toronto, combined with increased on-going costs as a consequence of internalizing property management function for properties West of Quebec.

## Fair Value Gains and Losses

The fair value gain of $0.7 million for the six months ended June 30, 2016 million was recognized as a result of capital recoveries realized that were in excess of amounts allowed for. During the first six months of 2016, the REIT obtained six independent external appraisals representing 13.3% of the fair value of the income producing portfolio.

## OPERATING RESULTS

### Net Operating Income – All Properties

As there have been no property acquisitions or dispositions in the current or comparative period, same property NOI is equivalent to all property NOI.

The amortization of the cost of tenant allowances and leasing fees (commissions and legal) included in income producing properties are recognized as a reduction of rental income over the lease term on a straight-line basis. In order to calculate NOI as defined above in Part II, the amortization of tenant allowances and leasing fees that otherwise reduce revenues are added back in calculating NOI.

### All Properties NOI

The REIT's complete property portfolio is included in the "All Properties NOI" data below.

| **Three months ended** | | **Jun 30, 2016** | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Revenues from income producing properties | **$** | **13,937,629** | $ | 13,856,589 | $ | 81,040 | 1% |
| Property operating expenses | | **(2,084,441)** | | (2,043,652) | | (40,789) | (2%) |
| Realty taxes | | **(3,264,136)** | | (3,500,758) | | 236,622 | 7% |
| Property management fees | | **(469,166)** | | (443,318) | | (25,848) | (6%) |
| | | **8,119,886** | | 7,868,861 | | 251,025 | 3% |
| Amortization of tenant costs | | **195,573** | | 212,118 | | (16,545) | (8%) |
| Net operating income | **$** | **8,315,459** | $ | 8,080,979 | $ | 234,480 | 3% |
| *NOI as a % of revenues* | | ***59.7%*** | | *58.3%* | | | *1.3%* |

All property NOI for the second quarter was $8.3 million, a $0.2 million (3%) decrease when compared to $8.1 million for the second quarter of 2015. This increase was a result of recoveries of amounts previously allowed for.

| **Six months ended** | | **Jun 30, 2016** | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Revenues from income producing properties | **$** | **28,340,812** | $ | 28,380,709 | $ | (39,897) | (0%) |
| Property operating expenses | | **(4,494,074)** | | (4,450,253) | | (43,821) | (1%) |
| Realty taxes | | **(6,763,997)** | | (6,926,684) | | 162,687 | 2% |
| Property management fees | | **(827,398)** | | (815,524) | | (11,874) | (1%) |
| | | **16,255,343** | | 16,188,248 | | 67,095 | 0% |
| Amortization of tenant costs | | **406,065** | | 385,438 | | 20,627 | 5% |
| Net operating income | **$** | **16,661,408** | $ | 16,573,686 | $ | 87,722 | 1% |
| *NOI as a % of revenues* | | ***58.8%*** | | *58.4%* | | | *0.4%* |

All property NOI for the six months ended June 30, 2016 was $16.7 million a $0.1 million (1%) increase when compared to $16.6 million for the same prior year period. This increase was a result of recoveries of amounts previously allowed for.

### Funds from Operations ("FFO") and Adjusted Funds from Operations ("AFFO")

A reconciliation of IFRS net income to FFO and AFFO for the three months ended June 30, 2016 is as follows:

| Three months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| **Net income** | **$** | **3,344,790** | $ | 789,020 | $ | 2,555,770 | 324% |
| Amortization of deferred leasing costs | | **195,574** | | 212,118 | | (16,544) | (8%) |
| Other transaction costs | | **22,233** | | 194,995 | | (172,762) | (89%) |
| Fair value (gains) losses | | **(1,024,664)** | | 2,038,886 | | (3,063,550) | (150%) |
| Insurance proceeds | | **-** | | (1,059,763) | | 1,059,763 | 100% |
| FFO | | **2,537,933** | | 2,175,256 | | 362,677 | 17% |
| Straight-line rent | | **(43,230)** | | (137,291) | | 94,061 | 69% |
| Deferred financing amortization, interest accretion | | **505,397** | | 560,348 | | (54,951) | (10%) |
| Sustaining capex | | **(631,000)** | | (631,000) | | - | 0% |
| AFFO | **$** | **2,369,100** | $ | 1,967,313 | $ | 401,787 | 20% |
| Weighted average units outstanding - basic | | **33,620,643** | | 26,489,542 | | 7,131,101 | 27% |
| FFO per unit | **$** | **0.08** | $ | 0.08 | $ | - | 0% |
| AFFO per unit | **$** | **0.07** | $ | 0.07 | $ | - | 0% |

FFO for the second quarter was $2.5 million, a $0.4 million increase when compared to the same prior year period. The increase was primarily a result of reduced interest expense following the repayment of the Series I Debentures and higher NOI, partially offset by higher general and administrative expenses. When compared to the FFO of $2.9 million for the first quarter of 2016, FFO decreased by $0.4 million primarily due to higher general and administrative expenses.

FFO includes non-cash straight line rent in revenues and income deductions for the amortization of deferred financing costs and excludes any deduction for the cost of sustaining capital expenditures. As a consequence, AFFO is presented herein as an alternative measure of determining available cash flow. AFFO for the second quarter was $2.4 million and improvement of $0.4 million when compared to $2.0 million for the second quarter of 2015. The improvement in AFFO is primarily the result of lower interest expense following the repayment of the Series I Debentures, partially offset by higher general and administrative expenses.

A reconciliation of IFRS cash flow provided by operating activities to FFO and AFFO for the three months ended June 30, 2016 is as follows:

| Three months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| **Cash flow provided by operating activities** | **$** | **5,209,572** | $ | 6,062,436 | $ | (852,864) | (14%) |
| Straight line rent | | **43,230** | | 137,291 | | (94,061) | (69%) |
| Deferred financing amortization, interest accretion | | **(505,397)** | | (560,348) | | 54,951 | 10% |
| Interest differential | | **257,095** | | 221,695 | | 35,400 | 16% |
| Change in working capital and accrued interest | | **(2,488,800)** | | (2,821,050) | | 332,250 | 12% |
| Other transaction costs | | **22,233** | | 194,995 | | (172,762) | (89%) |
| Insurance proceeds | | **-** | | (1,059,763) | | 1,059,763 | 100% |
| FFO | | **2,537,933** | | 2,175,256 | | 362,677 | 17% |
| Straight-line rent | | **(43,230)** | | (137,291) | | 94,061 | 69% |
| Deferred financing amortization, interest accretion | | **505,397** | | 560,348 | | (54,951) | (10%) |
| Sustaining capex | | **(631,000)** | | (631,000) | | - | 0% |
| AFFO | **$** | **2,369,100** | $ | 1,967,313 | $ | 401,787 | 20% |
| Weighted average units outstanding - basic | | **33,620,643** | | 26,489,542 | | 7,131,101 | 27% |
| FFO per unit | **$** | **0.08** | $ | 0.08 | $ | - | 0% |
| AFFO per unit | **$** | **0.07** | $ | 0.07 | $ | - | 0% |

For the three months ended June 30, 2016, the REIT had distributions of $2.1 million and cash flow from operating activities of $5.2 million, resulting in an aggregate cash surplus of $3.1 million. The main driver of the second quarter's cash surplus is the REIT's semi-annual debenture interest payment of $1.7 million which is paid semi-annually in the first and third quarters and improvements in the REIT's working capital position. The entire current period's distributions would be considered a return on capital.

A reconciliation of IFRS net income to FFO and AFFO for the six months ended June 30, 2016 is as follows:

| **Six months ended** | | **Jun 30, 2016** | | Jun 30, 2015 | | Change ($) | (%) |
|---|---|---|---|---|---|---|---|
| **Net income** | **$** | **5,723,935** | $ | (3,307,301) | $ | 9,031,236 | 273% |
| Amortization of deferred leasing costs | | **406,065** | | 385,438 | | 20,627 | 5% |
| Other transaction costs | | **29,533** | | 340,917 | | (311,384) | (91%) |
| Fair value (gains) losses | | **(734,284)** | | 8,179,214 | | (8,913,498) | (109%) |
| Insurance proceeds | | **-** | | (1,059,763) | | 1,059,763 | 100% |
| FFO | | **5,425,249** | | 4,538,505 | | 886,744 | 20% |
| Straight-line rent | | **(209,303)** | | (276,499) | | 67,196 | 24% |
| Deferred financing amortization, interest accretion | | **921,489** | | 1,193,575 | | (272,086) | (23%) |
| Sustaining capex | | **(1,261,000)** | | (1,009,000) | | (252,000) | (25%) |
| AFFO | **$** | **4,876,435** | $ | 4,446,581 | $ | 429,854 | 10% |
| Weighted average units outstanding - basic | | **33,544,654** | | 26,444,711 | | 7,099,943 | 27% |
| FFO per unit | **$** | **0.16** | $ | 0.17 | $ | (0.01) | (6%) |
| AFFO per unit | **$** | **0.15** | $ | 0.17 | $ | (0.02) | (12%) |

FFO for the six months ended June 30, 2016 was $5.4 million, a $0.9 million increase when compared to $4.5 million for the same prior year period. The increase was primarily a result of reduced interest expense following the repayment of the Series I Debentures.

FFO includes non-cash straight line rent in revenues and income deductions for the amortization of deferred financing costs and excludes any deduction for the cost of sustaining capital expenditures. As a consequence, AFFO is presented herein as an alternative measure of determining available cash flow. AFFO for the six months ended June 30, 2016 was $4.9 million and improvement of $0.4 million when compared to $4.5 million for the same prior year period. The improvement in AFFO is primarily the result of lower interest expense following the repayment of the Series I Debentures.

A reconciliation of IFRS cash flow provided by operating activities to FFO and AFFO for the six months ended June 30, 2016 is as follows:

| Six months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| **Cash flow provided by operating activities** | **$** | **5,499,196** | $ | 4,361,751 | $ | 1,137,445 | 26% |
| Straight line rent | | **209,303** | | 276,499 | | (67,196) | (24%) |
| Deferred financing amortization, interest accretion | | **(921,489)** | | (1,193,575) | | 272,086 | 23% |
| Interest differential | | **471,818** | | 447,904 | | 23,914 | 5% |
| Change in working capital and accrued interest | | **136,888** | | 1,364,772 | | (1,227,884) | (90%) |
| Other transaction costs | | **29,533** | | 340,917 | | (311,384) | (91%) |
| Insurance proceeds | | **-** | | (1,059,763) | | 1,059,763 | 100% |
| FFO | | **5,425,249** | | 4,538,505 | | 886,744 | 20% |
| Straight-line rent | | **(209,303)** | | (276,499) | | 67,196 | 24% |
| Deferred financing amortization, interest accretion | | **921,489** | | 1,193,575 | | (272,086) | (23%) |
| Sustaining capex | | **(1,261,000)** | | (1,009,000) | | (252,000) | (25%) |
| AFFO | **$** | **4,876,435** | $ | 4,446,581 | $ | 429,854 | 10% |
| Total weighted average units | | **33,544,654** | | 26,444,711 | | 7,099,943 | 27% |
| FFO per unit | **$** | **0.16** | $ | 0.17 | $ | (0.01) | (6%) |
| AFFO per unit | **$** | **0.15** | $ | 0.17 | $ | (0.02) | (12%) |

For the six months ended June 30, 2016, the REIT had distributions of $4.2 million and cash flow from operating activities of $5.5 million, resulting in an aggregate cash surplus of $1.3 million. The entire current period's distributions would be considered a return on capital.

In assessing its distribution policy, the REIT considers whether certain costs are expected to recur and the impact of items that may not be included in cash from operations, where the timing of cash flows may differ from the timing of payment of distributions. The future sustainability of the distributions will be dependent on the REIT being able to continue to generate similar cash flow from operating activities and the continued ability to re-finance mortgages as they come due (while obtaining cash from the refinancing of these maturing mortgages at regular loan to asset value ratios for commercial retail real estate companies and REITs). Management expects distributions will be sustainable from similar cash flows from operating activities while also obtaining net cash from the regular refinancing of maturing mortgages. Management and the REIT's Trustees review the REIT's distribution plans on a quarterly basis, with the objective of establishing distributions that are sustainable for a reasonably foreseeable period.

## Statement of Cash Flows

The following table summarizes cash flows for the three months ended June 30, 2016:

| Three months ended | | Jun 30, 2016 | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Cash flow provided by operating activities | **$** | **5,209,572** | $ | 6,062,436 | $ | (852,864) | (14%) |
| Cash flow used by financing activities | | **(3,774,625)** | | (3,581,599) | | (193,026) | (5%) |
| Cash flow used by investing activities | | **(210,627)** | | (2,202,401) | | 1,991,774 | 90% |
| NET INCREASE IN CASH | | **1,224,320** | | 278,436 | | 945,884 | 340% |
| CASH, OPENING | | **2,080,764** | | 2,108,118 | | (27,354) | (1%) |
| CASH, ENDING | **$** | **3,305,084** | $ | 2,386,554 | $ | 918,530 | 38% |

Operating Activities

Cash flow from operating activities for the second quarter was $5.2 million, a $0.9 million decrease when compared to $6.1 million for the first quarter of 2015. This decrease to operating cash flows was primarily the result of an insurance recovery in the prior year that was the final settlement from the 2013 fire at Evergreen Shopping Centre located in Sooke, BC.

Financing Activities

Cash flows used by financing activities for the second quarter was $3.8 million, which is a $0.2 million decrease to cash as compared to the $3.6 million used in the prior year's comparative period. The current period's $3.8 million net cash outflow from financing activities was the result of netted repayments of $3.5 million on the REIT's credit facility, $2.3 million of regular principal mortgage repayments, $1.6 million of cash distributions and $0.2 million of financing costs to obtain a new mortgage. These outflows exceeded the $3.8 million additional financing received from mortgage refinancing activity.

Investing Activities

Cash outflows from investing activities for the second quarter were $0.2 million, a reduction of $2.0 million when compared to the $2.2 million used during 2015's comparable period. The decrease to the cash outlay was the result of both lower spending and $1.0 million of recoveries from previous capital expenditures.

For the three months ended June 30, 2016 and 2015, capital expenditures were as follows:

| Three months ended | | Jun 30, 2016 | | Jun 30, 2015 |
|---|---|---|---|---|
| Recoverable from tenants | **$** | **50,706** | $ | 289,963 |
| Non-recoverable from tenants | | **659,889** | | 72,276 |
| Development or re-development | | **(159,026)** | | 8,656 |
| | | **551,569** | | 370,895 |
| Leasing activities | | **(340,942)** | | 1,831,506 |
| | **$** | **210,627** | $ | 2,202,401 |

Ignoring $1.0 million in capital recoveries from prior years' capital expenditures, actual sustaining capital expenditures for the three months ended June 30, 2016 were $1.1 million (three months ended June 30, 2015 - $1.6 million).

The following table summarizes cash flows for the six months ended June 30, 2016:

| **Six months ended** | | **Jun 30, 2016** | | Jun 30, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Cash flow provided by operating activities | **$** | **5,499,196** | $ | 4,361,751 | $ | 1,137,445 | 26% |
| Cash flow used by financing activities | | **(4,175,861)** | | (1,120,406) | | (3,055,455) | (273%) |
| Cash flow used by investing activities | | **(688,272)** | | (3,007,062) | | 2,318,790 | 77% |
| NET INCREASE IN CASH | | **635,063** | | 234,283 | | 400,780 | 171% |
| CASH, OPENING | | **2,670,021** | | 2,152,271 | | 517,750 | 24% |
| CASH, ENDING | **$** | **3,305,084** | $ | 2,386,554 | $ | 918,530 | 38% |

Operating Activities

Cash flow from operating activities for the six months ended June 30, 2016 was $5.5 million, a $1.1 million increase when compared to $4.4 million for the same prior year period. This increase to operating cash flows was primarily the result of a lower cash outflows from changes in working capital and lower interest expense following the repayment of the Series I Debentures in the fourth quarter of 2015, partially offset by insurance recoveries collected in the same prior year period.

Financing Activities

Cash flows used for financing activities for the six months ended June 30, 2016 was $4.2 million, which is a $3.1 million decrease as compared to the $1.1 million used in the prior year's comparative period. This year over year decrease in cash from financing activities is as a result of the $2.0 million in cash generated from credit facility borrowings during 2015's comparable period.

Investing Activities

Cash outflows from investing activities for the six months ended June 30, 2016 were $0.7 million, a reduction of spending of $2.3 million when compared to the $3.0 million used during 2015's comparable period. The decrease to cash outlay was the result of both lower spending and $1.0 million in recoveries of previous capital expenditures.

For the six months ended June 30, 2016 and 2015, capital expenditures were as follows:

| Six months ended | | **Jun 30, 2016** | | Jun 30, 2015 |
|---|---|---|---|---|
| Recoverable from tenants | **$** | **55,756** | $ | 606,812 |
| Non-recoverable from tenants | | **848,884** | | 73,346 |
| Development or re-development | | **(116,902)** | | 226,409 |
| | | **787,738** | | 906,567 |
| Leasing activities | | **(99,466)** | | 2,100,495 |
| | **$** | **688,272** | $ | 3,007,062 |

Ignoring $1.0 million in capital recoveries from prior years' capital expenditures, actual sustaining capital expenditures for the six months ended June 30, 2016 were $1.6 million (six months ended June 30, 2015 - $2.1 million).

## FINANCIAL POSITION ANALYSIS

### Statement of Financial Position – Total Assets

| As at | | Jun 30, 2016 | | Dec 31, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Income producing properties | $ | **513,032,027** | $ | 511,817,617 | $ | 1,214,410 | 0% |
| Other assets | | **5,344,530** | | 3,146,165 | | 2,198,365 | 70% |
| Accounts receivable | | **2,587,773** | | 3,336,619 | | (748,846) | (22%) |
| Cash | | **3,305,084** | | 2,670,021 | | 635,063 | 24% |
| Total assets | $ | **524,269,414** | $ | 520,970,422 | $ | 3,298,992 | 1% |

Income producing properties

The REIT elected to use the fair value model under IFRS, and as a result, income producing properties are carried at their fair value at the reporting date. Gains or losses arising from changes in the fair value of income producing properties are included in profit and loss in the period in which they arise.

The increase of $1.2 million in income producing properties at June 30, 2016 over December 31, 2015 was a result of the recognition of fair value gains and capital improvement work.

During the six months ended June 30, 2016, the REIT had six of its properties appraised representing an aggregate fair value of $68.0 million, or 13.3% of the total portfolio value. During fiscal 2015, the REIT had thirteen of its properties appraised, representing an aggregate fair value of $237.7 million, or 46.4% of the total portfolio value at that date.

It is the REIT's accounting policy that properties acquired within the year are valued at the purchase price plus closing costs and at least one third of the portfolio is externally appraised each fiscal year on a rotating basis.

Other assets

Other assets are composed of prepaid realty taxes and insurance, deferred acquisition costs, amounts held in escrow and other prepaid expenses. During 2016, the balance of other assets has increased by $2.2 million (70%), due primarily to prepayments of property taxes which will be expensed evenly throughout the year.

Accounts receivable

Accounts receivable decreased by $0.7 million (22%) during the six months ended June 30, 2016. The decrease was primarily the result of the collection of a significant construction reimbursement received from one of the REIT's tenants.

### Net Asset Value

| As at | | Jun 30, 2016 | | Dec 31, 2015 | | Change ($)/(units) | Change (%) |
|---|---|---|---|---|---|---|---|
| Units outstanding, end of period | | **33,688,697** | | 33,387,646 | | 301,051 | 1% |
| Unitholders' equity | $ | **151,405,073** | $ | 148,888,084 | $ | 2,516,989 | 2% |
| Net asset value per unit | $ | **4.49** | $ | 4.46 | $ | 0.03 | 1% |

Net asset value ("NAV") is a measure of the REIT's total assets less its liabilities and is represented on the balance sheet as unitholders' equity. As at June 30, 2016, the net asset value of the REIT was $151.4 million as compared to $148.9 million at December 31, 2015. This $2.5 million increase to NAV is as a result of units issued under the DRIP and net income exceeding cash distributions paid to unitholders.

On a per unit basis, NAV was increased $0.03 to $4.49 per unit. The NAV per unit is a result of increased NAV as discussed above, offset by an increase in units outstanding resulting from the issuance of DRIP units.

## Capital

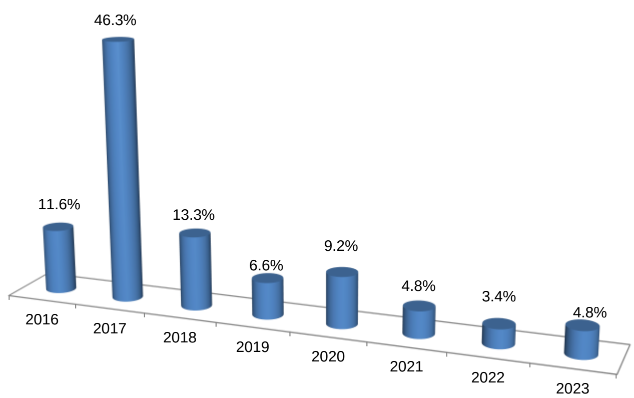
The REIT's capital consists of debt and equity capital. Real estate is a capital intensive industry and as a result, debt capital, in particular, is a very important aspect of managing the business. In addition, financial leverage is used to enhance returns from acquired real estate. Given the importance of debt capital, the REIT monitors its debt regularly for compliance with debt covenants contained in its loan agreements.

The following table shows the REIT's capital as at June 30, 2016 and December 31, 2015:

| As at | | **Jun 30, 2016** | | Dec 31, 2015 | | Change ($) | Change (%) |
|---|---|---|---|---|---|---|---|
| Mortgages payable | **$** | **303,918,903** | $ | 304,948,995 | $ | (1,030,092) | (0%) |
| Debentures | | **56,395,122** | | 56,014,181 | | 380,941 | 1% |
| Credit facilities | | **1,994,290** | | 1,976,561 | | 17,729 | 1% |
| Unitholders' equity | | **151,405,073** | | 148,888,084 | | 2,516,989 | 2% |
| Total capital | **$** | **513,713,388** | $ | 511,827,821 | $ | 1,885,567 | 0% |

## Mortgages and Other Financing

The following is a debt maturity chart for the REIT's mortgages payable and debentures as at June 30, 2016:




Over the next two years, the REIT has approximately $168.0 million in mortgages maturing which carry an average contractual interest rate of 4.77%. Refinancing the mortgages at current market rates would result in a reduction to the REIT's average rate of interest. The REIT also needs to re-finance two series of convertible debentures totaling $57.5 million, carrying a weighted average coupon interest rate of 5.8%.

Interest coverage and debt service coverage ratios are as follows:

| For the rolling four quarters ended | **Jun 30, 2016** | Dec 31, 2015 |
|---|---|---|
| Interest coverage ratio(1) | **1.59** | 1.59 |
| Debt service coverage ratio(2) | **1.06** | 1.07 |

(1) Interest coverage ratio, a non-IFRS measure, is calculated on a rolling four-quarter basis as EBITDA divided by interest expense, where EBITDA is net income before fair value gains or losses, interest expense, incentive unit option compensation expense, depreciation and amortization and other transaction costs. EBITDA is a non-IFRS financial measure of operating performance.

(2) Debt service coverage ratio, a non-IFRS measure, is calculated on a rolling four-quarter basis as EBITDA divided by debt service, where debt service is principal repayments plus interest expense (before amortization of financing fees included in interest expense).

The interest coverage and debt service coverage ratios for the rolling four quarters ended June 30, 2016 did not change significantly in comparison to December 31, 2015.

**Mortgages Payable**

The REIT's current weighted average term to maturity on mortgages payable is approximately two and a half years, and the weighted average contractual interest rate is 4.38%. Future principal repayments on the mortgages payable are as follows for 2016 to 2020 and thereafter:

| Year | Principal installment payments | Principal maturing | Total | W.A. contractual rate on debt maturing |
|---|---|---|---|---|
| 2016 (6 months) | 4,568,572 | 35,593,307 | 40,161,879 | 4.27% |
| 2017 | 6,967,434 | 118,092,125 | 125,059,559 | 4.97% |
| 2018 | 4,270,562 | 18,439,813 | 22,710,375 | 4.71% |
| 2019 | 4,095,516 | 18,590,780 | 22,686,296 | 3.61% |
| 2020 | 2,973,017 | 28,734,621 | 31,707,638 | 3.65% |
| Thereafter | 5,564,834 | 56,360,911 | 61,925,745 | 3.85% |
| Total | $ 28,439,935 | $ 275,811,557 | $ 304,251,492 | 4.38% |

The REIT's objective in securing mortgages for its properties and managing its long-term debt is to stagger the maturities in order to mitigate the risk of short-term volatilities in the debt markets. With the exception of certain mortgages, most of the REIT's mortgages do not contain cross-default provisions that would be triggered by the breach of a financial covenant.

As at December 31, 2015 the REIT was in technical violation of annual financial covenants on two mortgages secured by properties in Quebec. These mortgages do not contain cross-default provisions that would trigger the breach of other financial covenants. During the six months ended June 30, 2016 the REIT obtained a covenant tolerance waiver letter for both of these mortgages.

**Convertible Debentures**

During the fourth quarter of 2015, the REIT repaid its $28.8 million, Series I Debentures. As at June 30, 2016, the REIT has two outstanding series of unsecured convertible debentures, details are as follows:

| Series | Issuance Date | Expiry Date | Principal Amount | Contractual Interest rate | Fixed Conversion Price |
|---|---|---|---|---|---|
| Series II | September 5, 2012 | September 30, 2017 | 34,500,000 | 6.00% | 10.35 |
| Series III | March 12, 2013 | March 31, 2018 | 23,000,000 | 5.50% | 10.25 |
| | | | $ 57,500,000 | 5.80% | $ 10.31 |

The debentures' interest payments are payable semi-annually (March 31st and September 30th) in arrears. The debentures are convertible into units of the REIT at the option of the holder at any time on the earlier of the maturity date, or the date fixed for redemption of the debentures.

As at June 30, 2016, none of the debenture holders had converted their debentures to units of the REIT and given the conversion prices, it would be unlikely for any of the debenture holders to do so. Accordingly, the REIT will be pursuing alternative financing options as the debentures mature.

**Credit Facilities**

During the six months ended June 30, 2016, the REIT's credit facility was drawn to $2.0 million. The remaining availability of the REIT's credit facility is as follows:

| | | Jun 30, 2016 | | Dec 31, 2015 |
|---|---|---|---|---|
| Credit facility | $ | **10,000,000** | $ | 10,000,000 |
| Line of credit outstanding | | **(2,000,000)** | | (2,000,000) |
| Remaining unused credit facility | $ | **8,000,000** | $ | 8,000,000 |

The REIT's credit facility contains a debt to equity covenant that requires the REIT to be less than 2.50 to 1 for the 2016 quarterly reporting periods. As of June 30, 2016, the REIT's debt to equity ratio was 2.46 and therefore is in compliance with the covenant.

The Credit Facility matures December 1, 2016.

**Financing Costs**

Financing costs represent commitment fees, funding fees and other fees paid in connection with securing mortgages, debentures and the credit facility.

The unamortized balance of financing costs related to mortgages, debentures and the credit facility at June 30, 2016 was $2.6 million, which is $0.6 million lower than the December 31, 2015 year-end balance of $3.2 million. The decrease in the unamortized financing costs as at June 30, 2016 is due to recognition of deferred financing costs through financing expense in accordance with the effective interest method. The unamortized portion of the financing costs is netted against the REIT's mortgages payable, debentures and credit facility on the statement of financial position.

**Debt-to-Gross Book Value**

The REIT monitors its debt-to-gross book value ratio, a non-IFRS ratio that has become a common industry metric reviewed by analysts, unitholders and others within the industry. The REIT does not have a specific debt-to-gross book value threshold imposed on it in its Declaration of Trust. Management believes that the REIT's financial and strategic flexibility would be improved by a reduction in its debt-to-gross book value ratio. As the opportunity arises, management intends to reduce the debt to gross book value. At June 30, 2016 the REIT has a debt-to-gross book value ratio of 69.0% (December 31, 2015 – 69.5%), calculated as follows:

| As at | Jun 30, 2016 | Dec 31, 2015 |
|---|---|---|
| Debt:[1] | | |
| Mortgage principal | **304,251,492** | 305,050,117 |
| Debentures | **57,500,000** | 57,500,000 |
| Credit facilities | **2,000,000** | 2,000,000 |
| | **363,751,492** | 364,550,117 |
| Gross Book Value of Assets: | | |
| Book value of income producing properties | **513,032,027** | 511,817,617 |
| Book value of all other assets | **11,237,387** | 9,152,805 |
| Deferred financing fees | **2,649,218** | 3,225,396 |
| | **526,918,632** | 524,195,818 |
| Debt-to-Gross Book Value | **69.0%** | 69.5% |
| Debt-to-Gross Book Value Excluding Debentures | **58.1%** | 58.6% |

[1] Debt refers to the principal balance of mortgages, debentures and the credit facility.

### Unitholders’ Equity

For the six months ended June 30, 2016, unitholders’ equity increased $2.5 million over the balance at December 31, 2015. This increase was due to $5.7 million of net income and $1.0 million of distributions re-invested through the REIT’s DRIP program exceeding the $4.2 million in declared distributions.

*Distributions*

The REIT’s Trustees have discretion in declaring distributions and formally review the distributions on a quarterly basis. As of June 30, 2016 the REIT pays a distribution of $0.25 per unit on an annualized basis.

*Outstanding units*

As at June 30, 2016, the REIT had 33,688,697 (December 31, 2015 - 33,387,646) issued and outstanding units. The total aggregate principal amount of two series of convertible debentures due between 2017 and 2018 is $57.5 million with a total of 5,577,236 units issuable upon conversion of these debentures. The conversion prices for each series of convertible debenture is significantly higher than the current trading price of REIT units, as such it is not expected that any conversions will take place in the near future.

## LIQUIDITY REQUIREMENTS

The REIT’s main liquidity requirements arise from ongoing working capital requirements, debt servicing and repayment obligations, capital and leasing expenditures on existing properties, property acquisitions and distributions to unitholders. All of the aforementioned liquidity requirements, except for debt repayment obligations at maturity and property acquisitions, are generally funded from cash flows from operations or from drawing on the REIT’s credit facility. Debt repayment obligations for mortgages and convertible debentures are generally funded from refinancing the related debt and property acquisitions are generally funded from capital raises as well as obtaining debt financing on the related property. However, between capital raises, the REIT may use its $10.0 million credit facility to fund the equity portion of property acquisitions. For more on Liquidity Requirements – see part V – RISKS & UNCERTAINTIES – Liquidity Risk.

## QUARTERLY PERFORMANCE

The following is a summary of the interim results for each of the last eight quarterly periods.

| | Q2 2016 | Q1 2016 | Q4 2015 | Q3 2015 | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 |
|---|---|---|---|---|---|---|---|---|
| Total revenues | $ 13,937,629 | $ 14,403,183 | $ 14,374,728 | $ 14,334,061 | $ 13,856,589 | $ 14,524,120 | $ 14,935,452 | $ 14,507,888 |
| Operating expenses | 5,817,743 | 6,267,726 | 6,355,685 | 6,050,379 | 5,987,728 | 6,204,733 | 7,000,844 | 5,909,836 |
| Other expenses | 5,799,760 | 5,465,932 | 5,302,939 | 6,216,054 | 5,040,955 | 6,275,380 | 7,128,299 | 7,234,404 |
| Fair value gains (losses) | 1,024,664 | (290,380) | (14,348,545) | (1,684,003) | (2,038,886) | (6,140,328) | (3,900,519) | (14,538,979) |
| Net income (loss) | 3,344,790 | 2,379,145 | (11,632,441) | 383,625 | 789,020 | (4,096,321) | (3,094,210) | (13,175,331) |
| Net income (loss) per unit - basic | 0.10 | 0.07 | (0.41) | 0.01 | 0.03 | (0.16) | (0.11) | (0.47) |
| FFO | 2,537,933 | 2,887,316 | 2,830,049 | 2,444,179 | 2,175,256 | 2,344,810 | 1,091,535 | 2,458,189 |
| FFO per unit - basic | 0.08 | 0.09 | 0.10 | 0.09 | 0.08 | 0.09 | 0.04 | 0.09 |

## PART V – RISKS & UNCERTAINTIES

Income producing properties are inherently subject to certain risks and uncertainties due to their relative illiquidity and long term nature of the investment. Partners REIT's financial results, are therefore, dependent on the performance of its properties and by various external factors that impact the real estate industry and geographic markets in which the REIT operates. Some of the external factors that the REIT is exposed to include fluctuations in interest and inflation rates, access to debt, fulfilling legal and regulatory requirements and expansion or contraction in the economy as a whole.

Partners REIT's current business strategy is to focus on acquiring and managing a portfolio of retail and mixed-use retail community and neighbourhood centres, in both primary and secondary markets throughout Canada; and that generate stable cash flows over the long term. The quality of the REIT's current portfolio, management believes, provides the leverage the REIT needs to expand the business in new markets and acquire high performing properties. Management believes this strategy will enable the REIT's operations to achieve highly sustainable cash flows.

The following is an examination of the key factors that influence Partners REIT's operations. Further description of our risk factors is contained in the REIT's most recently filed Annual Information Form.

### INDUSTRY RISK

The REIT operates in the Canadian commercial and retail markets and is dependent on the ability to access financing. Fluctuations in real estate market values and general industry and economic circumstances affect the amount that can be borrowed and the terms and conditions under which funds are available. This may limit the REIT's ability to execute its operating and growth plans. Partners REIT manages this risk by maintaining sufficient resources to meet its obligations without undue risk to the REIT.

### INTEREST RATE AND FINANCING RISK

The REIT attempts to stagger the maturities of its debt portfolio evenly over a ten year time horizon in order to effectively manage both interest rate and liquidity risks. As the REIT re-finances its existing mortgages at maturity, management will obtain new financing terms that provide more balance to the current maturity profiles.

The REIT has an ongoing obligation to access debt markets to refinance maturing debt as it becomes due. There is a risk that lenders will not refinance such maturing debt on terms and conditions that are acceptable to Partners REIT or on any terms at all. The REIT's strategy of staggering the maturities of its debt portfolio attempts to limit the exposure to excessive amounts of debt maturing in any one year.

There is interest rate risk associated with the REIT's credit facility and certain variable rate mortgages since the interest rates are impacted by changes in the bank rate. There is also interest rate risk associated with the REIT's fixed interest rate and term mortgages and unsecured debentures due to the expected requirement to refinance such debts in the year of maturity. The following table outlines the impact to the REIT's annual net income if interest rates at June 30, 2016 would have been 100 basis points higher or lower, calculated on all debts maturing over the next 24 months, with all other variables held constant.

| | | Approximate Change in Annual Interest Expense | | Approximate Change in Interest Expense per Unit per Annum |
|---|---|---|---|---|
| Mortgages | $ | 1,680,075 | $ | 0.050 |
| Convertible Debentures | | 575,000 | | 0.010 |
| Credit Facility | | 20,000 | | 0.001 |
| | $ | 2,275,075 | $ | 0.061 |

Partners REIT's strategy to mitigate interest rate price risk for its variable rate mortgages is to enter into interest rate swap arrangements when deemed necessary. As at June 30, 2016, Partners REIT has three mortgages whereby the Lender has imbedded swap agreements to fix the interest rate. Partners REIT does not use swaps for speculative purposes.

Management is of the opinion that all debt can be extended, renewed, or refinanced from alternative debt or equity sources. Included with the debt are two series of convertible debentures that are set to mature on September 30, 2017 ($34.5 million) and March 31, 2018 ($23.0 million). Refinancing these debentures through debt financing, an equity issue or a combination thereof is required and management is considering their alternatives which include property disposition(s).

**CREDIT RISK**

Credit risk arises primarily from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease commitments. The REIT attempts to mitigate this risk by conducting credit assessments on new lessees, and by ensuring its tenant mix is diversified and by limiting its exposure to any one tenant. The maximum credit risk exposure at June 30, 2016 relates to the carrying value of the accounts receivable balance without taking into consideration any collateral held or other credit enhancements. Collateral held on certain leases are letters of credit or security deposits from tenants.

The REIT establishes an allowance for doubtful accounts that represents the estimated loss in respect of rents receivable. This amount is determined on a tenant by tenant basis based on the specific tenant related factors.

For cash and cash equivalents, accounts receivable and other short term assets, Partners REIT's credit risk is limited to the carrying value on the statements of financial position. To reduce credit risk, cash and cash equivalents are only held at major financial institutions.

**LIQUIDITY RISK**

The REIT's main liquidity requirements arise from ongoing working capital requirements, debt servicing and repayment obligations, capital and leasing expenditures and distributions to unitholders. All of the aforementioned liquidity requirements, except for debt repayment obligations are generally funded from cash flows from operations or from drawing on the $10.0 million Credit Facility ($2.0 million drawn at June 30, 2016). Property debt repayment obligations are generally funded from obtaining debt refinancing on maturing mortgages. Convertible debenture obligations that are not converted to equity can be repaid at maturity from either a new convertible debenture issue, mortgage financing on existing properties or disposition and/or from an equity raise.

Within the next 12 months the REIT has $72.9 million in maturing mortgages on eight properties. The REIT's financial condition and results of operations would be adversely affected if it were unable to obtain financing/refinancing, cost-effective financing/refinancing, or if it were unable to meet its other liquidity requirements from on-going operating cash flows.

The REIT attempts to mitigate its liquidity risk by:

- staggering the maturities of its maturing mortgages;
- not entering into property acquisitions unless it has secured or knows that it can secure the appropriate capital (debt and equity) to fund the particular acquisitions;
- planning capital spending around the availability of cash from operations or debt/equity funding; and
- reviewing the current liquidity position and forecasted cash flows in advance of the quarterly approval of monthly distributions.

Except for the periodic impact to cash for the $1.7 million in bi-annual interest payments on the two series of debentures (interest payments are due March 31$^{st}$ and September 30$^{th}$) most operating revenues and expenses are consistent on a month to month basis thereby assisting managements' forecasting of cash flows and liquidity.

As at June 30, 2016, the REIT had $3.3 million in cash and $8.0 million of capacity available under its Credit Facility, thereby providing $11.3 million in liquidity. Despite this liquidity, management will need to complete re-financings of maturing mortgages and continue to reduce other transaction costs or the REIT may be required to obtain further financing(s) or sell property(s).

In addition to re-financing maturing mortgages, the REIT will need to raise funds from a debt / equity issue(s) or net cash from property disposition(s), or a combination thereof, so that there is sufficient cash to repay two series of convertible debentures. There is currently a significant spread between the REIT's unit price and the conversion price for the two series of convertible debentures, and this reduces the likelihood that the debentures will be converted to equity in advance of their maturity. The convertible debentures are set to mature on September 30, 2017 ($34.5 million) and March 31, 2018 ($23.0 million). Obtaining replacement capital through new debt financing, new equity raises, the sale of properties, or any combination of these options will be essential to ensuring the REIT's continued financial flexibility.

As at June 30, 2016, the REIT has $93.9 million in current liabilities:

- $10.6 million is made up of accounts payable, accruals and distributions payable. These payables are to be repaid from a combination of working capital assets and ongoing cash flows from operations;
- $72.9 million from eight maturing loans across eight properties to be repaid from regular mortgage re-financings at their respective maturity dates;
- $8.4 million in regularly scheduled mortgage payments. These payments are to be made from a combination of working capital assets, ongoing operating cash flows and regular mortgage re-financings;
- $2.0 million from the maturing credit facility. Management expects to renew this facility at its maturity.

The REIT's interest coverage ratio of 1.59 (1.59 at December 31, 2015) and debt service coverage ratio of 1.06 (1.07 at December 31, 2015) both allow sufficient coverage to service the loans in the current and past reporting periods and management forecasts that there will continue to be sufficient cash being generated to allow for the regularly scheduled payments (interest and principal) of the REIT's debt obligations.

**ENVIRONMENTAL RISK**

Partners REIT is subject to various federal, provincial and municipal laws and regulations relating to environmental matters, which deal primarily with the costs of removal and remediation of hazardous substances. Environmental risk is relevant to the REIT's ability to sell or finance affected assets and could potentially result in liabilities for removal and remediation or legal claims against the REIT. Management is not aware of any material non-compliance with environmental laws or regulations at any of the REIT's properties, or of any pending or threatened actions, investigations or claims against the REIT relating to environmental matters.

Management will continue to make capital and operating expenditures to ensure that the REIT is compliant with environmental laws and regulations. At this time, management does not believe these costs will have a material adverse impact on the REIT's business. Management understands that environmental laws and regulations are subject to change and the REIT can be adversely impacted if laws and regulations become more rigorous.

**LEGAL AND REGULATORY RISKS**

Contingent Liability

As a condition of closing the Holyrood Rescission in October 2014, the REIT provided a $35.0 million loan guarantee to the lender of a loan to Holyrood Holdings Ltd. The loan was scheduled to mature June 30, 2015. The REIT has been advised that the loan was not repaid at maturity and that Holyrood is in the process of refinancing the loan with another lender. The current lender has advised that all interest payments on the loan are up-to-date and that the loan is being extended on a short-term basis. The REIT has taken the position with the lender that its guarantee has expired, but the lender disputes that. Should the lender make a demand on the REIT as a guarantor, the REIT may deny that it has any continuing liability under the guarantee or may at its sole discretion purchase the lender's interest in the loan thus granting the REIT a first charge over Hamilton City Centre. The REIT currently has a registered second mortgage on the property. The REIT has no ongoing interest in the Hamilton City Centre and does not intend to guarantee any debt in connection with Holyrood's refinancing of the property.

Uncertified Class Action Update

The REIT has been notified that a Statement of Claim dated November 28, 2014 has been issued in the Ontario Superior Court seeking certification of a class action on behalf of persons who held units of the REIT on April 1, 2014 against certain parties, including a former officer and Trustees of the REIT. The REIT itself has not been named as a defendant in the legal proceedings which allege that the conduct of the defendants in connection with the acquisition by the REIT of three properties from Holyrood in April 2014 caused harm to the plaintiffs.

The Holyrood transaction was rescinded by the REIT and Holyrood in October 2014. The REIT has certain indemnity obligations to its Trustees and officers (current and former) with respect to this claim, subject to exceptions including where it is determined that there has been a failure to act honestly and in good faith. The REIT has insurance which it expects to be applicable in these circumstances. Given that the REIT has not been named in the litigation, the REIT does not believe it will be material to its business and affairs.

## PART VI – CRITICAL ACCOUNTING POLICIES & ESTIMATES

The REIT's critical accounting policies are those that management has determined to be the most important in portraying the REIT's financial condition and results, and which require substantive estimates and judgment.

The preparation of financial statements requires certain estimates and judgments that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The REIT's significant accounting policies are described in Note 2 to the condensed consolidated financial statements for the three and six months ended June 30, 2016.

### DISCLOSURE CONTROLS AND INTERNAL CONTROLS

### CONTROL ASSESSMENT

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), on a timely basis so that appropriate decisions can be made regarding public disclosure. Management maintains appropriate information systems, procedures and controls to ensure the information that is publicly disclosed is complete, reliable and timely. This includes establishing adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

The REIT's Chief Executive Officer and the Chief Financial Officer assessed, or caused an assessment under their direct supervision, the design and operating effectiveness of the Trust's internal controls over financial reporting as at June 30, 2016 using the Committee of Sponsoring Organizations ("COSO") Internal Control – Integrated Framework (as published in 2013).

### LIMITATIONS OF INTERNAL CONTROLS

All internal control systems, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Given the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under potential future conditions, regardless of how remote.