MELCOR | REIT

Tradition. Growth. **Results.**

2013
Annual
Report

MELCOR | REIT

Tradition. Growth. **Results.**

Melcor REIT is an unincorporated, open-ended real estate investment trust. We own, acquire, manage and lease quality retail, office and industrial income-generating properties with exposure to high growth Western Canadian markets. Our portfolio is currently made up of interests in 30 properties representing approximately 1.76 million square feet of gross leasable area located in and around Edmonton, Calgary, Lethbridge, and Red Deer, Alberta; Regina, Saskatchewan; and Kelowna, British Columbia.

Backed by Melcor Development's 90-year history, Melcor REIT was born out of a proud tradition of real estate excellence in Western Canada.

Our growth potential is a true competitive advantage, with the right of first offer on Melcor's pipeline of high quality retail, industrial and office developments.

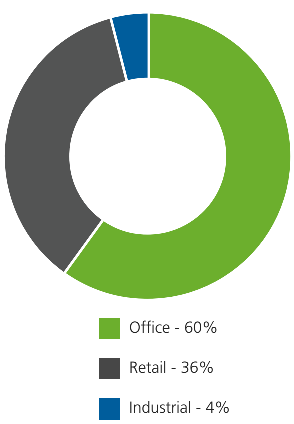
Through the REIT, we offer a new way to invest in Melcor's experience and we're proud to share our results. We're also excited to share with you some of the things that make us unique: Experience. Signature Customer Care. Sustainability. Asset Enhancement. Redevelopment Expertise.

For more information, please visit www.**MelcorREIT**.ca.

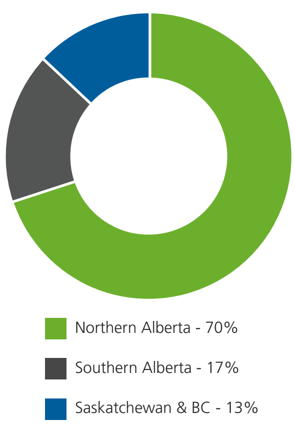
Facts & Data:

30 Assets (IPO:27) | **$39.3M** Revenue (2012: $37.5M) | **$455M Asset** Fair Value (2012: $397M)

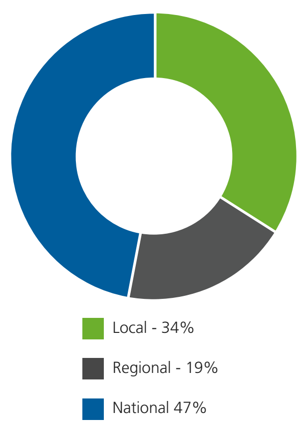
GLA by Property Type



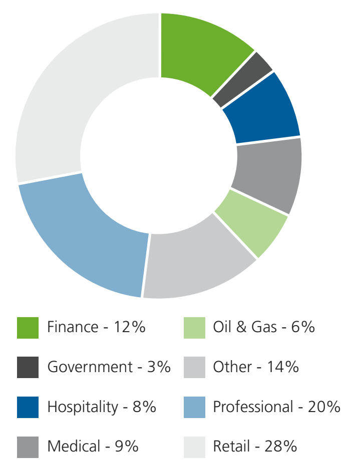
GLA by Region



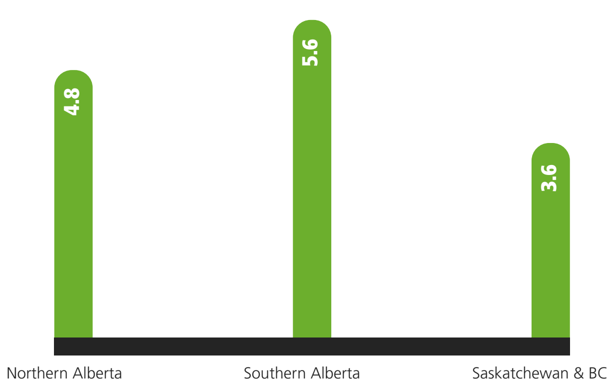
Retail GLA by Tenant Profile



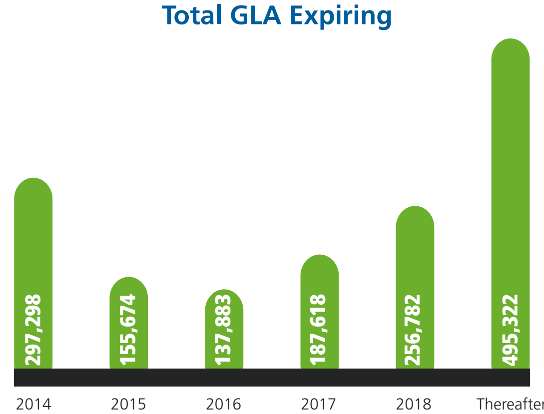
GLA by Tenant Industry



Weighted Average Lease Term (Years)



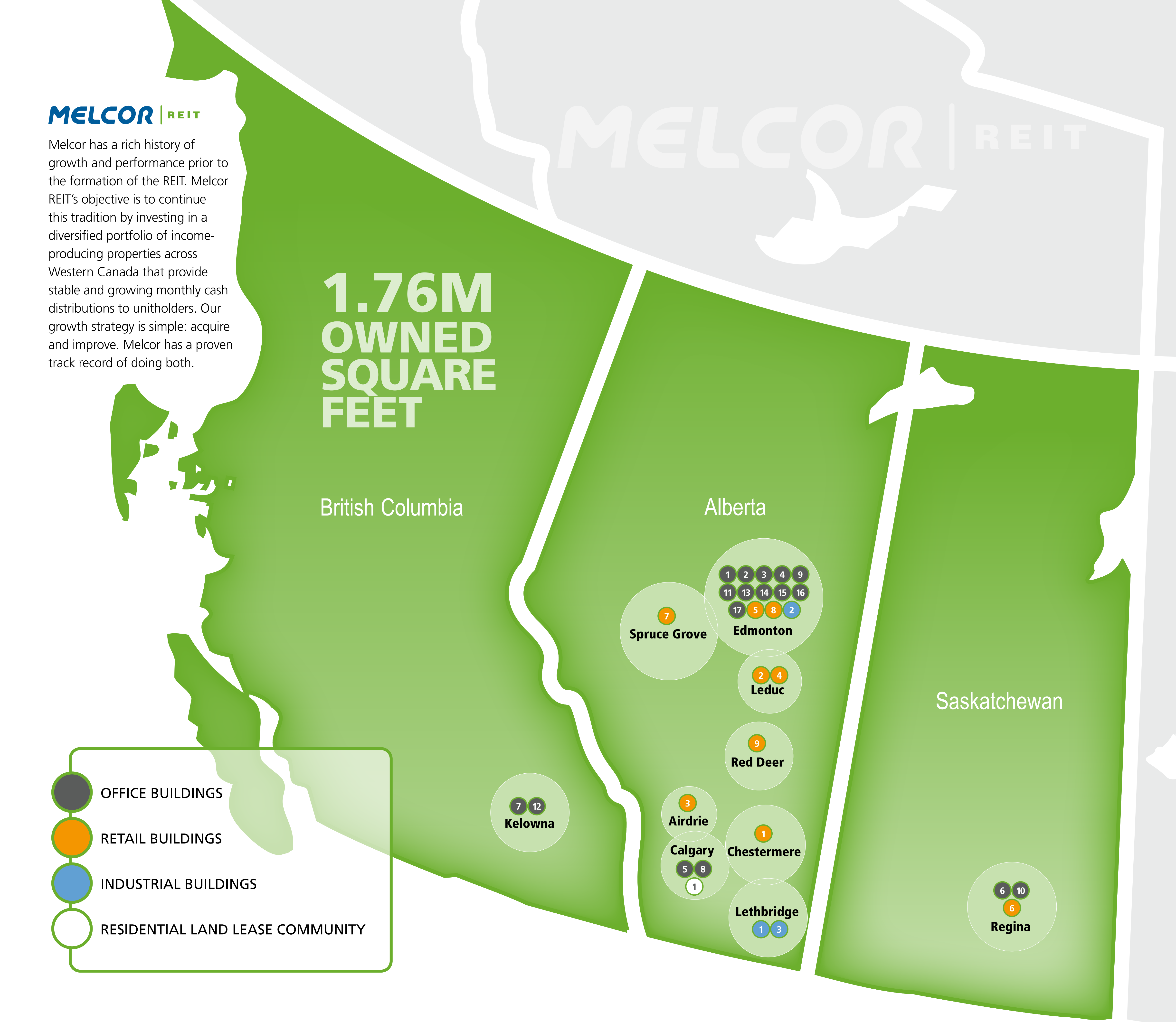
Total GLA Expiring



MELCOR | REIT

Melcor has a rich history of growth and performance prior to the formation of the REIT. Melcor REIT's objective is to continue this tradition by investing in a diversified portfolio of income-producing properties across Western Canada that provide stable and growing monthly cash distributions to unitholders. Our growth strategy is simple: acquire and improve. Melcor has a proven track record of doing both.

1.76M OWNED SQUARE FEET



	OFFICE BUILDINGS	LOCATION	GLA	OCC %
1	100 Street Place	Edmonton	44,295	77
2	Trail Business Centre	Edmonton	77,296	73
3	Birks Building	Edmonton	35,106	70
4	Capilano Centre	Edmonton	45,150	99
5	Crowfoot Business Centre	Calgary	67,603	100
6	Executive Terrace	Regina	42,843	77
7	Kelowna Business Centre	Kelowna	72,076	74
8	Kensington Road Building	Calgary	24,050	93
9	Melton Building	Edmonton	114,612	93
10	Parliament Place	Regina	24,411	100
11	Princeton Place	Edmonton	59,081	93
12	Richter Street	Kelowna	28,978	97
13	Royal Bank Building	Edmonton	132,376	90
14	Stanley Buildings	Edmonton	34,976	99
15	Sterling Business Centre	Edmonton	67,909	92
16	Westcor Building	Edmonton	72,810	88
17	Westgate Business Centre	Edmonton	75,141	94
	TOTAL		**1,018,713**	**89**

	RETAIL BUILDINGS	LOCATION	GLA	OCC %
1	Chestermere Station	Chestermere	48,704	96
2	Corinthia Plaza	Leduc	23,179	100
3	Kingsview Market	Airdrie	36,003	100
4	Leduc Common	Leduc	213,692	82
5	Miller Crossing	Edmonton	27,473	78
6	Towers Mall	Regina	114,331	94
7	Westgrove Common	Spruce Grove	21,810	99
8	Coast Home Centre	Edmonton	59,725	72
9	Liberty Crossing	Red Deer	63,317	100
	TOTAL		**608,234**	**93**

	INDUSTRIAL BUILDINGS	LOCATION	GLA	OCC %
1	Lethbridge Industrial	Lethbridge	49,005	100
2	TKE Building	Edmonton	15,968	100
3	LC Industrial	Lethbridge	67,610	100
	TOTAL		**132,583**	**100**

	LAND LEASE COMMUNITY	LOCATION	GLA	OCC %
1	Watergrove	Calgary	NA	100

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MELCOR | REIT

Westcor
Edmonton

Experience

Experience matters. It is a key component of our ability to deliver results. We may be a new company, but our team is made up of real estate experts with substantial knowledge of the markets where we operate and the buildings we own. In fact, we collectively have over 350 years of real estate and property management experience.

Melcor has been actively involved in each of the markets where we operate for decades, both as property manager and land developer.

We also have intimate experience with our assets. We've owned them for an average of over nine years. And Melcor either built or substantially redeveloped 58% of our total gross leasable area.

Our team is focused on growth while remaining committed to stewardship and solid governance. Our mandate is to provide stable and growing returns to our unitholders.

Andrew Melton
Executive Chairman
Years with Melcor: **29**
Industry Experience: **35**

Darin Rayburn
Chief Executive Officer
Years with Melcor: **11**
Industry Experience: **20**

Jonathan Chia
Chief Financial Officer
Years with Melcor: **3**
Industry Experience: **3**

Bob Brown
Vice President, Investment Properties
Years with Melcor: **4**
Industry Experience: **21**

Greg Stevenson
Senior Property Manager
Years with Melcor: **10**
Industry Experience: **10**

Signature Customer Care

Our goal is to be the Landlord of Choice in our markets by providing outstanding customer care and dependable, high quality service to our clients.

Hands-On Office Building Management

Our hands-on, on-site building management delivers exceptional customer care and identifies issues early on for prompt resolution.

Continuous Improvement

We continually improve our assets with value-add investments that enhance quality and the tenant experience while also contributing to sustainability and environmental best practices including practices such as xeriscaping and LED lighting in common areas. We use our intimate knowledge of the buildings we operate to support our capital investment decisions, optimize operating efficiency and continuously improve our buildings for improved client satisfaction.

Enhancements to improve sustainability

Many of our continuous improvement initiatives focus on sustainability and energy reduction strategies to ensure our buildings are green. We are dedicated to achieving and maintaining BOMA BESt standards where applicable and have 3 BOMA BESt rated buildings.

Relationship Focused

We have many long-term clients – some who have been with us for over 20 years. We take pride in building strong relationships with our tenants and continually meeting their needs as their businesses evolve.

Responsive Care

Help is always just a phone call or a click away. We upgraded our customer care program in 2013 with our new online Customer Care portal (care.Melcor.ca) to complement our 1-866-MELCOR1 number. No matter how our tenants contact us, we respond within 30 minutes over 95% of the time.

Asset Enhancement & Redevelopment

Our capital expenditures strategy is to PRESERVE our existing assets and ENHANCE their desirability.

Preservation activities include the inner works of the buildings: boilers, roofs, and on-going maintenance that helps to maintain asset value through routine care. We also look at ways to improve efficiencies as we are upgrading to help reduce building operating costs. These activities are driven by annual building and equipment condition assessments.

Enhancement activities include high visibility items such as common area and washroom upgrades, landscaping, improved comfort and aesthetics.

We have a proven track record of successfully redeveloping and improving our assets. This success is a result of our experience: both with the properties in our portfolio and with the markets we serve.

In 2013, we completed two major redevelopment projects.

Capilano Centre
Edmonton

The Capilano building was modernized to increase aesthetic appeal and improve building function. The new façade includes architectural paneling to add dimension to the building. Common areas – including the main lobby and washrooms – were also upgraded. In addition, new HVAC, elevators and windows improve tenant comfort and convenience. In conjunction with the redevelopment, a vacant retail space was converted to a parking garage for increased revenue and unused common area space was converted to storage units. Prior to the renovations, occupancy hovered at around 80%. Today the building is fully occupied.

Princeton Place
Edmonton

Princeton Place underwent a complete façade overhaul, including redevelopment of the main floor retail space to increase street presence, making the building more welcoming and modern. In addition to a beautiful new façade, the building received new HVAC, washroom upgrades and a new lobby. Prior to the redevelopment, the building had occupancy in the mid 80s. With the improved curb appeal, occupancy is now at 97%.

Sustainability

While we continually improve our properties to enhance tenant experience through redevelopment, we always look to do so in a way that will reduce our environmental footprint over the long term. Many of our continuous improvement initiatives focus on sustainability and energy reduction strategies to ensure our buildings are green. As we upgrade and replace equipment, we do so with technology that promotes energy efficiency and best practices. We also engage a third party to monitor and analyze our energy usage to identify ways it can be improved.

Preventative maintenance is a large part of our overall sustainability program. Each of our buildings is assessed annually.

We employ leading edge technologies where possible, especially as older buildings are modernized. These practices include:

BOMA BESt

We are dedicated to achieving and maintaining BOMA BESt standards where possible. BOMA BESt is the leading environmental certification program for existing buildings in Canada. We have 3 BOMA BESt certified Green & Responsible buildings and continually assess our buildings against the BOMA BESt standards.

Westcor
Edmonton

Light Harvesting

You don't turn your lights on at home when sunshine is streaming in, so why should your office environment? Our light harvesting system measures ambient light and adjusts accordingly.

Motion Sensitive Lights

With motion sensitive lighting systems, you don't need to remember to turn off the lights. Office and washroom lights turn on and off automatically based on motion.

Paper Recycling

Our office buildings have active paper recycling programs. In 2012, we saved over 500 trees and kept 28 tonnes out of landfill.

Royal Bank Building
Edmonton

Other Recycling

We recycle wherever possible, including light bulbs and fluorescent lamps.

Our retail developments benefit from LED lighting and light timers. We also use xeriscaping and irrigation systems to keep our properties looking great with minimum water usage.

Where it makes sense, we employ co-generation in our office towers to simultaneously generate electricity and useable heat. This decreases operating costs and increases energy efficiency.

STATS:

- 3 BOMA BESt certified Green & Responsible buildings
- Royal Bank Building Co-Generation Project:
  776 tonne carbon footprint reduction
  = getting 158 cars off the road or planting 660 acres of forest.
- Paper recycling programs in office towers saved over 500 trees in 2012.

Building Environmental Standards BOMA BESt

Crowfoot Business Centre
Calgary

Letter from the Chairman

Andrew Melton

Dear unitholders,

I am honored to report to you in our first annual report. 2013 was an eventful and exciting year for us as we completed the initial public offering of Melcor REIT in order to better take advantage of capital markets to continue to grow both Melcor Developments Ltd. and the Melcor REIT. Looking back over the past year, there are a number of things that we can be proud of.

One of the things that we're most proud of is that we did what we said we would. It may seem simple, but ensuring we deliver as promised is one component of the culture of integrity that Melcor has held dear for 90 years. We had a terrific year, which is a tribute to our team and the excellent real estate assets found in the REIT.

I am delighted with the quality our team. They worked diligently to make the Melcor REIT initial public offering a reality. Our team, including Melcor Developments staff, also ensured that the transition to the REIT occurred seamlessly for our tenants. In reality, operations remain unchanged. The team is the same, and that means that Melcor's proud culture continues on in the REIT.

I am also pleased with the group of outside trustees who have agreed to come onboard and share their time and wisdom. With Melcor Development's as a majority unitholder, we wanted to ensure that our minority unitholders have a strong voice, and you can be assured that you are well represented with these trustees as the stewards of our company. I am honored to work with them.

As we look towards the future, all indicators remain favourable for our growth, including the Western Canadian economy, and a growing pipeline of potential acquisitions. 2014 looks very promising.

The pipeline of Melcor Development's assets under development is one of our key differentiators. We look forward to taking advantage and growing our asset base through this high quality pipeline, but we will also continue to look at third party acquisitions as a means to achieve our growth objectives.

Our close relationship with Melcor means that we also share the management philosophies that are part of Melcor's enduring success: while we focus on growth, we do so in a conservative way – always protecting our unitholders investment in the company. Melcor is committed to maintaining majority ownership in the REIT. They have a deeply vested interest in ensuring that the REIT is successful, as the success of Melcor REIT also contributes to the success of Melcor.

Ours is a business built on relationships, and we cherish our continued great relationships with all our stakeholders – including our tenants, lenders and partners.

Finally, I would like to personally thank you – our investors – for taking a chance on us. We appreciate your commitment and hope that you will stay on board as our story unfolds. Our goal is to reward your confidence in us with stable and growing cash distributions.

Letter from the CEO

Darin Rayburn

Dear unitholders,

It is a great privilege to report to you. It has been an exciting year for us and I'd like to share our journey thus far and our plans for the future.

TRADITION

Although it is our inaugural annual report, our pedigree is an important part of who we are and what makes us unique. Melcor REIT is a spin-off of Melcor Developments Ltd., which has a 90-year tradition of excellence in the real estate business. Melcor Developments continues to manage the assets in our portfolio. For our clients (how we refer to our tenants), the transition was seamless. They continue to call on the same building managers and property managers whom they've come to rely on over the years.

In fact, Melcor has owned the buildings in our portfolio for an average of over 9 years and built or substantially enhanced 58% of our total gross leasable area. In short, we know our assets really well. And we're continuing to build on our solid reputation through ongoing improvements to our signature customer care and asset enhancement programs. Our team has over 350 years combined real estate experience in the markets where are properties are located.

We are very proud to carry on some key Melcor traditions, including providing a consistent return to unitholders and an unrelenting focus on providing excellent service to our clients and our partners.

GROWTH

Our pedigree provides us with the right background and experience to achieve our growth objectives, and our close relationship with Melcor provides us with a unique property pipeline for continued growth. Melcor Developments is currently developing some of the most innovative industrial, office and retail properties the likes of which are simply not available in our markets today, and it's very exciting for us to see this pipeline coming together.

The Village at Blackmud Creek, a 33-acre business park with planned total development of 725,000 square feet.

Letter from the CEO (continued)

In addition to growth through this proprietary pipeline (where we have the Right of First Offer on the properties), we plan to continue to seek out third party acquisitions. In 2013, we completed two acquisitions and a third was completed early in 2014. Each of these acquisitions meets our acquisition criteria: in the markets we know best, quality construction, strong occupancy, accretive to AFFO, and with potential to benefit from our asset enhancement capability.

These acquisitions added 173,652 sq. ft. to our portfolio. They add depth to our industrial and retail properties, and one is our first property in the important connector community of Red Deer, a market that Melcor has been active in for many years.

RESULTS

Since May 1, 2013, we've been focused on delivering the results that we promised to you in our prospectus documents. I'm pleased to say that we've done just that: we've not only delivered as promised, we exceeded forecast on all significant measures.

Throughout the year, even though it was "business as usual" for operations, we took the formation of the Melcor REIT as an opportunity to polish up and improve on some of the things that we've historically done so well, including expanding our signature customer care program with the addition of an online portal for service requests.

STRATEGY

Our goal is to be the best at what we do. We're focused on quality assets in the markets that we know best and applying our exceptional knowledge of real estate fundamentals to operate our portfolio for maximum return to our unitholders. This means achieving optimum operating efficiency, annual building assessments and follow on preventative maintenance, paying attention to our clients through our signature customer care program and ongoing enhancements to protect our investment in our assets and maximize occupancy.

OUTLOOK

Today, there are many positive factors that will continue to shape our growth and our future. We have a well established and diversified portfolio of assets in high growth Western Canadian markets. We have a solid pipeline of over 3.8 million square feet of high quality assets being developed over the next 5-10 years. The experienced Melcor team continues to manage and lease our properties exceptionally well while building strong relationships with our clients. This team also has proven ability to redevelop assets to maximize their potential – we've invested over $17 million in our asset portfolio over the past 5 years and plan to invest an additional $6 million over the next 10 years. We expect reasonable interest rate stability over the medium term, and we were able to refinance a number of mortgages at lower interest rates over the past year.

We remain confident in our future and our ability to continue to deliver results according to plan and consistent returns to unitholders.

Financial Highlights

- Adjusted Funds from Operations per unit increased 24% to $0.75
- Annual net operating income grew by 5% to $25.30 million, and exceeded 9 month forecast by 4%
- Annual rental revenue grew by 5% to $39.33 million, and exceeded 9 month forecast by 4%

Transactions

Property	Coast Home Centre	LC Industrial	Liberty Crossing
Acquisition Date	September 12, 2013	January 10, 2014	December 2013
Location	Edmonton, AB	Lethbridge	Red Deer, AB
Property Type	Retail	Industrial Warehouse	Retail
GLA	59,725 l 4.21 acre site	67,610 l 2.89 acre site	63,328 l 4.72 acre site
Purchase Price	$12.3 million	$5.9 million	$13.25 million

Board of Trustees & Corporate Governance Practices

We are committed to effective corporate governance practices as a core component of our operating philosophy. Strong governance practices lay the foundation for a sustainable company and long-term value creation for our unitholders.

As governance practices evolve, we periodically review, evaluate and enhance our governance program. Here are a few highlights of our program.

Independence

The majority of our trustees are independent. Committees are comprised by a majority of independent trustees. The audit committee is 100% independent. The independent trustees meet in camera (without management and related trustees) for a portion of each board and committee meeting held. As our executive chairman is related to Melcor, we have appointed a lead trustee, Don Lowry, who is independent. Mr. Lowry chairs the in camera sessions of the board and ensures that the board conducts itself in accordance with good governance practices. Each of the arrangements with Melcor (Asset Management, Property Management, and Development and Opportunities Agreements) require the agreement of the majority of independent trustees, providing independent oversight on all transactions to represent the interests of minority unitholders.

Integrity: the Heart of our Business

The highest standard of ethical conduct has always been at the heart of Melcor's operating philosophy. Trustees and officers follow our Code of Business Conduct and Ethics, which governs the work environment, regulatory compliance and the protection of our assets and reputation. The Code can be found on our website at www.MelcorREIT.ca. Melcor Development employees, who manage our properties, follow the Melcor Code of Business Conduct and Ethics, which is largely the same.

Andrew Melton
Executive Chair of the Board

RELATED
Since: 2013
Attendance: 100%
Unitholdings: 54,600
Compensation*: $nil
Committees: -

Brian Hunt
President & Director, Taviston Inc.

INDEPENDENT
Since: 2013
Attendance: 100%
Unitholdings: 40,000
Compensation: $28,667
Committees: Audit, Compensation & Governance, Investment

Larry Pollock
Corporate Director

INDEPENDENT
Since: 2013
Attendance: 100%
Unitholdings: 50,000
Compensation: $20,500
Committees: Audit, Investment

Ralph Young
Chancellor, University of Alberta

RELATED
Since: 2013
Attendance: 100%
Unitholdings: 17,800
Compensation*: $nil
Committees: Compensation & Governance

Board of Trustees & Corporate Governance Practices
(continued)

Strategic Planning Process

The board ensures that we establish a solid strategy designed to optimize unitholder value. This process includes active consultation with management on the issues, business environment, assumptions, goals and financial budgets that underpin the strategy and ensures that risk levels are appropriate.

To ensure that the board is fully informed and engaged in the strategic issues and critical risks of our business, one meeting each year is dedicated to the review and approval of our strategic plan to manage risk, protect unitholder value and build a sustainable business.

Alignment with Unitholder Interests

All trustees and officers took part in the REIT initial public offering and own on, average, over 23,000 units. This ensures alignment with unitholder interest and a focus on long-term value creation.

Additional information on our governance practices can be found in our 2013 Information Circular.

**Melcor employees do not receive trustee compensation.*

Brian Baker
Chief Executive Officer, Melcor Developments Ltd.

RELATED
Since: 2013
Attendance: 100%
Unitholdings: 5,000
Compensation*: $nil
Committees: -

Donald Lowry
Lead Director, Corporate Director

INDEPENDENT
Since: 2013
Attendance: 100%
Unitholdings: 5,000
Compensation: $25,333
Committees: Audit, Compensation & Governance

Patrick Kirby
Counsel, Felesky Flynn LLP

INDEPENDENT
Since: 2013
Attendance: 100%
Unitholdings: 5,000
Compensation: $17,500
Committees: -

Chestermere Station
Chestermere

Management's Discussion & Analysis

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March 10, 2014

The following Management's Discussion and Analysis ("MD&A") of Melcor Real Estate Investment Trust's (the "REIT" or "Melcor REIT") results should be read in conjunction with the consolidated financial statements and related notes for the year ended December 31, 2013. The discussion outlines strategies and provides analysis of the financial performance for fourth quarter and the full year. The analysis also provides a comparison to the REIT's forecast provided in its prospectus dated April 19, 2013.

The underlying financial statements in this MD&A, including 2012 comparative information, have been prepared in accordance with International Financial Reporting Standards (IFRS) unless otherwise noted.

The REIT's Board of Trustees, on the recommendation of the Audit Committee, approved the content of this MD&A on March 10, 2014. Disclosure contained in this MD&A is current to March 10, 2014, unless otherwise indicated.

Non-Standard Measures

We refer to terms and measures which are not specifically defined in the CICA Handbook and do not have any standardized meaning prescribed by IFRS. These measures include funds from operations ("FFO"), adjusted funds from operations ("AFFO") and net operating income ("NOI"), which are key measures of performance used by real estate businesses. We believe that these measures are important in evaluating the REIT's operating performance, financial risk, economic performance, and cash flows. These non-standard measures may not be comparable to similar measures presented by other companies and real estate investment trusts and should not be used as a substitute for performance measures prepared in accordance with IFRS.

Non-standard measures are defined on page 35: "*Non-Standard Measures.*"

Financial Reporting: Reorganization and Recapitalization

The Offering and acquisition of the Initial Properties is accounted for as a reorganization and recapitalization using the continuity of interests method as Melcor Developments Ltd. ("Melcor") will retain control over the REIT. Under this method, the REIT records the assets acquired and liabilities assumed at their carrying amounts on the closing date of the transaction. The difference between the consideration given and the aggregate value of the net assets acquired is recorded as an adjustment to unitholders' equity. Refer to note 6 of the consolidated financial statements for details of the accounting treatment for the acquisition of the Initial Properties. This MD&A includes financial information for periods prior to the formation of the REIT, including the comparative periods. This information is based on the historical combined financial information for the Initial Properties as previously reported by Melcor. Note 19 of the consolidated financial statements contains statements of income and comprehensive income and cash flows for the periods separated by the activities of the REIT, and its predecessor, Melcor.

Throughout this MD&A we make reference to the terms "we", "our" and "management". These terms are used to describe the activities of the REIT through the eyes of management, as provided by Melcor under the asset management and property management agreements entered into as part of the Offering and acquisition of the Initial Properties.

Regulatory Filings

Additional information about the REIT, including our annual information form, management information circular and quarterly reports, is available on our website at melcorREIT.ca and on SEDAR at sedar.com.

Formation of Melcor REIT

The REIT is an unincorporated, open-ended real estate investment trust established pursuant to a declaration of trust dated January 25, 2013, which was subsequently amended and restated May 1, 2013.

We began operations on May 1, 2013 when our trust units were issued for cash pursuant to the initial public offering ("Offering" or "IPO"). Units of the REIT trade on the Toronto Stock Exchange under the symbol MR.UN.

We initially issued 8,300,000 trust units at a price of $10.00 per unit for total gross proceeds of $83.00 million. The total proceeds received by the REIT, net of underwriters' fee was $78.02 million.

On May 1, 2013, the REIT used a portion of the proceeds of the IPO to indirectly acquire interests in a portfolio of 27 income-producing properties (the "Initial Properties") located in Western Canada, through a limited partnership (the "Partnership"). These Initial Properties are primarily retail, office and industrial assets with a total carrying value of $397.90 million. As partial consideration for the Initial Properties, Melcor received Class B LP Units of the Partnership and special voting units of the REIT. On May 10, 2013, the underwriters exercised their over-allotment option to purchase an additional 830,000 trust units from Melcor, at a price of $10.00 per unit, for gross proceeds of $8.30 million.

The over-allotment was fulfilled through conversion of the Class B LP Units owned by Melcor into trust units. Following closing of the over-allotment option, Melcor, through an affiliate, holds an approximate 51.1% effective interest in the REIT through ownership of all remaining 9,530,798 Class B LP Units of the Partnership and a corresponding number of special voting units of the REIT. The Class B LP Units are economically equivalent to, and exchangeable for, trust units.

The Partnership also assumed mortgages on certain properties totaling $92.36 million at April 30, 2013. Melcor retained the debt on certain properties (the "Retained Debt") with a fair value of $96.51 million at April 30, 2013. In consideration of the Retained Debt, Melcor received Class C LP Units of the Partnership. These units will receive priority distributions in an amount expected to be sufficient to cover the interest and principal on the Retained Debt, which Melcor will remain responsible for.

Declaration of Trust

The investment guidelines and operating policies of the REIT are outlined in the Amended and Restated Declaration of Trust ("DOT") dated May 1, 2013. A copy of the DOT is filed on SEDAR at sedar.com and is available on request to all unitholders. At March 10, 2014, the REIT was in compliance with all investment guidelines and operating policies stipulated in the DOT.

Caution Regarding Forward-Looking Statements

In order to provide our investors with an understanding of our current results and future prospects, our public communications often include written or verbal forward-looking statements.

Forward-looking statements are disclosures regarding possible events, conditions, or results of operations that are based on assumptions about future economic conditions, courses of action and include future-oriented financial information.

This MD&A and other materials filed with the Canadian securities regulators contain statements that are forward-looking. These statements represent the REIT's intentions, plans, expectations, and beliefs and are based on our experience and our assessment of historical and future trends, and the application of key assumptions relating to future events and circumstances. Forward-looking statements may involve, but are not limited to, comments with respect to our strategic initiatives for 2014 and beyond, future leasing, acquisition and financing plans and objectives, targets, expectations of the real estate, financing and economic environments, our financial condition or the results of or outlook of our operations.

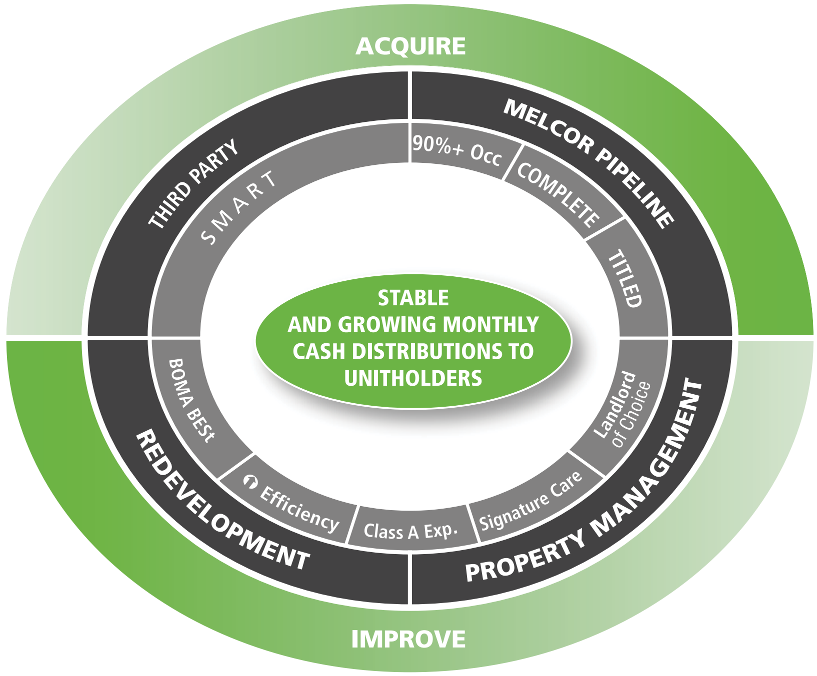
By their nature, forward-looking statements require assumptions and involve risks and uncertainties related to the business and general economic environment, many beyond our control. There is significant risk that the predictions, forecasts, valuations, conclusions or projections we make will not prove to be accurate and that our actual results will be materially different from targets, expectations, estimates or intentions expressed in forward-looking statements. We caution readers of this document not to place undue reliance on forward-looking statements. Assumptions about the performance of the Canadian economy and how this performance will affect the REIT's business are material factors we consider in determining our forward-looking statements. For additional information regarding material risks and assumptions, please see the discussion under Business Environment and Risks.

Readers should carefully consider these factors, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. Except as may be required by law, we do not undertake to update any forward-looking statement, whether written or oral, made by the REIT or on its behalf.

Our Business: Vision, Goals & Strategy

Melcor REIT has an established and diversified portfolio focused on high-growth markets in Western Canada. We owned 29 income-producing office, retail and industrial properties representing 1.69 million square feet in gross leasable area (GLA) at December 31, 2013. These high-quality properties feature stable occupancy and a diversified tenant mix of tenants, some of whom have been in place for over 20 years. The REIT is externally managed, administered and operated by Melcor Developments Ltd. ("Melcor") pursuant to the asset management and property management agreements entered into in connection with the IPO.

Melcor, a real estate company founded in 1923, has a rich history of growth and performance prior to the formation of the REIT. Our objective is to continue that tradition by expanding our portfolio of income-producing properties across Western Canada to provide stable and growing monthly cash distributions to unitholders. Our growth strategy is simple: acquire and improve. Melcor has a proven track record of doing both.



Acquire

Our acquisition growth strategy is focused on:

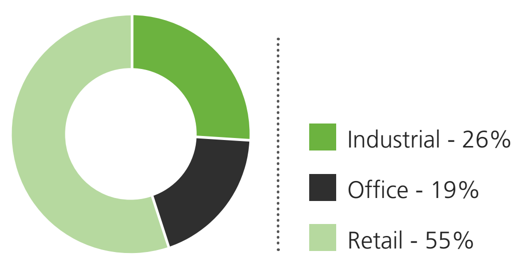
- Increasing penetration in existing geographic markets to exploit existing competitive advantage
- Expanding to adjacent geographic markets, and
- Diversifying our property portfolio.

We focus on two channels to support our acquisition growth strategy:

- Acquiring properties via our proprietary pipeline: As Melcor develops and leases commercial properties, the REIT has a right to purchase each asset. This organic asset pipeline is unique to the REIT. Based on projects currently being developed or planned to begin in the near-term, we expect this current acquisition pipeline to yield 3.8 million square feet of GLA over the next 5-10 years. Under the development and opportunities agreement entered into at the IPO, the REIT also has the opportunity to participate in investment opportunities, joint ventures and mezzanine financing on Melcor projects.

Melcor currently has 590,000 square feet under development.

GLA Under Development



Construction continues on each of these projects; however, no properties met the REIT acquisition criteria (90%+ occupied, construction completed and titled) in 2013.

- Acquiring accretive income-producing properties: We actively seek strategic property acquisitions that fit our SMART investment criteria: properties that have a good Story, are in the right Market, Accretive to AFFO per unit, at the Right price and in our Targeted areas. Target acquisitions include properties with potential to increase value through expansion, redevelopment or improved property management.

The section titled Our Business: Vision, Goals & Strategy above and on the following pages contains forward-looking statements. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. Please refer to the Caution Regarding Forward-looking Statements on page 14.

Our Business: Vision, Goals & Strategy

SMART Acquisition Strategy

Story **M**arket **A**ccretive **R**ight Price **T**argeted	**Acquisition Targets** • Stable, accretive properties • Penetrate existing geographic markets • Expand into adjacent geographic markets • Properties with redevelopment and repositioning potential **Acquisition & Integration Strengths** • Proven due diligence process • Agility to quickly execute on decisions • Ability to close within 30 days (broker preference for access to unmarketed opportunities) • Clustering of properties for efficient management & strong market knowledge

In 2013, we completed 2 external acquisitions, adding 123,042 sq. ft. of retail GLA to our portfolio for a total purchase price of $25.85 million. Early in 2014, we completed an additional external acquisition which added 67,610 sq. ft. of industrial GLA to our portfolio for $5.9 million. Each of these acquisitions was consistent with our acquisition growth strategy and helped to further diversify our portfolio.

In contemplating and completing strategic acquisitions, we use our proven due diligence process and ability to quickly execute on opportunities.

Improve

There are two key components to improving our existing assets – property management and asset enhancement. The goals of our property management and asset enhancement programs are to:

- Maximize occupancy
- Maximize tenant retention
- Increase rental income

Property Management

To ensure that our occupancy rates remain high and that our space is leased at attractive rates, we are committed to being the Landlord of Choice by providing consistent, high quality service and our signature customer care program to our clients.

Efficient property management optimizes operating costs, occupancy and rental rates. Our hands-on, on-site building management identifies issues early on for prompt resolution, and with continuous logging and monitoring of all maintenance activity, we can make capital investment decisions at the right time to sustain long-term operating margins.

Our property management practices are designed to improve operating efficiency and reduce cost while at the same time increasing client satisfaction and thus retention rates. We enjoy strong, long-term relationships with our clients, some of whom have been with Melcor for over 20 years.

Our signature customer care program is focused on responsiveness. We are proud of our track record of responding to over 95% of service requests within 30 minutes during business hours. Our signature customer care program was enhanced and rebranded shortly after the REIT IPO. We added an online customer care portal and extended the program to our retail and industrial properties.

With 17.6% (297,298 sq. ft.) of total GLA expiring in 2014, we developed an early renewal strategy focused specifically on larger tenants. As a result of this program, over half of the GLA expiring in 2014 has already been renewed.

Asset Enhancement

Capital Expenditures Program Strategy

PRESERVE	• Inner works (boilers, roofs, maintenance) • Maintain asset value through routine care • Improve efficiencies through upgrades (lower building operating costs) • Driven by annual building & equipment condition assessments
ENHANCE	• Visible improvements (common areas upgrades, landscaping, improved comfort & aesthetics • Upgrades the help lease buildings & retain tenants • Driven by lease expiries/vacancy and need

We continually improve our assets with value-adding investments that enhance property quality, which leads to higher occupancy and rental rates. These upgrades typically focus on increasing operating efficiency, property attractiveness, functionality and desirability. We use our intimate knowledge of the buildings we operate to support capital investment decisions, optimize operating efficiency and continuously improve our buildings for improved client satisfaction. Each building undergoes an annual assessment to identify preventative maintenance and capital investment requirements, and we continuously monitor and log all equipment and maintenance activity.

Our Business: Vision, Goals & Strategy

Melcor invested over $17 million in asset preservation and enhancement over the past 5 years and we expect to invest a further $6 million over the coming 10 years based on building condition assessment reports.

Many of our continuous improvement initiatives focus on sustainability and energy reduction strategies to ensure our buildings are green. As we upgrade and replace equipment, we do so with technology that promotes energy efficiency. We also engage a third party to monitor and analyze our energy usage to identify ways it can be improved.

We are dedicated to achieving and maintaining BOMA BESt standards. BOMA BESt is the leading environmental certification program for existing buildings in Canada. We had 2 BOMA BESt certified Green & Responsible buildings at the end of December and we were pleased to receive BOMA BESt certification on a third building in January 2014. We continue to assess our buildings against the BOMA BESt standards.

Key Metrics

Metric	Target	2013
Debt/Gross Book Value	50-55%	51%
Tenant Retention	75%	75.5%
Occupancy	90%+	90.6%
Portfolio Diversification	40% Retail 40% Office 20% Industrial	36% Retail 60% Office 4% Industrial
Weighted Average Base Rent	$16.35+	$17.49
Customer Care On-time Response	95%+	95.3%

2013 Highlights & Key Performance Indicators

	Year Ended December 31		
Metric	**2013**	**2012**	**Change**
Non-Standard KPIs			
Net operating income (NOI)	25,295	24,060	5%
Funds from operations (FFO)	15,903	13,742	16%
Adjusted funds from operations (AFFO)	13,916	11,197	24%
Rental revenue	39,325	37,485	5%
Income before fair value adjustments and taxes	9,317	12,141	(23)%
Fair value adjustment on investment properties	16,953	30,163	(44)%
Distributions to unitholders	4,109	n/a	
Cash flows from operations	10,502	13,922	(25)%
Per Unit Metrics [1]			
Income - diluted	3.80	1.90	100%
FFO	0.85	0.74	16%
AFFO	0.75	0.60	24%
Distributions	0.45	n/a	
IFRS Measures			
Total assets ($000s)	454,743	396,845	14%
Equity ($000s)[2]	186,608	168,331	11%
Debt ($000s)[3]	215,601	180,002	20%
Weighted average interest rate on debt	3.98%	4.57%	(13%)
Debt to GBV ratio	51%	46%	11%
Finance costs coverage ratio[4]	2.96	2.60	14%
Debt service coverage ratio[5]	2.72	2.65	3%
Operational Highlights			
Number of properties	29	27	7%
Gross leasable area (GLA) sq. ft.	1,691,920	1,571,474	8%
Occupancy % (weighted by GLA)	90.6%	91.0%	—%
Retention % (weighted by GLA)	75.5%	77.0%	(2)%
Weighted average remaining lease term (years)	4.75	4.70	1%
Weighted average base rent (per sq. ft.)	$17.49	$16.35	7%

1. Calculated as if the trust units and Class B LP Units were outstanding during the entire current and comparative periods.
2. Calculated as the sum of trust units and Class B LP Units. Comparative period reflects the divisional surplus as reported by Melcor.
3. Calculated as the sum of total amount drawn on revolving credit facility, mortgages payable and Class C LP Units, excluding unamortized fair value adjustment on Class C LP Units.
4. Calculated as the sum of FFO and finance costs; divided by finance costs, excluding distributions on Class B LP Units.
5. Calculated as FFO; divided by sum of contractual principal repayments on mortgages payable and distributions of Class C LP Units, excluding amortization of fair value adjustment on Class C LP Units.

2013 Highlights

- We completed the successful IPO of Melcor REIT and acquired 27 income-producing properties representing 1.57 million sq. ft. from Melcor. The underwriters subsequently exercised their over allotment option, leaving 9,130,000 units outstanding and providing gross proceeds of $9.13 million to the REIT.
- We executed on the strategy set out in our prospectus (dated April 19, 2013) through our first eight-months of operations, leading to financial and operating results which exceeded forecast. These strategies include:.
  - **Focus on leasing programs and strong leasing activity**, which led to increased rental rates on new and renewed leases signed in 2013. In conjunction with higher rates on leases with escalating rent leases, this led to a 7% increase in weighted average base rent.
  - **Growth through acquisition**: we completed two acquisitions in the year, which diversified our portfolio and increased GLA by 8% since the IPO on May 1, 2013. With an additional acquisition subsequent to year-end, GLA has grown by 12% since the IPO.
  - **Asset enhancement**: we completed substantial redevelopment of two office properties, leading to significantly increased occupancy for these properties.

The successful execution of these strategies contributed to:

  - 5% growth in both Revenue and NOI over 2012
  - FFO and AFFO 6% and 5% ahead of forecast, respectively

Other financial highlights include:

- **Fair value gains of $16.95 million** resulted in a 4% increase in the fair value of our portfolio over December 31, 2012.
- **Distributions of $0.05625 per trust unit** (as forecast) were paid in each of the REIT's eight months of operations.
- **Weighted average interest rate on our revolving credit facility, mortgages and Class C LP Units decreased by 59 basis points or 13%** as a result of lower average interest rates on the Class C LP Units achieved through refinancing prior to the IPO.

Acquisitions completed:

- Coast Home Centre, Q3-2013: a 59,725 sq. ft. retail property in Edmonton for $12.30 million excluding closing costs.
- Liberty Crossing, Q4-2013: a 63,317 sq. ft. retail property in Red Deer for $13.25 million excluding closing costs.
- LC Industrial, Q1-2014: a 67,610 sq. ft. industrial warehouse in Lethbridge for $5.93 million excluding closing costs.

Property Profile

At December 31, 2013 our portfolio includes interests in 29 income-producing properties located in Western Canada, made up of retail, office, and industrial properties, comprising 1,691,920 square feet of GLA and a land lease community.

The following table summarizes the composition of our properties at December 31, 2013 by property type:

	Number of Properties	GLA (sq. ft.) / Lots	% of Portfolio (GLA)	Fair value ($000s)	NOI ($000s)
Retail	9	608,234	35.9%	180,902	9,126
Office	17	1,018,713	60.2%	228,406	14,896
Industrial	2	64,973	3.8%	5,459	419
Land Lease Community	1	308 lots	n/a	14,350	854
	29	1,691,920	100%	429,117	25,295

Retail – our 9 retail properties include multi-building retail power centres and neighborhood shopping centres containing 608,234 sq. ft.

Office – our 17 office properties include low and medium-rise buildings located in strategic urban and suburban centres, containing 1,018,713 sq. ft.

Industrial – at December 31, we had two industrial properties with a total of 64,973 sq. ft. In Q1-2014 we completed the acquisition of an additional industrial property which more than doubled our industrial GLA to 132,583 sq. ft.

Land Lease Community – we have one land lease community in Calgary, AB, consisting of 308 pad lots. It was 100% occupied at December 31, 2013 (December 31, 2012 – 100%).

Portfolio Occupancy – Occupancy at year end was 90.6% compared to 91.0% at the end of the 2012. Our tenants include a diversified mix of national, regional and local businesses operating in a variety of industries. This diversified tenant base helps mitigate our exposure to negative trends occurring in any one sector.

Consolidated Revenue & Net Operating Income

($000s unless noted)	Year Ended December 31 2013	2012	Change
Base rent	25,196	24,137	4%
Recoveries	14,457	14,441	—%
Other	1,572	905	74%
Amortization of tenant incentives	(2,297)	(2,447)	(6)%
Straight-line rent adjustment	397	449	(12)%
Rental revenue	39,325	37,485	5%
Operating expenses	8,009	7,889	2%
Utilities and property taxes	7,921	7,534	5%
Direct operating expenses	15,930	15,423	3%
Net rental income	23,395	22,062	6%
NOI	25,295	24,060	5%
Same asset NOI	22,457	21,969	2%
Operating margin	59%	59%	—%

Revenue

Rental revenue for the year ended December 31, 2013 increased $1.84 million or 5% over 2012. Base rent was 4% or $1.06 million higher than 2012; driven by higher average base rent (per sq. ft.) and the increase in GLA following two acquisitions. GLA grew by 8% or 120,446 over 2012 due to the acquisition of Coast Home Centre ("Coast") in Q3-2013 and Liberty Crossing ("Liberty") in Q4-2013.

Average base rent was $17.49 per sq. ft. in 2013 compared to $16.35 per sq. ft. in 2012. The increase is a result of increased rental rates on new and renewed leases signed in 2013, and higher rates on leases with rent rates that escalate over time.

The table below summarizes the REIT's average base rent, GLA, occupancy and retention:

	Year Ended December 31 2013	2012	Change
Average base rent (per sq. ft.)	$17.49	$16.35	7%
Weighted average remaining lease term	4.75	4.70	1%
GLA	1,691,920	1,571,474	8%
Occupancy %	90.6%	91.0%	—%
Retention %	75.5%	77.0%	(2)%

Recoveries are amounts recovered from tenants for direct operating expenses incurred during the year and include a nominal administrative charge. Direct operating expenses increased by 3% over 2012, but recoveries, which generally track with direct operating expenses, were comparable to 2012. This divergence is the result of slightly lower occupancy and non-recoverable expenses on certain properties. This was in-line with our forecast.

Other revenue is comprised of parking revenue and other miscellaneous revenue. These revenues can fluctuate from period to period.

Non-cash adjustments related to amortization of tenant incentives and straight-line rent adjustment had a net positive impact on rental revenue during the year. Amortization of tenant incentives decreased as there were fewer new properties requiring tenant incentives compared to the prior year. Straight-line rent adjustments relate to new leases entered into during the period which have escalating rent rates and/or rent-free periods. Straight-line rent adjustments fluctuate from period to period due to the timing of leases signed.

Direct operating expenses

Direct operating expenses increased by $0.51 million or 3% as a result of increased GLA following the acquisition of properties in Q3-2013 and Q4-2014. GLA has grown 8% since 2012 as a result of these acquisitions. Higher than anticipated snow removal costs due to heavy snow fall in Alberta in Q4-2013, and an increase of $0.39 million or 5% in property taxes due to higher appraised property values compared to 2012 also contributed to the increase in direct operating expenses.

NOI and Same Asset NOI

Net operating income ("NOI") and same asset NOI are non-standard metrics used in the real estate industry to measure the performance of investment properties. The IFRS measurement most directly comparable to NOI and same asset NOI is net income.

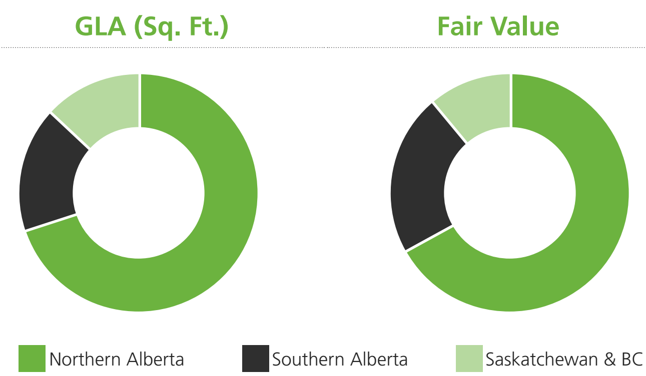
NOI and same asset NOI increased by $1.24 million and $0.49 million respectively compared to 2012. This growth is primarily a result of increased average base rent and other revenue. NOI also increased due to new property acquisitions in the year. The calculation of same asset NOI is as follows (refer to Non-Standard Measures for calculation of NOI and reconciliation to net income):

	Year Ended December 31		
($000s)	2013	2012	Change
Same asset NOI	22,457	21,969	2%
Acquisitions & Property Development	938	93	
NOI before adjustments	23,395	22,062	6%
Amortization of tenant incentives	2,297	2,447	
Straight-line rent adjustment	(397)	(449)	
NOI	25,295	24,060	5%

Regional Analysis

The following table summarizes the composition of our properties at December 31, 2013 by geographic region:

	Number of Properties	GLA (sq. ft.)	% of Portfolio (GLA)	Fair value ($000s)	NOI ($000s)
Northern Alberta	18	1,183,916	70.0%	289,000	16,441
Southern Alberta	6	282,639	16.7%	94,232	5,737
Saskatchewan & British Columbia	5	225,365	13.3%	45,885	3,117
	29	1,691,920	100.0%	429,117	25,295



The following table details key financial and operational metrics for each of our geographic regions for the year ended December 31, 2013:

	Northern Alberta		Southern Alberta		Saskatchewan & British Columbia	
	2013	2012	2013	2012	2013	2012
Year ended December 31 ($000s)						
Rental revenue	25,531	24,663	8,246	7,451	5,548	5,371
NOI	16,441	15,966	5,737	4,979	3,117	3,115
As at December 31						
Average base rent (per sq. ft.)	$17.19	$16.52	$23.22	$21.12	$12.88	$11.68
Occupancy %	90.0%	89.5%	98.4%	96.8%	86.8%	88.6%

Higher rental revenue in Northern Alberta is a result of new properties and higher average base rent per sq. ft. in the region. The Initial Properties included a retail commercial unit ("CRU") which was completed by Melcor in late 2012 and therefore the prior year comparative did not fully reflect the annual impact of this CRU on rental revenue. We also increased GLA with the acquisitions of two properties in Northern Alberta in Q3 and Q4.

Increased rental revenue in Southern Alberta is due to higher average base rent and increased occupancy. Rental revenue in Saskatchewan and BC increased slightly due to increased average base rent, offset by a slight decline in occupancy.

General & Administrative Expense

	Year Ended December 31		
($000s)	2013	2012	Change
Asset management fee	676	—	100%
Salaries and benefits	315	1,073	(71%)
Professional fees	232	47	394%
Public company costs	172	—	100%
Other	333	249	34%
	1,728	1,369	26%

The analysis of general & administrative components year over year is not meaningful due to the formation of the REIT and resulting change in cost structure in 2013. The increase in general & administrative expenses in 2013 is consistent with our forecast and reflects the higher costs associated with the REIT being a stand-alone publicly traded entity . Refer to note 21 of the consolidated financial statements for additional discussion on the management fee structure.

Finance Costs

	Year Ended December 31		
($000s)	2013	2012	Change
Interest on mortgages payable and revolving credit facility	5,586	8,575	(35%)
Interest on Class C LP Units	2,721	—	100%
Amortization of fair value adjustment on Class C LP Units	(293)	—	(100%)
Amortization of deferred financing costs	108	—	100%
Finance costs before distributions	8,122	8,575	(5%)
Distributions on Class B LP Units	4,289	—	100%
Finance costs	12,411	8,575	45%

Finance costs for the year ended December 31, 2013 were $3.84 million or 45% higher compared to the same period in the prior year. Analysis of the components of finance costs is not meaningful due to the formation of the REIT and resulting conversion of certain mortgages into Class C LP Units. As part of the IPO, Melcor retained the debt on certain Initial Properties (the "Retained Debt") with a fair value at April 30, 2013 of $96.51 million. Distributions made on Class B LP Units, issued to Melcor as part of the IPO, are classified as finance costs as the units are accounted for as a financial liability measured at fair value through profit and loss. Distributions on Class B LP Units are equivalent to those declared on trust units, as approved by the Board of Trustees.

Finance costs before distributions on Class B LP Units were 5% lower during the year ended December 31, 2013 compared to 2012. The decrease is consistent with the financial forecast and reflects the lower weighted average interest rates on the Class C LP Units. As at December 31, 2013 the weighted average interest rate on our revolving credit facility, mortgages payable and Class C LP Units was 3.98% based on period end balances (December 31, 2012 – 4.57%). Distributions on Class B LP Units are lower than forecast due to the conversion of 830,000 units to fulfill the underwriters' over-allotment option.

Income Taxes

As at December 31, 2013, the REIT qualifies as a mutual fund trust within the meaning of the Income Tax Act (Canada) and as a real estate investment trust eligible for the 'REIT Exception' under the Specified Investment Flow-Through (SIFT) rules; accordingly, no current or deferred income tax expense has been recognized on income earned or capital gains recognized subsequent to the formation of the REIT.

We recorded a deferred income tax recovery of $40.59 million related to the de-recognition of a deferred income tax liability as a result of qualifying for the REIT Exception at the IPO.

Funds from Operations & Adjusted Funds from Operations

Funds From Operations (FFO) and Adjusted Funds From Operations (AFFO) are non-standard measures used in the real estate industry as a measure of operating performance of investment properties. We believe that AFFO is an important measure of economic performance and is indicative of the REIT's ability to pay distributions, while FFO is an important measure of operating performance and the performance of real estate properties. The IFRS measurement most directly comparable to FFO and AFFO is net income.

	Year Ended December 31		
($000s, except per unit amounts)	2013	2012	Change
Net income for the period	62,719	35,490	
Add / (deduct)			
Fair value gain on investment properties	(16,953)	(30,163)	
Fair value loss on Class B LP Units	3,812	—	
Amortization of tenant incentives	2,297	2,447	
Distributions on Class B LP Units	4,289	—	
Deferred income taxes	(40,261)	5,968	
Funds From Operations (FFO)	15,903	13,742	16%
Add / (deduct)			
Straight-line rent adjustment	(397)	(449)	
Amortization of deferred financing costs	108	—	
Accretion on decommissioning obligation	60	60	
Net impact of amortization of fair value adjustment and interest subsidy [1]	432	—	
Normalized capital expenditures [2]	(729)	(722)	
Normalized tenant incentives and leasing commissions [2]	(1,461)	(1,434)	
Adjusted Funds from Operations (AFFO)	13,916	11,197	24%
FFO/Unit	0.85	0.74	16%
AFFO/Unit	0.75	0.60	24%

1. Adjustment includes the following: amortization of the fair value adjustment recognized on the Class C LP Unit liability; and usage of the interest rate subsidy provided by Melcor as part of the transfer of the Initial Properties.
2. Represents 3% and 6% of annual NOI for capital expenditures and tenant incentives and leasing commissions respectively. Amounts are net of usage of the capital expenditure subsidy provided by Melcor as part of the transfer of Initial Properties. Amounts presented in the comparative and pre-acquisition periods are based upon the respective percentages of annual NOI for comparative purposes.

Distributions

In order to continue to qualify for the 'REIT Exception', as provided under the SIFT rules we must allocate substantially all taxable income. As such, we allocate monthly distributions to unitholders as determined and approved by the Board of Trustees. Our initial distribution rate represents approximately 93% of AFFO for the 12 months ended March 31, 2014 based on our financial forecast. Distributions to unitholders for the year (commencing on the formation of the REIT in May 2013) were $4.11 million (2012 - $nil).

Fair Value of Investment Properties

We carry our investment properties at fair value in accordance with IAS 40, Investment property. The following table summarizes key metrics of our investment properties and components of the fair value calculation:

	December 31	
	2013	2012
Number of properties	29	27
Total GLA (sq. ft)	1,786,447	1,667,440
GLA (REIT owned %)	1,691,920	1,571,474
Fair value of portfolio ($000s)	440,349	393,461
Value per square foot	$260	$250
NOI ($000s)	25,295	24,060
Weighted average capitalization rate	6.41%	6.48%
Weighted average discount rate	7.57%	7.59%
Weighted average terminal cap rate	6.69%	6.72%

Investment properties were valued by qualified independent external valuation professionals as at December 31, 2013 and 2012 which resulted in fair value gains of $16.95 million (2012 - $30.16 million) on investment properties recorded to income during the year. Refer to Note 26 to the consolidated financial statements for additional information on the calculation of fair value adjustments.

A breakdown of our fair value adjustment on investment properties by geographical region are as follows:

	Year Ended December 31		
($000s)	2013	2012	Change
Northern Alberta	7,969	24,287	(67)%
Southern Alberta	7,683	5,060	52%
Saskatchewan & British Columbia	1,301	816	59%
	16,953	30,163	(44)%

Fair value gains in the current year were primarily the result of a decrease in capitalization rates on certain retail and office properties and increased leasing activity.

Fair values are most sensitive to changes in capitalization rates.

	December 31, 2013			December 31, 2012		
	Min	**Max**	**Weighted Average**	Min	Max	Weighted Average
Capitalization rate	5.50%	9.00%	6.41%	5.50%	9.00%	6.48%
Terminal capitalization rate	5.75%	9.25%	6.69%	5.75%	9.25%	6.72%
Discount rate	6.50%	10.00%	7.57%	6.50%	10.00%	7.59%

A capitalization rate increase of 50 basis points (+0.5%) would decrease the fair value of investment properties by $31.88 million (2012 - $28.10 million) while a 50 basis points decrease (-0.5%) would increase it by $37.28 million (2012 - $32.79 million).

Liquidity & Capital Resources

We employ a range of strategies to fund operations and facilitate growth. Our principal liquidity needs are to:

- Fund recurring expenses;
- Meet debt service requirements;
- Make distribution payments;
- Fund capital projects; and
- Purchase investment properties.

Cash Flows

The following table summarizes cash flows from operating, investing and financing activities:

	Year Ended December 31		
($000s)	**2013**	**2012**	**Change**
Cash from operating activities	10,502	13,922	(3,420)
Cash used in investing activities	(34,867)	(12,921)	(21,946)
Cash from financing activities	29,608	(1,185)	30,793
Increase (decrease) in cash and cash equivalents	5,243	(184)	5,427
Cash and cash equivalents, beginning of year	689	873	(184)
Cash and cash equivalents, end of year	5,932	689	5,243

Operating activities

Cash from operating activities was $3.42 million lower than 2012. This decrease is primarily due to distributions on Class B LP Units, which were $4.29 million during the year, and are included in finance costs. Changes in operating assets and liabilities also negatively affected cash flow from operating activities due to lower payables and higher prepaids compared to 2012.

Investing activities

In 2013 we invested $25.85 million with the acquisitions of Coast and Liberty. Spending on property improvement and development decreased as we completed some multi-year asset enhancement and redevelopment activities on certain properties in 2013. We continue to invest in targeted and strategic value enhancing capital projects to improve the appeal of our investment properties to prospective and existing tenants. We also invested $2.05 million in tenant incentives during the year, a decrease of $0.58 million over the comparative period. The decrease is due to timing differences between the signing of leases and actual completion of improvement work.

At IPO we received $4.58 million in investment subsidies from Melcor. The subsidies are presented as restricted cash in the statement of financial position as the usage of the funds is restricted to capital expenditures, environmental remediation costs and tenant incentive payments. In 2013 we recognized the subsidies received, net of amounts drawn for these purposes.

Financing activities

During 2013 we drew $24.00 million on our revolving credit facility to fund the acquisition of Coast and Liberty and to meet day-to-day cash flow needs. In addition, we made principal repayments of $5.85 million on our mortgages payable and Class C LP Units. During 2013 we refinanced six mortgages for total proceeds of $60.00 million, we obtained new financing on one property for total proceeds of $7.00 million and we repaid outstanding mortgages on four properties totaling $12.72 million.

We paid $4.11 million in distributions to unitholders during the year ended December 31, 2013.

On May 1, 2013 we received $74.41 million from the issuance of 8,300,000 of trust units, net of transaction costs, as part of the completion of the IPO. The proceeds from the IPO were used to purchase the Initial Properties from Melcor for cash consideration of $66.02 million.

At IPO we received $3.60 million in interest payment subsidies from Melcor. These subsidies are presented as restricted cash in the statement of financial position as the usage of the funds is restricted to interest payments. During the period we recognized the subsidies received, net of amounts drawn for this purpose.

We recognized $7.45 million cash flows in net distributions to Melcor during the year, compared to net distributions of $16.34 million in 2012. Net distributions to Melcor represents the net financing funded/received by Melcor prior to the formation of the REIT to fund operating and investing activities.

Liquidity & Capital Resources

We are able to meet our capital needs through a number of sources, including cash generated from operations, short-term borrowings under our revolving credit facility, mortgage financings, and the issuance of trust units to purchase investment properties.

We believe that internally generated cash flows, supplemented by borrowings through our revolving credit facility and mortgage financings, where required, will be sufficient to cover our normal operating, debt service, distribution and capital expenditure requirements. We regularly review our credit facility limits and manage our capital requirements accordingly.

As at December 31, 2013 we had $5.93 million in cash and cash equivalents, $5.97 million in restricted cash and $1.00 million in available funds under our revolving credit facility. Subsequent to year-end we received $10.90 million in proceeds from funding of two mortgages on previously unencumbered properties. Part of the proceeds were used to repay $5.50 million of amounts drawn under the revolving credit facility.

Capital Structure

We define capital as the total of trust units, Class B LP Units, Class C LP Units, mortgages payable, and amounts drawn under our revolving credit facility.

Pursuant to the DOT, the REIT may not incur or assume any indebtedness if, after incurring or assuming such indebtedness, the total indebtedness of the REIT would be more than 60% of Gross Book Value ("GBV") ("Degree of Leverage Ratio") (65% including any convertible debentures). At December 31, 2013, and throughout the period, we were in compliance with the Degree of Leverage Ratio and had a ratio of 51% as at December 31, 2013.

As at December 31, 2013, the REIT's total capitalization was $402.21 million and is comprised as follows:

($000s)	December 31, 2013
Revolving credit facility [1]	24,000
Mortgages payable [1]	99,023
Class C LP Units [2]	92,578
Indebtedness	215,601
Class B LP Units [3]	95,308
Trust units	91,300
Equity	186,608
Total capitalization	402,209
Gross book value (GBV) [4]	425,162
Debt to GBV	51%
Maximum threshold [5]	60%

1. Debts are presented excluding unamortized transaction costs.
2. Class C LP Units excluding unamortized fair value adjustment on Class C LP Units.
3. Class B LP Units are classified as equity for purposes of this calculation and are included at their book value of $10.00 per unit.
4. GBV is calculated as the cost of the total assets acquired in the Initial Properties and on the purchase of Coast Home Centre and Liberty Crossing.
5. As prescribed by the operating policies in the DOT (65% including any convertible debentures).

We are also subject to financial covenants on our $25.00 million revolving credit facility. The covenants include a maximum debt to total capital ratio of 60%, a minimum interest coverage ratio of 1.50, and a minimum net book value of unitholders' equity of $140.00 million. As at December 31, 2013, and throughout the period, we were in compliance with our financial covenants with a debt to total capital ratio of 51%, interest coverage ratio of 1.71, and a net book value of unitholders equity of $220.72 million. We also have financial covenants on certain mortgages for investment properties. At December 31, 2013, and throughout the period, we were in compliance with our financial covenants on our mortgages. We prepare financial forecasts to monitor the changes in our debt and capital levels and ability to meet our financial covenants.

Indebtedness

Debt Repayment Schedule – the following table summarizes our contractual obligations and illustrates certain liquidity and capital resource requirements:

($000s)	Revolving Credit Facility	Mortgages Payable	Class C LP Units	Total	% of Portfolio
Total	**24,000**	**99,023**	**92,578**	**215,601**	**100%**
2014	—	19,911	3,059	22,970	11%
2015	24,000	22,126	25,825	71,951	33%
2016	—	13,822	11,180	25,002	12%
2017	—	1,516	4,584	6,100	3%
2018	—	34,080	13,108	47,188	22%
Thereafter	—	7,568	34,822	42,390	19%

We ladder the renewal and maturity dates on our borrowings as part of our capital management strategy to mitigate the concentration of interest rate and financing risk associated with refinancing in any particular period.

Debt Analysis – our mortgages payable and Class C LP Units bear interest at fixed rates; the following table summarizes the interest rates and terms to maturity:

($000s)	Revolving Credit Facility	Mortgages Payable	Class C LP Units	Total
Total	**24,000**	**99,023**	**92,578**	**215,601**
Fixed	—	99,023	92,578	191,601
Variable	24,000	—	—	24,000
Weighted average interest rate	3.65%	4.20%	3.84%	3.98%
Weighted average term to maturity	1.33	2.96	4.89	3.61

The weighted average interest rate on our debts was reduced by 13% as we renew facilities under more favorable interest rates. During 2013 we refinanced six mortgages totaling $60.00 million and obtained financing of $7.00 million on a previously unencumbered property. The weighted average interest rate on new and renewed financings during the year was 3.66%.

Debt Service Coverage Ratio and Finance Costs Coverage Ratio – we calculate debt service coverage ratio as FFO for the period divided by principal repayments on mortgages payable and Class C LP Units made during the period. We calculate interest coverage as FFO plus finance costs for the period divided by finance costs expensed during the period, less distributions on Class B LP Units. We consider these measures to be useful in evaluating our ability to service our debts. These metrics are not calculated for purposes of covenant compliance on any of our debt facilities.

($000s)	December 31, 2013
FFO	15,903
Principal repayments on Mortgages payable	3,881
Principle repayments on Class C LP Units	1,966
Debt service coverage ratio	**2.72**
FFO plus finance costs	24,025
Finance costs [1]	8,122
Finance costs coverage ratio	**2.96**

1. Finance costs excluding finance expense recognized on Class B LP Unit distributions.

Credit Facility - On April 20, 2013, we entered into a revolving term facility credit agreement with two major Canadian chartered banks. Under the terms of the agreement the REIT has an available credit limit based on the carrying values of specific investment properties, as calculated quarterly, up to a maximum of $25.00 million for general corporate purposes. The agreement also provides the REIT with $5.00 million in available letters of credit which bear interest at 2.25%. As at December 31, 2013 we had an available credit limit of $25.00 million of which $24.00 million was drawn; and posted letters of credit of $nil. The facility matures on May 1, 2015, with a one year extension period at the discretion of the lenders.

Equity

The REIT is authorized to issue an unlimited number of trust units and an unlimited number of special voting units. Each trust unit represents a holder's proportionate undivided beneficial ownership interest in the REIT and will confer the right to one vote at any meeting of the unitholders and to receive any distributions by the REIT. Special voting units have no economic entitlement in the REIT but entitle the holder to one vote per special voting unit. Special voting units may only be issued in connection with securities exchangeable into trust units (including Class B LP Units).

Class B LP Units of the Partnership are economically equivalent to, and exchangeable into, trust units at the option of the holder, and therefore, are considered a dilutive instrument. The Class B LP Units are classified as financial liabilities in accordance with IAS 32, Financial Instruments – presentation, due to their puttable feature.

The following table summarizes the change in units for the period May 1, 2013 to December 31, 2013 and the fully diluted number of Units outstanding at December 31, 2013:

Issued and fully paid units ($000s)	Units	$ Amount
Balance, May 1, 2013	—	—
Issuance of Units - IPO	8,300,000	83,000
Issuance of Units - over-allotment option	830,000	8,300
Balance, December 31, 2013	**9,130,000**	**91,300**
Dilutive securities		
Class B LP Units [1]	9,530,798	95,308
Diluted balance, December 31, 2013	**18,660,798**	**186,608**

1. A corresponding number of special voting units are held by Melcor through an affiliate.

Off Balance Sheet Arrangements

As at December 31, 2013, we had no off-balance-sheet arrangements.

Quarterly Results

	2013			
($000s except per unit amounts)	Q4	Q3	Q2	Q1
Revenue	10,070	9,794	9,773	9,688
Net income	7,466	5,945	44,492	4,816
Income per unit [1]	$0.51	$0.65	$2.38	$0.26

	2012			
($000s except per unit amounts)	Q4	Q3	Q2	Q1
Revenue	10,566	9,195	9,002	8,722
Net income	12,822	6,731	13,362	2,575
Income per unit [1]	$0.68	$0.36	$0.72	$0.14

1. Calculated as if the trust units were outstanding during the entire period.

Fourth Quarter Results

Consolidated Revenue & Net Operating Income

	Three Months Ended December 31		
($000s)	2013	2012	Change
Base rent	6,434	6,198	4%
Recoveries	3,582	4,214	(15)%
Other	589	250	136%
Amortization of tenant incentives	(616)	(545)	13%
Straight-line rent adjustment	81	449	(82)%
Rental revenue	10,070	10,566	(5)%
Operating expenses	2,392	2,921	(18)%
Utilities and property taxes	1,982	1,625	22%
Direct operating expenses	4,374	4,546	(4)%
Net rental income	5,696	6,020	(5)%
NOI	6,231	6,116	2%
Same asset NOI	5,172	5,984	(14)%
Operating margin	57%	57%	—%

Rental revenue for the fourth quarter was $10.07 million, with strong growth in base rent, up 4% over Q4-2012. Recoveries were 15% lower in 2013, due to a larger budget to actual variance in 2012. Recoveries are trued up to actual expenses in the fourth quarter each year.

General & Administrative Expense

	Three Months Ended December 31		
($000s)	2013	2012	Change
Asset management fee	257	—	100%
Salaries and benefits	—	(7)	(100%)
Professional fees	27	3	800%
Public company costs	76	—	100%
Other	99	108	(8)%
	459	104	341%

The analysis of general & administrative components year over year is not meaningful due to the formation of the REIT and resulting change in cost structure. The increase in general and administrative expenses in 2013 is consistent with forecast and reflects higher costs associated with the REIT being a stand alone publicly traded entity.

Finance Costs

	Three Months Ended December 31		
($000s)	2013	2012	Change
Interest on mortgages payable and revolving credit facility	1,169	2,170	(46%)
Interest on Class C LP Units	1,014	—	100%
Amortization of fair value adjustment on Class C LP Units	(110)	—	(100%)
Amortization of deferred financing costs	72	—	100%
Finance costs before distributions	2,145	2,170	(1%)
Distributions on Class B LP Units	1,608	—	100%
Finance costs	3,753	2,170	73%

Finance costs for the fourth quarter were $3.75 million or 73% higher compared Q4-2012. Analysis of the components of finance costs is not meaningful due to the formation of the REIT and resulting conversion of certain mortgages into Class C LP Units. Finance costs before distributions on Class B LP Units were 1% lower during the period compared to Q4-2012. The decrease reflects the lower weighted average interest rates on the Class C LP Units.

Funds from Operations & Adjusted Funds from Operations

($000s, except per unit amounts)	Three Months Ended December 31 2013	2012	Change
Net income for the period	7,466	12,822	
Add / (deduct)	—	—	
Fair value gain on investment properties	(9,488)	(11,371)	
Fair value loss on Class B LP Units	3,521	—	
Amortization of tenant incentives	616	545	
Distributions on Class B LP Units	1,608	—	
Deferred income taxes	—	3,619	
Funds From Operations (FFO)	3,723	5,615	(34)%
Add / (deduct)			
Straight-line rent adjustment	(81)	(449)	
Amortization of deferred financing costs	72	—	
Accretion on decommissioning obligation	20	20	
Net impact of amortization of fair value adjustment and interest subsidy [1]	157	—	
Normalized capital expenditures [2]	(182)	(180)	
Normalized tenant incentives and leasing commissions [2]	(365)	(361)	
Adjusted Funds from Operations (AFFO)	3,344	4,645	(28)%
FFO/Unit	0.20	0.30	(34)%
AFFO/Unit	0.18	0.25	(28)%

1. Adjustment includes the following: amortization of the fair value adjustment recognized on the Class C LP Unit liability; and usage of the interest rate subsidy provided by Melcor as part of the transfer of the Initial Properties.
2. Represents 3% and 6% of annual NOI for capital expenditures and tenant incentives and leasing commissions respectively. Amounts are net of usage of the capital expenditure subsidy provided by Melcor as part of the transfer of Initial Properties. Amounts presented in the comparative and pre-acquisition periods are based upon the respective percentages of annual NOI for comparative purposes.

Funds from operations (FFO) and Adjusted funds from operations (AFFO) for the fourth quarter were 34% and 28% lower than the comparative period. The decrease was due to lower NOI and higher general & administrative costs during the period. Year over year analysis is not meaningful due to the formation of the REIT and resulting change in cost structure.

Distributions to unitholders for the fourth quarter were $0.51 million (2012 - $nil).

Outlook

We have a solid portfolio of income-producing assets in high growth regions and we continue to actively seek out suitable acquisitions to expand our asset base. We will also continue to improve existing assets through asset enhancement programs and efficient and effective property management. Our disciplined approach helps to ensure that our assets remain profitable over the long-term while at the same time achieving our objective of providing growing monthly cash distributions to unitholders .

Subsequent to year-end we obtained mortgage financing on two previously unencumbered properties for total proceeds of $10.90 million. The mortgages are amortized over a 20 and 25 year period, with a 5 year term and bear interest at a weighted average fixed rate of 3.54%. Part of the proceeds were used to repay $5.50 million of amounts drawn under the revolving credit facility.

We have two mortgages on one property which will come up for renewal in the next year. These mortgages have an outstanding principal balance of $17.42 million and a weighted average interest rate of 4.53% as at December 31, 2013. We expect to be able to refinance this mortgage with our lenders at lower interest rates based upon comparable recent refinancings.

Management anticipates that commercial real estate fundamentals will remain healthy in Western Canada, with stable to slightly increasing occupancy rates. We see continued stability in activity levels in all our markets and anticipate growth in both rental renewals and rental rates as leases renew.

Forecast

The following details our results for the fourth quarter and for the nine-months ended December 31, 2013 against our financial forecast covering the period from April 1, 2013 to December 31, 2013, as provided in our prospectus dated April 19, 2013.

	Three Months Ended December 31, 2013			Nine Months Ended December 31, 2013		
($000s, except per unit amounts)	Actual	Forecast	Change	Actual	Forecast	Change
Rental revenue	10,070	9,556	5%	29,637	28,544	4%
Direct operating expenses	(4,374)	(3,944)	11%	(12,088)	(12,025)	1%
Net rental income	5,696	5,612	1%	17,549	16,519	6%
General and administrative expenses	(459)	(397)	16%	(1,334)	(1,190)	12%
Income before finance costs	5,237	5,215	—%	16,215	15,329	6%
Interest income	15	8	88%	55	24	129%
Interest expense						
Interest expense on mortgages debt	(1,241)	(1,033)	20%	(3,653)	(3,131)	17%
Distribution on Class C LP Units	(904)	(901)	—%	(2,428)	(2,727)	(11)%
Distribution on Class B LP Units	(1,608)	(1,747)	(8)%	(4,289)	(5,239)	(18)%
Net finance costs	(3,738)	(3,673)	2%	(10,315)	(11,073)	(7)%
Net income and comprehensive income	1,504	1,542	(2)%	5,900	4,256	39%
Add / (deduct):						
Amortization of tenant improvements	616	652	(6)%	1,719	1,788	(4)%
Distribution on Class B LP Units	1,608	1,747	(8)%	4,289	5,239	(18)%
Funds from Operations (FFO)	3,723	3,941	(6)%	11,908	11,283	6%
Add / (deduct):						
Straight-line rent adjustment	(81)	(52)	56%	(315)	(155)	103%
Deferred financing costs	72	19	279%	108	57	89%
Net impact of mark to market adjustment and interest subsidy	157	157	—%	432	487	(11)%
Normalized capital expenditures	(182)	(182)	—%	(547)	(547)	—%
Normalized tenant inducements and leasing commissions	(365)	(365)	—%	(1,096)	(1,096)	—%
Adjusted funds from operations (AFFO)	3,324	3,518	(6)%	10,490	10,029	5%
FFO	0.20	0.21	(6)%	0.64	0.60	6%
AFFO	0.18	0.19	(6)%	0.56	0.54	5%
Net Operating Income (NOI)	6,231	6,212	- %	18,953	18,152	4%

Our financial results for the nine-month period reflect the execution of our strategic objectives. We finished the year ahead of forecast on all key indicators. Strong leasing activity throughout 2013 and three successful property acquisitions (one subsequent to year end), position us for continued growth in 2014.

Net rental income for the three and nine-months ended December 31, 2013 was 1% and 6% ahead of forecast respectively. Higher rental revenues are due to improved leasing conditions, strong lease renewals and the acquisition completed in the third quarter. The acquired property contributed $0.27 million in base rent during the nine-month period. Direct operating expenses for the nine-month period are consistent with forecast.

Direct operating expenses in Q4 were 11% higher than forecast due to variations in the actual timing of expenditures.

Compared to forecast, general & administrative expense was $0.06 million and $0.14 million higher for the three and nine-months ended December 31, 2013. The variation from forecast is due to annual fees for audit, tax and property appraisal services being expensed in post-formation earnings (eight month period) versus the forecast 12 month period. We expect general & administrative expense to be in the range of 3 - 4% of revenue going forward.

Net finance costs were 2% higher and 7% lower than forecast for the three and nine-month periods respectively. Distribution on Class B LP Units are lower than forecast due to the conversion of

830,000 units to fulfill the underwriters' over-allotment option. Interest on mortgages payable and Class C LP Units was 17% higher during the nine-month period due to the forecast period including conversion of the mortgages to Class C LP Units at April 1, 2013, compared to the actual conversion which occurred on May 1, 2013. Higher interest expense on mortgage debt in the fourth quarter reflects the higher balance outstanding under the revolving credit facility which was used to fund property acquisitions during the period.

At December 31, 2013 we reviewed and re-assessed the accuracy of our financial forecast for the remaining three months of the forecast period in accordance with National Instrument 51-102 and OSC Staff Notice 51-721. We examined our results to date against our financial forecast, as detailed above; in conjunction with our expected financial results for the remaining three months of the forecast period. Included in our analysis is the financial impact of the acquisition of Coast Home Centre in Q3-2013, Liberty Crossing in Q4-2013 and LC Industrial in Q1-2014 on our portfolio as a whole. We examined the percentage impact on key metrics (Revenue, NOI, FFO, and AFFO) and concluded that the incremental impact of the properties purchase on our key metrics meet the materiality threshold to require re-forecasting for the remaining three months. Management did not identify any other key variables with significant variances for Q1 2014 which would require re-forecasting.

	Three Months Ended March 31, 2014		
($000s, except per unit amounts)	**Prospectus Forecast**	**Acquisition Forecast**	**Revised Forecast**
Rental revenue	9,631	753	10,384
Direct operating expenses	(4,059)	(208)	(4,267)
Net rental income	5,572	545	6,117
General and administrative expenses	(397)	(20)	(417)
Income before finance costs	5,175	525	5,700
Interest income	9	—	9
Interest expense			
Interest expense on mortgages debt	(1,011)	(174)	(1,185)
Distribution on Class C LP Units	(893)	—	(893)
Distribution on Class B LP Units	(1,747)	—	(1,747)
Net finance costs	(3,642)	(174)	(3,816)
Net income and comprehensive income	1,533	351	1,884
Add / (deduct):			
Amortization of tenant improvements	670	—	670
Distribution on Class B LP Units	1,747	—	1,747
Funds from Operations (FFO)	3,950	351	4,301

	Three Months Ended March 31, 2014		
($000s, except per unit amounts)	**Prospectus Forecast**	**Acquisition Forecast**	**Revised Forecast**
Add / (deduct):			
Straight-line rent adjustment	(49)	(15)	(64)
Deferred financing costs	19	—	19
Net impact of mark to market adjustment and interest subsidy	143	—	143
Normalized capital expenditures	(182)	(19)	(201)
Normalized tenant inducements and leasing commissions	(365)	(38)	(403)
Adjusted funds from operations (AFFO)	3,516	279	3,795
FFO	0.21	0.02	0.23
AFFO	0.19	0.01	0.20
Net Operating Income (NOI)	6,193	530	6,723

Business Environment & Risks

We are exposed to various risks and uncertainties, many of which are beyond our control. The following risk factors could materially impact our financial condition, results of operations, cash flows and the value of our trust units. We take steps to mitigate these risks; however, there is no assurance that the steps taken will avoid future loss.

General Risks

We are subject to market conditions in the geographic areas where we own and manage properties. Where strong market conditions prevail, we are able to achieve higher occupancy rates. Market conditions are influenced by outside factors such as general inflation and interest rate fluctuations; population growth and migration; job creation and employment patterns; consumer confidence; government policies, regulations and taxation; extreme weather events; and availability of credit and financing.

Credit Risk

We are subject to credit risk as our tenants may not be able to fulfil their financial obligations on current balances and contracted future rents. We manage our credit risk through careful selection of tenants and look to obtain national tenants or tenants in businesses with a long standing history, or perform financial background checks including business plan review for smaller tenants. We manage our concentration risk by renting to an expansive tenant base, with no dependency on rents from any one specific tenant.

The following table illustrates the ten largest tenants for the portfolio, as measured by their percentage contribution to the total contracted future minimum lease payment for 2014 and corresponding areas leased by each tenant.

Rank	Tenant (Operating Name)	% of Total Minimum Rent	Lease GLA (sq. ft.)	% of Total GLA	Remaining Term (yrs)	Locations	Credit Rating (S&P/Moody's/ DBRS)
1	Royal Bank of Canada	7.2%	72,296	4.3%	2	4	AA-/ Aa3/ AA
2	Government of Alberta	2.9%	45,690	2.7%	4	2	AAA / Aaa/ AAA
3	Shoppers Drug Mart	2.9%	26,726	1.6%	12	2	BBB+/-/ BBB
4	Melcor Developments Ltd.	1.4%	23579	1.4%	4	1	---
5	Rexall Drugs	1.4%	11,827	0.7%	11	1	---
6	TD Bank	1.4%	9491	0.6%	5	2	AA-/ Aa1/ AA
7	RONA	1.2%	52,170	3.1%	12	1	BB+/-/ BB High
8	Peavey Industries	1.2%	24,264	1.4%	12	1	---
9	Enbridge Pipelines	1.2%	20,484	1.2%	5	1	A-/ Baa1/A
10	Government of Saskatchewan	1.1%	17,436	1.0%	10	1	AAA/ Aa1/ AA

Lease Maturity Risk

We are subject to lease maturity risk as there is no assurance that we will be able to renew or replace expiring leases at similar terms. We manage our lease maturity risk by pro-actively engaging tenants whose leases are expiring for early identification of potential vacancy risk. In addition, where possible we ladder maturity dates to minimize exposure in any particular period and to maintain a diversified portfolio.

The following table illustrates the number of leases maturing over the next five years and beyond.

Year of Maturity	Number of Leases	Renewal GLA (sq. ft.)	% of GLA	Average Base Rent Expiring Per Annum
2014	89	297,298	17.6%	$15.02
2015	59	155,674	9.2%	$13.75
2016	49	137,883	8.1%	$14.74
2017	69	187,618	11.1%	$17.53
2018	48	256,782	15.2%	$18.17
Thereafter	117	495,322	29.3%	$23.10
Vacant Space	—	161,343	9.5%	—
	431	1,691,920		$18.32

Industry Risk

Real estate investments are subject to varying levels of risk. These risks include changes to general economic conditions, government and environmental regulations, local supply/demand, and competition from other real estate companies. Real estate assets are relatively illiquid in down markets. As a result, the REIT may not be able to rebalance its portfolio in response to changing economic or investment conditions.

Other real property risks include:

- The value of the property and any improvements made to it;
- Rollover of leases and the ability to rent unleased suites;
- Financial stability of tenants and their ability to pay rent and fulfill their lease obligations; and
- Geographic concentration.

Cash available for distribution will be adversely affected if a significant number of tenants are unable to meet their obligations under their leases or if a significant amount of available space in the properties becomes vacant and cannot be leased on economically favourable lease terms.

Financing

We use debt and other forms of leverage in the ordinary course of business to execute on our strategy.

We are subject to general risks associated with debt financing. The following risks may adversely affect our financial condition and results of operations:

- Cash flow may be insufficient to meet required payments of principal and interest;
- Payments of principal and interest on borrowings may leave us with insufficient cash resources to pay operating expenses;
- We may not be able to refinance indebtedness on our assets at maturity due to company and market factors;
- The fair market value of our assets;
- Liquidity in the debt markets;
- Financial, competitive, business and other factors, including factors beyond our control;
- Refinancing terms that are not as favourable as the original terms of the related financing.

We attempt to mitigate these risks through the use of long-term debt and diversifying terms and maturity dates.

The terms of various credit agreements and other financing documents require that we comply with a number of financial and other covenants, such as maintaining debt service coverage and leverage ratios, and minimum insurance coverage. These covenants may limit our flexibility in our operations, and breaches of these covenants could result in defaults under the instruments governing the applicable indebtedness even if we had satisfied our payment obligations.

If we are unable to refinance assets/indebtedness on acceptable terms, or at all, we may need to use available liquidity, which would reduce our ability to pursue new investment opportunities. Alternately we may be required to dispose of one or more of our assets on disadvantageous terms. In addition, unfavourable interest rates or other factors at the time of refinancing could increase interest expense.

A large proportion of our capital is invested in physical, long-lived assets, which can be difficult to liquidate, especially if local market conditions are poor. This circumstance could limit our ability to diversify our portfolio of assets promptly in response to changing economic or investment conditions.

The liabilities of the REIT have fixed and floating interest rate components resulting in an exposure to interest rate fluctuations. These fluctuations in interest rates will have an impact on the earnings of the REIT. As a result of increased interest rates, the REIT's financial results and condition or operating results could be materially adversely affected.

The REIT may implement hedging programs in order to offset the risk of revenue losses and to provide more certainty regarding the payment of distributions to unitholders should current variable interest rates increase. However, to the extent that the REIT fails to adequately manage these risks, its financial results, and its ability to pay distributions to unitholders and interest payments on debt and future financings may be adversely affected. Increases in interest rates generally cause a decrease in demand for properties. Higher interest rates and more stringent borrowing requirements, whether mandated by law or required by banks, could have a material adverse effect on the REIT's ability to sell any of its properties.

We may enter into financing commitments in the normal course of business and, as a result, may be required to fund these, particularly through joint arrangements. If we are unable to fulfill any of these commitments, damages could be pursued against the REIT.

Competitive Conditions

The real estate market is highly competitive, with a large number of well-financed companies operating in the same markets as Melcor REIT. We may compete for real property acquisitions with individuals, corporations, institutions and other entities, which may increase the purchase price and reduce the yield of an acquired property. The REIT's rights under the Development and Opportunities Agreement entered into with Melcor helps to mitigate competition risk.

We also compete with other developers, managers and property owners in attracting tenants. Some of our competitors are better capitalized or financially stronger, and would be in a better position to withstand an economic downturn. The existence of competition for tenants could have an adverse effect on our ability to lease space in our properties and on the rents charged or concessions granted, and could materially and adversely affect our cash flows, operating results and financial condition. The REIT focuses on providing exceptional customer care and building solid relationships with our clients to increase the likelihood that they will renew leases.

Joint Arrangements

Some of our properties are jointly owned. These joint arrangements may involve risks that would not otherwise be present if the third parties were not involved, including the possibility that the partners have different economic or business interests or goals. Also, within these arrangements, the REIT may not have sole control of major decisions relating to these assets, such as: decisions relating to the sale of the assets and businesses; timing and amount of distributions of cash from such entities to the REIT and its joint arrangement partners; and capital expenditures.

Geographic Concentration

Of the total GLA, 86.7% is located in Alberta. Consequently, the market value of REIT's properties, the income generated by the REIT and the REIT's performance are particularly sensitive to changes the real estate markets in Alberta and economic conditions in Alberta generally. The factors impacting on the real estate markets in Alberta and the Alberta economy in general may differ from those affecting other regions of Canada.

Adverse changes in the economic conditions in Alberta may have a material adverse effect on the REIT's business, cash flows, financial condition and results of operations and ability to make distributions to holders of Units.

Significant Ownership by Melcor

Melcor holds a 51.1% effective interest in the REIT, where each Class B LP Unit is attached to a Special Voting Unit of the REIT. Melcor also holds all of the Class C LP Units of the Partnership.

The Class C LP Units have been designed to provide Melcor with an interest in the Partnership that entitle Melcor to distributions, in priority to distributions to holders of the Class A LP Units and Class B LP Units in an amount, if paid, that is expected to be sufficient (without any additional amounts) to permit Melcor to satisfy amounts payable under the Retained Debt.

In addition, the Declaration of Trust grants Melcor the right to nominate certain Trustees of the REIT based on Melcor's direct and indirect ownership interest in the REIT. For so long as Melcor maintains a significant effective interest in the REIT, Melcor will have the ability to exercise certain influence with respect to the affairs of the REIT and significantly affect the outcome of Unitholder votes, and may have the ability to prevent certain fundamental transactions. As a result, Melcor has the ability to influence many matters affecting the REIT.

Accordingly, the Units may be less liquid and trade at a relative discount compared to such Units in circumstances where Melcor did not have the ability to influence or determine matters affecting the REIT. Additionally, Melcor's significant effective interest in the REIT may discourage transactions involving a change of control of the REIT, including transactions in which an investor, as a holder of the Units, might otherwise receive a premium for its Units over the then-current market price.

Pursuant to the Exchange Agreement, each Class B LP Unit is exchangeable at the option of the holder for one Unit of the REIT (subject to customary anti-dilution adjustments). If Melcor exchanges some or all of its Class B LP Units for Units and subsequently sells such Units in the public market, the market price of the Units may decrease. Moreover, the perception in the public market that these sales will occur could also produce such an effect.

Dependence on Melcor

The REIT is dependent on Melcor for management, administrative and operations services relating to the REIT's business. The Asset Management Agreement has a term of 5 years, with automatic 5 year renewals, and may at times in the future not reflect current market terms for duties and responsibilities of Melcor. There is a risk that, because of the term and termination provisions of the Asset Management Agreement, termination of the Asset Management Agreement may be uneconomical for the REIT and accordingly not in the best interest of the REIT.

Should Melcor terminate the Asset Management Agreement or the Property Management Agreement, the REIT may be required to engage the services of an external asset manager and/or property manager. The REIT may be unable to engage an asset manager and/or property manager on acceptable terms, in which case the REIT's operations and cash available for distribution may be materially adversely affected. Alternatively, it may be able to engage an asset manager and/or property manager on acceptable terms or it may elect to internalize its external management structure, but the process undertaken to engage such manager(s) or to internalize management could be costly and time-consuming and may divert the attention of management and key personnel away from the REIT's business operations, which could materially adversely affect its financial condition.

Additionally, the Development and Opportunities Agreement provides that, subject to certain exceptions, the REIT will not engage a party other than Melcor or its affiliates to perform any of the services to be performed by Melcor pursuant to the Asset Management Agreement.

While the Trustees have oversight responsibility with respect to the services provided by Melcor pursuant to the Asset Management Agreement and the Property Management Agreement, the services provided by Melcor under such agreements will not be performed by employees of the REIT or the Partnership, but by Melcor directly, and through entities to which it may subcontract its duties. Further, the foregoing arrangements are subject to limited termination rights in favour of the REIT. As a result, Melcor directly, and indirectly through entities to which it may subcontract, has the ability to influence many matters affecting the REIT and the performance of its properties now and in the foreseeable future.

While the Melcor name and trade-mark and related marks and designs will be licensed to the REIT by Melcor under a non-exclusive, royalty-free trademark license agreement, such license will not be on a perpetual basis and may be terminated by Melcor at any time on 30 days' notice following the date of termination of the Asset Management Agreement. Termination of the license would require the REIT to rebrand its business, which could be costly and time-consuming and may divert attention of management and key personnel from the REIT's business operations, which could materially adversely affect its financial condition.

Potential Conflicts of Interest with Melcor

Melcor's continuing businesses may lead to conflicts of interest between Melcor and the REIT. The REIT may not be able to resolve any such conflicts, and, even if it does, the resolution may be less favourable to the REIT than if it were dealing with a party that was not a holder of a significant interest in the REIT. The agreements that the REIT entered into with Melcor on Closing may be amended upon agreement between the parties, subject to applicable law and approval of the Independent Trustees. As a result of Melcor's significant holdings in the REIT, the REIT may not have the leverage to negotiate any required amendments to these agreements on terms as favourable to the REIT as those the REIT could secure with a party that was not a significant holder of Units.

Taxation Matters

Although we currently meet the requirements of the REIT Exception, there can be no assurance that the REIT will be able to qualify for the REIT Exception to not to be subject to the tax imposed by the SIFT Rules in future years.

The SIFT Rules may have an adverse impact on the REIT and the Unitholders, on the value of the Units and on the ability of the REIT to undertake financings and acquisitions and if the SIFT Rules were to apply, the distributable cash of the REIT may be materially reduced. The effect of the SIFT Rules on the market for the Units is uncertain.

If certain tax proposals released on September 16, 2004 are enacted as proposed (the "September 16th Tax Proposals"), the

REIT would cease to qualify as a "mutual fund trust" for purposes of the Tax Act if, at any time after 2004, the fair market value of all Units held by non-residents, partnerships that are not Canadian partnerships or any combination of the foregoing is more than 50% of the fair market value of all issued and outstanding Units unless not more than 10% (based on fair market value) of the REIT's property is at any time "taxable Canadian property" within the meaning of the Tax Act and certain other types of specified property. Restrictions on the ownership of Units are intended to limit the number of Units held by non-residents, such that non-residents, partnerships that are not Canadian partnerships or any combination of the foregoing may not own Units representing more than 50% of the fair market value of all Units. The September 16th Tax Proposals were not included in budget implementation and technical amendment bills including Bill C-52 of the First Session of the Thirty-Ninth Parliament, which received Royal Assent on June 22, 2007, Bill C-45 and Bill C-48 of the First Session of the Forty-first Parliament, 60-61 Elizabeth II, 2011-2012.

Fixed Costs

The failure to rent unleased space on a timely basis or at all would likely have an adverse effect on the REIT's financial condition and results of operation and decrease the amount of cash available for distribution. Certain significant expenditures, including property taxes, ground rent, maintenance costs, mortgage payments (including those associated with the Retained Debt), insurance costs and related charges must be made throughout the period of ownership of real property regardless of whether a property is producing any income. If the REIT is unable to meet mortgage payments on any property (including those associated with the Retained Debt), losses could be sustained as a result of the mortgagee's exercise of its rights of foreclosure or sale or the landlord's exercise of remedies. Costs may also be incurred in making improvements or repairs to property required by a new tenant and income may be lost as a result of any prolonged delay in attracting suitable tenants to the vacant space.

The timing and amount of capital expenditures by the REIT will indirectly affect the amount of cash available for distribution to Unitholders. Distributions may be reduced, or even eliminated, at times when the REIT deems it necessary to make significant capital or other expenditures.

Environmental Risk

The REIT is subject to various requirements (including federal, provincial and municipal laws) relating to the protection of the environment.

Under these requirements, the REIT could be, or become, liable for environmental or other harm, damage or costs, including with respect to the release of hazardous, toxic or other regulated substances into the environment and/or affecting persons, and the removal or other remediation of hazardous, toxic or other regulated substances that may be present at or under its properties.

Such requirements often impose liability without regard to whether the owner or operator knew of, or was responsible for, the release or presence of such substances. Additional liability may be incurred by the REIT with respect to the release of such substances from the REIT's properties to properties owned by third parties, including properties adjacent to the REIT's properties or with respect to the exposure of persons to such substances. The failure to remove or otherwise address such substances may materially adversely affect the REIT's ability to sell such property, maximize the value of such property or borrow using such property as collateral security, and could potentially result in claims or other proceedings against the REIT.

It is the REIT's operating policy to obtain, or be entitled to rely on, a Phase I environmental site assessment prior to acquiring a property. Where a Phase I environmental site assessment warrants further investigation, it is the REIT's operating policy to conduct further environmental investigations. Although such environmental assessments provide the REIT with some level of assurance about the condition of the properties, the REIT may become subject to liability for undetected contamination or other environmental conditions of its properties against which it cannot insure, or against which the REIT may elect not to insure where insurance premium costs are considered to be disproportionate to the assessed risk, which could have a material adverse effect on the REIT's business, cash flows, financial condition and results of operations and ability to make distributions to holders of Units.

Environmental laws and other requirements can change and the REIT may become subject to more stringent environmental laws or other requirements in the future. Compliance with more stringent environmental laws or requirements, the identification of currently unknown environmental issues or an increase in the costs required to address a currently known condition may have a material adverse effect on the REIT's business, cash flows, financial condition and results of operations and ability to make distributions to holders of Units.

Subject to the obligations of Melcor described above, the REIT will bear the risk of assessment, remediation or removal of such contamination, hazardous substances or other residual pollution. The discovery of any such residual pollution on the sites and/or in the buildings, particularly in connection with the lease or sale of properties or borrowing using the real estate as security, could trigger claims for rent reductions or termination of leases for cause, for damages and other breach of warranty claims against the REIT. The remediation of any contamination and the related additional measures the REIT would have to undertake could have a materially adverse effect and could involve considerable additional costs that the REIT may have to bear. The REIT will also be exposed to the risk that recourse against the polluter or the previous owners or occupants of the properties might not be possible, for example, because they cannot be identified, no longer exist or have become insolvent. Moreover, the existence or even the mere suspicion of the existence of contamination, hazardous materials or other residual pollution can materially adversely affect the value of a property and our ability to lease or sell such a property.

The REIT employs a rigorous due diligence process, including obtaining a Phase I environmental site assessment, prior to acquiring property to mitigate its exposure to these potential issues.

Other Financial Information

Joint Arrangements

We record only our share of the assets, liabilities, revenue and expenses of our joint arrangements. In 2013, we had three joint arrangement. Refer to note 22 to the consolidated financial statements for additional information. The following table illustrates selected financial data related to joint arrangements at 100% as well as the net portion relevant to the REIT:

	Joint arrangement activity at JV%		Joint arrangement activity at 100%	
($000s)	31-Dec-13	31-Dec-12	31-Dec-13	31-Dec-12
Revenue	3,741	3,526	7,482	7,052
Earnings	4,138	4,484	8,276	8,968
Assets	48,712	45,476	97,424	90,952
Liabilities	22,472	21,747	44,944	43,494

Related Party Transactions

Please refer to note 21 to the consolidated financial statements for information pertaining to transactions with related parties.

Subsequent Events

Please refer to note 27 to the consolidated financial statements for information pertaining to subsequent events.

Critical Accounting Estimates

The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with IFRS. In applying IFRS, we make estimates and assumptions that affect the carrying amounts of assets and liabilities, disclosure of contingent liabilities and the reported amount of income for the period. Actual results could differ from estimates previously reported. We have discussed the development, selection and application of our key accounting policies, and the critical accounting estimates and assumptions they involve, with the Audit Committee and the Board of Trustees.

Our significant accounting policies and accounting estimates are contained in the consolidated financial statements. Please refer to note 3 to the consolidated financial statements for a description of our accounting policies and note 4 for a discussion of accounting estimates and judgments.

Changes in Accounting Policies

Refer to note 5 to the consolidated financial statements for information pertaining to accounting pronouncements that will be effective in future years.

Internal Control over Financial Reporting and Disclosure Controls

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant and material information is gathered and reported to senior management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), in a timely manner. Under the supervision of the CEO and CFO, we carried out an evaluation of the effectiveness of our disclosure controls and procedures as defined in Canada by National Instrument 52-109 as of December 31, 2013. Based on this evaluation, our CEO and CFO concluded that the design and operation of our disclosure controls and procedures related to the REIT and its subsidiaries and joint arrangements were effective.

Internal control over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. Management designed these controls based on the criteria set out in Internal Control - Integrated Framework (COSO 1992 Framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The CEO and CFO have certified that the internal controls over financial reporting were properly designed and effective for the year ended December 31, 2013.

There has been no change in the REIT's disclosure controls and procedures of internal control over financial reporting during the year ended December 31, 2013, that materially affected, or is reasonably likely to materially affect, the REIT's internal control over financial reporting.

Notwithstanding the foregoing, no assurance can be made that the REIT's controls over disclosure and financial reporting and related procedures will detect or prevent all failures of people to disclose material information otherwise required to be set forth in the REIT's reports.

Non-Standard Measures

Throughout this MD&A, we refer to terms that are not specifically defined in the CICA Handbook or in IFRS. These non-standard measures may not be comparable to similar measures presented by other companies.

We believe that these non-standard measures are useful in assisting investors in understanding components of our financial results.

The non-standard terms that we refer to in this MD&A are defined below.

Calculations

We use the following calculations in measuring our performance.

Net operating income (NOI): NOI is defined as rental revenue, adjusted for amortization of tenant improvements and straight-line rent adjustments, less direct operating expenses as presented in the statement of income and comprehensive income. A reconciliation of NOI to the most comparable IFRS measure, net income, is as follows:

	Three Months Ended December 31		
($000s)	2013	2012	Change
Net income for the period	7,466	12,822	
Income tax (recovery) expense		2,301	
Net finance costs	3,738	2,164	
Fair value loss on Class B LP Units	3,521	—	
Fair value adjustment on investment properties	(9,488)	(11,371)	
General and administrative expenses	459	104	
Amortization of tenant incentives	616	545	
Straight-line rent adjustment	(81)	(449)	
NOI	6,231	6,116	2%

	Year Ended December 31		
($000s)	2013	2012	Change
Net income for the period	62,719	35,490	
Income tax (recovery) expense	(40,261)	6,814	
Net finance costs	12,350	8,552	
Fair value (gain) loss on Class B LP Units	3,812	—	
Fair value adjustment on investment properties	(16,953)	(30,163)	
General and administrative expenses	1,728	1,369	
Amortization of tenant incentives	2,297	2,447	
Straight-line rent adjustment	(397)	(449)	
NOI	25,295	24,060	5%

Same asset NOI: this measure compares the NOI, less amortization on tenant incentives, plus straight-line rent adjustment, on assets that have been owned for the entire current and comparative period.

Funds from operations (FFO): FFO is defined as net income in accordance with IFRS, excluding: (i) fair value adjustments to investment properties; (ii) gains (or losses) from sales of investment properties; (iii) amortization of tenant incentives; (iv) fair value adjustments, interest expense and other effects of redeemable units classified as liabilities; (v) acquisition costs expensed as a result of the purchase of a property being accounted for as a business combination; (vi) deferred income tax expense; and (vii) non-recurring current income taxes on formation of the REIT, after adjustments for equity accounted entities, joint ventures and non-controlling interests calculated to reflect FFO on the same basis as consolidated properties.

Adjusted funds from operations (AFFO): AFFO is defined as FFO subject to certain adjustments, including: (i) amortization of fair value mark-to-market adjustments on mortgages acquired; (ii) interest rate subsidy amounts received; (iii) amortization of deferred financing and leasing costs; (iv) adjusting for any differences resulting from recognizing property revenues on a straight-line basis; (v) deducting a reserve for normalized maintenance capital expenditures, tenant inducements and leasing costs, as determined by us. Other adjustments may be made to AFFO as determined by the Board in its discretion.

Operating margin: is calculated as net rental income divided by rental revenue.

Debt to Gross Book Value: is calculated as the sum of mortgages payable and Class C LP Units, less unamortized fair value adjustment; divided by the total asset value assumed on acquisition of the Initial Properties plus total assets acquired from third parties subsequently.

Finance costs coverage ratio: is calculated as FFO plus finance costs for the period divided by finance costs expensed during the period, less distributions on Class B LP Units.

Debt service coverage ratio: is calculated as FFO for the period divided by principal repayments on mortgages payable and Class C LP Units made during the period.

Management's Responsibility for Financial Reporting

The consolidated financial statements, management's discussion and analysis (MD&A) and all financial information contained in the annual report are the responsibility of management. The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and, where appropriate, have incorporated estimates based on the best judgment of management.

To discharge its responsibility for financial reporting, management is responsible for implementing and maintaining adequate internal controls to provide reasonable assurance that the Trusts's assets are safeguarded, that transactions are properly authorized and that reliable financial information is relevant, accurate and available on a timely basis.

The consolidated financial statements have been examined by PricewaterhouseCoopers LLP, the Trust's external auditors. The external auditors are responsible for examining the consolidated financial statements and expressing their opinion on the fairness of the financial statements in accordance with International Financial Reporting Standards. The auditor's report outlines the scope of their audit examination and states their opinion.

The Board of Trustees, through the Audit Committee, is responsible for ensuring management fulfils its responsibilities for financial reporting and internal controls. The Audit Committee is comprised of three financially literate and independent directors. This committee meets regularly with management and the external auditors to review significant accounting, financial reporting and internal control matters. PricewaterhouseCoopers LLP have unrestricted access to the Audit Committee with and without the presence of management. The Audit Committee reviews the financial statements, the auditor's report, and MD&A and submits its report to the board of trustees for formal approval. The Audit Committee is also responsible for reviewing and recommending the annual appointment of external auditors and approving the external audit plan. These consolidated financial statements and Management's Discussion and Analysis have been approved by the Board of Trustees for inclusion in the Annual Report based on the review and recommendation of the Audit Committee.

Darin Rayburn
Chief Executive Officer

Jonathan Chia, CA
Chief Financial Officer

Edmonton, Alberta
March 10, 2014

Auditors' Report to Unitholders

We have audited the accompanying consolidated financial statements of Melcor Real Estate Investment Trust and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2013 and December 31, 2012 and the consolidated statements of income and comprehensive income, changes in unitholders' equity and cash flows for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Melcor Real Estate Investment Trust and its subsidiaries as at December 31, 2013 and December 31, 2012 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Accountants
Edmonton, Alberta
March 10, 2014

Consolidated Statements of Financial Position

($000s)	2013	2012
ASSETS		
Current Assets		
Cash and cash equivalents	5,932	689
Accounts receivable	1,478	2,457
Other assets (note 9)	1,015	238
	8,425	3,384
Non-Current Assets		
Restricted cash	5,969	—
Investment properties (note 8 and 26)	429,117	382,381
Other assets (note 9)	11,232	11,080
	446,318	393,461
TOTAL ASSETS	454,743	396,845
LIABILITIES		
Current Liabilities		
Revolving credit facility (note 10)	23,748	—
Accounts payable	1,989	2,098
Distribution payable	1,050	—
Accrued liabilities and other payables (note 11)	3,690	5,101
Class C LP Units (note 13)	3,059	—
Mortgages payable (note 12)	19,911	54,291
	53,447	61,490
Non-Current Liabilities		
Accrued liabilities and other payables (note 11)	1,459	1,052
Class B LP Units (note 14 and 26)	99,120	—
Class C LP Units (note 13)	91,188	—
Deferred income taxes (note 18)	—	40,261
Mortgages payable (note 12)	78,911	125,711
TOTAL LIABILITIES	324,125	228,514
UNITHOLDERS' EQUITY	130,618	168,331
TOTAL LIABILITIES AND UNITHOLDERS' EQUITY	454,743	396,845

See accompanying notes to the consolidated financial statements

On behalf of the REIT's Board of Trustees

Brian Hunt
Audit Committee Chair

Andrew Melton
Executive Chairman

Consolidated Statements of Income & Comprehensive Income

($000s)	2013	2012
Rental revenue (note 16 and 21)	39,325	37,485
Direct operating expenses (note 21)	(15,930)	(15,423)
Net rental income	23,395	22,062
General and administrative expenses (note 21)	(1,728)	(1,369)
Fair value adjustment on investment properties (note 8 and 26)	16,953	30,163
Fair value loss on Class B LP Units (note 14 and 26)	(3,812)	—
Income before finance costs and income taxes	34,808	50,856
Interest income	61	23
Finance costs (note 17 and 21)	(12,411)	(8,575)
Net finance costs	(12,350)	(8,552)
Net income before income taxes	22,458	42,304
Current income tax expense (note 18)	—	(846)
Deferred income tax recovery (expense) (note 18)	40,261	(5,968)
Income tax recovery (expense)	40,261	(6,814)
Net income and comprehensive income	62,719	35,490

See note 20 for basic and diluted earnings per trust unit.

See accompanying notes to the consolidated financial statements

Consolidated Statements of Changes in Unitholders' Equity

($000s except unity amounts)	Number of Trust Units	Trust Units	Contributed Surplus	Divisional Surplus	Retained Earnings	Total Unitholders' Equity
Balance at December 31, 2011	—	—	—	149,185	—	**149,185**
Net income	—	—	—	35,490	—	**35,490**
Net distributions to Melcor Developments Ltd.	—	—	—	(16,344)	—	**(16,344)**
Balance at December 31, 2012	—	—	—	168,331	—	**168,331**
Net income for the period January 1, 2013 to April 30, 2013 (note 19)	—	—	—	47,524	—	**47,524**
Net distributions to Melcor Developments Ltd.	—	—	—	(7,447)	—	**(7,447)**
Balance at April 30, 2013	—	—	—	208,408	—	208,408
Reorganization and recapitalization (note 6 and 15)	8,300,000	74,409	36,823	(208,408)	—	(97,176)
Conversion of Class B LP Units (note 6 and 14)	830,000	8,300	—	—	—	8,300
Net income for the period May 1, 2013 to December 31, 2013 (note 19)	—	—	—	—	15,195	15,195
Distributions to unitholders	—	—	—	—	(4,109)	(4,109)
Balance at December 31, 2013	9,130,000	82,709	36,823	—	11,086	130,618

See accompanying notes to the consolidated financial statements

Consolidated Statements of Cash Flows

($000s)	2013	2012
CASH FLOWS FROM (USED IN)		
OPERATING ACTIVITIES		
Net income for the year	62,719	35,490
Non cash items:		
Amortization of tenant incentives (note 16)	2,297	2,447
Straight-line rent adjustments (note 16)	(397)	(449)
Fair value adjustment on investment properties (note 8 and 26)	(16,953)	(30,163)
Fair value loss on Class B LP Units (note 14 and 26)	3,812	—
Amortization of fair value adjustment on Class C LP Units (note 17)	(293)	—
Amortization of deferred financing costs (note 17)	108	—
Accretion on decommissioning obligation	60	60
Deferred income tax (recovery) expense (note 18)	(40,261)	5,968
	11,092	13,353
Changes in operating assets and liabilities (note 3o)	(590)	569
	10,502	13,922
INVESTING ACTIVITIES		
Additions to investment properties (note 7 and 8)	(25,851)	(2,760)
Payment of tenant incentives (note 9)	(2,052)	(2,632)
Investment property improvements and development (note 8)	(3,823)	(7,529)
Change in restricted cash	(3,141)	—
	(34,867)	(12,921)
FINANCING ACTIVITIES		
Proceeds from issuing units, net of costs (note 15)	74,409	—
Acquisition of Initial Properties (note 6)	(66,016)	—
Proceeds from revolving credit facility (note 10)	24,000	—
Proceeds from mortgages payable	67,000	29,400
Repayment of mortgages payable	(53,435)	(14,241)
Repayment on Class C LP Units	(1,966)	—
Change in restricted cash	(2,828)	—
Net distribution to Melcor Developments Ltd.	(7,447)	(16,344)
Distributions to unitholders	(4,109)	—
	29,608	(1,185)
INCREASE (DECREASE) IN CASH & CASH EQUIVALENTS DURING THE YEAR	5,243	(184)
CASH AND CASH EQUIVALENTS, BEGINNING OF THE YEAR	689	873
CASH AND CASH EQUIVALENTS, END OF THE YEAR	5,932	689

See accompanying notes to the consolidated financial statements

1. DESCRIPTION OF THE TRUST

Melcor Real Estate Investment Trust (the "REIT" or "we") is an unincorporated, open-ended real estate investment trust established pursuant to a declaration of trust ("DOT") dated January 25, 2013 and subsequently amended and restated May 1, 2013.

The REIT began operations on May 1, 2013 when its trust units were issued for cash pursuant to the initial public offering ("IPO" or "Offering").

The REIT issued 8,300,000 trust units at a price of $10.00 per unit for total gross proceeds of $83,000. The REIT used the proceeds of the Offering to indirectly acquire, through a subsidiary of the REIT (the "Partnership"), interests in a portfolio of 27 income producing properties located in Western Canada (the "Initial Properties"). On May 10, 2013, the underwriters exercised, in full, their over-allotment option to purchase an additional 830,000 trust units from Melcor Developments Ltd. ("Melcor"), at a price of $10.00 per unit, for gross proceeds of $8,300. The over-allotment was fulfilled through conversion of Class B LP Units, owned by Melcor, into trust units.

Following closing of the over-allotment option, Melcor, through an affiliate, holds an approximate 51.1% effective interest in the REIT through ownership of all remaining 9,530,798 Class B LP Units of the Partnership. The Class B LP Units are economically equivalent to, and exchangeable for, trust units.

The principal business of the REIT is to acquire, own and manage office, retail and industrial properties in select target markets in Western Canada.

The REIT is governed under the laws of the Province of Alberta. The registered office of the REIT is located at Suite 900, 10310 Jasper Avenue Edmonton, Alberta, Canada. Our trust units are traded on the Toronto Stock Exchange under the symbol "MR.UN".

2. BASIS OF PRESENTATION

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standard Board ("IASB").

As the REIT is a newly formed entity and Melcor retained control over the REIT, the Offering and acquisition of the Initial Properties is accounted for as a reorganization and recapitalization using the continuity of interests method. Financial information for the pre-acquisition period, including the comparative period are presented based on historical combined financial information for the Initial Properties as previously reported by Melcor.

These consolidated financial statements are presented in Canadian dollars, which is the presentation and functional currency of the REIT; and were authorized for issue by the Board of Trustees on March 10, 2014.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used in the preparation of these consolidated financial statements are described below.

a. Basis of measurement

These consolidated financial statements have been prepared under the historical cost convention, except for investment properties and Class B LP Units which are measured at fair value.

We prepare our consolidated financial statements in conformity with IFRS which requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying our accounting policies. Changes in assumptions may have a significant impact on the consolidated financial statements in the period the assumptions change. We believe that the underlying assumptions are appropriate. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

b. Basis of consolidation

i. Subsidiaries

Subsidiaries are entities controlled by the REIT. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. These consolidated financial statements include the accounts of the REIT and its subsidiaries, its controlled partnership Melcor REIT Limited Partnership (the "Partnership"), and its general partner, Melcor REIT GP Inc.

ii. Joint arrangements

These arrangements are undivided interests in the assets, liabilities, revenues and expenses under arrangement and we record our proportionate share in accordance with the agreements as joint operations. These consolidated financial statements include investments in 3 joint arrangements (2012 – 3) with 50% interests. Refer to note 22 for additional details on our joint arrangements.

All intercompany transactions and balances are eliminated on consolidation.

c. Cash and cash equivalents

Cash and cash equivalents are comprised of cash and short-term deposits with maturity dates of less than three months from the date they were acquired.

d. Restricted cash

Restricted cash can only be used for specified purposes. The REIT's restricted cash represents subsidies funded by Melcor as part of the Offering to subsidize finance costs on assumed debt and Class C LP Units, and to fund capital expenditures, environmental expenditures, tenant incentives and lease costs.

e. Investment properties

Investment properties include commercial and industrial properties, and a manufactured home community held for the long term to earn rental income or for capital appreciation, or both.

Acquired investment properties are measured initially at cost, including transaction costs associated with the acquisition when the acquisition is accounted for as an asset purchase.

After initial recognition, investment properties are recorded at their fair value, which is determined by either a direct capitalization or discounting projected future cash flows approach based on property specific capitalization rates. Valuations are performed as of the period end date by independent, external professional valuators who hold recognized and relevant professional qualifications and have recent experience in the location and category of the investment property being valued. The fair value of investment property reflects, among other things, rental income from current leases and assumptions about rental income from future leases based on current market conditions. The value also reflects any cash outflows that could be expected in respect of the property. Changes in fair value are recognized in the consolidated statement of income.

Subsequent expenditures are capitalized to the asset's carrying amount only when it is probable that future economic benefits associated with the expenditure will flow to the REIT and the cost of the item can be measured reliably. All repairs and maintenance costs are expensed when incurred.

Initial direct leasing costs incurred in negotiating and arranging tenant leases are added to the carrying amount of investment properties.

f. Other assets

Other assets include prepaid expenses, deposits, straight-line rent adjustments and tenant incentives incurred in respect of new or renewed leases. Tenant incentives are amortized on a straight-line basis over the lease term and are recorded as a reduction of revenue.

g. Provision for decommissioning obligation

Decommissioning obligations are measured at the present value of the expected cost to settle the obligation. A corresponding decommissioning cost is added to the carrying amount of the associated investment property. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows as well as any changes in the discount rate. Actual costs incurred upon settlement of the decommissioning obligation are recorded against the provision.

h. Class B LP Units

The Class B LP Units are exchangeable into trust units at the option of the holder and, therefore, are considered a puttable instrument in accordance with International Accounting Standard ("IAS") 32, Financial instruments — presentation ("IAS 32"). The Class B LP Units, as puttable instruments, are required to be accounted for as financial liabilities. The Class B LP Units are designated as fair value through profit or loss financial liabilities and are remeasured to fair value at each period end date based on the trading price of the trust units at the period end date with any changes in fair value recognized in the consolidated statements of income and comprehensive income. Distributions declared on Class B LP Units are recorded as finance costs in the statement of income and comprehensive income.

i. Unit capital

The trust units are redeemable at the option of the holders and, therefore, are considered a puttable instrument in accordance with IAS 32. Puttable instruments are required to be accounted for as financial liabilities, except where certain conditions are met in accordance with IAS 32, in which case, the puttable instruments may be presented as equity. The trust units meet the conditions of IAS 32 and are, therefore, classified and accounted for as equity.

j. Distributions

Distributions to unitholders are recognized as a liability in the period in which the distributions are approved by the Board of Trustees and are recorded as a reduction of retained earnings.

k. Recognition of revenue

Tenant leases are accounted for as operating leases given that we have retained substantially all of the risks and benefits of the ownership of our investment properties. Revenue from investment properties includes base rents, recoveries of operating expenses including property taxes, parking revenue and incidental income. Revenue recognition under a lease commences when the tenant has a right to use the leased asset. The total amount of contractual rent to be received from operating leases is recognized on a straight-line basis over the term of the lease; a straight-line rent receivable, which is included in other assets, is recorded for the difference between the rental revenue recognized and the contractual amount received. When incentives are provided to our tenants, the cost of these incentives is recognized over the lease term, on a straight-line basis, as a reduction to rental revenue. Recoveries from tenants are recognized as revenues in the period in which the corresponding costs are incurred. Other revenues are recorded as earned.

l. Finance costs

Finance costs are comprised of interest expense on mortgages, interest and other finance fees on our credit facility, interest on Class C LP Units, amortization of fair value adjustment on Class C LP Units, distributions on Class B LP Units, and amortization of deferred transaction costs. Borrowing costs are recognized in income using the effective interest rate method.

m. Income taxes

The REIT qualifies as a mutual fund trust within the meaning of the Income Tax Act (Canada) ("Tax Act") and as a real estate investment trust eligible for the 'REIT Exception', as defined in the rules applicable to Specified Investment Flow-Through ("SIFT") trusts and partnerships in the Tax Act. We expect to allocate all taxable income and to continue to qualify for the REIT Exception. Accordingly, no income tax expense or deferred income tax assets or liabilities have been recorded in these consolidated financial statements subsequent to the formation of the REIT.

n. Financial instruments

At initial recognition, we classify our financial instruments in the following categories depending on the purpose for which the instruments were acquired:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans to third parties and receivables are initially recognized at fair value plus transaction costs. Subsequently, loans and receivables are measured at amortized cost using the effective interest rate method less a provision for impairment, if necessary. Loans and receivables are comprised of accounts receivable, cash and cash equivalents and restricted cash.

At each reporting date, we assess whether there is objective evidence that a financial asset is impaired, considering delinquencies in payments and financial difficulty of the debtor. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through use of an allowance account. The amount of any losses is recognized in income.

Financial liabilities

We record our financial liabilities at fair value on initial recognition. Subsequently, "other liabilities" are measured at amortized cost using the effective interest rate method and financial liabilities designated as fair value through profit or loss ("FVTPL") are remeasured at fair value with changes in their fair value recorded through income. Other liabilities include the revolving credit facility, accounts payable, accrued liabilities and other payables, distributions payable, mortgages payable, and Class C LP Units. Class B LP Units are classified as FVTPL.

o. Statements of cash flows

Operating assets and liabilities is defined as the net change of accounts receivable, prepaid expense, and other, accounts payable, distribution payable and accrued liabilities and other payables. Excluded from operating assets and liabilities are investment property additions that are unpaid and included in accounts payable at period end.

4. SIGNIFICANT JUDGEMENTS AND CRITICAL ACCOUNTING ESTIMATES

Estimates and judgments are continually evaluated and are based on historical experience as adjusted for current market conditions and other factors.

Significant judgments

In the process of applying our accounting policies, we make various judgments, apart from those involving estimations, that can significantly impact the amounts recognized in the consolidated financial statements. These include:

a. Business combinations under common control

Business combinations under common control ("BCUCC") are business combinations involving entities or businesses under common control, in which all of the combining entities or businesses are ultimately controlled by the same party both before and after the business combination. BCUCC are not within the scope of IFRS 3, Business combinations.

As the REIT is a newly formed entity and Melcor retained control over the REIT, the Offering and acquisition of the Initial Properties is accounted for as a reorganization and recapitalization using the continuity of interests method. Under this method, the REIT records the assets acquired and liabilities assumed at their carrying amounts on the closing date of the transaction. The difference between the consideration given and the aggregate value of the net assets acquired is recorded as an adjustment to unitholders' equity. Refer to note 6 for details of the accounting treatment for the acquisition of the Initial Properties. Financial information for the pre-acquisition period, including the comparative periods are presented based on historical combined financial information for the Initial Properties as previously reported by Melcor. Refer to note 19 for statements of income and comprehensive income and statements of cash flows for the period disaggregated by the activities of the REIT, and its predecessor, Melcor.

b. Investment properties

Our accounting policies related to investment properties are described in note 3e. In applying this policy, judgment is required in determining whether certain costs are additions to the carrying amount of an investment property.

c. Classification of tenant incentives

Payments are often made to, or on behalf of, tenants of our commercial properties when new leases are signed. When the payments add future value to the space independent of the lease in place, such costs are capitalized to the investment property. If the costs incurred are specific to the lessee, and do not have stand-alone value, these costs are treated as tenant incentives and amortized on a straight-line basis to revenue over the lease term in accordance with SIC 15, Operating leases – incentives.

d. Compliance with REIT exemption under ITA

Under current tax legislation, a real estate investment trust is not liable for Canadian income taxes provided that its taxable income is fully allocated to unitholders during the year. In order to continue to be taxed as a mutual fund trust, we need to maintain our REIT status. At inception, we qualify as a REIT under the specified investment flow-through ("SIFT") rules in the Income Tax Act (Canada). The REIT's current and continuing qualification as a REIT depends on our ability to meet the various requirements imposed under the SIFT rules, which relate to matters such as our organizational structure and the nature of our assets and revenues. We apply judgment in determining whether it continues to qualify as a REIT under the SIFT rules. Should we cease to qualify, we would be subject to income tax on our earnings and would reflect current and deferred tax balances on our consolidated financial statements.

Critical accounting estimates

We make estimates and assumptions that affect the carrying amounts of assets and liabilities, disclosure of contingent liabilities and the reported amount of income for the period. Actual results could differ from estimates previously reported. The estimates and assumptions that are critical to the determination of the amounts reported in the consolidated financial statements relate to the following:

Valuation of investment properties

Investment properties are valued using either a direct capitalization or discounted cash flow approach, as completed by qualified external professional valuators with key assumptions reviewed and updated quarterly. Key estimates and assumptions include expected occupancy rates and lease payments, expenditures for operating costs and capital expenditures as well as discount and capitalization rate. Refer to note 8 and 26 for further information about methods and assumptions used in determining fair value.

5. NEW STANDARDS NOT YET ADOPTED

IFRIC 21, Levies is an interpretation of IAS 37, 'Provisions, contingent liabilities and contingent assets'. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. This standard is required to be applied for accounting periods beginning on or after January 1, 2014, with earlier adoption permitted.

IFRS 9, Financial instruments addresses the classification, measurement and recognition of financial assets and financial liabilities. It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortized cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the IAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The standard also results in one impairment method replacing the numerous impairment methods in IAS 39 that arise from the different classification categories. This standard is required to be applied for accounting periods beginning on or after January 1, 2015, with earlier adoption permitted.

($000s except unit and per unit amounts)

We are currently assessing the impact of adopting these standards on our consolidated financial statements.

6. ACQUISITION OF INITIAL PROPERTIES

On May 1, 2013, the REIT completed the purchase of 27 income-producing properties located in Western Canada, comprised primarily of retail, office and industrial properties (the "Initial Properties") from Melcor Developments Ltd. ("Melcor") with a carrying value of $397,896. As part of the acquisition of the Initial Properties, the REIT also assumed mortgages on certain properties totaling $92,360 at April 30, 2013. Deferred financing fees of $97 were netted against the assumed mortgages. In addition, the working capital, which is comprised of cash balances, accounts receivable, prepaid expenses, accounts payable and accrued liabilities, and other liabilities were transferred on closing. The purchase price was satisfied with cash consideration of $66,016 and issuance of 10,360,798 Class B LP Units of the Partnership. Melcor retained the debt on certain properties (the "Retained Debt") with a fair value of $96,506 at April 30, 2013. In consideration of the Retained Debt, Melcor received Class C LP units of the Partnership on which it will receive priority distributions.

The allocation of the purchase price to the assets acquired and liabilities assumed, based on their carrying values at the date of acquisition, is as follows:

Net assets acquired:	
Real estate properties	397,896
Working capital, net	(2,680)
Assumed mortgages	(92,263)
	302,953
Distributions to Melcor	
Class C LP Units	96,506
Class B LP Units	103,608
Cash paid out by the REIT	66,016
	266,130
Net contribution by Melcor	**36,823**

On May 10, 2013, the underwriters exercised, in full, their over-allotment option to purchase an additional 830,000 trust units from Melcor. The transaction resulted in an increase in unitholders' equity of $8,300 (underwriters' fee was paid by Melcor) and a decrease in Class B LP Units of $8,300.

Following closing of the over-allotment option, Melcor, through an affiliate, holds an approximate 51.1% effective interest in the REIT through ownership of all remaining 9,530,798 Class B LP Units. As Melcor will retain control over the REIT, the transaction constitutes a business combination under common control which is outside the scope of IFRS 3 – Business combinations. The IPO and acquisition of the Initial Properties by the REIT is accounted for as a reorganization and recapitalization using the continuity of interests method, where by the REIT recorded the assets acquired and liabilities assumed at their carrying amounts. The difference between the consideration given and the aggregate value of the net assets acquired is recorded as an adjustment to unitholders' equity.

Transaction costs directly related to the Offering and acquisition of the Initial Properties were $8,591 and were charged directly to unitholders' equity.

7. INVESTMENT PROPERTY ACQUISITIONS

On September 12, 2013, the REIT completed the purchase of Coast Home Centre ("Coast"), located in Edmonton, Alberta. We acquired 100% interest in the property for total consideration of $12,462 (including transaction costs).

On December 24, 2013, the REIT acquired Liberty Crossing ("Liberty"), located in Red Deer, Alberta. We acquired 100% interest in the property for total consideration of $13,389 (including transaction costs).

The acquisitions were funded through the REIT's line of credit and available cash.

The purchases have been accounted for as asset purchases, in accordance with our policy, as detailed in note 3e.

8. INVESTMENT PROPERTIES

	2013	2012
Balance - beginning of period	382,381	345,246
Additions		
Direct acquisition (note 7)	25,851	2,760
Property improvements	3,035	3,566
Property development activities	—	3,574
Direct leasing costs	788	389
Fair value adjustment on investment property (note 26)	16,953	30,163
Change in provision (note 11)	109	(3,317)
Balance - end of period	429,117	382,381

In accordance with our policy, as detailed in note 3e, we record our investment properties at fair value. Fair value adjustments on investment properties are primarily driven by changes in capitalization rates and stabilized net operating income ("NOI"). Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 26.

The cost of investment properties as at December 31, 2013 totalled $205,992 (December 31, 2012 - $176,318).

Presented separately from investment properties is $10,386 (December 31, 2012 - $10,631) in tenant incentives and $846 (December 31, 2012 - $449) in straight-line rent adjustments (note 9). The fair value of investment properties has been reduced by these amounts.

($000s except unit and per unit amounts)

Our investment properties are leased to tenants primarily under long term operating leases. Rentals are receivable from tenants monthly. Minimum lease payments under non-cancellable operating leases of investment properties are receivable as follows:

	2013	2012
Within one year	23,683	21,798
Later than one year but not later than 5 years	67,490	59,761
Later than 5 years	40,386	45,984
	131,559	127,543

9. OTHER ASSETS

	2013	2012
Current Assets		
Prepaid expense, and other	1,015	238
Non-Current Assets		
Straight-line rent adjustments	846	449
Tenant incentives	10,386	10,631
	11,232	11,080
	12,247	11,318

During the year we provided tenant incentives of $2,052 (December 31, 2012 - $2,632) and recorded $2,297 (December 31, 2012 - $2,447) of amortization expense respectively. In accordance with SIC 15, Operating leases - incentives, amortization of tenant incentives is recorded on a straight-line basis over the term of the lease against rental revenue.

10. REVOLVING CREDIT FACILITY

On April 20, 2013, we entered into a revolving term facility credit agreement with two major Canadian chartered banks. Under the terms of the agreement the REIT has an available credit limit based upon the carrying values of specific investment properties, as calculated quarterly, up to a maximum of $25,000 for general purposes. The agreement also provides the REIT with $5,000 in available letters of credit which bear interest at 2.25%. The facility matures on May 1, 2015, with a one year extension period at the discretion of the lenders. Depending on the form under which the credit facility is accessed, rates of interest will vary between prime plus 1.25% or bankers acceptance plus 2.25% stamping fee. Interest payments are due and payable based upon the form of the facility drawn upon, and principal is due and payable upon maturity. The agreement also bears a standby fee of 0.50% for the unused portion of the revolving facility. The lenders hold demand debentures, a first priority general security and a general assignment of leases and rents over specific investment properties as security for the facility. As at December 31, 2013, the carrying value of pledged properties was $66,700. We capitalized $252 in transaction costs associated with the facility, of which $170 was unamortized at December 31, 2013 and is presented net of the outstanding balance.

As at December 31, 2013 we had an available credit limit of $25,000, of which $24,000 was drawn; and posted letters of credit of $nil. The weighted average effective interest rate on borrowings, based on period end balances, is 3.72%. The following table summarizes the components of the balance at December 31, 2013:

	2013
Amount drawn on facility	24,000
Unamortized transaction fees	(170)
Unamortized discount on bankers acceptance	(82)
	23,748

11. ACCRUED LIABILITIES AND OTHER PAYABLES

	2013	2012
Current Liabilities		
Accrued liabilities and other payables	3,508	4,353
Decommissioning obligation	182	748
	3,690	5,101
Non-Current Liabilities		
Decommissioning obligation	1,459	1,052
	5,149	6,153

The REIT's decommissioning obligation relates to one of our commercial properties. The total decommissioning obligation is estimated based on the future obligation and timing of these expenditures to be incurred. We estimate the net present value of the obligation based on an undiscounted total future provision of $2,298 (2012 - $2,428). At December 31, 2013, a discount rate of 4.0% (2012 - 4.5%) and an inflation rate of 2.0% (2012 - 2.0%) were used to calculate the net present value of the obligation. Due to uncertainty surrounding the nature and timing of this obligation amounts are subject to change.

12. MORTGAGES PAYABLE

	2013	2012
Mortgages amortized over 15-25 years at fixed interest rates	99,023	172,502
Variable rate mortgage, due on demand	—	7,500
Unamortized deferred financing fees	(201)	—
	98,822	180,002
Current portion of mortgages payable	(19,911)	(54,291)
	78,911	125,711
Interest rate ranges	(3.01%-5.86%)	(2.90%-6.16%)

Specific investment properties with a carrying value of $197,866 (December 31, 2012 - $375,061) and assignment of applicable rents and insurance proceeds have been pledged as collateral for the above mortgages. The weighted average effective interest rate for the above mortgages, based on period end balances, is 4.20% (December 31, 2012 – 4.57%).

The minimum contractual principal payments due within each of the next five years and thereafter are as follows:

($000s except unit and per unit amounts)

	Principal Instalment Repayments	Balance Maturing	Total
2014	2,972	16,939	19,911
2015	2,593	19,533	22,126
2016	1,921	11,901	13,822
2017	1,516	—	1,516
2018	1,574	32,506	34,080
Thereafter	414	7,154	7,568
	10,990	88,033	99,023

13. CLASS C LP UNITS

On closing of the Offering, Melcor retained the debt on certain Initial Properties (the "Retained Debt"), with an outstanding principal balance of $94,544 at April 30, 2013. The Class C LP Units were initially recognized at their fair value of $96,506. The fair value of the Class C LP Units was determined based upon future payments at market interest rates. In consideration of the Retained Debt, Melcor received 9,454,411 Class C LP Units of Melcor REIT Limited Partnership (the "Partnership"), a subsidiary of REIT, on which priority distributions are made to permit Melcor to satisfy required principal and interest payments. The Class C LP Units are classified as debt and a portion of the distributions are recognized as interest expense.

As at December 31, 2013 the carrying value of the Class C LP Units, included in the consolidated statement of financial position, were as follows:

	2013	2012
Class C LP Units amortized over 2-6 years at fixed interest rates	92,578	—
Unamortized fair value adjustment	1,669	—
	94,247	—
Current portion of Class C LP Units	(3,059)	—
	91,188	—
Effective interest rate	3.84%	—

Specific investment properties with a carrying value of $169,500 (December 31, 2012 - $nil) and assignment of applicable rents and insurance proceeds have been pledged as collateral for the above Class C LP Units, along with a guarantee by the Partnership.

The minimum contractual principal payments due within each of the next five years and thereafter are as follows:

	Principal Instalment Repayments	Balance Maturing	Total
2014	3,059	—	3,059
2015	2,780	23,045	25,825
2016	2,150	9,030	11,180
2017	2,006	2,578	4,584
2018	1,687	11,421	13,108
Thereafter	4,213	30,609	34,822
	15,895	76,683	92,578

During the year $2,428 was recognized in finance costs and $2,259 was recognized as a reduction in the Class C LP Units liability related to these distributions.

At December 31, 2013 there were 9,257,820 Class C LP Units issued and outstanding.

14. CLASS B LP UNITS

On closing of the Offering, Melcor received 10,360,798 Class B LP Units of the Partnership as partial consideration for the Initial Properties. The Class B LP Units are exchangeable at the option of the holder for one trust unit of the REIT and accompanied by one special voting unit (note 15b). Distributions on Class B LP Units are recorded and paid to holders equal to those declared on trust units. On May 10, 2013, Melcor exchanged 830,000 Class B LP Units for an equal number of trust units, which were then used to fulfill the over-allotment option held by the underwriters pursuant to the Offering. Distributions on Class B LP Units for the year were $4,289, and are included in finance costs.

In accordance with our policy, as detailed in note 3h, we record Class B LP Units at fair value. We remeasured the Class B LP Units at December 31, 2013 and recognized a fair value loss of $3,812 during the year. Supplemental information on fair value measurement, including valuation technique and the key input, is included in note 26.

At December 31, 2013 there were 9,530,798 Class B LP Units issued and outstanding at a fair value of $10.40 per unit or $99,120.

15. UNITHOLDERS' EQUITY

a. Trust Units

The REIT is authorized to issue an unlimited number of trust units and an unlimited number of special voting units. Each trust unit represents a holder's proportionate undivided beneficial ownership interest in the REIT and will confer the right to one vote at any meeting of the Unitholders and to participate pro rata in any distributions by the REIT.

Unitholders are entitled to demand, at any time, the REIT to redeem all or part of the trust units at a "Redemption Price" as defined in the REIT's DOT. Upon receipt of notice to redeem trust units, the Unitholder surrenders all rights to and under the units tendered for redemption.

b. Special Voting Units

Pursuant to the DOT, special voting units have no economic entitlement in the REIT or in the distributions or assets of the REIT but entitle the holder to one vote per special voting unit at any meeting of the Unitholders. Special voting units may only be issued in connection with or in relation to securities exchangeable into Units, including Class B LP Units, for the purpose of providing voting rights with respect to the REIT to the holders of such securities. Special voting units will not be transferable separately from the exchangeable securities to which they are attached and will be automatically transferred upon the transfer of such exchangeable securities.

c. Units Outstanding

The following table summarizes the changes in trust units for the period May 1, 2013 to December 31, 2013.

($000s except unit and per unit amounts)

Issued and fully paid units	Units	Amount
Balance, May 1, 2013	—	—
Issuance of Units - IPO, net of $8,591 in costs	8,300,000	74,409
Conversion of Class B LP Units	830,000	8,300
Balance, December 31, 2013	9,130,000	82,709

16. RENTAL REVENUE

The components of rental revenue are as follows:

	2013	2012
Rental revenue	41,225	39,483
Amortization of tenant incentives	(2,297)	(2,447)
Straight-line adjustment	397	449
	39,325	37,485

17. FINANCE COSTS

The components of finance costs are as follows:

	2013	2012
Interest on mortgages payable and revolving credit facility	5,586	8,575
Interest on Class C LP Units	2,721	—
Amortization of fair value adjustments on Class C LP Units	(293)	—
Distributions on Class B LP Units	4,289	—
Amortization of deferred financing costs	108	—
	12,411	8,575

Total finance costs paid during the year were $12,060 (2012 - $8,575).

18. INCOME TAXES

As at December 31, 2013 the REIT qualifies as a mutual fund trust within the meaning of the Tax Act and as a real estate investment trust eligible for the 'REIT Exception' under the Specified Investment Flow-Through ("SIFT"); accordingly, no current or deferred income tax expense has been recognized on income earned or capital gains recognized subsequent to the formation of the REIT. In addition, we recorded a deferred income tax recovery of $40,585 on May 1, 2013 related to the de-recognition of a deferred income tax liability as a result of qualifying for the REIT Exception at the time of the IPO.

The components of income tax (recovery) expense are as follows:

	2013	2012
Current tax expense	—	846
Deferred tax expense		
Origination and reversal of temporary differences	324	5,968
Reversal of deferred taxes upon reorganization and recapitalization and allocation of taxable income to Unitholders (note 3m and 6)	(40,585)	—
	(40,261)	5,968
	(40,261)	6,814

Reconciliation of income tax expense based on the statutory rate to the expense recorded using the effective tax rate is as follows:

	2013	2012
Net income before income taxes	22,458	42,304
Statutory rate	25%	25%
	5,615	10,576
Non-deductible expenses	79	2
Non-taxable portion of capital gains and fair value adjustments	(2,119)	(3,764)
Allocation of taxable income to unitholders (note 3m)	(3,251)	—
Reversal of current and deferred taxes upon reorganization and recapitalization (note 3m and 6)	(40,585)	—
	(40,261)	6,814

The movement of deferred tax balances for the year are as follows:

December 31, 2013	Opening	Recognized in net income	Closing
Investment properties	37,993	(37,993)	—
Tenant incentives	2,658	(2,658)	—
Straight-line rent adjustment	60	(60)	—
Provision for decommissioning obligation	(450)	450	—
	40,261	(40,261)	—

December 31, 2012	Opening	Recognized in net income	Closing
Investment properties	32,971	5,022	37,993
Tenant incentives	2,612	46	2,658
Straight-line rent adjustment	—	60	60
Provision for decommissioning obligation	(1,290)	840	(450)
	34,293	5,968	40,261

($000s except unit and per unit amounts)

19. RESULTS OF THE REIT AND ITS PREDECESSOR

The following consolidated statement of income and comprehensive income and consolidated statement of cash flows disaggregate the financial results of the REIT for the year ended December 31, 2013 between the activities of the REIT, subsequent to April 30, 2013, and those of Melcor, prior to May 1, 2013.

	Melcor 1-Jan to 30-Apr	REIT 1-May to 31-Dec	Year ended 31-Dec
Rental revenue (note 16 and 21)	12,942	26,383	**39,325**
Direct operating expenses (note 21)	(5,037)	(10,893)	**(15,930)**
Net rental income	7,905	15,490	**23,395**
General and administrative expenses (note 21)	(507)	(1,221)	**(1,728)**
Fair value adjustment on investment properties (note 8 and 26)	2,594	14,359	**16,953**
Fair value loss on Class B LP Units (note 14 and 26)	—	(3,812)	**(3,812)**
Income before finance costs and income taxes	9,992	24,816	**34,808**
Interest income	8	53	**61**
Finance costs (note 17 and 21)	(2,737)	(9,674)	**(12,411)**
Net finance costs	(2,729)	(9,621)	**(12,350)**
Net income before income taxes	7,263	15,195	**22,458**
Current income tax expense (note 18)	—	—	**—**
Deferred income tax recovery (note 18)	40,261	—	**40,261**
Income tax recovery	40,261	—	**40,261**
Net income and comprehensive income	47,524	15,195	**62,719**

	Melcor 1-Jan to 30-Apr	REIT 1-May to 31-Dec	Year ended 31-Dec
CASH FLOWS FROM (USED IN)			
OPERATING ACTIVITIES			
Net income for the year	47,524	15,195	**62,719**
Non cash items:			
Amortization of tenant incentives (note 16)	773	1,524	**2,297**
Straight-line rent adjustments (note 16)	(125)	(272)	**(397)**
Deferred income tax (recovery) expense (note 18)	(40,261)	—	**(40,261)**
Fair value adjustment on investment properties (note 8 and 26)	(2,594)	(14,359)	**(16,953)**
Fair value loss on Class B LP Units (note 14 and 26)	—	3,812	**3,812**
Amortization of fair value adjustment on Class C LP Units (note 17)	—	(293)	**(293)**
Amortization of deferred financing costs (note 17)	—	108	**108**
Accretion on decommissioning obligation	20	40	**60**
	5,337	5,755	**11,092**
Changes in operating assets and liabilities (note 3o)	(1,975)	1,385	**(590)**
	3,362	7,140	**10,502**
INVESTING ACTIVITIES			
Additions to investment properties (note 7 and 8)	—	(25,851)	**(25,851)**
Payment of tenant incentives (note 9)	(743)	(1,309)	**(2,052)**
Investment property improvements and development (note 8)	(1,746)	(2,077)	**(3,823)**
Change in restricted cash	—	(3,141)	**(3,141)**
	(2,489)	(32,378)	**(34,867)**
FINANCING ACTIVITIES			
Proceeds from issuing units, net of costs (note 15)	—	74,409	**74,409**
Acquisition of Initial Properties (note 6)	—	(66,016)	**(66,016)**
Proceeds from revolving credit facility (note 10)	—	24,000	**24,000**
Proceeds from mortgages payable	55,000	12,000	**67,000**
Repayment of mortgages payable	(48,195)	(5,240)	**(53,435)**
Repayment on Class C LP Units	—	(1,966)	**(1,966)**
Change in restricted cash	—	(2,828)	**(2,828)**
Net distribution to Melcor	(7,447)	—	**(7,447)**
Distributions to unitholders	—	(4,109)	**(4,109)**
	(642)	30,250	**29,608**
INCREASE IN CASH & CASH EQUIVALENTS DURING THE PERIOD	231	5,012	**5,243**
CASH AND CASH EQUIVALENTS, BEGINNING OF THE YEAR	689	920	**689**
CASH AND CASH EQUIVALENTS, END OF THE YEAR	920	5,932	**5,932**

20. INCOME PER UNIT

Basic and diluted earnings per trust unit for the period May 1, 2013 to December 31, 2013 are calculated as follows:

	1_May-13 to 31-Dec-13
Income and comprehensive income - basic ($000s) (note 19)	15,195
Impact of Class B LP Unit fair value adjustment and distributions ($000s)	8,101
Income and comprehensive income - diluted ($000s)	23,296
Basic weighted average trust units outstanding during the period	9,099,385
Impact of conversion of Class B LP Units	9,530,798
Diluted weighted average trust units outstanding during the period	18,630,183
Basic earnings per trust unit	$1.67
Diluted earnings per trust unit	$1.25

21. RELATED PARTY TRANSACTIONS

Pursuant to the transaction as detailed in note 6, the consolidated financial statements of the REIT include the following related party transactions with Melcor, and its affiliates, as the controlling Unitholder of the REIT:

a. Property and Asset Management Agreements

Effective May 1, 2013, the REIT and Melcor entered into a Property Management Agreement and an Asset Management Agreement which set forth the terms and conditions under which the REIT is managed, administered and operated.

Asset Management Agreement – we pay a quarterly management fee which is comprised of the following: (a) a base annual management fee calculated and payable on a quarterly basis, equal to 0.25% of the REIT's gross book value; (b) a capital expenditures fee equal to 5% of all hard construction costs incurred on capital projects in excess of $0.10 million; (c) an acquisition fee equal to 0.50% - 1.00% of the purchase price; (d) a financing fee equal to 0.25% of the debt and equity of all financing transactions completed for the REIT to a maximum of actual expenses incurred by Melcor.

Property Management Agreement – we pay a monthly fee which is comprised of the following: (a) a base fee of 1/12 of 3% of gross property revenue; (b) a leasing fee equal to 5% of aggregate base rent for new leases for the first 5 years and 2.5% thereafter, and 2.5% of aggregate base rent for lease renewals and expansions for the first 5 years.

Pursuant to the terms of the agreements the REIT incurred the following fees during the period:

For the year ended December 31	2013
Asset Management Agreement	
Base Annual Management Fee	676
Capital Expenditure Fee	—
Acquisition Fee	256
Financing Fee	—
Property Management Agreement	
Monthly Fee	746
Lease Fee	511
	2,189

The Base Annual Management Fee is included in general and administrative expenses. Monthly Fees are included in direct operating expenses. In accordance with our policy (3e), Acquisition Fees and Lease Fees are capitalized to investment properties. As at December 31, 2013 there was $447 payable to Melcor related to these fees.

b. Distributions on Class B LP Units and Redemptions of Class C LP Units

From May 1, 2013 to December 31, 2013, $4,289 in distributions were recorded on Class B LP Units held by Melcor. These distributions were recorded as finance costs. As at December 31, 2013 there was $536 payable to Melcor for the September distribution.

Also during the same period, Melcor, as holder of all Class C LP Units, was paid $4,687 to fund principal and interest payments on the Retained Debt. These redemptions were recorded as a reduction of the Class C LP Unit liability and as finance costs.

c. Rental Revenue

From the period of May 1, 2013 to December 31, 2013 the REIT collected $470 in rental revenue from Melcor and an affiliate for use of office space. This amount is included in rental revenue.

d. Key Management Remuneration

The REIT does not directly or indirectly pay any compensation to named executive officers of the REIT. The REIT has no employees and is externally managed, administered and operated by Melcor pursuant to the Asset Management Agreement and Property Management Agreement.

All related party transactions occurred in the normal course of operations, at market rates and under normal commercial terms.

($000s except unit and per unit amounts)

22. JOINT ARRANGEMENTS

The table below discloses our rights to and share of the assets, liabilities, revenues, and earnings of three joint arrangements (2012 – three) that are recorded in these consolidated financial statements:

	Interest
Capilano Investments Joint Venture	50%
Westmere Properties Joint Venture	50%
Watergrove Developments Joint Venture	50%

	Assets	Liabilities	Revenue	Earnings
2013	48,712	22,472	3,741	4,138
2012	45,476	21,747	3,526	4,484

23. SEGMENTED INFORMATION

All the properties included in these consolidated financial statements are located in Western Canada, and are viewed by the Chief Operating Decision Maker (determined to be the Chief Executive Officer) as one operating segment in the context of these consolidated financial statements.

24. MANAGEMENT OF CAPITAL RESOURCES

We define capital as unitholders' equity, Class B LP Units, Class C LP Units, mortgages payables and our revolving credit facility. Our objective when managing capital is to ensure sufficient funds are available to make unitholder distributions, support the growth of our assets, and finance capital requirements. Specifically, we plan to utilize a combination of short, medium and long-term debt financing that aligns with the characteristics of each property.

Pursuant to the DOT, the REIT may not incur or assume any indebtedness if, after incurring or assuming such indebtedness, the total indebtedness of the REIT would be more than 60% of Gross Book Value ("GBV") ("Degree of Leverage Ratio") (65% including any convertible debentures). At December 31, 2013, and throughout the period, we were in compliance with the Degree of Leverage Ratio and had a ratio of 51% as at December 31, 2013.

We are also subject to financial covenants on our $25,000 revolving credit facility. The covenants include a maximum debt to total capital ratio of 60%, a minimum interest coverage ratio of 1.50, and a minimum net book value of unitholders' equity of $140,000. As at December 31, 2013, we were in compliance with our financial covenants with a debt to total capital ratio of 51%, interest coverage ratio of 1.71, and a net book value of unitholders equity, based on the definition of unitholders equity in our revolving credit facility agreement, of $220,715. We also have financial covenants on certain mortgages for investment properties. At December 31, 2013, and throughout the period, we were in compliance with our financial covenants on our mortgages. We prepare financial forecasts to monitor the changes in our debt and capital levels and our ability to meet our financial covenants.

25. FINANCIAL RISK MANAGEMENT

We are exposed to the following risks as a result of holding financial instruments:

a. Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Our financial assets that are exposed to credit risk consist of cash and cash equivalents, restricted cash and accounts receivable. Our maximum exposure to credit risk is the carrying amount of these instruments.

We invest our cash and cash equivalents and restricted cash in bank accounts with major Canadian chartered banks. Accounts receivable balances include amounts due from tenants and other joint arrangement participants for their portion of management fees due to us. There have been no impairment adjustments made to these accounts.

We manage our credit risk through careful selection of tenants and look to obtain national tenants or tenants in businesses with a long standing history, or perform financial background checks including business plan review for smaller tenants. We manage our concentration risk by renting to an expansive tenant base, with no dependency on rents from any one specific tenant. Management has reviewed outstanding receivable balances at December 31, 2013 and expect full payment of balances outstanding. No allowance for doubtful accounts has been recorded.

b. Liquidity Risk

Liquidity risk is the risk that we will not be able to meet our financial obligations as they fall due. We manage liquidity risk to ensure that we have sufficient liquid financial resources to finance operations, meet long-term mortgage repayments, Class C LP Unit redemptions, and make monthly distributions on Class B LP Units and trust units. We monitor rolling forecasts of our liquidity, which includes cash, on the basis of expected cash flows. In addition, we monitor balance sheet liquidity ratios against capital requirements and maintain on-going debt financing plans. We believe that we have access to sufficient capital through internally generated cash flows, external sources and undrawn committed borrowing facilities to meet current spending forecasts.

Refer to notes 12 and 13 for the maturity analysis of mortgages payable and Class C LP Units. Amounts drawn under the revolving credit facility are due upon the maturity of the facility, on or before May 1, 2015. Accounts payable are expected to be repaid in the next twelve months. Distributions declared on trust units and Class B LP Units are paid one month following the date of declaration.

c. Market Risk

We are subject to interest rate cash flow risk as our revolving credit facility bears interest at rates that vary in accordance with borrowing rates in Canada. For each 1% change in the rate of interest on our revolving credit facility, the change in annual finance costs is approximately $240 (2012 - n/a) based upon applicable period end debt balances. We are also subject to interest rate risk on refinancing of our fixed rate debts in the year of maturity. We are not subject to other significant market risks pertaining to our financial instruments.

26. FAIR VALUE MEASUREMENT

Fair value is the price that market participants would be willing to pay for an asset or liability in an orderly transaction under current market conditions at the measurement date.

($000s except unit and per unit amounts)

The fair value of the REIT's financial instruments were determined as follows:

- the carrying amounts of cash and cash equivalents, restricted cash, accounts receivables, revolving credit facility, accounts payable and distribution payable approximate their fair values based on the short term maturities of these financial instruments.
- fair values of mortgages payable and Class C LP Units are estimated by discounting the future cash flows associated with the debt at market interest rates (Level 2).
- fair value of Class B LP Units are estimated based on the closing trading price of the REIT's trust units (Level 1).

In addition, the REIT carries its investment properties at fair value, as detailed in note 3e, which is determined by either the direct capitalization approach or by discounting future cash flows at a property specific discount rate (Level 3).

The following table summarizes the REIT's assets and liabilities carried at fair value and its financial assets and liabilities where carrying value does not approximate fair value.

	December 31, 2013			
	Fair Value	Amortized Cost	Total Carrying Value	Total Fair Value
Non-financial assets				
Investment properties	429,117	—	429,117	429,117
Financial liabilities				
Mortgages payable	—	99,023	99,023	105,165
Class B LP Units	99,120	—	99,120	99,120
Class C LP Units	—	94,247	94,247	94,247

	December 31, 2012			
	Fair Value	Amortized Cost	Total Carrying Value	Total Fair Value
Non-financial assets				
Investment properties	382,381	—	382,381	382,381
Financial liabilities				
Mortgages payable	—	180,002	180,002	197,387
Class B LP Units	—	—	—	—
Class C LP Units	—	—	—	—

The table below analyzes assets and liabilities carried at fair value in the consolidated statement of financial position, by the levels in the fair value hierarchy. The fair hierarchy categorizes fair value measurement into three levels based upon the inputs to valuation technique, which are defined as follows:

- Level 1: quote prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: unobservable inputs for the asset or liability.

There were no transfers between the levels of the fair value hierarchy during the year.

	Level 1	Level 2	Level 3	Level 4
Non-financial assets				
Investment properties	—	—	429,117	429,117
Financial liabilities				
Class B LP Units	99,120	—	—	99,120

Investment properties

Investment properties are remeasured to fair value on a recurring basis and categorized as Level 3 in the fair value hierarchy. Investment properties were valued by qualified independent external valuation professionals as at December 31, 2013 and 2012 which resulted in fair value gains of $16,953 (2012 - $30,163) recorded as fair value adjustment on investment properties in income during the year. Fair values are primarily determined by discounting the expected future cash flows over ten years plus a terminal value determined by applying a discount rate to estimated year eleven cash flows, or by applying a capitalization rate to the estimated future net operating income under the direct capitalization approach. The significant unobservable inputs in the Level 3 valuations are as follows:

- Capitalization rate - based on actual location, size and quality of the property and taking into consideration available market data as at the valuation date;
- Stabilized net operating income - revenue less direct operating expenses adjusted for items such as average lease up costs, vacancies, non-recoverable capital expenditures, management fees, straight-line rents and other non-recurring items;
- Discount rate - reflecting current market assessments of the uncertainty in the amount and timing of cash flows;
- Terminal rate - taking into account assumptions regarding vacancy rates and market rents; and
- Cash flows - based on the physical location, type and quality of the property and supported by the terms of existing leases, other contracts or external evidence such as current market rents for similar properties.

An increase in the cash flows or stabilized net operating income results in an increase in fair value of investment property whereas an increase in the capitalization rate, discount rate or terminal capitalization rate decreases the fair value of the investment property.

In determining the fair value of our investment properties judgment is required in assessing the 'highest and best use' as required under IFRS 13, Fair value measurement. We have determined that the current uses of our investment properties are their 'highest and best use'.

The REIT's management company, Melcor, lead by Melcor's executive management team is responsible for determining fair value measurements including verifying all major inputs included in the valuation and reviewing the results with the independent valuator. Melcor's management, along with the REIT's Audit Committee, discuss the valuation process and key inputs on a quarterly basis.

Weighted average stabilized net operating income for investment properties is $1,176 (2012 - $1,161). Other significant valuation metrics and unobservable inputs are set out in the following table. Fair values are most sensitive to changes in capitalization rates.

($000s except unit and per unit amounts)

	December 31, 2013			December 31, 2012		
	Min	Max	Weighted Average	Min	Max	Weighted Average
Capitalization rate	5.50%	9.00%	6.41%	5.50%	9.00%	6.48%
Terminal capitalization rate	5.75%	9.25%	6.69%	5.75%	9.25%	6.72%
Discount rate	6.50%	10.00%	7.57%	6.50%	10.00%	7.59%

An increase in the capitalization rates by 50 basis points would decrease the carrying amount of investment properties by $31,881 (2012 - $28,095). A decrease in the capitalization rates by 50 basis points would increase the carrying amount of investment properties by $37,278 (2012 - $32,793).

Class B LP Units

Class B LP Units are remeasured to fair value on a recurring basis and categorized as Level 1 in the fair value hierarchy. The units are fair valued based on the trading price of the trust units at the period end date. At December 31, 2013 the fair value of the Class B LP Units was $99,120, resulting in a fair value loss of $3,812 in income for the year.

27. SUBSEQUENT EVENTS

On January 10, 2014 we completed the acquisition of an industrial property, LC Industrial, located in Lethbridge, Alberta for $5,934 (excluding closing costs). The purchase has been accounted for as an asset purchase, in accordance with our policy, as detailed in note 3e.

On January 16, 2014 we declared a distribution of $0.05625 per unit for the months of January, February and March 2014. The distributions will be payable as follows:

Month	Record Date	Distribution Date	Distribution Amount
January	January 31, 2014	February 17, 2014	$0.05625 per unit
February	February 28, 2014	March 17, 2014	$0.05625 per unit
March	March 31, 2014	April 15, 2014	$0.05625 per unit

Corporate & Unitholder Information

Annual General Meeting

Please join us at our annual general meeting. We look forward to seeing you there. Note: breakfast will be served prior to the meeting.

April 24, 2014
8:30 am Breakfast
9:00 am Meeting Start (MDT)
Fairmont Hotel Macdonald, Empire Ballroom

Trustees

Andrew Melton – Chairman
Brian Baker
Brian Hunt
Donald Lowry – Lead Director
Larry Pollock
Patrick Kirby
Ralph Young

Officers

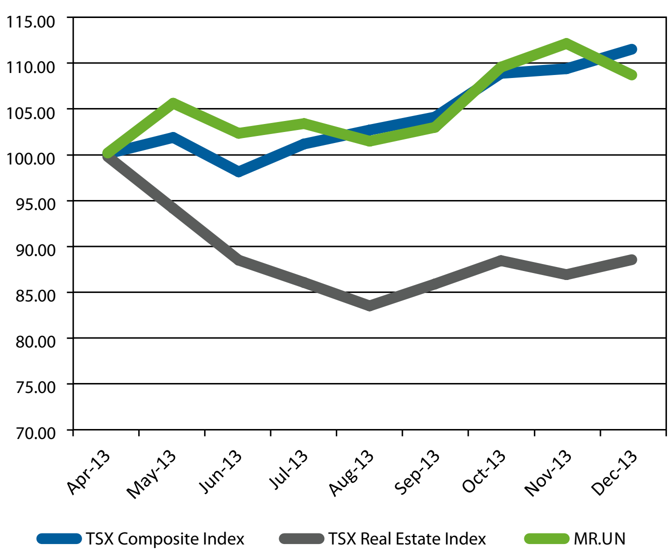
Darin Rayburn, Chief Executive Officer

Jonathan Chia, Chief Financial Officer

Distributions

$0.05625 per month (May – December)
60% of distributions to unitholders were classified as return of capital.

Eight Month Return



Unitholder Services

For unitholder services including distribution information, contact:

Valiant Trust Company
Shareholder Services
Suite 3000, 10303 Jasper Avenue
Edmonton, AB T5J 3X6
P| 1-780-441-2267
F| 1-780-441-2247
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Investor Relations

For all other shareholder inquiries and requests, including institutional investors and research analysts, contact:

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P| 1-855-673-6931
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Customer Service

For tenant service, contact:

P| 1-866-MELCOR1
care.melcor.ca
service@care.melcor.ca

Auditors

PricewaterhouseCoopers LLP

Legal Counsel

Bryan & Company LLP

Stock Exchange Listing

Toronto Stock Exchange: MR.UN

Key Dates

Annual General Meeting: April 24, 2014
Q1 Earnings Announcement: May 2, 2014
Q2 Earnings Announcement: August 5, 2014
Q3 Earnings Announcement: October 31, 2014
Q4 Earnings Announcement: March 2, 2015

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