

Minto Apartment REIT

Third Quarter 2021 Financial Results

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PRESENTATION

Operator

Good morning. My name is Brittany and I'll be your conference operator today. At this time I would like to welcome everyone to the Minto REIT Third Quarter 2021 Results Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. If you would like to ask a question during this time, simply press star then the number one on your telephone keypad. If you would like to withdraw your question, please press star followed by the two.

Before we begin, I want to remind listeners that certain statements about future events made on this conference call are forward-looking in nature. Any such information is subject to risks, uncertainties, and assumptions that could cause actual results to differ materially. Please refer to the cautionary statements on forward-looking information in the REIT's news release and MD&A dated November 9, 2021 for more information.

During the call management will also reference certain non-IFRS financial measures. Although the REIT believes these measures provide useful supplemental information about its financial performance, they are not recognized measures and do not have standardized meanings under IFRS. Please see the REIT's MD&A for additional information regarding non-IFRS financial measures, including reconciliations to the nearest IFRS measures. Thank you.

Mr. Waters, you may begin your conference.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thank you, Brittany, and good morning, everyone. I'm Michael Waters, Chief Executive Officer of Minto Apartment REIT. Julie Morin, our Chief Financial Officer, is also with me on the call. I'll begin the call by discussing highlights from the third quarter as well as recent developments. Julie will review our financial and operating results in detail and then I'll wrap up with our business outlook. After that, we will be pleased to take any of your questions.

The urban rental market conditions continued to gradually improve in the third quarter. This was reflected in our increased occupancy and continued strong leasing activity. There's still a ways to go before the market returns to pre-pandemic normalcy; however, we continued to successfully execute on our strategy during the quarter while positioning the REIT for success in the long term.

We entered into an all-time record 555 new leases during Q3, exceeding the previous high of 534 leases that we set in the second quarter of the year. The 555 leases represent a 38% increase compared to the 403 new leases we signed in the same quarter a year ago. So we're seeing demand for urban rentals improve. We realized a gain to lease of 4.4% on new leases signed. This is slightly lower than the second quarter but still driving significant sustained revenue growth. Average monthly rent in the quarter reached \$1,651 per unfurnished suite.

Average occupancy increased to 92.9% in Q3, up from 91.5% in the second quarter. Our point-in-time occupancy, however, at the end of the quarter was 94.8% and so while average occupancy was lower compared to 94% in Q3 last year, this is the second consecutive quarter in which occupancy has

increased. Move-ins are now outpacing move-outs by a substantial amount, which is highly encouraging. Julie will cover this in more detail shortly.

We've also made progress in other organic initiatives in the quarter. We completed the repositioning of 120 suites, a quarterly record for the REIT. Repositioning improves asset quality, reduces future repair costs, and also drives strong growth in rental revenue. We made progress in our intensification development projects where we're achieving important financing and permitting milestones. Construction at our Richgrove project has begun and we have secured a construction financing commitment from CMHC, while Leslie York Mills is poised to get underway during the fourth quarter as well.

Finally, we recorded a fair value gain of \$34.7 million on our investment properties during the third quarter, based primarily on strong valuations from multi-res rental properties. Recall that we also recorded a fair value gain on investment properties of \$50.5 million in the second quarter of 2021. That's a substantial increase in a six-month period.

Subsequent to the end of the third quarter we agreed to acquire Le Hill-Park, a high-quality 261-suite property in Montreal that's an ideal fit to our portfolio. After the closing of the transaction next month we'll have four properties and almost 1,800 suites in Montreal, which is a highly attractive rental market. We had no properties in that geography at the time of our IPO in 2018.

On October 29th we completed an \$87 million bought deal equity offering including the full exercise of the overallotment. The deal was fully subscribed, reflecting strong demand from the

investment community. The proceeds will be used to fund acquisition development opportunities, including Le Hill-Park, while increasing our financial flexibility.

Finally, I'll conclude with the best news of all for our unitholders. As you probably saw yesterday, our board has approved the 4.4% increase to the REIT's monthly cash distributions beginning with the November distribution which is payable in December. The increase reflects the board's high level of confidence in our business outlook, including our ability to execute on our strategy. The REIT has now increased distribution to each of the three years since it went public and two of those were during the pandemic. I'd also note that while we're committed to raising distributions over the long term, we also plan to maintain a strong balance sheet and conservative payout ratio that allows us to continue to reinvest capital to fund future growth.

To sum up, we're pleased with the positive momentum we're seeing in our business and the fact that we continue to capitalize on attractive growth opportunities. We expect the REIT's financial performance to continue to improve as the pandemic dissipates and urban market conditions gradually return to normal.

I'll now ask Julie to discuss our third quarter financial and operating performance in a little bit more detail. Julie?

Julie Morin — Chief Financial Officer, Minto Apartment REIT

Thank you, Michael.

Let's start on slide four where I'll begin by reviewing our Q3 operating results. We reported revenue excluding furnished suites of \$29 million in Q3 2021 compared to \$29.3 million last year, a slight decline of 1.2%. The decrease was mainly due to lower occupancy and promotions, partially offset by higher rent. The majority of the decline continues to be focused on several core properties in urban centres where the negative impact of COVID-19 has been most pronounced. Total revenue including furnished suites was \$31.2 million, an increase of 0.3% compared to Q3 last year, reflecting higher occupancy and rental rates for furnished suites.

NOI excluding furnished suites in the third quarter was \$18.1 million or 62.4% of revenue, a decline of 6% compared to \$19.2 million or 65.6% of revenue last year. Total NOI including furnished suites was \$19.4 million or 62.1% of revenue, a decline of 3.7% compared to \$20.2 million or 64.7% of revenue in Q3 last year. Lower NOI in Q3 2021 reflected the lower revenue from unfurnished suites as well as increased property operating costs, property taxes, and utilities expense.

FFO was \$12.5 million in Q3 2021 compared to \$13.2 million last year, a decline of 5.5%. This mainly reflected the negative NOI variance. AFFO declined 6.3% year over year to \$10.9 million from \$11.6 million in Q3 2020, mainly due to lower FFO. AFFO per unit was approximately \$0.184 compared to \$0.197 last year. The REIT declared cash distribution in the third quarter of \$0.1138 per unit, resulting in an AFFO payout ratio of 61.7%. Cash distributions were \$0.1125 per unit in Q3 last year, resulting in an AFFO payout ratio of 57.2%

As at September 30, 2021 our portfolio consisted of 7,277 suites with an average monthly rent of \$1,651 per occupied unfurnished suite. Average monthly rent increased by \$38 or 2.4% compared to

\$1,613 at the end of Q3 last year. The average occupancy rate in Q3 was 92.9% compared to 94% last year.

Turning to slide five, as Michael noted in his introduction, our quarterly move-ins have now outpaced move-outs for two consecutive quarters. This is a very positive trend that is driving growth in occupancy and highlights the steady recovery of urban rental markets in Canada. We had 615 move-ins during Q3 2021 versus 517 move-outs, a positive differential of 98. That compares to 36 net move-ins during the second quarter of 2021 and 65 net move-outs during the first quarter of the year. Occupancy has steadily increased from 91.1% in the first quarter to 91.5% in the second and 92.9% in the third quarter.

On slide six we've provided our revenue analysis as of the end of September. We break down gain to lease activity for Q3 2021 in the upper chart and our estimate of the gain to lease potential of the portfolio in the lower one. Beginning with the upper chart, as Michael noted, we signed 555 new leases in the quarter following suite turnover. Leasing activity was strong and we were pleased to generate positive gain (inaudible) in all of our markets. The average rent on new leases increased by 4.4% from \$1,630 to \$1,701. This resulted in an annualized incremental revenue gain of approximately \$392,000. The strongest performance came in Montreal where we generated a gain on new leases of 8.2%.

Turning to the gain to lease potential on the lower chart, we believe we can generate approximately \$7.3 million of annualized incremental revenue growth by bringing rents in 6,664 suites to market levels. We expect to realize a significant portion of this potential over the next three to five years. We should also note that this chart does not include the Le Hill-Park property in Montreal in

which average sitting rents are well below market rents. We expect to complete the acquisition of Le Hill-Park next month.

Turning to slide seven, the upper chart tracks our gain to lease and average monthly rent growth on a quarterly basis. Gain to lease has been negatively impacted by the pandemic but, as you can see, has remained highly positive throughout this challenging period. Average monthly rent continues to hit new highs every quarter despite the impact of COVID-19 on urban rental markets.

Moving to slide eight, I want to provide you with an update on furnished suites. The lower chart shows that we are generating significantly stronger performance from our furnished suites than we have at any point in more than a year. Average monthly rent for furnished suites were nearly \$4,000 at the end of the third quarter and average occupancy for the quarter was 86.3%. These figures represent a dramatic improvement from the levels we saw in early 2021. We expect a recovery and demand for the furnished suites in the coming quarters as restrictions are lifted and economic growth continues to improve.

On slide nine you'll find a summary of our repositioning activities. We renovated a record total of 120 suites in the third quarter or 91 of the REIT's proportionate ownership share. The average cost per renovation was approximately \$48,400 per suite. The average annual rental increase following repositioning was \$4,298 per suite, which generated a healthy return on investment of 8.9%. In total, we have approximately 3,000 remaining suites to reposition in our portfolio, again not including the potential repositioning opportunity at Le Hill-Park. We expect to reposition another 100 to 110 suites in

the fourth quarter for a total of approximately 350 suites for the year. This is above our prior guidance of approximately 250 to 300 repositioned suites in 2021.

On slide 10 we highlight the strong predictable returns on invested capital that we generate from repositioning. Over the last four quarters our average annual unlevered return has remained in a narrow window between 8.4% and 9% per quarter with an overall average return of 8.7% on 310 renovated suites. The average renovation cost per suite was approximately \$48,100 and the average annual rental increase per suite was \$4,185.

We've mentioned Le Hill-Park a few times already on this call, so let's take a closer look at it on slide 11. We're paying \$80.1 million for the property, which comprises 20 stories and 261 suites. Part of the reason it is so appealing is that it provides significant organic growth potential, both from gain to lease and repositioning. We estimate that sitting rents are approximately 20% below current market rent and only 72 of the 261 suites have undergone a repositioning program, which provides additional potential upside in rents of approximately 20% to 25% upon completion of renovation. We expect the acquisition to close on or around December 7th. The purchase price will be satisfied in part by proceeds from the bought deal we completed last month and a new mortgage loan of approximately \$41 million. This is our fourth acquisition in Montreal and brings total our suite count in the city to 1,793 suites or roughly a quarter of our total suites.

The map on slide 12 shows the location of Le Hill-Park. It's located in close proximity to our three other properties in Montreal, Rockhill, Le 4300, and Haddon Hall. This creates a potential for operating synergies. The property is also located close to the Côte-des-Neiges metro station and the planned new

station at Édouard-Montpetit, which is part of the Réseau express métropolitain, or REM, a massive expansion that the city's existing metro network. In addition, Le Hill-Park is near the University of Montreal, McGill University, three major hospitals, Summit Woods, and Mount Royal Park.

Now I'd like to review our intensification and development initiatives on slide 13. We currently have investments in six projects in various stages of development. Each of these is advancing at a steady rate. I'll provide highlights on a few properties over the next few slides and you can find more detail about the current status of each project in our Q3 MD&A.

One important recent development is that we have obtained a construction financing commitment from CHMC for the Richgrove project under their rental construction financing initiative that will provide construction financing on attractive terms and construction has commenced. Construction at Leslie York Mills is also expected to begin later this quarter. Combined, these six projects could expand the REIT's portfolio by 1,570 suites by 2029. That represents an increase of approximately 21% from the current level inclusive of Le Hill-Park.

I'll now provide updates on a few of the individual development projects, beginning with the Fifth + Bank redevelopment in Ottawa on slide 14. You can see from the photo on the upper right that construction is very near completion. Seventy-eight out of the 162 suites have been leased already with first occupancies beginning this month. The project is on schedule to be stabilized in mid-2022, at which point the REIT will have an exclusive option to purchase it at a 5% discount to its then appraised fair market value.

Turning to Lonsdale Square in North Vancouver on slide 15, our first development project in Greater Vancouver is making good progress. Site excavation is complete, as you can see on the upper right photo, and the formwork has commenced. The project is comprised of 113 suites and approximately 7,800 square feet of retail space. Construction completion is expected in the first quarter of 2023 with stabilization of the fourth quarter of that year. We'll have a purchase option at that point with the same terms as Fifth + Bank. These (inaudible) really highlight the benefits of the REIT's unique relationship with the Minto Group.

Moving onto the Richgrove project on slide 16, we are taking advantage of excess land on this site to add a new rental tower with 225 suites, including 100 affordable housing suites, and 213 parking stalls. Construction is underway and stabilization is expected in early 2026. One additional benefit to this property is that it is adjacent to the future site of the Martingrove LRT Station, which should be completed around 2030 or 2031.

Finally, I'd like to review our debt financing and liquidity on slide 17. An essential part of our strategy is maintaining a conservative leverage ratio and balance in our debt maturity schedule. The chart demonstrates that maturities between 2022 and 2026 are highly manageable. As of September 30, 2021, the weighted average term to maturity on our fixed rate debt was 5.17 years with a weighted average interest rate of 2.9%. Approximately 91% of our debt is fixed rate and 73% is CMHC insured debt. Our total liquidity was approximately \$126 million at quarter end and debt to gross book value was 37.9%.

I'll now turn it back over to Michael.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Julie.

I'll wrap up with our business outlook on slide 18 before we take your questions.

When the pandemic struck in March of 2020, of course the impact on urban multi residential real estate in Canada was significant. With the border shut, shops and restaurants closed, immigration delayed, and post secondary institutions operating largely remotely, the benefits of urban living were temporarily disrupted. But that's changing rapidly. Pandemic restrictions are being eased on a regular basis as COVID-19 vaccination increases and case counts continue to improve. Borders are reopening, including the land border with the US. Restaurants and sports venues are welcoming customers without capacity limits. Post secondary education has returned largely to in person learning. Immigration is rapidly picking up again with the federal government increasing its targets for new permanent residents over the next three years to catch up on the immigration that was delayed by border closures. Although we must remain vigilant, COVID case counts have not been nearly as high this fall as some had feared.

These are all really, highly positive developments for the REIT. We're seeing market demand and occupancy increase as the benefits of urban living gradually reassert themselves. It'll take some time to get back to normal but we're confident that our focus on high-quality multi-res housing in desirable areas will outperform in the long term, as it has done historically. The increase to our distribution that we just announced sort of underscored this confidence. Our positive outlook is supported by strong fundamentals in Canada, including expansive immigration policy, inelastic supply, and the growing affordability gap between owning and renting a home. As population growth continues to increase in

2021 and beyond, rental housing demand is expected to strengthen. We expect to see further increases in occupancy and stronger growth in rent rates, driving improved financial performance; however, we still do anticipate lower than normal occupancy for the remainder of this year.

To sum up, we continue to believe that Minto Apartment REIT has the right assets and strategy for long-term success. We'll continue to focus on four key areas to grow the REIT; namely, capitalizing on organic growth through gain to lease, creating value from suite repositioning, exploring attractive acquisitions, and capitalizing on our relationship with the Minto Group. These have been the key elements of our strategy since the day the REIT was created and we're confident by sticking to these principles we'll generate strong returns for unitholders as the impact of the pandemic subsides.

That concludes the formal portion of our presentation this morning. Julie and I would now be pleased to answer any questions you might have. Brittany, please open the line for questions.

Q & A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press the star followed by the one on your touchtone phone. You will hear a three-tone prompt acknowledging your request and your questions will be polled in the order that they are received. Should you wish to decline from the polling process, please press the star followed by the two. If you are using a speakerphone, please lift the handset before pressing any keys. One moment for your first question.

Your first question is coming from Jonathan Kelcher from TD. Please go ahead.

Jonathan Kelcher — Analyst, TD Securities

Thanks. Good morning.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Hey, Jonathan.

Jonathan Kelcher — Analyst, TD Securities

First question just on the leasing. If you just look at where September ended versus the average, it's obvious September was a very strong quarter on the leasing front for you guys. Has that continued into October?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah, October saw a few more than 200 leases, so it was continued strength, basically continued where we are in September. And that was true in almost all of our markets. Toronto has been perhaps the slowest to really recover, but we signed more than 90 leases in October in Toronto, which has been fantastic. It continues to still be the largest consumer of incentives, I'll say, if we look at our different markets, Jonathan, but when I look at Ottawa as well, that market has been steady and strong for awhile. We're seeing that housing price growth, both new home and resale, has really pushed main buyers into rental, and so we've done more than 60 leases in Ottawa in October and we're seeing promotion there being really peeled off quite rapidly.

Montreal has been resilient. It's been supported by a pretty strong job market there. We've signed 22 leases in October. We would have done more, but we had many suites offline for the repositioning programs, particularly at Haddon Hall and Le 4300.

Alberta, I would say Edmonton remains a soft market, but Calgary has been surprisingly strong actually. We have very little availability in our Calgary portfolio and we see continued strength there just economically with job growth in Alberta. I think what we saw was really strong momentum through the quarter and that continued through October. Just (inaudible) out of caution that seemingly, of course, we see leasing demand tend to taper towards the end of Q4 and the first part of Q1.

Jonathan Kelcher — Analyst, TD Securities

Okay. Fair enough. That's helpful. And then just, I guess, switching gears a little bit, as you're in the ground at Richgrove, expect to be at Leslie York Mills this quarter, what are the yields you're targeting on development there and how much of your cost would be fixed?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Typically we're targeting return on investment of somewhere between 4% and 4.5%. And if you compare that to kind of margin cap rates for new multi-res in the city, they would be sort of 3% to 3.5%, so a fairly significant margin of kind of 100 plus or minus basis points, which translates to, and we tend to think of it in terms of levered IRRs, but levered IRRs that would be in the high teens, so pretty decent, and in some cases higher.

Jonathan Kelcher — Analyst, TD Securities

Okay. And do you have a lot of the costs fixed on that or...?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah. We, of course, before we put a shovel in the ground we would tender the vast, vast majority of the bill of materials. So our internal rule is we want to tender more than 70% to 75%. I think at Richgrove we're approaching almost 90% of cost tendered and on those, the tenders that we've done and started to award contracts, we are at our favourable to our pro forma, so tracking quite well on that one. Leslie York Mills is not quite as far advanced, but the tendering process is moving along nicely there as well.

Jonathan Kelcher — Analyst, TD Securities

Okay. And then I guess just last question. In the past, when you've done sort of infill things like you're doing with Richgrove, has the construction, I guess, process, does that impact the performance of the existing asset at all?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Well, in the short term of course there's some noise and dust and disruption for existing tenants, particularly on access in and out of the site, and so it does have a very short-term impact. We have a fairly detailed construction management plan that we put forward for each of those communities. It's multi-pronged. It would include communication with our residents and our resident engagement

strategy and really try and give tenants a lot of visibility on what we're doing, including communicating the benefits, like what's in it for those existing tenants in terms of improvements to amenities, improvements to (inaudible). If you think of Leslie York Mills, for example, we're completely redoing the entire suite of amenities, generating very significant improvement to that. So from a selling proposition, often we're able to lessen the sting, if you will, of the construction inconvenience. Obviously, long term, the impact of having these new suites refreshed or brand-new amenities, expanded amenities, and the landscape, it rises the potential of the entire property. So there is a near-term impact. I think we work as hard as we can to manage and mitigate that, but it's something that you're right to note that we work very hard on that.

Jonathan Kelcher — Analyst, TD Securities

Okay. That's helpful. I'll turn it back. Thanks.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Jonathan.

Operator

Your next question comes from Mike Markidis from Desjardins. Please go ahead.

Mike Markidis — Analyst, Desjardins Capital Markets

Hi there. Just (inaudible) the chart, I know it's small, but the furnished suite segment, and you've kind of got it going back, I guess, four quarters, but what would be helpful maybe is just thinking about

how that looked pre-pandemic and how much runway you think we have to go, both from an occupancy average perspective and maybe potentially AMR, not suggesting it gets there in the next two quarters but just in terms of thinking about the normalization going forward.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

So you think about furnished suites going back pre-COVID, so if we went back to sort of late 2019, let's say, if you were to look at the fall of that year, October, November, December, then of course our suite count was higher. We were sort of in the almost 250 range or a little bit over. And we were seeing average daily rates that were in the \$140 range and occupancy that quarter started the quarter very strong. In October we were in the low 90s, which was absurdly high. We don't typically see that level of occupancy. So, producing RevPARs that were like \$136, which is really, really high. The balance of that quarter we saw occupancy drop, which is more typical. We were dropping into the low 80s in November and sort of getting into the high 60s by December.

And so I think that illustrates a couple things. I mean, one, the furnished suite segment is highly seasonal, depending on the property. You'll see seasonal trends, for example, in Toronto often tied to the movie business and other things. And secondly, it is obviously a little bit more volatile than the unfurnished. You typically are generating much, much higher rate, but at the expense of a little bit more vacancy and some more volatility there. Again, not ever intended to be a huge part of our business. Right now, we're kind of low 200s suite count, probably getting into the high 180s at least at this stage as we complete the renovation repositioning program at Roehampton where we had 48 furnished suites at the beginning of the renovation program. But it is a fantastic yield management tool, particularly in

steady or rising markets, because they are very short tenancies, which allows us to reset to market rent, and from that perspective is a fantastic yield management tool.

Again, right now we really have furnished suites at only a handful of properties. 185 Lyon in Ottawa, our Yorkville property in Toronto, Roehampton still has surprisingly strong, you know, 20 suites there, they're 79% to 80% occupied at this stage, and so we're waiting for those contracts to burn off, obviously, and then we've got just a handful at (Inaudible), our property in Calgary. I think what you'd expect to see is that we've maintained a meaningful inventory at 185 and Yorkville, but that Roehampton inventory will disappear in The Laurier as well. It's possible that we could bring more suite count back online at some point in the future if market conditions merited, but at this stage right now we're sort of focused on the plan we communicated way back for the Q4 reporting back in March.

Mike Markidis — Analyst, Desjardins Capital Markets

Okay. Thank you. And then just last question. In terms of the, obviously more leasing done, but in terms of the amount and intensity of incentives maybe offered on a first-week basis, would it be fair to say that that declined through 3Q and is declining in 4Q? That would be the first part. And secondly, I think you mentioned Toronto coming back slower than expected on that front, so maybe just a little bit more colour on how that's unfolding on the incentive side in the Toronto market in particular.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

So, as we talked about in our Q2 reporting back in August, we really saw the market bottom in April and it just has strengthened sort of month over month sequentially since then. And our use of

promotions certainly peaked in Q2, early part of Q2 or very late part Q1, and have really dropped very, very significantly subsequent to that. And, as I mentioned in my response to Jonathan's question earlier, if you think about promotions defined as a number of months' rent per lease signed, we have brought that number way down. The area where we're seeing it still the highest has been Toronto, which has been the slowest to recover, though it is recovering strongly. So it's been the area, the last one where we've been peeling them off, you know, we've pulled them off in Ottawa and Montreal much sooner. Now, I think with the strength that we're seeing, I mean 94 leases signed in October in Toronto I think is a pretty strong sign. So we think that the amortization impact of promotions will have peaked in Q3. So the P&L impact, of course, lags, right? The granting of the promotions probably peaked back in March. The amortization impact in the P&L will have peaked in Q3 and we'll start to see a tail off. It will still be meaningful as we get into Q1 and Q2, but by Q3 next year we anticipate that that promotion expense, which is really amortization of promotions granted the prior year, will largely have tailed off.

Mike Markidis — Analyst, Desjardins Capital Markets

Okay. So in Q4 the amortization effect will have decreased though, this year, just to be clear, right?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

It will come down. It will definitely come down.

Mike Markidis — Analyst, Desjardins Capital Markets

It will come down in Q4 this year.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Oh, yeah. Yeah.

Mike Markidis — Analyst, Desjardins Capital Markets

Okay. No, that's great. And then obviously next year, yeah, by late 2022 I hope we're not discussing incentives anymore. Appreciate that. Thanks very much. I'll turn it back.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Mike.

Operator

Your next question comes from Matt Logan from RBC. Please go ahead.

Matt Logan — Analyst, RBC Capital Markets

Thank you and good morning. Michael, if we roll up some of your commentary on the positive post quarter leasing demands, where do you think occupancy can trend over the next two or three quarters?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Well, we finished the quarter September 30, that number was 94.8%. You look at the continued, well, we had very strong leasing, as we talked about in Q3. Leasing is a leading indicator of move-ins. Not

all of those leases would have moved in in the quarter. We were plus 98 net move-ins in Q3. We expect that that momentum of move-ins to continue into Q4. So we're looking to see occupancy in Q4 would be likely in the 95-ish range. And you might anticipate that the ending occupancy, so that's the average 95-ish, by the end of the year would be probably a little bit higher. Now of course we get into that slower Q4, particularly the latter part of Q4, Q1 is typically a slower leasing demand quarter, but we anticipate that, going into Q2 and Q3 next year, that we'd be in the 96, 97 plus kind of range, which is sort of what we would consider to be more full occupancy, you know, pursuant to our kind of yield management philosophy there.

Matt Logan — Analyst, RBC Capital Markets

And in terms of the realized gains on the leases that you're signing, at least the new leases, would it be fair to think about that 4% print in Q3 as a function of perhaps low single digit spreads in the early part of the quarter, three or four months ago, you know, strengthening perhaps somewhere into the mid single digit range today?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Definitely. Yeah. Because we mark this on a lease-by-lease basis and just when you look at the volume of leasing, which was fairly balanced through the quarter, but certainly the trend in terms of what we were achieving continued month over month sequentially during the quarter July through September. So I would expect that the gain to lease would be, I think, more representative of the future. I think we'll see, you know, our estimate at the end of the quarter was 6.6 of potential, I think that that

number will continue to climb if we look out into 2022, hopefully getting back to the range we were pre-COVID, seeing double digits on some of those.

Matt Logan — Analyst, RBC Capital Markets

That's good colour. And maybe just following up on some of Mike Markidis' questions on the furnished suite business, what would be a fair kind of annual target for occupancy and the monthly rent for that business?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

That is a good question. Give me a second. I'll come back to that a little later in the call, if that's okay. I just, I need to...

Matt Logan — Analyst, RBC Capital Markets

No rush if you don't have that handy. Just wanted to think, you know, could we see some of that pricing moderate seasonally, similarly with occupancy, but not a big part of the business overall.

Maybe just one other housekeeping question from me. I didn't see it in the press release, but are you able to provide a cap rate for Le Hill-Park?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

It would be roughly 3%. We underwrite not on a cap rate basis. We look at a couple metrics. Levered IRR, which would be right around 7% over a 10-year basis. What we see there is, I mean if you

were to look out two and three years, the cap rate would be rising into the mid 3s, like 3.4, 3.6. And a lot of that is, you know, our going in is always a little bit lower with our renovation program and this one has a very substantial renovation program. Like it really had about 70 suites renovated, leaving something like 190 suites. And it's a fantastic program. I think we build off what the vendor did there, our sense of what they've done, their execution was quite strong, and so we look at that and think, you know, that we could do quite well. The only gating factor for us there is the pace of turnover because, of course, you can only renovate an un-renovated suite as it turns. So we're hoping over the next five years to get well into more than 120 of those suites renovated. But that will drive, to some extent, the return from the investment. But as I say, even on an un-renovated market basis, we're seeing very significant gap to market, like more than 20%.

Just back to your furnished suite question, if we were to think about the year ahead, 2022, typically we would look for something like an occupancy that would be kind of 80%-ish, 81%, like low 80%, and then that average daily rate for the two big properties, 185 Lyon, would be something like 120, and Yorkville would be substantially higher, something like 170, so an average of about 140 between the two of them. I'm doing this rough math here but that's kind of what that would look like.

Matt Logan — Analyst, RBC Capital Markets

That's great. And maybe just one last question for me before I turn it back. If we kind of take a bit of a 30,000-foot view of the next 12 months, what do you see as the REIT's biggest opportunity to capitalize on?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

We see opportunity on development for sure. I think that obviously starting LYM and Richgrove are big steps. We've been talking about those projects since the time of the IPO. I think as well some of the opportunity through the convertible development loan program that we've been doing, if you think about Lonsdale or Fifth + Bank or Beechwood. I think Fifth + Bank, when it stabilizes sometime in probably Q2, will be the first of those projects to roll off the assembly line. And I think that they really demonstrate the value of the Minto pipeline, and not only the pipeline of deals but also the strategic relationship with Minto Group in terms of development and construction expertise. And that, I think, will be a fantastic project. 163 suites and, as we said earlier, it's almost 50% pre-leased. We haven't even started to occupy the building yet. So I think that one will be fantastic. It's obviously not subject to Ontario's rent control provisions and I think there are more opportunities like that.

I think as well, you know, broadly speaking, the Minto pipeline is something that we think also has substantial potential for the REIT, as we saw in the past with Leslie York Mills and High Park were acquisitions of Minto Properties Inc. investments in stabilized assets. And the Minto portfolio outside the REIT has some attractive candidates, I think, that would fit very nicely into the REIT portfolio. So we're going to continue to work those deals and see if there's an opportunity to bring those forward.

And then of course, as we talked about earlier, the repositioning program that we've done has been so strong. I mean this has been our strongest quarter in terms of just sheer number of repositionings, 120 suites in the quarter, bringing us to 254 year to date, and if we do add another 90 to 110 in Q4, jeez, we'd be almost 350 and the guidance we gave everybody was 250 to 300. Generating

very strong ROI's, north of 8%, very dumb, simple ROI like that, it's a pretty nice program. So, with the addition of Le Hill-Park and some of the other deals that we're looking at in the portfolio, completing the feasibility, I think if we can add to the potential on the repositioning side, that's certainly an area of focus. It's our best use of capital on a risk-adjusted basis. The only limiting factor is we can only do so much of it and it's really gated by the turnover of un-renovated suites.

Matt Logan — Analyst, RBC Capital Markets

Thanks for the colour, Michael. I appreciate it. I'll turn the call back.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Matt.

Operator

Your next question comes from Joanne Chen from BMO. Please go ahead.

Joanne Chen — Analyst, BMO Capital Markets

Hi. Good morning.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Hey, Joanne.

Joanne Chen — Analyst, BMO Capital Markets

Sorry if I missed this earlier, but just on the furnished suites, it's nice to see the turnaround this quarter for sure, but what are you guys thinking with respect to the overall percentage of furnished suites in your portfolio going forward? Or it continues to be quite flexible on your end?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Well, at the time of the IPO that number would have been about 6% of the portfolio. Today the furnished suite count is something like less than 3%. So we've brought it down as a proportion of the total portfolio but also in absolute terms quite substantially. And as I've said in the past, Joanne, the beauty of furnished suites is they're short tenancies, so you can reset to market. It is very easy for us to bring unfurnished suites on line as furnished and to go the other way. We can take them off line very, very quickly. It's really purely about demand and what are the demand lead indicators that we're seeing, advanced bookings and things of that nature.

So we don't want to make furnished suites a big part of our business. We see it as a yield management tool. When the unfurnished rental market is stable or growing, it is a fantastic tool for us and so we'll continue to use it opportunistically, but not meant to be a big part of the portfolio. And so if you think about where we're at now, just a little bit less than 3%, you know, it could grow a little bit in terms of suite count, but probably not materially as a percentage of the portfolio. And it's really only effective at a handful of properties. You can't do furnished suites in every property. And so that's the other limiting factor.

Joanne Chen — Analyst, BMO Capital Markets

Right. That makes sense. That's helpful. And I guess just on your repositioning efforts, has the current inflation rate environment impacted your thinking kind of on the pace and the magnitude or has that not made a substantial difference thus far?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Are you talking about inflation on construction costs?

Joanne Chen — Analyst, BMO Capital Markets

Yes. And labour and I guess everything these days.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah. Well, speaking about the repositioning program, it's typically a different trade base. Not entirely, but it is a bit of a different trade base from new construction. But some of it is certainly caught up in some of the same supply chain disruption. Like if you think of cabinets, for example, those are issues. But we are able to leverage the relationship with Minto Group in the strong buying power that we get through that because of the substantial number of new home and development stuff that we're doing outside the REIT. So we're not shy about leveraging those relationships to sort of get some volume pricing incentives and things.

I would say generically about inflation more broadly, obviously we saw in the quarter, you know, insurance, property taxes, certainly salaries is an area where we're seeing some price pressure for sure.

We'd struggled to fill some of the vacancies, we saw higher turnover, and some of that was coming out in higher salary expense. So inflation's certainly something that we're seeing in the business and something, you know, we're conservatively sort of working that into our planning. Hopefully the net result will be better than what we're sort of providing for, but it's something that we're definitely mindful of.

On the new construction side, as I said earlier in the call, our safeguard there is that we would tend to tender the vast, vast majority of our cost categories before we put a shovel in the ground and so we're locking in pricing for that. And so that's, I think, from that perspective. But we've seen that typically that inflation does pass through rents. If you were to look at Ontario's rent control regime and you go back to 1975 and you look at the guideline increases that were promulgated each year, they tend to track inflation pretty closely, so certainly that would be our expectation going forward.

Joanne Chen — Analyst, BMO Capital Markets

That's good to hear. And I guess just one more. How should we be thinking kind of the acquisition pipeline kind of for the remainder of the year and into early 2022? You know, obviously the environment is very competitive right now. Are you still seeing kind of a healthy pipeline on your end?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah. We are very active, Joanne, always looking at deals. We're pretty choosy about what we pursue. We are looking for investments. If we're buying stabilized assets, we're looking for properties that, one, hit the location tests that we set, but number two, we're looking for assets where there's

significant embedded rent and where there's repositioning potential and/or intensification potential. And those are, as you've said, are pretty hotly contested right now. And it's not just the usual suspects, our peers in the publicly-traded REIT space, but also pension fund and institutional investors and then private investors are bidding aggressively.

So I think we're spending as much or more time on development. I think that's one of our differentiators. Because of our strategic relationship with Minto Group, we're able to underwrite and pursue development deals. And some of them, many of them, we've been doing through the convertible development loan structure, such as Fifth + Bank, which, I think from our perspective, yields huge advantages to the unitholders, because the unitholders see an accretive return to AFFO through the development period from the coupon on the instrument and then with the discount on the stabilized future value often we're seeing those unlevered returns on those investments sort of in the mid teens. So they're fantastic. And buying a stabilized new asset at a 5% discount to fair value is a huge advantage there. They're obviously NAV accretive almost right away. So we like that. And we'll just continue to maintain our discipline on the acquisition front. And we're not growing for growth's sake, so it's not chasing every deal. And they come in bunches. We went nine months or twelve months really without anything and we did the Beechwood deal and that was pretty much it and then suddenly we've seen a flurry of opportunity. It's just kind of the way it works sometimes.

Joanne Chen — Analyst, BMO Capital Markets

For sure. Okay, no, that's very helpful. That's it from me. I will turn it back. Thanks.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Joanne.

Operator

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

Your next question comes from Brad Sturges from Raymond James. Please go ahead.

Brad Sturges — Analyst, Raymond James

Hi there. Good colour on the trends you're seeing from leasing activity and move-ins. Just curious if, you know, last year turnover move-outs was elevated, if you're seeing maybe a little bit more normalization of move-outs heading into the end of this year.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

So move-outs, thinking about, like 2020 was kind of bonkers in terms of total, totally turned upside-down kind of the normal seasonal patterns. If you recall, we saw massive move-outs in Q4, which was unseasonable, and Q1 had a very high number of move-outs, which is sort of unusual. I think what we're looking for is to see move-outs return to kind of normal patterns looking ahead to Q4. We have fantastic visibility because of the way the notices work that we're seeing Q4 look sort of more like normal kind of fourth quarters in terms of the number of move-outs.

If you think of turnover, which we define as new leases divided by total suites, I mean actually Q3 had, because we had such strong leasing, we had a huge turnover number, you know, approaching kind of 30% overall. You can see that through the tables that we put in the teleconference deck. On a trailing 12 months or four quarters that would be, like I say, 30%, which is pretty high, which is fantastic if you're seeing a growth in market rates, because you're able to realize on some of that imbedded rent there. So, what we'd seen in the lead up to COVID with turnover was dropping down substantially and so what we saw now, at least the most recent couple, three quarters, is strong leasing activity generating higher turnover.

Brad Sturges — Analyst, Raymond James

Right. And I guess it depends on what type of unit turns, but it seems like the renovation program's been seeing, I guess, higher levels of suites repositioned than I think what you were forecasting. I guess do you see that as repeatable in 2022 or will it be the expectation, I guess, for the amount of suites you might be able to get to next year?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah, so, I mean we used the crisis, I would say, starting in Q4, but really picking up steam in Q1 of this year to, you know, weaker, softer demand for unfurnished suites meant that, rather than furiously discounting those suites just to fill them, we took them off line and renovated them. And then we built up a substantial inventory of renovated suites. And as we got into Q2 and Q3 with the strong leasing season, that really reflects the numbers that you saw, the 120 in the quarter, 254 year to date,

which is substantially higher than the guidance we'd given, 250 to 300, earlier in the year. We were maybe a little bit conservative on that.

I think looking ahead into 2022, the gating factor, as we always talk about, is the turn of un-renovated suites. And so of course, unless you're adding new buildings to the program, there'd be a natural tailing off of the program, but adding Le Hill-Park to the program, completing the feasibility on a couple of other buildings as well, means that we can, hopefully, keep the program going.

Now I don't know if we're going to get to 350 again next year. That's probably wishful thinking. Probably looking at something more like 250, which is kind of where we started 2021. But we're always exploring opportunities, always looking for the potential to deploy some value-add capital, and sometimes, as we've seen in the past with Parkwood Hills, the enhanced turn program was very small amounts of capital but we were generating very nice ROIs kind of in that, you know, well in excess of our target. And some of those were kind of \$10,000 a suite or less even and generating 8% ROI. So we're always pretty opportunistic if we see these opportunities and we'll keep doing that. Our asset management team is always on the hunt for ideas like that.

Brad Sturges — Analyst, Raymond James

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

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Brad.

Operator

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

Matt Kornack — Analyst, National Bank Financial

Hi, all. Just a quick one on operating costs this quarter. Was there anything specific to this quarter or maybe to the prior year quarter in terms of the growth there?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

I would say when you drive a huge volume of leases it does tend to be associated with higher marketing costs and higher repairs and maintenance, so lots and lots of turns in the quarter, as I mentioned. If you look at the new leases, on a quarterly basis it was 8%, so it was a pretty strong number. If you annualize that over the last four quarters, that's kind of (inaudible). So that's certainly, that amount of new leases, new move-ins, certainly have an impact on that.

The other ones we talked about in prior quarters, insurance, certainly we're seeing insurance really moving. We don't have a lot of control over insurance. The other, I'll say, uncontrollable categories are property taxes. You know, we'd highlighted in the past Calgary certainly but Montreal as well where we're seeing property taxes moving. Utilities in certain cases for sure impacting us. Not all utilities, because a lot of our suites are sub-metered, but that's an area that we're keeping an eye on. We're watching gas prices and other things pretty closely. And I would say the last one, which we touched on earlier, Matt, was staffing, particularly our frontline staff. More modestly paid, strong job market in many cases, and we did have a lot of vacancies going into the quarter. We were, I think, quite

successful in getting a lot of fantastic new members on the team and so that partly is playing out as well in the OpEx numbers is that we did have a little bit salary expense there too. So I don't know if that colour helps.

Matt Kornack — Analyst, National Bank Financial

That's very helpful. So I guess in terms of trajectory going forward, it sounds like Q4 you're still going to see some elevated leasing activity, Q1 maybe slows down a bit, although who knows these days, and then into the balance of the year, I guess, some of the additional sort of marketing and other costs may fall away. Is that fair?

Michael Waters — Chief Executive Officer, Minto Apartment REIT

They will. Though I, again, continue to highlight some of those non-controllable categories that we can't manage. What I think we're looking at for 2022 is that revenues will outstrip the cost growth on the OpEx side, but it's certainly something we're very conscious of.

Matt Kornack — Analyst, National Bank Financial

Okay. That makes sense. And then last one for me. Can you just give a little bit of colour around, obviously we've seen a substantial uptick in occupancy, but sort of what's happening with High Park Village, Roehampton, and maybe Yorkville in the context of what's going on around those assets as well? Are you sort of in line with the market or trailing or ahead? Any colour you can give there would be helpful.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Yeah, a good question. Certainly in the quarter what we had seen was that we had good performance. High Park, we signed something like 64 leases. Roehampton, 31 leases. So Roehampton had significant vacancy owing for the renovation program there. That really got momentum in the quarter and we did quite well on that. Minto Yorkville, 19 leases. It was one of our problem children earlier in the crisis but now I think if you look at Yorkville, and I'm looking at the stats from the beginning of November, we had no availability in that building. So those are very, very encouraging signs for us.

Now, as I'd said in the past, Matt, leases signed is a leading indicator of move-ins, which is a leading indicator of revenue, so there is that lag effect, and I just want to caution people from over-exuberance about Q4, because we'll see that impact but it will continue to follow the move-ins, which follow the leases. But yeah, so I think we look at those ones. I feel real positive about it. As I'd said earlier, I think Toronto was probably the slowest market to really come back, but it is coming back and it's looking good. I think Roehampton, particularly as those renovation programs continues to steam along, we're going to see even more leasing in Q4 than we saw in Q3, for example. So I'm very, very optimistic on that front.

Matt Kornack — Analyst, National Bank Financial

Okay, perfect. Appreciate that colour. It was very helpful.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

Thanks, Matt.

Operator

Mr. Waters, there are no further questions at this time. Please proceed.

Michael Waters — Chief Executive Officer, Minto Apartment REIT

That's great. Thank you, everyone. That concludes our call this morning. Thanks for joining us and for your interest in the REIT and its results. We look forward to speaking with you again after we report our Q4 2021 results early next year. So thank you so much and we'll talk to you all again real soon.

Operator

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