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# THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

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**THE WALL STREET TRANSCRIPT**

## CEO/COMPANY INTERVIEW

**JOHN P. VAN HAASTRECHT**  
Morguard Real Estate Investment Trust

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# Morguard Real Estate Investment Trust (MRTu.TO)



**JOHN P. VAN HAASTRECHT** became President and CEO of Morguard Real Estate Investment Trust in August 1999. Prior to this period, Mr. van Haastreht founded Devan Properties Ltd. in 1985, and successfully grew the company to be a major force in the Canadian real estate industry. The company was sold in 1998, and subsequently rolled into Morguard Real Estate Investment Trust in 1999. Mr. van Haastreht started his career as a pilot in the Canadian Navy, breaking into the Canadian real estate

industry with A.E. LePage in Toronto in 1969. He has held a number of senior positions in the real estate industry, including with Columbia Commonwealth Limited, a company involved in the development of regional shopping centers and office buildings throughout Canada and the United States. Mr. van Haastreht has also acted as a developer and real estate advisor to a variety of companies and to the Ontario government. From 1980 to 1985, Mr. van Haastreht was with Campeau Corporation, where he was responsible for the Shopping Center Division, the National Capital Region, and the Western Office and Industrial Division. Mr. van Haastreht is a graduate of the Royal Military College in Kingston, Ontario, with a degree in Applied Science.

## SECTOR – REITS

### (KAM618) TWST: Can we start with a history and an overview of Morguard?

**Mr. van Haastreht:** Morguard is a Real Estate Investment Trust with assets just under \$850 million. It was created in 1997, when a number of pension funds rolled some of their real estate assets into the Trust. The Trust then went public in October of 1997.

Initially, the Trust was externally managed by Morguard Investments Ltd., both from the point of view of asset management and property management.

In August of 1999, all the assets of a private real estate company called Devan Properties Ltd. — a company which had assets worth approximately \$363 million — was rolled into the

Trust and the Devan Management Group, which I was a part of, became the internalized management of the Trust. Therefore, there was a distinctive shift in management philosophy and method of operations starting in August 1999. As the new management group, we have been highlighting this shift to the investment community, telling them of the changes and the different approach that this management group has for operating real estate assets.

From an historical point of view, Devan had an entrepreneurial background while Morguard Investment Ltd., with an ongoing relationship with pension funds, had a more passive attitude toward the operation of real estate. The new management group has taken an innovative ap-

proach with all the Trusts' assets, which now comprise of 69 properties, and as previously mentioned, with just under \$850 million in book value. We are moving forward aggressively enhancing these assets and developing a strategy, which will benefit all our unitholders, the value of the units they hold, and the stability of their distribution.

**TWST: Can we talk about the changes that have taken place and the changes that will take place?**

**Mr. van Haastreht:** When the new management group took control of the Trust, our first action was to undertake a complete review of all the assets retained by the Trust. As a result of this review, all the assets were placed into four separate and distinct categories.

The first category was properties that the Trust should hold long term and continue benefiting from a stable and enhancing cash flow. This group consisted of generally the large market dominant properties.

The second group was properties that were well positioned with substantial

potential, but needed some form of re-development or upgrade.

The third group was properties that were not important long term to the Trust, but could be viewed as in the medium to long-term future as being properties that could be disposed of.

The fourth and last group was properties that should be disposed of immediately and in this category we have approximately \$40 to \$50 million of total assets. This group generally

comprises older industrial properties, well located, but obsolete from a point of view of present market demand.

It is management's belief that the best performance for our unitholders will be achieved by concentrating on large, dominant properties and creating value in those properties rather than diverting resources to a number of smaller individual properties.

The second activity we commenced was a review of the management procedures and the level of service being provided to tenants and their customers. Since the Devan management group was mostly involved in retail real estate, we have a

great sensitivity to customer service, the state, and the visual impact of each of the properties. As a result, a program was started in all the office buildings to introduce property enhancements such as the services of a concierge, improved meeting rooms, lobbies, and elevator services, among others.

**TWST: How would you describe the strategy that you are going to follow in the future?**

**Mr. van Haastreht:**

Our strategy going forward is divided into two parts — we realize as a REIT, investors will perceive us from the point of view of the value of our quarterly distributions, and second, we are cognizant of the impact of long-term value creation. We are trying to reach the middle ground, where we can satisfy our unitholders with the distributions and at the same time provide a conservative approach to this subject in order to retain sufficient capital to be able to continue to enhance the real

### Highlights

*Morguard is a Canadian REIT. CEO John P. van Haastreht says that the company is one of Canada's most conservative REITs in its distribution policy, but he feels that in order to be prudent and to retain capital for re-deployment, the company should reduce the distributions to where they are equal to the free cash available. This can be done by concentrating on the major properties in order to obtain the greatest value enhancement in rental increases and cash flow increases. The major focus at present is on three areas of Canada: British Columbia, Alberta and Ontario. Where there is real estate in other provinces, the company will sell it if the company is not market dominant there, and will re-deploy the capital in those three markets.*

estate value of the individual properties. At the end of the day, we want to make sure our unitholders have value left in their units.

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At the moment, we are distributing \$0.90 per unit, on a quarterly basis of \$0.225. Based on this year’s income it will be between approximately 85% and 88% of our distributable income. Our long-term goal is to reduce the percentage of our distributions in the range of 70% to 75% of our distributable income. At the moment, we are among the most conservative of the Canadian REITs in our distribution policy, but we feel that in order to be prudent and to retain capital for re-deployment, we should reduce the distribution to be equivalent to free cash available. Free cash is distributable income less principal payments, the sinking fund requirements on our first mortgage bonds, and major capital/repair requirements.

**TWST:** How are you going to go about that?

**Mr. van Haastreht:** We intend to accomplish this by concentrating on our major properties in order to obtain the greatest value enhancement; i.e., rental increases and cash flow increases. We have a number of properties that came into the REIT through the Devan acquisition that are major dominant regional shopping centers which, with the appropriate attention, have great cash flow en-

hancement capabilities. As cash flow increases for the entire company, and we maintain our distribution levels, the result will be a decrease in our payout ration.

**TWST:** Considering your market in Canada, what is the outlook for your type of properties?

**Mr. van Haastreht:** The real estate market in Canada is quite similar to that of the United States. We are benefiting from a very strong economy. Real estate has not been in better shape for years. Unfortunately, the capital markets are not reflecting the true value of our units.

Real estate today is generally stable. We are very confident about the outlook for this industry, and in addition, we are concentrating our efforts so that in the future we develop a completely or as near to complete as possible a recession-resistant portfolio. In respect to retail real estate, we are concentrating on market dominant shopping centers, which have the benefit of withstanding competition and major economic downturns. As far as office properties are concerned, we want to make sure that these properties are well located and have a conservative leasing policy, i.e., long-term stable leases, and good stable tenancies.

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***“We like to think that the Morguard REIT is somewhat unique in that none of our portfolio was ever in difficulty. For that matter, the predecessor company, Devan, which was a private real estate company, survived the recession without any capital reorganization or any deferment in any interest payments.”***

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We are de-emphasizing investments in industrial real estate and eventually plan to eliminate these altogether from our portfolio completely. It is management’s opinion that although industrial

properties are stable, they do not have great future cash enhancement capability.

**TWST: Within the REIT industry in Canada, what changes are taking place?**

**Mr. van Haastrecht:** The REIT industry in Canada came into existence as a by-product of the recent real estate recession. A number of REITs were created in order to shift assets from financial institutions that were acquired during the recession to other investment entities. In many cases it allowed financial institutions to exit real estate and allowed a different class of investors to participate in this new investment vehicle. These investors were inclined to look at the distributions rather than the actual assets.

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We like to think that the Morguard REIT is somewhat unique in that none of our portfolio was ever in difficulty. For that matter, the predecessor company, Devan, which was a private real estate company, survived the recession without any capital reorganization or any deferment in any interest payments. It was not a positive experience during the recession, but we survived it totally intact.

Going forward, we intend to continue to enhance the quality of our assets. Our goal is to have the investment community recognize us as a stable vehicle for investing in real estate, one that provides the benefit of a stable distribution.

**TWST: How do you go about changing that perception?**

**Mr. van Haastrecht:** It is a matter of distributing information. Talking with you is one method of helping our story. We have been conducting a road show that we present to retail brokers of the various large institutional brokerage firms in Canada. We continue to keep in contact with our large investors, telling them of our ongoing plans and we attempt to distribute much information to the general marketplace. Our message is that we are acting in the best interest of our unitholders — enhancing our real estate in order to increasingly stabilize and grow distributions and unit value.

**TWST: We have seen some consolidation going on here in the US market. Is the same thing going on in Canada?**

**Mr. van Haastrecht:** Absolutely. In 1997, it was a banner year for real estate companies doing IPOs. It was a banner year for companies revisiting the capital markets offering secondary stock offerings. Today that has very much dried up. The capital markets are virtually non-existent for real estate, so companies have to find different ways of bulking up, creating value, and there has been pressure on the REITs in the form of consolidation and a number of the original REITs that went public have disappeared through consolidation.

From our point of view, we do not see this happening to the Morguard REIT. We have one major unitholder who owns slightly over 50%, so we are not vulnerable to a takeover. We think that long term it is better for unitholders to buy assets one-by-one that have true value enhancement capabilities. It is management’s opinion that bulking up with another company that has a number of properties in difficulty would not be in the best interest of our unitholders long term.

**TWST: Are you not going to be a consolidator of other REITs?**

**Mr. van Haastrecht:** No. That is not our plan at the moment.

**TWST: When you go out looking for properties, what are you looking for at this point? What type of properties?**

**Mr. van Haastrecht:** We are focused on retail properties, particularly market dominant shopping centers. We want to be in a market where that facility with our expertise and our management style creates an ever increasing cash flow. As a management group we are very tuned in to customer service and that includes both customers in our retail entities, as well as our tenant customers. We have a number of specific programs, both in office buildings and shopping centers, which reflect that attitude such as “shopping” all the stores in each of our shopping centers monthly to ensure that our retail customer acquires the best in services. This intensive management attitude goes a long way to ensuring stability of cash flow as well as enhancement of cash flow. This is why we are emphasizing shopping centers, however, we will look at office properties that are located in close proximity to our major shopping centers. We believe there is a synergy between these properties and our major shopping complexes.

**TWST: When you say you have unique entertainment in the malls, what are you offering that other people are not?**

**Mr. van Haastrecht:** What we are offering is a completely different facility in our shopping centers. For instance, in our St. Laurent Shopping Center in Ottawa, we have an historical balloon display.

This is a presentation of six different shows, highlighting the history of ballooning, as well as certain contemporary aspects of ballooning. In one instance we have a “Leonardo da Vinci” creation, where two individuals are pedaling a bicycle to attempt to become airborne. In an-

other instance we have a turn-of-the-century balloon race. Each of these shows has animations, smoke, sounds and music. They last for four to six minutes, and occur somewhere in the shopping center every 30 minutes.

In our latest re-development of a property in Brandon, Manitoba, we are creating reliefs which highlight the history of the area of Brandon in six different presentations. One’s a train that is coming into a station, and tells the history of the railroad and the local area. The second is a highlight of the educational system, and the third is a history of the farming community which developed the economy of the area. All have story lines, animation, music, etc.

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**TWST: Is that a totally different approach?**

**Mr. van Haastrecht:** I hate to admit it, but we took a page out of the book of Las Vegas, although it’s much lower-key than the presentations that Las Vegas has created. The idea came from seeing the shops at the Forum, and also the unique laser show that exists in downtown Las Vegas.

In St. Laurent, the balloon program has been in place now for almost two years. Sales in the shopping center, when we first acquired it, were \$400 per square foot and it is now reaching \$550 per square foot.

**TWST: Then it makes it worthwhile. Throughout Canada, are there enough properties available for the type you want to satisfy your needs?**

**Mr. van Haastreht:** Yes, there are. What has happened is that real estate companies are shifting their assets in order to emphasize one category of real estate or another. So there has been synergy where one company may be exiting retail while another company such as us wishes to eliminate industrial.

**TWST: Is pricing in line with what you think it should be?**

**Mr. van Haastreht:** Pricing is always based on a willing buyer and willing seller. However, with the capital markets being as unresponsive to secondary issues, there are more willing sellers than there are willing buyers at the moment. This has made the purchase of real estate advantageous for the buyer.

**TWST: From that point of view, do you have the capital you need?**

**Mr. van Haastreht:** We have about \$92 million available to us in potential debt creation. If the Morguard REIT does become involved in major purchases, in all probability we will have to search for ways of financing such acquisitions through Rights Issues, Convertible Debenture or something similar to that. As a company, we have a very conservative structure for debt and on a combined basis, we cannot exceed 55% of debt to gross book value.

**TWST: Is that in your by-laws?**

**Mr. van Haastreht:** We have various forms of financing. We have a Mortgage Bond Issue which restricts the Trust to 50% debt to gross book value on certain properties. Furthermore, this Mortgage Bond Trust Indenture and our Declaration of Trust restricts us to a maximum of 60% of debt to gross book value on the balance of our portfolio.

**TWST: What do analysts expect in the way of growth?**

**Mr. van Haastreht:** A number of analysts have picked us as a buy. They see the entrepreneurial qualities of the management group and believe we have the experience and capability to enhance value and income flows. I would hope that we could at least maintain a 5% to 6% increase on our distributable income on a conservative basis. We also realize that we are in a transitional period at the moment. As we are liquidating some of our smaller properties and buying larger properties we expect our efforts to take approximately 18 to 24 months to truly manifest themselves.

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***“Our major focus is on three areas of Canada: British Columbia, Alberta and Ontario. That is where the major growth is occurring today, and that is where the greatest stability is from a point of view of economics.”***

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**TWST: Do you have the management team in place that you need to accomplish this?**

**Mr. van Haastreht:** Yes. It is basically the same management team that worked at Devan and we have been together for many years. We understand the industry. We understand the marketplace.

**TWST: As CEO of the Trust, where are you focusing your attention today?**

**Mr. van Haastreht:** Our major focus is on three areas of Canada: British Columbia, Alberta and Ontario. That is where the major growth is occurring today, and that is where the greatest stability is from a point of view of economics.

Now, we have real estate in other provinces. The ones that are market dominant we will stay in. The ones that are not, we will look at eventually selling them in the marketplace and re-deploying the capital in those three markets.

My focus is on the value creation. So I

have substantial input in development, in the purchase of new product and also looking at the debt structure and equity structure. So I take an overall view. But we all work as a team. We look at the company and have eliminated middle management. We all work as a team, and therefore we are able to direct our resources very efficiently. We are all workers.

**TWST: How would you describe the culture that you have developed at the Trust as you try to melt the two together?**

**Mr. van Haastreht:** The culture is that of basically working people. We do not take a “corporate” view of anything, but instead have a hands-on approach. As an example, when I walk through one of our properties, I pick up the papers on the floor, if the floor is dirty. It is a total commitment to what we do. It is a total commitment to our properties. It is a total commitment to our unitholders. I think every one of our staff feels the same way. It means that something as small as when business related Christmas gifts come into the company at Christmas time, nobody keeps them. We raffle them off to the staff because we don’t think that anybody is that important in the company that they should deserve to receive these gifts due to their title or position in the company.

**TWST: In this tight labor market, are you able to get the people you need?**

**Mr. van Haastreht:** There is always talent around. Our compensation packages are very good. We recognize that to have a good person on staff, compensation has to be at the market or maybe slightly ahead because good people produce the values.

**TWST: How do you feel about the value the market is currently putting on the Trust?**

**Mr. van Haastreht:** We think that the

Trust is undervalued. For example, we distribute \$0.90 at the moment. Our distributable income will be in the range of \$1.02 to \$1.04 this year. We are trading in the range of \$8.20 to \$8.40. So those are very good returns.

**TWST: What is the market missing?**

**Mr. van Haastreht:** It is not only us. I think the whole real estate sector has fallen out of favor as a vehicle for the investment community. It is small percentage of the overall Toronto Stock Exchange so it does not receive the attention from the large investor groups. Eventually, the Real Estate Index — unless more companies go public — probably will have to join with another Index to acquire proper market momentum.

**TWST: What two or three summary reasons would you give some potential investors to invest in Morguard?**

**Mr. van Haastreht:** One, stability; two, the quality of our assets; and three, the experience and quality of our management team.

**TWST: Thank you.**

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