Mainstreet Equity Corp Reports 16% Growth in Revenues

Double-digit, year-over-year growth across all key operating metrics for the sixth consecutive quarter; counter-cyclical business model continues to prove itself

May 9, 2023 – CALGARY – In Q2 2023, Mainstreet Equity Corp. (“Mainstreet”, TSX:MEQ) once again achieved double-digit, year-over-year growth across all key operating metrics for the sixth consecutive quarter, extending a period of high performance from Q1 as we continue to exhibit solid results despite economic volatility. Funds from operations (“FFO”) grew 25% in Q2, net operating income (“NOI”) increased 18%, and revenues rose 16% (on a per-share basis, FFO grew 26% from $1.21 to $1.52 in Q2 2023).

Bob Dhillon, Founder, President and CEO of Mainstreet, said, “Despite the uncommon economic volatility of the last few years, Mainstreet has continued to deliver results to its shareholders and prove the viability of our 100% organic, non-dilutive growth model.” He added, “This latest quarter is yet more evidence of the resilient nature of the mid-market rental market, as favourable macroeconomic trends continue to bolster our underlying fundamentals and position Mainstreet as a key provider of affordable living in Western Canada.”

We believe these positive Q2 results once again prove the sustainability of Mainstreet’s non-dilutive business model, which has allowed our management team to deliver value-added growth to shareholders despite the uncommon turbulence of recent economic cycles. Core to that success is Mainstreet’s long-term management philosophy, anchored by a counter-cyclical strategy of leveraging our ample liquidity position ($317 million estimated, or $34 per share) and low-cost capital to acquire undervalued assets at opportunistic prices. Once acquired, we rapidly reposition and improve the condition of these assets through renovations to bolster net operating income and margins (NOI is currently up 11% year-over-year on a same-asset basis, while same-asset operating margins have improved to 60%).

Mainstreet’s Q2 achievements also come as structural supply-demand imbalances in the affordable rental market continue to accelerate, underscoring the extraordinary resilience of this particular asset class. Soaring immigration levels have pushed Canada’s population to nearly 40 million, with the country gaining a record-high one million people in 2022 alone largely due to immigration, according to Statistics Canada data. That trend is likely to continue as the federal government plans to accept 500,000 immigrants every year for the next three years—well higher than previous averages—as a core piece of its economic policy. This sharp influx has accelerated the supply gap that had already persisted for years in the Canadian rental market, causing vacancy rates to fall and rents to rise. According to CHMC estimates, vacancy rates in the Calgary rental market are forecast to fall from 2.2% to 1.2% between 2023 and 2025; in Edmonton they will fall from 2.3% to 1.3%. The tightening trend is evident across Mainstreet’s core markets, including Saskatoon (falling from 2.5% to 1.8%) and Regina (from 2.8% down to 2.0%). Vancouver’s rental vacancy is predicted to remain around the lowest in the country at 0.9% by 2025.

Mainstreet, with a tangible real estate portfolio that includes nearly 17,000 rental units strategically located across western Canadian urban centres, is well-positioned to remain a crucial provider of affordable living in this current macroeconomic context. Even amid high inflation and rising costs, Mainstreet has managed to maintain highly affordable rental rates (our average mid-market rental rate remains around $1,000), making us a preferred option for young families, working Canadians, students and immigrants that make up the core of Mainstreet’s customer base.

As we continue fiscal 2023, Mainstreet is well positioned to continue asserting our 100% organic, non-dilutive growth model and extend our acquisition pipeline, despite economic uncertainty in the remainder of the year. Already Mainstreet has strategically acquired over $116 million (999 units) in new assets across five diversified cities year-to-date, including subsequent acquisitions, as we continue to aggressively expand and diversify our portfolio.

CHALLENGES

Despite opportunities for growth in the coming year, inflation and rising interest rates continue to pose a challenge. Canada's Consumer Price Index is increasing at a much lower rate than when inflation was at its peak—the CPI increased 4.3% in March 2023—but the Bank of Canada is warning it could be some time before it returns to its 2% target. While the vast majority of Mainstreet's debt is locked in at low and fixed terms, higher interest rates will raise the cost of any new refinancings (overall, debt is our largest expense alongside acquisitions).

Mainstreet, however, has spent years establishing its long-term debt position to fortify itself against such rate increases. By securing early financing pre-matured debts and agreeing to pay higher up-front borrowing costs on certain mortgages, we extended our obligations over longer periods (10 years instead of the typical five). Mainstreet has in turn locked in 99% of our debt into fixed-term debt with an average maturity and interest rate of 6.0 years and 2.66%, respectively.

Management believes that inflationary periods are ultimately transitory in nature. In recognition of this, we have strategically opted for shorter, two-year maturities on our latest debts in order to reduce our exposure to higher interest rates. When and if interest rates fall, Mainstreet will benefit not only from more competitive acquisition costs, but also lower interest expenses (resulting in higher FFO) on refinancing after stabilization.

Inflationary pressures, meanwhile, also increase the cost of everything, from labour to materials, raising our operating costs. Renovation and maintenance costs have increased in line with supply shortages for materials.

Canadian job vacancies have come down from their peak in Q2 2022, according to StatCan data, but competition for talent remains fierce amid persistent labour shortages. This has raised Mainstreet's labour costs and made hiring more challenging. That said, Mainstreet has managed to limit its exposure to such shortages through various avenues including foreign worker programs.

Major fixed expenses like property taxes, insurance, and utilities also remain high. Carbon taxes, which place the financial burden on property owners, are scheduled to rise annually. We have addressed higher energy costs by securing various longer-term natural gas contracts, pursuant to which Mainstreet currently pays well below current spot prices. We also managed to reduce our insurance costs more than 13% for fiscal 2023 by obtaining improved premium rates and coverage.

Regardless of our efforts to counteract inflation and rising interest rates, higher costs erode our operating margins and negatively impact our bottom line. Some of the financial burden will ultimately be passed onto tenants through soft rent increases. However, we are confident Mainstreet will remain the leading provider of quality, affordable housing in Western Canada, given our track record of operational efficiencies, value creation and sound management.

OUTLOOK

The 'first inning' of rental market tightening

As we continue into 2023, we expect high immigration rates, lack of new rental supply and subsequent supply-demand imbalance to persist in Canada. We believe immigration rates are unlikely to taper off in the near term as labour markets remain tight, and as the federal government indicates that immigration will remain a bedrock of its plan to grow the Canadian economy. With that, we expect average rental rates across Canada to grow in line with rising inflation rates and supply shortages, which could also lead to fewer home buyers (as for Mainstreet, we will continue to occupy our position as Canada's most competitive provider of affordable living).

Accelerated acquisitions

Mainstreet believes the acquisition environment has entered a period of transition. Our team continues to see risk-adjusted opportunities for growth supported by our sizeable liquidity position, as higher interest rates could force more distressed sellers onto the market and create more renters. Such dynamics create growth potential through opportunistic acquisitions. As ever, we will maintain our strategy of counter-cyclical growth by acquiring assets only when it prioritizes true value creation. In particular, these efforts will include targeted acquisitions outside of Alberta and Saskatchewan as we continue to diversify and expand our portfolio.

BC remains a standout

We expect Vancouver/Lower Mainland will continue to drive growth and performance, as vacancies remain among the lowest in the country and rental rates among the highest. British Columbia has become central to Mainstreet's portfolio, accounting for approximately 42% of our estimated net asset value ("NAV") based on IFRS value.

With an average monthly mark-to-market gap of $580 per suite per month, 95% of our customers in the region are below the average market rent. According to our estimates, that translates into approximately $23 million in NOI growth potential after accounting for tenancy turnover and gradual rent increases.

Western bound

Alberta had an in-migration rate of 41,210 in Q4 2022, as improved economic prospects and relatively affordable living drew a near record number of newcomers to the province. The figure is comparable to the previous quarter, when Alberta had the largest influx of international and interprovincial migrants in its history. Alberta's population grew 1.0% in Q4 2022, well above the national average of 0.7%, according to provincial government data.

Saskatchewan's provincial in-migration also grew sharply, with 8,650 people coming to the province in Q4, compared with 1,950 the year prior.

Manitoba diversification

Given the abundance of opportunity we've seen across Western Canada, Mainstreet has continued to diversify our asset base. We first entered the Manitoba market in 2021, and in Q2 2023, Mainstreet acquired another 291-suite high-rise property in Winnipeg (expanding our total city-wide portfolio to four properties with 405 units).

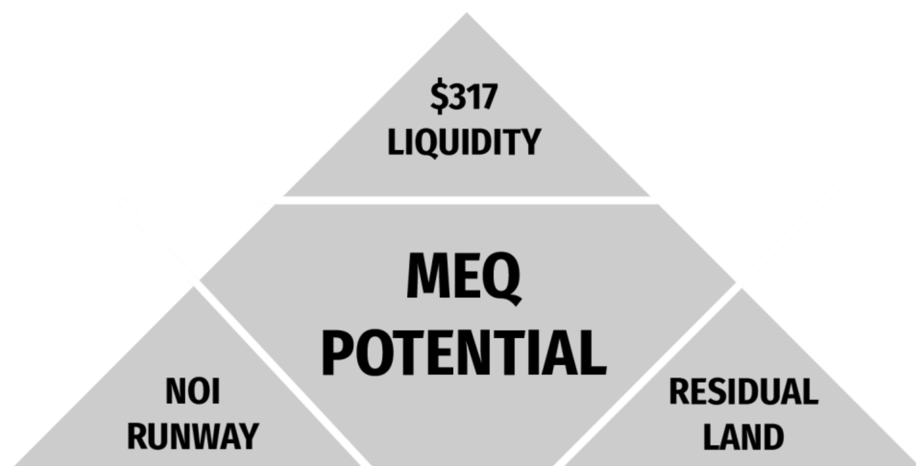
Closing the NOI gap

Current market conditions create a rare opportunity for Mainstreet. Our stabilization rates are higher than average due to our high rate of counter-cyclical acquisitions in recent quarters, while our vacancy rates are lower than average (4.5%, including newly acquired un-stabilized properties). This discrepancy provides substantial opportunity for Mainstreet to continue extracting value from existing assets by aggressively repositioning units.

The MEQ intangibles

While Mainstreet's many tangible assets are central to our strategic position amid rising rental demand, we also boast several less obvious upsides that speak to our inherent underlying value. They include:

- Residual lands and low-density portfolio: Many of Mainstreet's assets are ripe for further development and expansion, allowing new capacity to be added at low cost
- Strong management: Mainstreet's highly experienced team has operated through countless cycles in the market, giving us the ability to adapt as operating environments change
- Efficient operations: Mainstreet has invested resources over the past decade building a strong operating platform, including our adoption of Yardi's IT operating system, to streamline operational oversight
- Land aggregation and densification: Over Mainstreet's 23-year history, we have banked a considerable land portfolio (including both residual land and low-density apartment buildings) that translates into significant tangible value while also providing the option to convert existing assets into higher density developments should such opportunities emerge.



RUNWAY ON EXISTING PORTFOLIO

1. Pursuing our 100% organic, non-dilutive growth model: Using our strong potential liquidity position, estimated at $317 million, we believe there is significant opportunity to continue acquiring underperforming assets at attractive valuations.
2. Boosting NOI: As of Q2 2023, 15% of Mainstreet's portfolio was going through the stabilization process. Once stabilized, we remain confident same-asset revenue, vacancy rate, NOI and FFO will be meaningfully improved. We are cautiously optimistic that we can boost cash flow in coming quarters. In the BC market alone, we estimate that the potential upside based on mark-to-market gaps for NOI growth is approximately $23 million. The Calgary market also has substantial room for rent-to-market catch up.
3. Buying back shares at a discount: We believe MEQ shares continue to trade below their true NAV, and ongoing macroeconomic volatility could intensify that trend.

Forward-Looking Information

Certain statements contained herein constitute "forward-looking statements" as such term is used in applicable Canadian securities laws. These statements relate to analysis and other information based on forecasts of future results, estimates of amounts not yet determinable and assumptions of management. In particular, statements concerning estimates related to future acquisitions, dispositions and capital expenditures, increase or reduction of vacancy rates, increase or decrease of rental rates and rental revenue, future income and profitability, timing of refinancing of debt and completion, timing and costs of renovations, increased or decreased funds from operations and cash flow, the Corporation's liquidity and financial capacity, improved rental conditions, future environmental impact the Corporation's goals and the steps it will take to achieve them the Corporation's anticipated funding sources to meet various operating and capital obligations and other factors and events described in this document should be viewed as forward-looking statements to the extent that they involve estimates thereof. Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions of future events or performance (often, but not always, using such words or phrases as "expects" or "does not expect", "is expected", "anticipates" or "does not anticipate", "plans", "estimates" or "intends", or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved) are not statements of historical fact and should be viewed as forward-looking statements.

Such forward-looking statements are not guarantees of future events or performance and by their nature involve known and unknown risks, uncertainties and other factors, including those risks described in this Annual Information Form under the heading "Risk Factors", that may cause the actual results, performance or achievements of the Corporation to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such risks and other factors include, among others, costs and timing of the development of existing properties, availability of capital to fund stabilization programs, other issues associated with the real estate industry including availability but without limitation of labour and costs of renovations, fluctuations in vacancy rates, unoccupied units during renovations, rent control, fluctuations in utility and energy costs, credit risks of tenants, fluctuations in interest rates and availability of capital, and other such business risks as discussed herein. Material factors or assumptions that were applied in drawing a conclusion or making an estimate set out in the forward-looking statements include, among others, the rental environment compared to several years ago, relatively stable interest costs, access to equity and debt capital markets to fund (at acceptable costs) and the availability of purchase opportunities for growth in Canada. Although the Corporation has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, other factors may cause actions, events or results to be different than anticipated, estimated or intended. There can be no assurance that such statements will prove to be accurate as actual results and future events could vary or differ materially from those anticipated in such forward-looking statements. Accordingly, readers should not place undue reliance on forward-looking statements contained herein.

Forward-looking statements are based on Management's beliefs, estimates and opinions on the date the statements are made, and the Corporation undertakes no obligation to *update forward-looking statements if these beliefs, estimates and opinions should change except as required by applicable securities laws or as otherwise described therein. Certain information set out herein may be considered as "financial outlook" within the meaning of applicable securities laws. The purpose of this financial outlook is to provide readers with disclosure regarding the Corporations reasonable expectations as to the anticipated results of its proposed business activities for the periods indicated. Readers are cautioned that the financial outlook may not be appropriate for other purposes.*

SOURCE: Mainstreet Equity Corp.

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