Mainstreet Equity Corp achieved double digit growth across all key operating metrics including same store results

July 25, 2023 - CALGARY – In Q3 2023, Mainstreet Equity Corp. (“Mainstreet”, TSX:MEQ) achieved double-digit, year-over-year growth across all key operating metrics for the seventh consecutive quarter. Funds from operations (“FFO”) increased 32%, net operating income (“NOI”) grew 22% and rental revenues rose 18%. Same-asset revenue and NOI also accelerated, increasing 10% and 13%, respectively. Despite inflationary pressures, operating margins improved to 63%, up from 61% in 2022.

Bob Dhillon, Founder and Chief Executive Officer of Mainstreet, said, “Once again, the mid-market rental space has proven itself a safe and reliable investment haven during this time of widespread economic disruption.” He added, “At a time when supply shortages and inflationary pressures have sharply increased the costs of home ownership, Mainstreet prides itself in being a crucial provider of affordable living in Western Canada.”

We believe these highly positive results reflect the proven success of Mainstreet’s value-add business model. By strictly adhering to our 100% organic, non-dilutive growth strategy, Mainstreet has continued to create shareholder value throughout the economic cycle, including in periods of high volatility. Under this model, we leverage our sizeable liquidity position ($307 million) and historically low-cost financing to acquire underperforming apartment buildings. Once acquired, we rapidly reposition units through renovations to optimize operating income. Since Mainstreet began trading on the TSX in 2000, we have expanded our portfolio from a handful of rental units to over 17,000, and reached $3 billion in assets while avoiding any equity dilution (excluding small volumes of exercised share options). During that same period, our stock value has increased more than 3,500%.

Magnifying the success of Mainstreet’s countercyclical strategy is the strong macro fundamentals of the broader rental market, where a structural supply-demand imbalance has persisted. Canada’s population is growing fast—the country expected to accept a record-high 1.5 million new comers in 2022 (including 431,645 new permanent residents, 608,420 work permits under the Temporary Foreign Worker Program and International Mobility Program, and 551,405 study permits, based on Immigration, Refugees and Citizenship Canada) —at a time when new rental market supply is flat (the number of purpose-built rental units in the country increased by just 400,000 in the last decade, up to a total 2.2 million). As a result, vacancy rates have fallen to an all-time low of 1.9% in 2022, according to CMHC data. Those figures are particularly low in the provinces where Mainstreet operates: In Vancouver, rental vacancies remain among the lowest in the country at 0.9%, while vacancies in Calgary and Edmonton are expected to fall between 2023 and 2025, down to 1.2% and 1.3%, respectively (Statistics Canada).

We believe this core trend is evident in our Q3 performance, both on an overall and same-asset basis. Combined with high rates of in-migration into Western provinces and the steep cost of home ownership, we believe such trends further establish the rental market as an inherently reliable and resilient asset class. With Mainstreet's current average rental rates are among the most affordable in the mid-market sector, Mainstreet remains well positioned to meet this high demand while continuing our role as a crucial provider of affordable living in Western Canada. As we enter the final quarter of 2023, our management team sees ample opportunity to continue building on this advantaged position as we pursue acquisitions and boost NOI through our stabilization process.

CHALLENGES

Despite major opportunities for growth, rising costs continue to pose a challenge to Mainstreet. Primarily, higher interest rates raise the cost of any new debt. Mainstreet has spent years establishing a long-term debt position to fortify itself against eventual rate increases. By securing early finance 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 6.2 years and 2.69%, respectively. Recognizing that inflationary periods are often transitory in nature, we have strategically negotiated for shorter-term open mortgages that provide flexibility for early renewal when and if interest rates fall.

Inflationary pressures also increase the cost of everything from labour to materials. Canadian job vacancies have come down from their peak in Q2 2022, according to Statistics Canada, but competition for talent remains fierce. This has raised Mainstreet's labour costs and made hiring more challenging. That said, Mainstreet has managed to limit its exposure to shortages through various avenues including foreign worker programs.

Major fixed expenses like property taxes (up 2%), insurance, and utilities (up 13%) also remain high. Carbon taxes, which place the financial burden on property owners, are scheduled to rise annually, from $65 per tonne today to $170 by 2030. 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. \

Mainstreet continues our efforts to counteract inflation and rising interest rates. Although 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.

OUTLOOK

Rental market continues to tighten

We expect average rental rates across Canada to rise as demand continues to outpace supply. However, we believe supply shortages in the real estate market, combined with inflation and rising interest rate, will continue to deter first-time home buyers and incentivize renters. High immigration rates will also underpin those market fundamentals, a trend we view as unlikely to change given the federal government's indication that immigration and international students are a bedrock of its plan to grow the economy.

Accelerated acquisitions
Our team continues to see risk-adjusted opportunities for growth supported by our large liquidity position, as higher interest rates could force more distressed sellers onto the market. Such dynamics create growth potential through opportunistic acquisitions. As ever, we will maintain our strategy of countercyclical growth by acquiring assets only when it prioritizes true value creation. As in past quarters, our acquisition efforts will continue to emphasize portfolio diversification, evidenced by our recent expansion into the Winnipeg market.

BC remains a standout
We expect Vancouver/Lower Mainland will continue to drive growth and performance. Vacancies in the region remain among the lowest in the country while rental rates are 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 $638 per suite per month, 98% of our customers in the region are below the average market rent. According to our estimates, that translates into approximately $26 million in NOI growth potential after accounting for tenancy turnover and gradual rent increases.

Western bound
Alberta had an in-migration rate of 51,700 in Q1 2023, as improved economic prospects and relatively affordable housing drew a near-record number of newcomers to the province. The figure is comparable to the last two quarters of 2022, when Alberta had the largest influx of international and interprovincial migrants in its history. We believe high in-migration rates will in turn continue to push housing prices upward. Benchmark home prices rose 1.5% in Calgary and 1.6% in Edmonton in June as a flood of people entered Alberta. Saskatchewan's provincial in-migration also grew sharply, with 5,700 people coming to the province in Q4, compared with 2,500 the year prior.

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 acquisitions in recent quarters, while our vacancy rates are lower than average (4.7%, including our unstabilized properties which accounted for 14% of our portfolio). This discrepancy provides substantial opportunity for Mainstreet to continue extracting value from existing assets by aggressively repositioning units.

Turning intangibles to tangibles
Over our 23-year history, Mainstreet has strategically built up an extensive portfolio of 800+ buildings in desirable neighborhoods that we believe offers significant intangible value. Management is in the early stages of exploring a three-pronged plan to potentially capitalize on adding more value to our existing assets at low cost. This strategy involves three key pillars: turning unused/residual space within existing buildings into new units; exploring zoning and density relaxations to assess the excess 'capacity/density' to expand/build new within the existing land footprint; or subdividing residual lands to maximize useable space. While the plan is currently conceptual in nature, we view it as yet another aspect of Mainstreet's inherent value proposition over the long term. Given the ongoing housing shortage in Canada, our management team believes now is the ideal time for Mainstreet to explore such possibilities, particularly as we

aim to align our goals with policymakers, who are increasingly seeking densification options in order to reduce housing costs.

RUNWAY ON EXISTING PORTFOLIO

1. Pursuing our 100% organic, non-dilutive growth model: Using our strong potential liquidity position, estimated at $307 million, we believe there is significant opportunity to continue acquiring underperforming assets at attractive valuations.
2. Boosting NOI: As of Q3 2023, 14% of Mainstreet's portfolio was going through the stabilization process. Once stabilized, we remain confident same-asset revenue, vacancy rates, 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 $26 million. The Calgary market in particular 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 that 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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