



**ALLIED PROPERTIES REAL ESTATE INVESTMENT TRUST**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION**

**MARCH 31, 2007**

**DATED MAY 8, 2007**

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## PART I

### Forward-Looking Disclaimer

The terms “Allied Properties”, “the REIT”, “we”, “us” and “our” in the following Management’s Discussion and Analysis of Results of Operations and Financial Condition (“MD&A”) refer to Allied Properties Real Estate Investment Trust and its consolidated financial position and results of operations for the quarter ended March 31, 2007. This MD&A should be read in conjunction with our consolidated financial statements and notes thereto for the quarter ended March 31, 2007, and the year ended December 31, 2006. Historical results and percentage relationships contained in our consolidated financial statements and MD&A, including trends which might appear, should not be taken as indicative of our future results, operations or performance. Unless otherwise indicated, dollar amounts in this MD&A are in thousands.

Certain information included in this MD&A contains forward-looking statements within the meaning of applicable securities laws, including, among other things, statements concerning our objectives and our strategies to achieve those objectives, statements with respect to Management’s beliefs, plans, estimates and intentions and statements concerning anticipated future events, circumstances, expectations, results, operations or performance that are not historical facts. Forward-looking statements can be identified generally by the use of forward-looking terminology, such as “indicators”, “outlook”, “objective”, “may”, “will”, “expect”, “intend”, “estimate”, “anticipate”, “believe”, “should”, “plans”, “continue” or similar expressions suggesting future outcomes or events. Such forward-looking statements reflect Management’s current beliefs and are based on information currently available to Management.

The forward-looking statements in this MD&A are not guarantees of future results, operations or performance and are based on estimates and assumptions that are subject to risks and uncertainties, including those described below in this MD&A under “Risks and Uncertainties”, which could cause actual results, operations or performance to differ materially from the forward-looking statements in this MD&A. Those risks and uncertainties include risks associated with property ownership, property development, geographic focus, asset-class focus, competition for real property investments, financing and interest rates, government regulations, environmental matters, construction liability, unitholder liability and taxation. Material assumptions that were made in formulating the forward-looking statements in this MD&A include the following: that the general economy remains stable; that the REIT’s current target markets remain stable; that interest rates and capitalization rates are stable; and that the equity and debt markets continue to provide access to capital. Although the forward-looking statements contained in this MD&A are based on what Management believes are reasonable assumptions, there can be no assurance that actual results, operations or performance will be consistent with these statements.

All forward-looking statements in this MD&A are qualified by this forward-looking disclaimer. These statements are made as of May 8, 2007, and, except as required by applicable law, we undertake no obligation to update publicly or revise any such statements to reflect new information or the occurrence of future events or circumstances.

## Business Overview and Strategy

The REIT is an unincorporated closed-end real estate investment trust created pursuant to the Declaration of Trust dated October 25, 2002, as amended and restated on February 6, 2003 (“Declaration”). The REIT is governed by the laws of Ontario. The units of the REIT are publicly traded on the Toronto Stock Exchange under the symbol AP.UN. Additional information relating to the REIT is available on SEDAR at [www.sedar.com](http://www.sedar.com).

The objectives of the REIT are to provide stable and growing cash distributions to its unitholders and to maximize unitholder value through the effective management and the accretive growth of its portfolio.

### Property Portfolio

The REIT completed its Initial Public Offering (“IPO”) on February 20, 2003. The REIT used the net proceeds of the IPO to acquire a portfolio of 14 predominantly Class I office properties in downtown Toronto with 820,000 square feet of gross leasable area (“GLA”). By the end of 2006, the REIT had acquired another 25 office properties in downtown Toronto, 24 of them Class I office properties, bringing its total GLA in that market to over two million square feet. The REIT had also acquired five predominantly Class I office properties in downtown Montreal, seven in downtown Winnipeg and five in Quebec City, bringing its total portfolio at the end of 2006 to 56 properties with over 3.4 million square feet of GLA.

The REIT made the following acquisitions in 2007, bringing the portfolio to 58 properties with over 3.5 million square feet of GLA:

Property	Acquired	Office GLA	Retail GLA	Total GLA	Parking Spaces
193 Yonge Street, Toronto	January 12, 2007	32,966	16,318	49,284	22
451-481 Saint Catherine Street, Montreal	February 8, 2007	20,805	9,634	30,439	0
Total		53,771	25,952	79,723	22

Class I office properties are created through the adaptive re-use of light industrial structures in urban areas. They typically feature high ceilings, abundant natural light, exposed structural frames, interior brick and hardwood floors. When restored and retrofitted to the standards of the REIT’s portfolio, Class I buildings can satisfy the needs of the most demanding office and retail tenants. When operated in the coordinated manner of REIT’s portfolio, these buildings become a vital part of the urban fabric and contribute meaningfully to a sense of community.

The REIT’s portfolio accommodates a diverse base of tenants. At the end of 2006, business-service and professional tenants represented 35% of the REIT’s gross revenue, retail tenants 18%, telecommunications and IT tenants 16%, media and entertainment tenants 14%, financial-service tenants 11%, government tenants 3% and other tenants 3%.

The REIT is a leading provider of Class I office and ancillary retail space in Canada and intends to build on this advantage by continuing to make coherent office property acquisitions in its target markets. In doing so, the REIT will strive to enhance on an ongoing basis the quantity and quality of its net rental revenue.

Four Toronto properties—QRC South (103 Richmond Street East), 257 Adelaide Street West, 47 Fraser Avenue and 47A Fraser Avenue—and one Montreal property—the land adjacent to 4446 Saint Laurent Boulevard—are properties under development (“Properties Under Development” or “PUD”). They are undergoing the development or redevelopment necessary to function as high quality, income-producing, Class I office properties.

The REIT has an option agreement (“Option Agreement”) with Allied Canadian Development Corporation (“Developer”), a leading developer of Class I office properties, pursuant to which the Developer must offer to sell to the REIT at fair market value all developed or redeveloped office properties upon substantial completion. Six of the properties in the REIT’s portfolio were acquired pursuant to the Option Agreement. The Developer has two remaining properties subject to the provisions of the Option Agreement. Both properties are nearing substantial completion.

The REIT's portfolio has operated stably. The chart below summarizes the levels of GLA and leased area in the portfolio since the REIT's IPO:

	IPO	Dec. 31, 2003	Dec. 31, 2004	Dec. 31, 2005	Dec. 31, 2006
GLA (square feet)	820,120	984,856	1,636,343	2,321,507	3,415,279
% leased	96.9	97.5	99.2	97.0*	96.3*

\*not including Properties Under Development

Stable portfolio operations and manageable growth in assets have enabled the REIT to achieve its overriding objective of providing regular and growing cash distributions to its unitholders. The chart below summarizes the annualized cash distribution level and the total annual return for each fiscal year since the REIT's IPO:

	Dec. 31, 2003	Dec. 31, 2004	Dec. 31, 2005	Dec. 31, 2006
Distribution level per unit annualized	\$1.10	\$1.14	\$1.18	\$1.22
Total return with reinvestment through DRIP	40.7%	17.6%	32.3%	46.8%
Total return without reinvestment	38.0%	16.2%	31.3%	44.3%

### **Property Management**

Effective July 1, 2005, the REIT's wholly owned subsidiary, Allied Properties Management Limited Partnership ("Property Manager"), completed the acquisition of the property management business of the Developer. In addition to providing property management and related services in connection with the REIT's portfolio, the Property Manager provides property management and related services to third-party property owners on a fee-for-service basis.

### **Performance Indicators**

The REIT measures the success of its strategies through key financial and operating performance indicators.

### **Financial Indicators**

#### **1. Distributions**

The REIT is focused on increasing distributions to its unitholders on a regular and prudent basis. During its first 12 months of operations, the REIT made regular monthly distributions of \$1.10 per unit on an annualized basis. In March of 2004, the REIT increased its monthly distributions by 3.6% to \$1.14 per unit on an annualized basis. In March of 2005, the REIT increased its monthly distributions by 3.5% to \$1.18 per unit on an annualized basis. In March of 2006, the REIT increased its monthly distributions by 3.4% to \$1.22 per unit on an annualized basis. In March of 2007, the REIT increased its monthly distributions by 3.3% to \$1.26 per unit on an annualized basis.

#### **2. Distributable Income**

Increasing distributions can be achieved prudently by increasing Distributable Income ("DI"), as defined in the Declaration. See "Distributable Income" below. In 2006, DI per unit (diluted) was \$1.414, up 5.6% from 2005. In the first quarter of 2007, DI per unit (diluted) was \$0.371, up 10.4% from the comparable quarter in 2006.

#### **3. DI Pay-Out Ratio**

To ensure it retains sufficient cash to meet its capital improvement and leasing objectives, the REIT will strive to maintain an appropriate DI pay-out ratio, the ratio of actual distributions to DI in a given period. In 2006, the REIT achieved a DI pay-out ratio of 85.3%. In the first quarter of 2007, the REIT achieved a DI pay-out ratio of 81.6%.

#### **4. Adjusted Funds From Operations**

Increasing distributions cannot be achieved prudently without reference to adjusted funds from operations ("AFFO"), as this financial indicator takes account of regular maintenance capital expenditures and regular leasing expenditures while ignoring the impact of non-cash revenue. See "Adjusted Funds from

Operations” below. In 2006, AFFO per unit (diluted) was \$1.239, up 1.5% from 2005. In the first quarter of 2007, AFFO per unit (diluted) was \$0.373, up 18.4% from the comparable quarter in 2006

#### 5. AFFO Pay-Out Ratio

To ensure it retains sufficient cash to meet its capital improvement and leasing objectives, the REIT will strive to maintain an appropriate AFFO pay-out ratio, the ratio of actual distributions to AFFO in a given period. In 2006, the REIT achieved an AFFO pay-out ratio of 97.3%. In the first quarter of 2007, the REIT achieved an AFFO pay-out ratio of 81.1%.

#### 6. Debt Ratio

Gross Book Value (“GBV”) is defined as the book value of the assets of the REIT shown on the most recent balance sheet plus accumulated depreciation and amortization and an amount equal to the property management internalization expense recorded by the REIT. A conservative ratio of debt to GBV (“Debt Ratio”) mitigates unitholder risk. At the end of 2006, the Debt Ratio was 48.2%. At the end of the first quarter of 2007, the Debt Ratio was 50.7%.

### ***Operating Indicators***

#### 1. Tenant Retention and Replacement

The REIT places a high value on tenant retention, as the cost of retention is typically lower than the cost of securing new tenancies. If retention is neither possible nor desirable, the REIT will strive for high-quality replacement tenants. Leases representing 533,166 square feet of GLA mature in 2007. By the end of the first quarter of 2007, the REIT had renewed leases representing 193,073 square feet of this GLA and re-leased another 67,618 square feet of this GLA, representing 48.9% of the GLA covered by the maturing leases.

#### 2. Occupancy

The REIT strives to maintain consistently high levels of occupancy. At the end of 2006, the REIT’s leased area was 96.3% (not including Properties Under Development). At the end of the first quarter of 2007, the REIT’s leased area was 96.0% (not including Properties Under Development).

#### 3. Same-Asset Net Operating Income

The REIT strives to maintain or increase same-asset net operating income (“NOI”) over time. See “Net Operating Income” below. Same-asset refers to those properties that were owned and operated by the REIT for the entire period in question and for the same period in the prior year. Ignoring the step-rent revenue and the amortization of the fair value assigned to above-market and below-market rents with respect to acquired properties (the mark-to-market rent adjustment), same-asset NOI was \$10,465 in the first quarter of 2007, up 12.1% from the comparable quarter in 2006.

#### 4. Leasing Expenditures

The REIT monitors leasing expenditures carefully. 91,101 square feet of the GLA leased in the first quarter of 2007 involved new leases or lease-renewals that commenced in the quarter. \$89 in leasing expenditures relate to this space, representing \$0.98 per leased square foot.

#### 5. Capital Expenditures

The REIT strives to maintain the properties in its portfolio in top physical condition. In the first quarter of 2007, the REIT incurred \$463 in regular maintenance capital expenditures, representing \$0.13 per square foot of the REIT’s portfolio.

### ***Summary***

The following table summarizes the key financial and operating performance indicators for the first quarter of 2007 and the first quarter of 2006, as well as the change between the two.

	Q1 2007	Q1 2006	Change
Quarter-end distribution level per unit annualized	\$1.26	\$1.22	\$0.04
DI per unit (diluted)	\$0.371	\$0.336	\$0.035
DI pay-out ratio	81.6%	88.4%	(6.8%)
AFFO per unit (diluted)	\$0.373	\$0.315	\$0.058
AFFO pay-out ratio	81.1%	94.1%	(13.0%)
Debt Ratio	50.7%	51.2%	(0.5%)
Renewal/replacement % of leases maturing in year	48.9%	70.9%	(22.0%)
Quarter-end leased area (not including PUD)	96.0%	97.2%	(1.2)%
Same-asset NOI	\$10,465	\$9,334	\$1,131
Leasing expenditures	\$89	\$465	\$376
Leasing expenditures per leased square foot	\$0.98	\$3.30	\$2.32
Maintenance capital expenditures	\$463	\$115	\$348
Maintenance capital expenditures per portfolio square foot	\$0.13	\$0.10	\$0.03

## Business Environment and Outlook

The REIT operates in four target markets—downtown Toronto, downtown and midtown Montreal, downtown Winnipeg and downtown Quebec City. The following is a brief description of the REIT's target markets:

### 1. Downtown Toronto

This target market includes 13.2 million square feet of office inventory in three sub-markets, Downtown East (2.1 million square feet), Downtown West (9.2 million square feet) and King West (1.9 million square feet). Approximately half of the office inventory in this target market falls within the Class I category. The downtown Toronto office market strengthened in 2006, with the overall vacancy rate declining to 6.1% at the end of the year and the Downtown East, Downtown West and King West sub-markets finishing the year with vacancy rates of 5.1%, 5.6% and 12.0%, respectively.<sup>1</sup> The strengthening continued into 2007, with the overall vacancy rate declining to 5.4% at the end of the first quarter and the Downtown East, Downtown West and King West sub-markets finishing the quarter with vacancy rates of 9.2%, 5.0% and 11.3%, respectively.<sup>2</sup>

### 2. Downtown and Midtown Montreal

This target market includes 17.7 million square feet of office inventory in three sub-markets, Downtown East (7.5 million square feet), Old Montreal (7.7 million square feet) and Mile End (2.5 million square feet). Approximately half of the office inventory in this target market falls within the Class I category. The downtown Montreal office market was strengthened modestly in 2006, with the overall vacancy rate declining to 9.7% at the end of the year and the Downtown East and Old Montreal sub-markets finishing the year with vacancy rates of 5.2% and 8.8%, respectively.<sup>3</sup> The strengthening continued into 2007, with the overall rate declining to 9.3% at the end of the first quarter and the Downtown East and Old Montreal sub-markets finishing the quarter with vacancy rates of 3.5% and 8.4%, respectively.<sup>4</sup>

### 3. Downtown Winnipeg

This target market includes 1.8 million square feet of office inventory, principally in the Exchange District. Most of the office inventory in the Winnipeg target market falls within the Class I category. The downtown

<sup>1</sup> Cushman & Wakefield LePage, *Fourth Quarter 2006 Statistical Summary, Toronto Office Market*.

<sup>2</sup> Cushman & Wakefield LePage, *First Quarter 2007 Statistical Summary, Toronto Office Market*.

<sup>3</sup> Cushman & Wakefield LePage, *Fourth Quarter 2006 Statistical Summary, Montreal Office Market*.

<sup>4</sup> Cushman & Wakefield LePage, *First Quarter 2007 Statistical Summary, Montreal Office Market*.

Winnipeg office market was stable in 2006, with the overall vacancy rate declining to 8.1% at the end of the year.<sup>5</sup> The market remained stable into 2007, with the vacancy rate rising to 8.7% at the end of the first quarter.<sup>6</sup>

#### 4. Downtown Quebec City

This target market includes 1.5 million square feet of office inventory in the St. Roch office node. Most of the office inventory in this target market falls within the Class I category. The Quebec City office market strengthened in 2006, with the overall vacancy rate declining to 3.7%.<sup>7</sup> The strengthening is projected to continue into 2007.<sup>8</sup>

Demand for office space in the REIT's target markets is stable or strengthening. The state of the REIT's target markets, the quality of the REIT's portfolio and the capabilities of the REIT's personnel afford Management a reasonable basis for confidence in the REIT's near-term performance. The REIT intends to continue the acquisition of Class I and other office properties in its target markets.

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<sup>5</sup> Cushman & Wakefield LePage, *National Real Estate Market Intelligence, 2006*.

<sup>6</sup> Cushman & Wakefield LePage, *National Real Estate Market Intelligence, First Quarter 2007*.

<sup>7</sup> Avison Young, *Real Estate Forecast 2007*.

<sup>8</sup> Avison Young, *Real Estate Forecast 2007*.

## PART II

### Summary Information and Performance for the Quarter ended March 31, 2007

The following sets out summary information and financial results for the quarter ended March 31, 2007, and the comparable quarter and the change between the two.

(In thousands except for per unit and % amounts)	Q1 2007	Q1 2006	Change	%Change
Revenue from rental properties	20,546	14,943	5,603	37.5%
Rental property operating cost	7,999	5,543	2,456	44.3%
Net rental income	12,547	9,400	3,147	33.5%
Real estate service income	87	110	(23)	(20.9%)
Financing expense				
Interest	3,741	3,023	718	23.8%
Amortization - Mortgage premium	(92)	(42)	(50)	119.0%
Amortization - Deferred financing cost	77	-	77	-
Depreciation and amortization				
Rental properties	2,311	1,776	535	30.1%
Deferred leasing cost and tenant improvements	533	233	300	128.8%
Origination cost and acquired tenant relationships	2,799	1,880	919	48.9%
Acquired contracts and customer relationships	24	24	-	0.0%
Deferred financing cost	-	66	(66)	-
Computer and office equipment	10	8	2	25.0%
Income from operations	3,231	2,542	689	27.1%
Trust expense	690	518	172	33.2%
Net income	2,541	2,024	517	25.5%
Amortization				
Rental properties	2,311	1,776	535	30.1%
Mortgage premium	(92)	(42)	(50)	119.0%
Acquired leases	800	636	164	25.8%
M-T-M acquired leases	23	88	(65)	(73.9%)
Acquired tenant relationships	1,999	1,244	755	60.7%
Acquired contracts and customer relationships	24	24	-	0.0%
Step-rent adjustments	(125)	(355)	230	(64.8%)
Property management internalization expense	-	-	-	-
LTIP compensation expense	6	-	6	-
DI	7,487	5,395	2,092	38.8%
Weighted average units outstanding (basic)	19,793	15,809	3,984	25.2%
Weighted average units outstanding (diluted)	20,176	16,064	4,112	25.6%
Distributions	6,109	4,768	1,341	28.1%
DI per unit (basic)	\$0.378	\$0.341	\$0.037	10.9%
DI per unit (diluted)	\$0.371	\$0.336	\$0.035	10.4%
DI pay-out ratio	81.6%	88.4%	(6.8%)	
FFO	8,184	5,913	2,271	38.4%
FFO per unit (basic)	\$0.413	\$0.374	\$0.039	10.4%
FFO per unit (diluted)	\$0.406	\$0.368	\$0.038	10.3%
FFO pay-out ratio	74.6%	80.6%	(6.0%)	
AFFO	7,530	5,066	2,464	48.6%
AFFO per unit (basic)	\$0.380	\$0.320	\$0.060	18.8%
AFFO per unit (diluted)	\$0.373	\$0.315	\$0.058	18.4%
AFFO pay-out ratio	81.1%	94.1%	(13.0%)	
NOI	12,445	9,133	3,312	36.3%
Same-asset net operating income	10,465	9,334	1,131	12.1%
Total assets	\$532,302	\$384,963	\$147,339	38.3%
Total debt (excludes premium on assumed debt)	\$295,776	\$212,226	\$83,550	39.3%
Debt to GBV	50.7%	51.2%	(0.5%)	
Total GLA (s.f., excluding PUD)	3,409	2,266	1,143	50.4%
Leased GLA (s.f., excluding PUD)	3,272	2,202	1,070	48.6%
Leased GLA (% total GLA)	96.0%	97.2%	(1.2%)	

Net income for the quarter ended March 31, 2007, was \$2,541, as compared to \$2,024 in the quarter ended March 31, 2006. Net income per unit (diluted) for the quarter was \$0.126, as compared to net income per unit (diluted) of \$0.126 in the comparable quarter.

DI for the quarter ended March 31, 2007, increased by 38.8% to \$7,487 from \$5,395 for the quarter ended March 31, 2006. DI per unit (diluted) for the quarter was \$0.371, as compared to DI per unit (diluted) of \$0.336 in the comparable quarter.

#### ***Net Rental Income***

Net rental income for the quarter ended March 31, 2007, increased by 33.5% to \$12,547 from \$9,400 in the quarter ended March 31, 2006, as follows:

- (i) \$709 due to the increase in same-asset net rental income from properties owned for the entire period and the entire comparable period (which includes the period-over-period change in step-rent adjustments); and
- (ii) \$2,438 due to net rental income from properties not owned for the entire period and the entire comparable period.

Of the \$41,048 of net rental income for the year ended December 31, 2006, \$752 of operating cost recoveries is in dispute with a tenant. Of the \$12,547 of net rental income for the quarter ended March 31, 2007, \$59 of operating cost recoveries is in dispute with a tenant. Based on the advice of legal counsel, Management is of the view that there is no merit to the tenant's position and is diligently pursuing the matter.

Net rental income per occupied square foot for the quarter ended March 31, 2007, was \$15.32 annualized, as compared to \$17.08 annualized in the quarter ended March 31, 2006. The quarter-over-quarter decline is reflective of the fact that the REIT recently acquired more property in target markets with lower net rental rates than its Toronto target market.

#### ***Real Estate Service Income***

The Property Manager provides real estate services to third-party property owners. Real estate service income for the quarter ended March 31, 2007, was \$87, as compared to \$110 in the quarter ended March 31, 2006.

#### ***Financing Expense***

Financing expense includes interest cost on mortgage debt and other credit facilities and the amortization of the premiums and discounts on assumed mortgages. The amortization of the premiums and discounts on assumed mortgages reduced financing expense by \$92 in the quarter ended March 31, 2007.

Financing expense for the quarter ended March 31, 2007, increased by 25.0% to \$3,726 from \$2,981 in the quarter ended March 31, 2006, due to the increase in financing expense associated with additional properties acquired in 2006 and 2007 and the change in accounting policies described in note 3(o) of the REIT's consolidated financial statements for the quarter ended March 31, 2007.

#### ***Depreciation and Amortization***

The REIT records depreciation on its buildings on a straight-line basis over their expected life. Depreciation recorded on buildings for the quarter ended March 31, 2007, increased by 30.1% to \$2,311 from \$1,776 in the quarter ended March 31, 2006.

The REIT records amortization of deferred leasing cost, tenant improvements and the assigned fair value of the origination cost and tenant relationships for in-place leases acquired on acquisition of a rental property on a straight-line basis over the term of the corresponding lease. Deferred financing cost is amortized on a straight-line basis over the term of the corresponding debt.

### **Trust Expense**

Trust expense includes cost incurred by the REIT that is not directly attributable to rental property, such as officers' compensation, trustees' fees, professional fees for legal and audit services, trustees' and officers' insurance premiums and general administrative expenses.

Trust expense for the quarter ended March 31, 2007, increased by 33.2% to \$690 from \$518 in the quarter ended March 31, 2006, due to increased salary, audit, legal and occupancy costs.

### **Leasing Activity**

Leasing activity as at March 31, 2007, is summarized in the following table:

	<b>Vacant or Maturing</b>	<b>Leased End Q1</b>	<b>% Leased End Q1</b>	<b>Vacant End Q1*</b>
Vacant GLA on January 1, 2007*	124,436	24,457	19.7%	99,979
Vacant GLA on acquisition in 2007	na	na	na	na
GLA accessed through rationalization	na	na	na	na
GLA maturing in first quarter of 2007	160,736	122,944	76.5%	37,819
Subtotal	285,199	147,401	57.7%	137,798
GLA maturing in remainder of 2007	372,430	137,747	37.0%	na
Total	657,602	285,148	43.5%	

\*not including Properties Under Development

124,436 square feet of GLA were vacant at the beginning of 2007. By March 31, 2007, the REIT had leased 24,457 square feet of this originally vacant GLA, leaving 99,979 square feet vacant at the end of the quarter.

Leases for 533,166 square feet of GLA mature in 2007, of which 160,763 square feet of GLA matured in the quarter ended March 31, 2007. By March 31, 2007, the REIT had

- (i) renewed or replaced leases for 122,944 square feet of the GLA that matured in the first quarter, leaving 37,819 square feet vacant at the end of the quarter and
- (ii) renewed or replaced leases for 137,747 square feet of the GLA maturing in the remainder of 2007.

With respect to the maturing leases renewed or replaced in the first quarter of 2007 (260,691 square feet of GLA), the REIT achieved rental rates

- (i) above in-place rental rates with respect to 57% of this GLA and
- (ii) equal to in-place rental rates with respect to the balance of this GLA.

### **Capital Expenditures**

The REIT's portfolio requires ongoing maintenance capital expenditures and leasing expenditures. Leasing expenditures include the cost of in-suite or base-building improvements made in connection with the leasing of vacant space or the renewal or replacement of tenants occupying space covered by maturing leases, as well as improvement allowances and commissions paid in connection with the leasing of vacant space and the renewal or replacement of tenants occupying space covered by maturing leases.

In the quarter ended March 31, 2007, the REIT incurred or committed to (i) \$463 in regular maintenance capital expenditures (\$0.13 per portfolio square foot) and (ii) \$89 in leasing expenditures (\$0.98 per leased square foot) in connection with new leases or lease-renewals that commenced in the quarter. In addition, the REIT incurred \$402 in revenue-enhancing capital and leasing expenditures in connection with space that was significantly reconfigured and retrofitted to accommodate high-value new tenancies.

\$68 of the salary expense incurred by the REIT in the quarter ended March 31, 2007, was capitalized in connection with capital improvements to the REIT's rental properties and Properties Under Development. This amount was equivalent to approximately 5% of the associated construction costs.

### ***Properties Under Development***

Management believes that the Properties Under Development represent risk-appropriate opportunities to enhance DI per unit and create value for unitholders. Management also believes that the Properties Under Development represent an opportunity to capitalize more fully on the experience and expertise of the REIT's personnel.

The REIT acquired 145 Berkeley Street, Toronto, in November of 2005. At that time, 80% of the GLA in the property was vacant. The REIT has since leased all the vacant space in the property. From October 1, 2006, onward, the property ceased to be treated as a Property Under Development and was treated as a rental property for accounting purposes. The property was recently appraised at \$2,170 by an independent appraiser. The REIT has received a commitment for \$1,630 in first-mortgage financing on the property. On placement of the first mortgage, the REIT will have financed its entire investment in the property.

The REIT has repositioned the property as an annex to The Queen Richmond Centre, a Class I office complex acquired by the REIT in 2004 and known as QRC. The construction phase of the repositioning at QRC South is complete, and the re-leasing phase is well underway. The REIT has now filled the available space on the second floor and is close to securing an anchor office tenant for the fourth floor.

The REIT acquired 257 Adelaide Street West, Toronto, in June of 2006. At that time, less than 60% of the GLA in the property was occupied. The construction phase of the upgrade of the property is largely complete, and the re-leasing phase is underway.

The REIT acquired approximately 5,500 square feet of land adjacent to 4446 Saint Laurent Boulevard, Montreal, in April of 2006. The REIT has evaluated the potential development of a 22,000 square foot building on the land to accommodate office and ancillary retail users and concluded that it is feasible. The REIT is now working toward securing an anchor tenant for the development.

The REIT acquired 47 and 47A Fraser Avenue, Toronto (two satellite buildings at The Castle in Liberty Village). The upgrade of the two properties will be performed in conjunction with, and customized to, the re-leasing effort, which is underway.

Properties Under Development are stated at the lower of cost and net recoverable value. Cost includes the cost of acquisition, other direct cost, realty tax, other operating expense and applicable financing expense during the development period, less the amount of operating revenue during the development period. The principal factors in determining when the redevelopment-period ends are (i) the achievement of positive cash flow after applicable interest expense and (ii) the passage of a predetermined period of time. Other criteria may be considered in determining when a redevelopment-period ends if warranted by circumstances relating to the relevant Property Under Development.

As at March 31, 2007, the cost of the REIT's Properties Under Development was \$17,351, which was equivalent to 3.0% of the REIT's GBV.

### **Distributable Income**

The REIT defines DI as the net income of the REIT determined in accordance with Canadian generally accepted accounting principles ("GAAP") adjusted by adding back or deducting as required:

- (i) depreciation on rental properties;
- (ii) amortization of the premiums or discounts on assumed mortgages;
- (iii) non-cash rental revenue recorded to recognize rental income rateably over the life of each lease;

- (iv) non-cash compensation expense with respect to the REIT's long-term incentive plan ("LTIP");
- (v) amortization of values ascribed in a building acquisition to in-place leases and tenant relationships;
- (vi) amortization of values ascribed in a building acquisition to above-market and below-market leases;
- (vii) amortization of values ascribed in the property management internalization to acquired contracts and customer relationships; and
- (viii) property management internalization expense.

DI is a non-GAAP financial measure used by some Canadian real estate investment trusts as an indicator of financial performance and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. DI does not have any standardized meaning prescribed by GAAP. As computed by the REIT, DI may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management of the REIT considers DI to be a useful measure of cash available for distributions. The following reconciles cash flow from operations, as presented in the consolidated financial statements, to DI.

(In thousands)	Q1 2007	Q1 2006
Cash flow from operations	(\$12,333)	\$5,086
Amortization of deferred leasing cost, tenant improvements	(521)	(300)
Amortization of deferred financing cost	(77)	
Amortization of computer and office equipment	(10)	(8)
Amortization, tenant inducements	(8)	-
Change in non-cash operating items	20,436	617
DI	\$7,487	\$5,395

Distributions for the quarter ended March 31, 2007, were \$6,109, representing a DI pay-out ratio of 81.6%, as compared to distributions for the quarter ended March 31, 2006, of \$4,768, representing a DI pay-out ratio of 88.4%.

### Funds From Operations

Funds From Operations ("FFO") is a non-GAAP financial measure used by most Canadian real estate investment trusts as an indicator of financial performance and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. While FFO does not have any standardized meaning prescribed by GAAP, the Real Property Association of Canada ("REALpac") established a standardized definition of FFO in its White Paper on Funds From Operations dated November 30, 2004. Essentially, the REALpac definition is net income with most non-cash expenses added back. Management believes that this definition is followed by most Canadian real estate investment trusts and that it is a useful measure of cash available for distributions. The following reconciles net income, as presented in the consolidated financial statements, with FFO, as calculated in accordance with recommendations of the REALpac definition.

(In thousands)	Q1 2007	Q1 2006
Net income	\$2,541	\$2,024
Amortization on rental properties	2,311	1,776
Amortization of deferred leasing cost and tenant improvements	533	233
Amortization of origination cost and acquired tenant relationships	2,799	1,880
FFO	\$8,184	\$5,913

Distributions for the quarter ended March 31, 2007, represented an FFO pay-out ratio of 74.6%, as compared to distributions for the quarter ended March 31, 2006, which represented an FFO pay-out ratio of 80.6%.

## Adjusted Funds From Operations

AFFO is a non-GAAP financial measure used by most Canadian real estate investment trusts as an indicator of financial performance and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. AFFO does not have any standardized meaning prescribed by GAAP. As computed by the REIT, AFFO may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management of the REIT considers AFFO to be a useful measure of cash available for distributions. The principal advantage of AFFO is that it starts from the standardized definition of FFO and takes account of maintenance capital expenditures and regular leasing expenditures while ignoring the impact of non-cash revenue. Because maintenance capital expenditures and regular leasing expenditures are not incurred evenly throughout a fiscal year, there can be volatility in AFFO on a quarterly basis. The following reconciles net income, as presented in the consolidated financial statements, with AFFO, calculated in accordance with what Management believes to be industry practice.

(In thousands)	Q1 2007	Q1 2006
FFO	\$8,184	\$5,913
Step-rent adjustments	(125)	(355)
M-T-M acquired leases	23	88
Leasing expenditures	(89)	(465)
Maintenance capital expenditures	(463)	(115)
AFFO	\$7,530	\$5,066

Distributions for the quarter ended March 31, 2007, represented an AFFO pay-out ratio of 81.1%, as compared to distributions for the quarter ended March 31, 2006, which represented an AFFO pay-out ratio of 94.1%.

## Net Operating Income

NOI is a non-GAAP financial measure and should not be considered as an alternative to net income, cash flow from operations or any other measure prescribed under GAAP. NOI does not have any standardized meaning prescribed by GAAP. As computed by the REIT, NOI may differ from similar computations reported by other Canadian real estate investment trusts and, accordingly, may not be comparable to similar computations reported by such organizations. Management of the REIT considers NOI to be a useful measure of performance for rental properties. The following reconciles net rental income, as presented in the consolidated financial statements, to NOI.

(In thousands)	Q1 2007	Q1 2006
Revenue from rental properties	\$20,546	\$14,943
Rental property operating cost	7,999	5,543
Net rental income	12,547	9,400
M-T-M acquired leases	23	88
Step-rent adjustments	(125)	(355)
NOI	\$12,445	\$9,133

## PART III

### Financial Condition

The REIT finances its operations through three sources of capital: (i) mortgage debt secured by the REIT's rental properties, (ii) secured short-term debt financing with two Canadian chartered banks and (iii) equity. As at March 31, 2007, the REIT had mortgage debt of \$269,547, short-term debt of \$26,229 and unitholders' equity of \$212,972.

### Unitholders' Equity

As at March 31, 2007, the REIT had a market capitalization of approximately \$424,512 based on a closing unit price of \$21.00 on the Toronto Stock Exchange. As at March 31, 2006, the REIT had a market capitalization of approximately \$302,005 based on a closing unit price of \$18.80 on the Toronto Stock Exchange.

In the quarter ended March 31, 2007, the REIT issued a total of 84,525 units for equity contributions of \$1,876. Costs incurred to issue the units were \$2. Units were issued as follows:

- (i) 51,500 units at \$22.64 for \$1,166 to certain officers and trustees under the LTIP; and
- (ii) 33,025 units under its distribution re-investment plan at an average price of \$21.49 per unit for \$710.

The REIT adopted a Unit Option Plan at the time of its IPO and granted at that time options to the trustees and officers of the REIT to acquire 345,000 units at an exercise price of \$10.00 per unit prior to February 19, 2008. In 2004, the maximum number of units reserved for the Unit Option Plan was reduced from 604,390 units to 345,000 units. In 2004, 2005, 2006 and the quarter ended March 31, 2007, the trustees and officers of the REIT exercised 289,500 options in accordance with their terms. As at March 31, 2006, 55,500 options were outstanding, all of which had vested.

In May of 2004, the REIT adopted the LTIP whereby trustees and officers of the REIT ("Participants") may from time to time, at the discretion of the Trustees and subject to regulatory approval, subscribe for units at a market price established in accordance with the provisions of the LTIP. The price for the units is payable as to 5% upon issuance and as to the balance ("LTIP Loan") over 10 years with interest on the LTIP Loan at an annual rate established in accordance with the provisions of the LTIP. The units issued pursuant to the LTIP are registered in the name of a Custodian on behalf of the Participants who are the beneficial owners. The units are pledged to the REIT as security for payment of the LTIP Loan, and all distributions paid on the units are forwarded by the Custodian to the REIT and applied first on account of interest on the LTIP Loan and then to reduce the outstanding balance of the LTIP Loan. The maximum number of units authorized for issuance under the LTIP is equal to 5% of the issued and outstanding units from time to time.

### Mortgages Payable

Mortgages payable as at March 31, 2007, consisted of mortgage debt of \$269,547. The following sets out the maturity schedule of the REIT's mortgage debt, together with the weighted average interest on the mortgages that mature in the respective year.

	Periodic Principal Payments	Balance Due at Maturity	Total Principal	% of Total Principal	WA Interest Rate of Maturing Mortgages
2007	\$ 5,237	\$19,433	\$ 24,670	9.2%	6.44%
2008	6,810	6,437	13,247	4.9%	6.50%
2009	6,698	14,022	20,720	7.7%	6.40%
2010	6,772	4,478	11,250	4.2%	5.35%
2011	6,938	8,496	15,434	5.7%	6.57%
Thereafter	27,107	157,119	184,226	68.3%	5.68%
Total	\$ 59,562	\$ 209,985	\$ 269,547		

Interest rates on the mortgage debt are between 4.94% and 8.10% with a weighted average interest rate of 5.84%. The weighted average term of the mortgage debt is seven years.

Each individual mortgage loan of the REIT is secured by a mortgage registered on title of a rental property and by security agreements covering assignment of rents and personal property with respect to such property. The mortgage debt provides the holder with recourse to the assets of the REIT. The REIT attempts to stagger the maturity of its mortgages and to have mortgages maturing each year to be in a position to upward finance the principal amount of maturing mortgages as needed. Additionally, the REIT attempts to maintain 15 to 20% of its rental properties free from traditional long-term mortgage financing with a view to providing these assets as security for bank credit facilities.

### **Bank Credit Facilities**

The REIT has a \$25,000 revolving credit facility with a Canadian chartered bank bearing interest at bank prime plus 1.0% and maturing on May 31, 2007, as well as a \$10,000 revolving credit facility with another Canadian chartered bank bearing interest at bank prime plus 1.0% and maturing on May 31, 2007. Each credit facility is secured by a combination of mortgage charges and security agreements on certain of the REIT's rental properties. In the quarter ended March 31, 2007, the average borrowings under the credit facilities were \$14,530. As at March 31, 2007, the borrowings under the credit facilities were \$26,229. The REIT is working with one of the Canadian chartered banks referred to above to establish a \$50,000 revolving credit facility bearing interest at bank prime to replace the two facilities currently in place on or before May 31, 2007.

### **Liquidity and Commitments**

Net operating income generated from the rental properties is the primary source of liquidity to fund the REIT's financing expense, trust expense and distributions to unitholders. The Declaration requires the REIT to declare distributions each year not less than the greater of (i) 75% of its DI or (ii) an amount to ensure that the REIT will not be subject to tax on its income and capital gains. The REIT intends to pay distributions of approximately 85% to 90% of DI.

The REIT expects that increased financing on maturing mortgages will provide sufficient cash flow to fund mortgage repayments. The REIT plans to fund anticipated ongoing commitments, obligations, capital expenditures and leasing expenditures using cash flow from operations retained by the REIT and through available borrowing capacity under the credit facilities.

The credit facilities, new mortgage financing and the access to the public equity markets will provide the necessary capital the REIT requires for acquisitions. The REIT's acquisition capacity, meaning its ability to use un-utilized borrowing capacity while not exceeding the 60% Debt Ratio, is \$135,000.

As at March 31, 2007, the REIT had future commitments as set out below.

(In thousands)	March 31, 2007
Leasing commissions	\$ 369
Tenant improvements	678
Building renovations and maintenance capital expenditures	521
Revenue-enhancing capital and leasing expenditure	1,031
Properties Under Development	164
Expenses	519
<b>Total</b>	<b>\$3,282</b>

## PART IV

### Summary Quarterly Information and Performance

The following sets out summary information and financial results for the eight most recently completed fiscal quarters.

(In thousands except for per unit and % amounts)	Q1 2007	Q4 2006	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Q2 2005
Revenue from rental properties	20,546	17,871	15,948	15,467	\$14,943	\$14,291	\$12,822	\$12,260
Rental property operating cost	7,999	6,775	5,478	5,385	5,543	5,145	4,442	4,480
Net rental income	12,547	11,096	10,470	10,082	9,400	9,146	8,380	7,780
Real estate service income	87	113	110	103	110	78	84	-
Financing expense	3,726	3,395	3,262	3,188	2,981	2,711	2,360	2,218
Depreciation and amortization	5,677	5,264	4,366	4,047	3,987	3,919	3,075	2,910
Income from operations	3,231	2,550	2,952	2,950	2,542	2,594	3,029	2,652
Trust expense	690	597	495	767	518	631	404	469
PM internalization expense	-	900	-	-	-	-	7,877	-
Net income (loss)	2,541	1,053	2,457	2,183	2,024	1,963	(5,252)	2,183
Amortization								
Rental properties	2,311	2,107	1,908	1,837	1,776	1,692	1,549	1,461
Mortgage premium	(92)	(98)	(89)	(54)	(42)	(182)	(145)	(99)
Acquired leases	800	770	678	635	636	633	535	501
M-T-M acquired leases	23	67	(61)	68	88	181	-	24
Acquired tenant relationships	1,999	1,904	1,355	1,191	1,244	1,311	720	761
Acquired contracts and customer relationships	24	24	24	24	24	24	24	-
Step-rent adjustments	(125)	(165)	(192)	(209)	(355)	(339)	(287)	(350)
Property management internalization expense	-	900	-	-	-	-	7,877	-
LTIP compensation expense	6	-	-	270	-	-	-	-
DI	7,487	6,562	6,080	5,945	5,395	\$5,283	\$5,021	\$4,481
Weighted average units (basic)	19,793	18,445	16,397	15,848	15,809	15,350	14,471	14,036
Weighted average units (diluted)	20,176	18,824	16,772	16,166	16,064	15,606	14,727	14,289
Distributions	6,109	5,696	5,102	4,891	4,768	4,578	4,317	4,295
DI per unit (basic)	\$0.378	\$0.356	\$0.371	\$0.375	\$0.341	\$0.344	\$0.347	\$0.319
DI per unit (diluted)	\$0.371	\$0.349	\$0.363	\$0.368	\$0.336	\$0.339	\$0.341	\$0.314
DI pay-out ratio	81.6%	86.8%	83.9%	82.3%	88.4%	86.7%	86.0%	95.8%
FFO	8,184	7,125	6,734	6,139	5,913	5,782	5,616	5,045
FFO per unit (basic)	\$0.413	\$0.386	\$0.411	\$0.387	\$0.374	\$0.377	\$0.388	\$0.359
FFO per unit (diluted)	\$0.406	\$0.379	\$0.402	\$0.380	\$0.368	\$0.370	\$0.381	\$0.353
NOI	12,445	10,998	10,217	9,941	9,133	8,988	8,093	7,454
Net income (loss) per unit (basic)	\$0.128	\$0.057	\$0.147	\$0.138	\$0.128	\$0.128	\$(0.363)	\$0.156
Net income (loss) per unit (diluted)	\$0.126	\$0.056	\$0.144	\$0.135	\$0.126	\$0.126	\$(0.363)	\$0.153
Total assets	\$532,302	\$502,906	\$443,945	\$405,827	\$384,963	\$384,538	\$321,659	\$309,822
Total debt	\$295,776	\$263,464	\$241,765	\$224,498	\$212,226	\$210,093	\$163,182	\$144,596
Debt Ratio	50.7%	48.20%	50.2%	53.2%	51.2%	51.0%	47.7%	44.8%
Total GLA (s.f., excluding PUD)	3,409	3,321	2,657	2,387	2,266	2,266	1,985	1,925
Leased GLA (s.f., excluding PUD)	3,272	3,197	2,599	2,346	2,202	2,197	1,933	1,885
Leased Area (%GLA)	96.0%	96.3%	97.8%	98.3%	97.2%	97.0%	97.4%	97.3%

## PART V

### Critical Accounting Estimates

The significant accounting policies used in preparing the REIT's consolidated financial statements are described in Note 3 to those statements. The following is a discussion of Management's estimates that are most important to the presentation of the REIT's results of operations and financial condition and are most subjective as a result of matters that are inherently uncertain.

#### ***Fair Value of Assumed Mortgages Payable and Fair Value of Mortgages Payable***

Most of the mortgage indebtedness of the REIT was assumed in conjunction with rental property acquisitions. GAAP requires that the mortgages payable assumed on acquisition of properties be recorded at fair value. The fair value of the mortgages payable has been determined by discounting the cash flows of these financial obligations using market rates for debt of similar terms and credit risks. Market rates for debt are based on the yield of Canadian government bonds with similar maturity dates plus a credit spread based on Management's experience in obtaining financing and the current market conditions.

#### ***Impairment of Assets***

The REIT is required to write down to fair value any long-life assets that are determined to have been permanently impaired. The REIT's long-life assets consist of rental properties. The REIT's policy is to assess any potential impairment by making a comparison of the current and projected operating cash flow of a rental property over its remaining useful life, on an un-discounted basis, to the carrying amount of the rental property. If such carrying amount was in excess of the projected operating cash flow of the rental property, impairment in value would be recognized to adjust the carrying amount to its estimated fair market value. Current operating cash flows are based on leases in place and projected operating cash flows are based on Management's estimates of future rental rates. Prior to acquiring a rental property, the REIT commissions an appraisal and conducts due-diligence to satisfy itself that the acquisition price is representative of fair market value.

#### ***Depreciation***

A significant portion of the purchase price of rental properties is allocated to buildings. The depreciation recorded on buildings is based on the straight-line basis over their expected useful life. The allocation of purchase price to buildings and the estimated useful life are based on Management's estimates and, if these estimates prove incorrect, the depreciation will not be appropriately recorded.

## **PART VI**

### **Related Party Transactions**

At the time of the REIT's IPO, a subsidiary of the Developer leased 29,102 square feet of office space from the REIT pursuant to a lease expiring on September 30, 2010. Effective July 1, 2005, the REIT entered into a direct lease of this space with Loblaw's Properties Limited for a term ending October 31, 2010, on the condition that the original indemnity of the Developer protecting the REIT from any revenue shortfall (on a cash basis) from the original lease remain in full force and effect.

## PART VII

### Risk and Uncertainties

There are certain risk factors inherent in the investment and ownership of real estate. Real estate investments are capital intensive, and success from real estate investments depends upon maintaining occupancy levels and rental income flows to generate acceptable returns. These success factors are dependent on general economic conditions and local real estate markets, demand for leased premises and competition from other available properties.

The REIT's portfolio is focused on a particular asset class in four metropolitan real estate markets in Canada. This focus enables management to capitalize on certain economies of scale and competitive advantages that would not otherwise be available.

#### **Financing and Interest Rate Risk**

The REIT is subject to risk associated with debt financing. The availability of debt to re-finance existing and maturing loans and the cost of servicing such debt will influence the success of the REIT. In order to minimize risk associated with debt financing, the REIT will attempt to re-finance maturing loans with long-term fixed-rate debt and to stagger the maturities over time.

Interest rates on the REIT's mortgage debt are between 4.94% and 8.10% with a weighted average interest rate of 5.84%. The weighted average term of the REIT's mortgage debt is seven years. As at March 31, 2007, the borrowings under the REIT's credit facilities were \$26,229.

#### **Credit Risk**

The REIT is subject to credit risk. Credit risk arises from the possibility that tenants may not be able to fulfill their lease obligations. The REIT will strive to mitigate this risk by maintaining a diversified tenant-mix and limiting exposure to any single tenant.

The following sets out the REIT's tenant-mix on the basis of percentage of rental revenue for the quarter ended March 31, 2007.

<b>Category</b>	<b>% of Rental Revenue Q1 2007</b>
Business service and professional	35
Telecommunications and information technology	17
Retail (head office and storefront)	16
Media and entertainment	15
Financial services	10
Government	2
Other	5

The following sets out the percentage of rental revenue from the REIT's top-10 tenants by rental revenue for the quarter ended March 31, 2007.

<b>Tenant</b>	<b>% of Rental Revenue Q1 2007</b>
Desjardins	6.0
Cossette Communications	4.0
Publicis Toronto	2.8
MTS Allstream	2.2
St. Joseph Media	2.2
Algorithmics	2.1
Indigo Books & Music	2.0
Nelvana	1.8
Blast Radius	1.5
Veritprop	1.5

#### **Lease Roll-Over Risk**

The REIT is subject to lease roll-over risk. Lease roll-over risk arises from the possibility that the REIT may experience difficulty renewing or replacing tenants occupying space covered by leases that mature. The REIT strives to stagger its lease maturity schedule so that it is not faced with a disproportionately large level of lease maturity in a given year.

96.0% of the GLA in the REIT's portfolio was leased as at March 31, 2007 (not including Properties Under Development). The following sets out the total GLA of the leases that mature during the period from January 1, 2007, to December 31, 2011, assuming tenants do not exercise renewal options, and the percentage of total GLA represented by the maturing leases.

<b>Year Ended</b>	<b>Square Feet</b>	<b>% of Total GLA</b>
December 31, 2007	533,166	15.1%
December 31, 2008	416,808	11.8%
December 31, 2009	556,627	15.8%
December 31, 2010	367,500	10.4%
December 31, 2011	380,005	10.8%

Leases representing 260,691 square feet of the GLA that matures in 2007 were renewed or replaced by March 31, 2007. The weighted average term to maturity of the REIT's leases is four years.

### ***Environmental Risk***

As an owner of real property, the REIT is subject to various federal, provincial and municipal laws relating to environmental matters. Such laws provide that the REIT could be liable for the costs of removal of certain hazardous substances and remediation of certain hazardous locations. The failure to remove or remediate such substances or locations, if any, could adversely affect the REIT's ability to sell such real estate or to borrow using such real estate as collateral and could potentially also result in claims against the REIT. The REIT is not aware of any material non-compliance with environmental laws at any of the properties in its portfolio. The REIT is also not aware of any pending or threatened investigations or actions by environmental regulatory authorities in connection with any of the properties in its portfolio or any pending or threatened claims relating to environmental conditions at the properties in its portfolio.

### ***Development Risk***

As an owner of Properties Under Development, the REIT is subject to development risks, such as construction delays, cost over-runs and the failure of tenants to take occupancy and pay rent in accordance with lease arrangements. In connection with all Properties Under Development, the REIT incurs development costs prior to (and in anticipation of) achieving a stabilized level of rental revenue. In the case of the development of ancillary land, these risks are managed by not commencing construction until a satisfactory level of pre-leasing is achieved. Overall, these risks are managed by ensuring that Properties Under Development do not represent a large component of the REIT's GBV. As at March 31, 2007, the cost of Properties Under Development was equivalent to 3.0% of the REIT's GBV.

### ***Taxation Risk***

On October 31, 2006, the Minister of Finance (Canada) announced proposed changes to the taxation of income trusts. On December 21, 2006, the Ministry introduced the related draft legislation, under which qualifying REITs are excluded from the proposed changes, provided they meet a series of conditions relating to the nature of their income and investments. The Notice of Ways and Means Motion that accompanied the Federal Budget announced on March 19, 2007, proposed modifications to the draft legislation. Consistent with normal Canadian REIT practice, the REIT holds units in a management trust and engages in third party property management. As a result, the REIT may not be a qualifying REIT under the draft legislation. While the REIT may be able to restructure its operations and assets to become a qualifying REIT under the draft legislation, there can be no assurance in this regard. While Management does not believe this was the intended outcome of the draft legislation, there can be no assurance that the draft legislation will be amended to accommodate normal Canadian REIT practice. Further, the Minister of Finance introduced guidelines for permitted normal growth (measured by the issuance of new equity) for non-exempt income trusts which, if exceeded, will cause an income trust to lose its four year tax holiday. To date, the REIT has not exceeded the normal growth guidelines, but may exceed those guidelines by August, 2007, if the current percentage participation in the Dividend Reinvestment Plan is maintained. It is the intention of REIT to pursue an internal restructuring and/or apply for relief from the Canada Revenue Agency to avoid the application of the normal growth rules. However, there can be no assurance that such relief will be forthcoming or that any restructuring will be effective, as further amendments to the proposed legislation are expected but have not yet been tabled.

## PART VII

### Subsequent Events

On March 14, 2007, the REIT announced an agreement to acquire Cité Multimédia, an urban office campus in Old Montreal, for a purchase price of \$242,000 and a concurrent public offering on bought-deal basis of 4,825,000 units at a price of \$20.75 per unit for gross proceeds of just over \$100,000.

On April 5, 2007, the REIT completed the acquisition of 106 Front Street East, a 34,497 square-foot Class I office property in downtown Toronto with 16 surface parking spaces, for a purchase price of \$8,000.

On April 12, 2007, the REIT completed the public offering on a bought-deal basis of 4,825,000 units at a price of \$20.75 per unit for gross proceeds of just over \$100,000.

On April 18, 2007, the REIT completed the acquisition of Cité Multimédia, an urban office campus in Old Montreal.

## PART IX

### Property Table

March 31, 2007 Properties	Office GLA	Retail GLA	Total GLA	% Total GLA	Office Vacant	Retail Vacant	Total Leased	Leased %
<i>The Castle</i>	109,046	34,323	143,369		4,087	-	139,282	97.1%
<i>905 King W</i>	103,054	9,832	112,886			600	112,286	99.5%
<b>King West</b>	<b>212,100</b>	<b>44,155</b>	<b>256,255</b>	<b>7.26%</b>	<b>4,087</b>	<b>600</b>	<b>251,568</b>	<b>98.2%</b>
<i>468 King W</i>	65,039	-	65,039		-	-	65,039	100.0%
<i>425-439 King W</i>	74,053	25,134	99,187		-	-	99,187	100.0%
<i>441-443 King West</i>	6,820	3,065	9,885		-	-	9,885	100.0%
<i>445-455 King W</i>	27,565	23,048	50,613		-	-	50,613	100.0%
<i>469 King W</i>	62,594	11,250	73,844		-	-	73,844	100.0%
<i>King-Brant Parking</i>	-	-	-		-	-	-	
<i>500-522 King W</i>	94,945	27,705	122,650		-	-	122,650	100.0%
<i>602-606 King W</i>	37,299	23,113	60,412		-	-	60,412	100.0%
<i>420 Wellington W</i>	33,813	3,137	36,950		-	-	36,950	100.0%
<i>425 Adelaide W</i>	74,008	4,104	78,112		10,114	-	67,998	87.1%
<i>579 Richmond W (+ Land)</i>	29,311	-	29,311		-	-	29,311	100.0%
<i>141 Bathurst (+ Land)</i>	10,521	-	10,521		-	-	10,521	100.0%
<i>662 King West</i>	29,691	2,126	31,817		-	-	31,817	100.0%
<b>King West Central</b>	<b>545,659</b>	<b>122,682</b>	<b>668,341</b>	<b>18.93%</b>	<b>10,114</b>	<b>-</b>	<b>658,227</b>	<b>98.5%</b>
<i>116 Simcoe</i>	13,819	-	13,819		-	-	13,819	100.0%
<i>200 Adelaide W</i>	28,024		28,024		-	-	28,024	100.0%
<i>208-210 Adelaide W</i>	12,330		12,330		-		12,330	100.0%
<i>312 Adelaide W</i>	63,904	7,891	71,795		-	4,402	67,393	93.9%
<i>331-333 Adelaide W</i>	20,951	3,209	24,160		-	-	24,160	100.0%
<i>358-360 Adelaide W</i>	54,249	-	54,249		27,246		27,003	49.8%
<i>134 Peter</i>	29,218	19,804	49,022		-	3,666	45,356	92.5%
<i>364 Richmond W</i>	21,300	17,300	38,600		-	-	38,600	100.0%
<i>82 Peter</i>	38,623	8,287	46,910		-	-	46,910	100.0%
<i>388 King W</i>	32,529	11,765	44,294		-	-	44,294	100.0%
<i>99 Spadina</i>	39,267	12,613	51,880		-	-	51,880	100.0%
<i>185 Spadina</i>	55,814	-	55,814		-	-	55,814	100.0%
<i>217-225 Richmond W</i>	34,877	21,684	56,561		-	-	56,561	100.0%
<b>Entertainment District</b>	<b>444,905</b>	<b>102,553</b>	<b>547,458</b>	<b>15.51%</b>	<b>27,246</b>	<b>8,068</b>	<b>512,144</b>	<b>93.5%</b>
<i>67 Richmond W</i>	44,870	5,794	50,664		2,339	-	48,325	95.4%
<i>193 Yonge</i>	32,966	16,318	49,284		-	-	49,284	100.0%
<b>Downtown</b>	<b>77,836</b>	<b>22,112</b>	<b>99,948</b>	<b>2.83%</b>	<b>2,339</b>	<b>-</b>	<b>97,609</b>	<b>97.7%</b>
<i>35-39 Front E</i>	30,811	16,606	47,417		-	-	47,417	100.0%
<i>41-45 Front E</i>	19,799	13,735	33,534		-	-	33,534	100.0%
<i>50 Wellington E</i>	21,144	11,049	32,193		-	-	32,193	100.0%
<b>St. Lawrence Market</b>	<b>71,754</b>	<b>41,390</b>	<b>113,144</b>	<b>3.21%</b>	<b>-</b>	<b>-</b>	<b>113,144</b>	<b>100.0%</b>
<i>Queen Richmond Centre</i>	175,081	48,818	223,899		-	-	223,899	100.0%
<i>230 Richmond E</i>	62,514	-	62,514		29,851	-	32,663	52.2%
<i>145 Berkeley</i>	7,938	2,687	10,625		-	-	10,625	100.0%
<i>489 Queen E</i>	32,592	-	32,592		-	-	32,592	100.0%
<b>Queen Richmond</b>	<b>278,125</b>	<b>51,505</b>	<b>329,630</b>	<b>9.34%</b>	<b>29,851</b>	<b>-</b>	<b>299,779</b>	<b>90.9%</b>
<i>QRC South</i>	44,600	-	44,600		18,770	-	25,830	57.9%
<i>257 Adelaide W</i>	40,050	5,843	45,893		12,890	5,843	27,160	59.2%
<i>47 Fraser</i>	11,626	-	11,626		11,626	-	-	0.0%
<i>47A Fraser</i>	18,111	-	18,111		18,111	-	-	0.0%
<b>PUD</b>	<b>114,387</b>	<b>5,843</b>	<b>120,230</b>	<b>3.41%</b>	<b>61,397</b>	<b>5,843</b>	<b>52,990</b>	<b>44.1%</b>
Toronto Including PUD	1,744,766	390,240	2,135,006	60.49%	135,034	14,511	1,985,461	93.0%
<b>Toronto Excluding PUD</b>	<b>1,630,379</b>	<b>384,397</b>	<b>2,014,776</b>	<b>57.08%</b>	<b>73,637</b>	<b>8,668</b>	<b>1,932,471</b>	<b>95.9%</b>

<b>March 31, 2007</b>	<b>Office</b>	<b>Retail</b>	<b>Total</b>	<b>% Total</b>	<b>Office</b>	<b>Retail</b>	<b>Total</b>	<b>Leased %</b>
<b>Properties</b>	<b>GLA</b>	<b>GLA</b>	<b>GLA</b>	<b>GLA</b>	<b>Vacant</b>	<b>Vacant</b>	<b>Leased</b>	
<i>425 Viger W</i>	205,314	820	206,134		-	-	206,134	100.0%
<i>451-481 Saint Catherine</i>	20,805	9,634	30,439		-	-	30,439	100.0%
<i>3575 Saint-Laurent</i>	164,797	17,464	182,261		7,707	-	174,554	95.8%
<i>4446 Saint-Laurent</i>	72,613	10,000	82,613		1,354	-	81,259	98.4%
<i>Adjacent Land (PUD)</i>	-	-	-		-	-	-	
<i>6300 Avenue du Parc</i>	217,022	950	217,972		9,508	-	208,464	95.6%
<i>400 Atlantic</i>	86,034	-	86,034		7,775	-	78,259	91.0%
<b>Montreal</b>	<b>766,585</b>	<b>38,868</b>	<b>805,453</b>	<b>22.82%</b>	<b>26,344</b>	<b>-</b>	<b>779,109</b>	<b>96.7%</b>
<i>115 Bannatyne</i>	39,310	-	39,310		-	-	39,310	100.0%
<i>50-70 Arthur</i>	110,918	10,500	121,418		7,325	-	114,093	94.0%
<i>250 McDermot</i>	41,446	10,200	51,646		4,595	-	47,051	91.1%
<i>138 Portage East</i>	43,960	-	43,960		6,500	-	37,460	85.2%
<i>309 Hargrave</i>	21,460	1,400	22,860		4,929	-	17,931	78.4%
<i>165 Garry</i>	4,400	10,362	14,762		-	-	14,762	100.0%
<i>1500 Notre Dame</i>	111,400	-	111,400		3,300	-	108,100	97.0%
<b>Winnipeg</b>	<b>372,894</b>	<b>32,462</b>	<b>405,356</b>	<b>11.48%</b>	<b>26,649</b>	<b>-</b>	<b>378,707</b>	<b>93.4%</b>
<i>390 Charest</i>	66,771	6,348	73,119		700	-	72,419	99.0%
<i>410 Charest</i>	-	24,937	24,937		-	1,300	23,637	94.8%
<i>430 Charest</i>	44,051	13,285	57,336		500	-	56,836	99.1%
<i>622 Saint Joseph</i>	3,620	3,300	6,920		-	-	6,920	100.0%
<i>633 Saint Joseph</i>	15,558	6,000	21,558		-	-	21,558	100.0%
<b>Quebec City</b>	<b>130,000</b>	<b>53,870</b>	<b>183,870</b>	<b>5.21%</b>	<b>1,200</b>	<b>1,300</b>	<b>181,370</b>	<b>98.6%</b>
Total Including PUD	3,014,245	515,440	3,529,685	100.00%	189,227	15,811	3,324,647	94.2%
<b>Total Excluding PUD</b>	<b>2,899,858</b>	<b>509,597</b>	<b>3,409,455</b>	<b>96.59%</b>	<b>127,830</b>	<b>9,968</b>	<b>3,271,657</b>	<b>96.0%</b>