



H&R Real Estate Investment Trust

Insight beyond the rating.

RATING

<u>Current</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
STA-3 (high)	STA-3 (high)	STA-3 (high)	STA-3 (high)	STA-3 (high)	NR

STABILITY RATING SUMMARY

Legend: Superior Moderate Weak

Operating Characteristics	Asset Quality	Financial Profile	Diversification	Size & Market Position	Sponsorship & Governance	Growth

STABILITY RATING RATIONALE

DBRS has today confirmed the rating of H&R Real Estate Investment Trust (H&R or the Trust) at STA-3 (high). H&R's rating continues to be supported by stable cash flows from long average-lease maturities with quality tenants.

H&R continued its solid pace of growth in 2006, acquiring \$963 million of properties and increasing leasable area by 20%, although recent acquisitions have resulted in somewhat higher leverage given that valuations for attractive real estate continued to rise through 2006. However, as expected, H&R's payout ratio based on cash available for distribution returned to more-normal levels of 94% in 2006 despite a slight 2.3% increase in distributions. That was a decline from 2005 when the Trust paid out more than 100%, due to higher-than-usual leasing costs and maintenance capex. In 2007, DBRS expects H&R's payout ratio to remain manageable at 90% of cash

available after considering a 2.7% increase in cash distributions to \$1.37.

Looking forward, H&R is expected to increase its focus on development, specifically The Bow office complex in Calgary. The Bow is a \$1.1 billion project comprising a 59-story, 1.84 million square foot class-AAA office tower in the city's downtown core. DBRS notes that although this is a substantial development for H&R that is expected to place pressure on credit metrics during the construction phase, there are several factors that mitigate some of the usual risks of development. So far, DBRS is satisfied that the transaction remains within the parameters of the current rating. However, if major assumptions change (including the securing of a fixed cost for construction and/or changes in the terms of financing and lease terms), then it could have implications for the rating. (Continued on page 2.)

RATING CONSIDERATIONS

Strengths

- Long-term leases with average terms of 12.6 years
- Diversified portfolio with high-quality tenants
- High portfolio occupancy at over 99%

Challenges

- Limited internal growth opportunities
- Coverage ratios at lower end of peer group
- Portfolio concentration in Ontario and Alberta

FINANCIAL INFORMATION

	<u>3 mos. to</u>	<u>3 mos. to</u>	<u>For the year ended December 31</u>				
	<u>Dec. 31</u>	<u>Dec. 31</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Declared distributions per unit (\$)	0.33	0.33	1.33	1.30	1.24	1.22	1.20
Cash available for distribution per unit (\$)	0.32	0.30	1.42	1.21	1.38	1.36	1.28
Net income before extras, per unit (\$)	0.16	0.18	0.69	0.79	1.00	1.15	1.18
Total debt/total capital	66.8%	65.3%	66.8%	65.3%	66.1%	63.3%	61.8%
Cash flow/total debt	0.06	0.06	0.06	0.06	0.06	0.06	0.08
EBITDA interest coverage	2.11	2.09	2.03	2.03	2.10	2.07	2.27
Cash flow return on average equity	12.3%	12.9%	12.8%	13.0%	13.1%	12.5%	13.2%
Declared distributions/cash avail. for distribution	100.5%	109.9%	93.8%	109.3%	90.9%	91.2%	93.9%
Market capitalization (CAD millions)	3,001.2	2,301.0	3,001.2	2,301.0	1,786.5	1,369.7	946.7

THE TRUST

H&R REIT owns 292 properties diversified across the office (34), industrial (115) and retail (143) segments in Canada and the United States, totalling over 41 million square feet. The Trust also has development activities with a potential leasable area of 2.0 million square feet.



STABILITY RATING RATIONALE

(Continued from page 1.)

One mitigating factor is that the Bow is 100% pre-leased to Encana Corporation for 25 years, which significantly reduces exposure to the real estate market risk in Calgary, including any potential downturn in the energy sector or the risk of competing new supply.

The triple-net lease with a quality tenant, Encana (rated A (low) by DBRS) that escalates by 1.5% annually should ensure stable cash flows. As well, H&R plans to enter into a fixed-price construction contract that should reduce the risk of cost overruns in a labour-constrained market.

Looking forward, based upon DBRS' preliminary assumptions, the project is expected to result in a

decline in EBITDA interest-coverage ratios during construction to 1.7 to 1.8 times by late 2009 and into 2010. Excluding capitalized interest costs, interest coverage is expected to remain relatively stable at just over 2.0 times, supported by H&R's long-term lease profile, which averages over 12 years, among the highest of its peers.

H&R has improved geographic diversification by increasing its presence in the United States. However, DBRS notes that further significant expansion into the United States could risk H&R's tax-exempt status as a REIT under recently proposed tax rules for income trusts, and that could limit future growth.

OPERATING CHARACTERISTICS

Strengths

- H&R has long average-lease terms of 12.6 years, while lease maturities are minimal at 12.1% for the next five years in aggregate. The average lease terms are among the highest of any REIT rated by DBRS and are a key factor in the stability of H&R's cash flow.
- Most of the portfolio comprises single-tenant properties under long-term triple-net leases. They provide stable cash flows and assure cost recovery of almost all property expenses including maintenance capital.
- Portfolio occupancy has been consistently high at 99% or higher for the past five years. Despite difficulties in the Canadian office market, H&R has managed to maintain a high office occupancy rate above 95%, given that many of its office properties are occupied by single tenants under long-term leases.
- H&R's portfolio is diversified by asset with office at 48% of net operating income (NOI), industrial at 31% and retail at 21%. The industrial and retail segments have increased in importance in recent years and now contribute 52% of NOI between them, up from 40% in 2002. That is considered positive as these asset types tend to provide more stable cash flows over the long term.
- H&R is one of the largest REITs in Canada with a portfolio comprising 41 million square feet and market capitalization of \$3.1 billion, giving it access to lower-cost capital to fund growth. H&R's acquisitions in recent years have translated into steadily growing cash distributions.

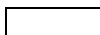
Superior

Challenges

- Internal growth is limited to contractual rent increases in existing leases. This could be offset by lower net rents achieved when re-leasing office space. H&R has some multi-tenant office properties that have experienced weakness and require capital investment to reposition the properties and improve performance.
- There is tenant concentration as Bell Canada, Bell Mobility Cellular Inc., TransCanada PipeLines Limited and Telus Communications account for 26% of the Trust's total gross rents, although the credit quality of these tenants is solid at A (low) or higher, as rated by DBRS. The strong negotiating position of larger tenants in single-tenant properties may limit the ability to increase net rents. However, most of these long-term leases have built-in rent steps.
- The portfolio is concentrated in Ontario and Alberta, representing 53% of the total leasable area. In particular, the office market in Ontario, at 15% of total space, has been difficult in recent years and could continue to place downward pressure on NOI growth.
- A rapid expansion into the United States has resulted in that country comprising 32% of the Trust's leasable space. That increases the risk of understanding the local markets (supply and demand) and understanding the tenant. H&R attempts to mitigate these risks through long-term leases with quality tenants. Although H&R appears to be exempt so far, a further significant expansion into the United States could be curtailed since under the proposed tax rules for income trusts, H&R may eventually lose its exemption from income taxes as a REIT.



ASSET QUALITY



Superior

- The Superior rating for asset quality reflects H&R's commercial real estate properties, which have long operating lives and require minimal maintenance capex compared with other asset classes. H&R's portfolio also benefits from a low average age of 12.1 years.
- The Trust has a majority of tenants under triple-net leases, which allows it to recover most of the property expenses, including maintenance capex.
- Over the past two years, the Trust has experienced higher tenant costs and capital spending related to its multi-tenant office properties as it repositions properties in order to improve future performance. This additional capital spending is expected to be largely completed in 2008.

FINANCIAL PROFILE



Moderate

	3 mos. to		For the year ended December 31				
	Dec. 31	Dec. 31	2006	2005	2004	2003	2002
(CAD thousands)							
Net income (before extras.)	21,117	18,738	63,384	59,779	67,486	84,603	81,032
Depreciation and amortization	27,434	24,838	112,405	90,302	66,012	23,799	19,457
Other non-cash (incl. non-controlling interest)	(3,177)	(3,696)	6,061	6,508	1,618	0	0
Cash Flow from Operations	45,374	39,880	181,850	156,589	135,116	108,402	100,489
Leasing costs and maintenance capex (1)	(5,565)	(6,913)	(13,699)	(31,192)	(10,155)	(6,756)	(10,681)
Cash Available for Distribution	39,809	32,967	168,151	125,397	124,961	101,646	89,808
Gross cash distributions (2)	(39,384)	(35,689)	(155,374)	(135,205)	(112,698)	(92,499)	(84,318)
Cash Available after Distributions	425	(2,722)	12,777	(9,808)	12,263	9,147	5,490
Change in working capital	1,213	(5,275)	(12,618)	(46,172)	(3,078)	(6,761)	(12,229)
Free Cash Flow	1,638	(7,997)	159	(55,980)	9,185	2,386	(6,739)
(Acquisitions)/dispositions	(263,549)	(66,913)	(783,842)	(362,130)	(420,797)	(351,433)	(363,687)
Other investments	(1,372)	(1,123)	(19,716)	22,041	(24,400)	(35,191)	(7,283)
Cash Flow Before Financing	(263,283)	(76,033)	(803,399)	(396,069)	(436,012)	(384,238)	(377,709)
Equity financing (net)	151,587	148,406	288,680	262,004	63,700	214,035	13,043
Debt financing (net)	110,149	(76,924)	521,238	136,743	359,402	179,536	350,543
Net Change in Cash	(1,547)	(4,551)	6,519	2,678	(12,910)	9,333	(14,123)
Key Financial Ratios							
Total debt/total capital	66.8%	65.3%	66.8%	65.3%	66.1%	63.3%	61.8%
Total debt/gross book value	61.0%	60.8%	62.0%	62.1%	62.6%	60.9%	59.3%
Cash flow/total debt	0.06	0.06	0.06	0.06	0.06	0.06	0.08
EBITDA interest coverage	2.11	2.09	2.03	2.03	2.10	2.07	2.27
EBIT interest coverage	1.54	1.49	1.40	1.44	1.56	1.84	2.02

(1) Includes leasing costs and non-recoverable maintenance capex.

(2) Includes cash distributions to unitholders and Class B Master LP units.

Summary

- As expected, H&R's cash available for distribution exhibited growth in 2006 that resulted in positive cash available after cash distributions, after a slight shortfall in 2005 that was caused by higher-than-usual leasing costs and maintenance capex related to its multi-tenant office portfolio. DBRS expects this positive trend to continue in 2007 as capital spending is expected to be just below 2006 levels at approximately \$12 million.
- H&R's leasing costs (including tenant inducements) were approximately \$7.7 million in 2006, while non-recoverable maintenance capex was \$6 million. The upgrades of several multi-tenant office properties is expected to continue in 2007, although leasing costs are expected to be more modest in 2007.
- H&R's leverage remained reasonably stable in 2006 with debt-to-gross book value of 62% remaining acceptable for the rating and within H&R's limit of 65%. H&R financed acquisitions totalling \$963.4 million in 2006 using equity issues totalling \$276 million, \$24 million through reinvested distributions and options, and just under \$700 million of assumed debt.
- EBITDA interest coverage remains just over two times, at the lower end of comparable REITs. This is acceptable given the scale and stability in cash flows from H&R's portfolio.
- H&R's payout ratio based on cash flow from operations improved slightly to 85.4% in 2006



from 86.3% in 2005, despite a modest increase of 2.6% in cash distributions in 2006. The improvement in payout ratio based upon cash available for distribution was more significant, falling to 94% from 109% as leasing costs and maintenance capex declined.

Outlook

- DBRS expects H&R to maintain leverage between 60% and 65% of gross book value, excluding the Bow development, which is expected to result in EBITDA interest coverage remaining just over two times.
- H&R will require changes to its current 65% limit to allow the Bow to be excluded from this leverage calculation (although debt related to the Bow may have recourse to H&R).
- If we include the Bow development and assume it is 80% debt-financed (approximately \$800 million in project debt), H&R's consolidated leverage will increase to 66% to 67% of gross book value, while interest coverage including capitalized interest is likely to decline to 1.7 to 1.8 times in 2010 when interest from construction financing reaches its peak.
- Although these metrics are approaching low levels for the current rating, as discussed below, there are several mitigating factors including the pre-leasing of 100% of the project to a solid investment-grade tenant, Encana.
- DBRS expects the payout ratio in 2007 to be approximately 90% of cash available for distribution, reflecting a 2.7% increase in cash distributions to \$1.37 per unit from \$1.33 in 2006.

LONG-TERM DEBT MATURITIES AND BANK LINES

(As at Dec. 31, 2006)	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Thereafter</u>	<u>Total</u>
Maturing debt (\$ thousands)	120.2	157.2	127.5	116.2	163.9	2,351.4	3,036.4
% of maturing debt	4.0%	5.2%	4.2%	3.8%	5.4%	77.4%	100.0%

Debt Outstanding

(C\$ millions)	<u>Interest</u>	
	<u>rate</u>	<u>Amount</u>
Secured mortgage debt	6.4%	3,036.4
Bank facility		70.8
Total Debt		<u><u>3,107.2</u></u>

Liquidity

	<u>Limit</u>	<u>Used</u>	<u>Available</u>
Cash and cash equivalents			15.8
Bank facility	180.0	70.8	109.2
Total			<u><u>125.0</u></u>

- H&R's debt comprises mainly secured mortgages, most (97.7%) with fixed rates and an average interest rate of 6.4%. H&R has low average-debt maturities due to its relatively long-term debt with an average remaining term-to-maturity of 11.1 years, which is closely aligned to average lease maturities.
- Approximately 55% of total debt is non-recourse to the Trust, which limits exposure of the remainder of the assets in the portfolio. H&R has used higher leverage of up to 70% to 75% of gross book value for properties secured using non-recourse debt.
- In 2006, in order to increase financial flexibility, H&R eliminated a requirement that Debt with recourse to the Trust be limited to 60% of the gross book value of those assets having recourse.
- H&R currently has drawn \$70.8 million on its \$180 million bank facility for recent acquisitions.
- As discussed below, H&R will be arranging approximately \$800 million in subsidiary debt to finance construction of the Bow office development in Calgary.



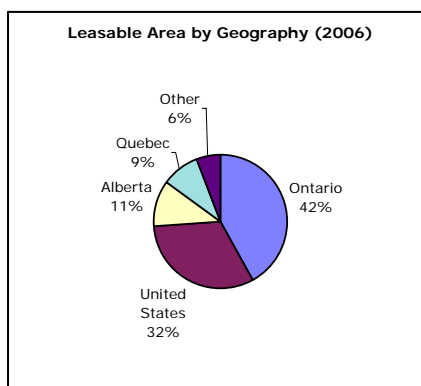
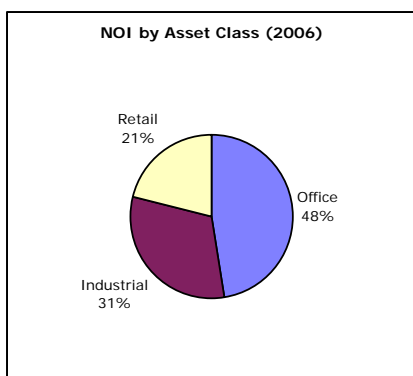
THE BOW OFFICE DEVELOPMENT (CALGARY)

- The Bow represents a significant project for H&R over the next five years with Phase 1 comprising a 1.84 million square foot office tower in downtown Calgary at a projected cost of \$1.1 billion (completion for fall 2011). The building will be 100% leased to Encana for 25 years, among the largest leasing transaction ever in Canada.
- Given the scale of the Bow, H&R is requesting that unitholders permit a carve-out for the purposes of calculating its debt-to-gross book value limit of 65% within its Trust Indenture. H&R is expected to finance the Bow with up to 80% leverage, which is expected to result in consolidated debt-to-gross book value increasing to 67% to 68%. The construction financing may have recourse to H&R to reduce interest costs for close to \$800 million in project debt. DBRS expects that, as a result, interest-coverage ratios could decline to 1.7 to 1.8 times in late 2009 and 2010 on a consolidated basis as construction progresses toward completion in 2011. Excluding the Bow, H&R is expected to maintain EBITDA interest coverage of 2.0 times.
- Normally such a significant development project would materially increase H&R's risk profile given the scale of investment (22% of current gross book value of assets) and negative cash flow during construction. However, H&R has so far mitigated many of the usual development risks from a credit perspective. The project is also consistent with H&R's overall strategy of entering into long-term leases with solid credit-quality tenants, thereby enhancing long-term cash-flow stability.
- First, the project is 100% pre-leased to a solid credit tenant, Encana (rated A (low) by DBRS), under a triple-net lease for 25 years at an agreed upon net rental rate of \$36.37 per square foot, including annual rent steps of 1.5%. The total expected NOI beginning in 2011 is \$71.3 million (including 700 parking spaces at \$450 per month), representing an initial capitalization rate of 6.25%, in line with current market values in Calgary. (The average NOI over the 25-year lease is \$85.7 million).
- Encana will represent the Trust's largest tenant on a pro forma basis, at 15% of rental income. It will also help diversify the Trust's tenant list. Telecom now represents 19.4% of total Trust revenue, through Bell Canada, Bell Mobility and Telus. Encana will, however, result in some concentration in a single tenant within the cyclical energy sector.
- From a credit perspective, the following are key: (a) H&R secures a fixed-cost construction contract, given the length of the project and shortage of labour in the Alberta market which could materially drive up costs. One positive is that Encana has agreed to be responsible for 100% of tenant improvements and will bear all cost increases or savings related to change orders; (b) it is important that H&R is able to secure long-term financing at interest rates that will ensure cash-flow accretion and stability in cash flow throughout much of the 25-year term of the Encana lease.

DIVERSIFICATION



Moderate



- Diversification of the Trust is considered Moderate due to some concentration in the following areas:
 - Geographically, the portfolio is focused on Ontario, which represents 42% of leasable area.
 - Bell Canada, TransCanada PipeLines Limited, Bell Mobility Cellular Inc. and



Telus are the dominant tenants for the Trust, representing 26% of total rental revenue.

- The Trust, however, mitigates such concentration through strong property diversification, having one of the largest portfolios among Canadian REITs with 292 properties (190 in Canada and 102 in the

United States) comprising 41 million square feet, thereby reducing exposure to any one property and enhancing cash-flow stability.

- H&R is also diversified by asset type, with exposure to office (48% of NOI), industrial (31%) and retail (21%).

SIZE & MARKET POSITION



Superior

- The Trust is one of the largest REITs in Canada, with a market capitalization of \$3.1 billion and a portfolio of 292 properties comprising over 41 million square feet of leasable area.
- The industrial portfolio benefits from its large scale with 115 properties having 23.3 million square feet, allowing it to accommodate changing tenant requirements.
- The office portfolio is moderate in size, while the retail portfolio is relatively small compared with other Canadian REITs. The Trust, however continues to increase the scale of its retail portfolio, especially in the United States.
- The Trust's large size improves diversification and provides better access to capital.

SPONSORSHIP & GOVERNANCE



Moderate

- There are currently six trustees, five of whom are independent of the Trust and provide third-party advice.
- The Trust has an external property management agreement with H&R Property Management Ltd., which provides property services to the Trust for prescribed fees. In 2006, H&R's fees were reduced as follows: (a) property management fees were reduced to 2% of gross rental revenue (from 3%), and (b) asset management fees are now two-thirds of 1% (from 1%) of the value of acquisitions and project development.
- Management of H&R as a group owns approximately 1% of the outstanding Trust units. Thomas Hofstедter, president and CEO, owns or controls approximately 0.5 million units and indirectly has an interest in 0.7 million Class B units (exchangeable into units at any time).

GROWTH



Moderate

	<u>3 mos. to</u>		<u>3 mos. to</u>				
	<u>Dec. 31</u>		<u>Dec. 31</u>				
	<u>2006</u>	<u>2005</u>	<u>For the year ended December 31</u>				
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Trust units outstanding as at (thousands)	124,585	110,624	124,585	110,624	96,306	86,198	70,911
Weighted-average trust units (basic) (thousands)	121,618	107,865	116,362	102,404	89,591	74,676	70,289
Net income before extras. per unit (\$)	0.16	0.18	0.69	0.79	1.00	1.15	1.18
Cash flow from operations per unit (\$)	0.37	0.37	1.56	1.53	1.51	1.45	1.43
Cash available for distribution per unit (\$)	0.32	0.30	1.42	1.21	1.38	1.36	1.28
Declared distributions per unit (\$)	0.33	0.33	1.33	1.30	1.24	1.22	1.20
Declared distributions/cash avail. for distribution	100.5%	109.9%	93.8%	109.3%	90.9%	91.2%	93.9%
Declared distributions/cash flow from operations	86.8%	89.5%	85.4%	86.3%	83.4%	85.3%	83.9%

- Cash flow from operations on a per unit basis grew by 2% in 2006. It was flat in Q4 2006 despite significant acquisitions due to dilution from the timing of equity issues, including \$150.5 million on November 8, 2006.
- Cash flow per unit is expected to increase further in 2007, but the continued rise in real estate valuations through 2006 has resulted in acquisitions becoming somewhat less accretive than the past.
- As expected, cash available for distribution per unit experienced solid growth of 17% in 2006 to \$1.42, after declining in 2005 due to a temporary increase in leasing costs and maintenance capex. The higher spending related to the negotiation of several large single-tenant leases including Bell Canada, Bell Mobility and TELUS, and higher capex to improve the positioning of H&R's multi-tenant office properties, which have experienced some weakness.



- As a result, H&R's payout ratio returned to closer to previous levels – below 100% of cash available for distribution – despite a 2.3% increase in cash distributions in 2006.
- Looking forward, H&R's payout ratio is expected to remain manageable at approximately 90% after including another 2.7% increase in cash distributions at the beginning of 2007. Leasing costs and maintenance capital spending are expected to moderate further, while accretive acquisitions in 2006 and internal growth from contractual rent steps contribute to overall growth.
- However, internal growth is constrained by the very low portfolio vacancy rate of 1% and the minimal lease maturities over the next five years.

THE PORTFOLIO

(As at Dec. 31, 2006)

	Office	Industrial	Retail	Total
Leasable area (thousands of sq. ft.)	8,002	23,254	10,123	41,379
% of leasable area	19.3%	56.2%	24.5%	100.0%
Number of properties	34	115	143	292
Occupancy	98.6%	99.9%	99.7%	99.6%
Average rent per square foot (\$)	18.61	5.17	11.69	9.35
Average age of buildings (years)	16.2	13.1	10.5	12.1

- H&R has one of the largest portfolios of any Canadian REIT. Acquisitions contributed to a 20% growth in leasable area through 2006 to just over 41 million square feet and 292 properties.
- The industrial and retail segments, which tend to be more stable through cycles, have grown in importance in recent years with the leasable area for industrial growing by 17% in 2006 and retail growing by 47%. Office still represents 48% of NOI (with industrial 31% and retail 21%), although this is down from 55% two years ago.
- The geographic focus for growth has been the United States, where H&R's portfolio increased by 28% to 13.2 million square feet, or approximately 32% of leasable area. Despite the potential increased risk from competitive pressures in the United States, most of H&R's recent acquisitions have been focused on single-tenant industrial and retail properties under long-term leases.
- Major acquisitions for H&R in 2006 included the following: (a) two Canadian Tire distribution centres for \$229 million, totalling 2.1 million square feet, located in Brampton, Ontario, and Calgary. The facilities are under long-term leases of 21 years, which should provide stable cash flows from this quality tenant; (b) Telus office tower in Burnaby, British Columbia for \$151 million leased for 20 years; (c) 33 retail properties mainly in Ontario for \$242 million, having 1.5 million square feet. The average levered returns for all 2006 acquisitions was 9.4%.

PORTFOLIO OCCUPANCY

	As at December 31					
	2006	2005	2004	2003	2002	2001
Office	98.6%	98.2%	97.5%	96.0%	97.0%	97.0%
Industrial	99.9%	99.5%	100.0%	99.0%	100.0%	100.0%
Retail	99.7%	99.9%	99.9%	100.0%	99.0%	99.0%
Total portfolio	99.6%	99.3%	99.4%	99.0%	99.0%	99.0%

- H&R has maintained consistently high occupancy levels at 99% or higher despite difficulties in the multi-tenant office segment in southern Ontario.
- DBRS expects the Trust's occupancy levels to remain stable given H&R's long-term average leases with many single-tenant properties. Most of its industrial properties are occupied by single tenant, and 20 of 34 office properties are single tenant.



LEASE MATURITIES BY ASSET TYPE

(As at Dec. 31, 2006)	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Total</u>
Office	0.2%	0.6%	0.9%	0.6%	0.7%	3.0%
Industrial	1.0%	2.7%	2.3%	1.0%	0.9%	7.9%
Retail	0.1%	0.2%	0.4%	0.3%	0.2%	1.2%
Total	1.3%	3.5%	3.6%	1.9%	1.8%	12.1%

- Lease maturities are well spread out at 1.3% to 3.6% per annum, and the average lease term is 12.6 years.
- In 2006, overall average rent per square foot across H&R's portfolio decreased by 3% to \$9.35 per square foot, due to the change in asset mix, with greater exposure to industrial and retail, two asset classes that tend to have lower net rents. In-place net rent for offices improved by 4.8% due mainly to contractual rent-steps for leases with TransCanada and Telus beginning in May 2006, while office acquisitions were relatively modest (3% increase in office space).
- Looking ahead, the minimal lease maturities should contribute to stability in cash flow and limit exposure over the next few years to changes in market rents.

TENANT PROFILE

(As at Dec. 31, 2006)	<u>% of rental revenue</u>	<u>Lease term to maturity (years)</u>
Tenants		
Bell Canada	8.9%	17.8
TransCanada PipeLines Limited	6.6%	14.0
Bell Mobility	5.3%	19.0
Telus Communications	5.2%	14.8
RONA Inc.	3.9%	13.0
Canadian Tire Corporation	3.5%	19.3
Royal Bank of Canada	2.8%	4.5
Lowe's Companies Inc.	2.5%	12.3
Nestlé Canada Inc.	2.1%	10.8
Shell Oil Products	1.8%	15.8
Total	42.6%	

- There is some concentration among the top five tenants, accounting for 30% of rental revenue, although this has decreased in recent years as H&R has increased its scale. A mitigating factor is the high credit quality of these tenants, rated BBB (high) to A by DBRS.
- The remaining tenants are well diversified, are nationally recognized and have long-term leases. The top ten tenants' average lease term is about 14.1 years.
- Many of the properties occupied by top tenants have non-recourse debt including TransCanada PipeLines Limited, Bell Mobility Cellular Inc., Lowe's Companies Inc., and TELUS Communications Inc.



H&R Real Estate Investment Trust

Balance Sheet

(CAD millions)

	As at December 31			Liabilities & Equity	Sept. 30			As at December 31		
	2006	2005	2004		2006	2005	2004			
Assets										
Cash & short-term investments	15.8	9.3	6.6	Mortgage debt	3,036.4	2,396.9	2,053.2			
Income properties	4,136.6	3,383.5	3,145.0	Bank debt	71.0	67.1	89.5			
Land under development	30.2	2.6	0.0	Other liabilities	59.4	55.1	61.6			
Intangible assets	401.2	271.4	0.0	Intangible liabilities	68.4	17.4	0.0			
Accounts receivable	90.7	65.1	4.9	Non-controlling interest	112.9	116.7	119.5			
Mortgages receivable	16.1	24.0	54.8	Unitholders' equity	1,430.9	1,191.1	977.1			
Other assets	88.4	88.4	89.6							
Total Assets	4,779.0	3,844.3	3,300.9	Total Liab. & Equity	4,779.0	3,844.3	3,300.9			

Balance Sheet &

Liquidity Ratios

	3 mos. to		3 mos. to		For the year ended December 31					
	Dec. 31	Dec. 31	Dec. 31	Dec. 31	2006	2005	2004	2003	2002	2001
Total debt/total capital	66.8%	65.3%	66.8%	65.3%	66.1%	63.3%	61.8%	63.3%	61.8%	49.7%
Net debt/total capital	66.7%	65.2%	66.7%	65.2%	66.1%	63.0%	61.6%	63.0%	61.6%	48.8%
Total debt/gross book value assets	61.0%	60.8%	62.0%	62.1%	62.6%	60.9%	59.3%	60.9%	59.3%	48.0%
Secured debt/total debt	97.7%	97.3%	97.7%	97.3%	95.8%	96.6%	99.9%	96.6%	99.9%	99.7%
Cash flow/total debt	0.06	0.06	0.06	0.06	0.06	0.06	0.08	0.06	0.08	0.11

Coverage Ratios

EBITDA interest coverage	2.11	2.09	2.03	2.03	2.10	2.07	2.27	2.07	2.27	2.48
EBIT interest coverage	1.54	1.49	1.40	1.44	1.56	1.84	2.02	1.84	2.02	2.22

Profitability Ratios

Net rental margin	65.3%	65.5%	67.4%	66.0%	66.6%	64.5%	61.9%	64.5%	61.9%	63.2%
Cash flow return on average equity	12.3%	12.9%	12.8%	13.0%	13.1%	12.5%	13.2%	12.5%	13.2%	12.6%
Cash flow return on average capital	8.4%	8.9%	8.6%	8.8%	8.8%	9.0%	10.2%	9.0%	10.2%	10.4%
G&A/rental revenue	1.3%	0.7%	1.7%	1.4%	1.5%	1.5%	1.5%	1.5%	1.5%	1.8%

Operating Statistics

Net interest in GLA (thousands of sq. ft.)	41,389	34,443	41,389	34,443	30,107	24,461	17,753	24,461	17,753	13,534
Portfolio occupancy rate	99.6%	99.3%	99.6%	99.3%	99.4%	99.0%	99.0%	99.0%	99.0%	99.0%

Income Statement

(CAD thousands)

	3 mos. to		3 mos. to		For the year ended December 31					
	Dec. 31	Dec. 31	Dec. 31	Dec. 31	2006	2005	2004	2003	2002	2001
Income from properties	156,548	134,828	549,332	474,547	382,307	320,059	286,926	320,059	286,926	197,620
Operating expense	(54,370)	(46,562)	(179,317)	(161,571)	(127,863)	(113,561)	(109,398)	(113,561)	(109,398)	(72,668)
Net rental income	102,178	88,266	370,015	312,976	254,444	206,498	177,528	206,498	177,528	124,952
Interest income	548	232	1,843	1,951	8,104	7,864	6,584	7,864	6,584	13,114
General and administrative	(1,970)	(918)	(9,101)	(6,866)	(5,796)	(4,843)	(4,372)	(4,843)	(4,372)	(3,835)
EBITDA	100,756	87,580	362,757	308,061	256,752	209,519	179,740	209,519	179,740	134,231
Interest expense	(47,705)	(41,991)	(178,620)	(151,559)	(122,178)	(101,117)	(79,251)	(101,117)	(79,251)	(54,224)
Income before Non-Cash Items	53,051	45,589	184,137	156,502	134,574	108,402	100,489	108,402	100,489	80,007
Depreciation and amortization	(27,434)	(24,838)	(112,405)	(90,302)	(66,012)	(23,799)	(19,457)	(23,799)	(19,457)	(13,693)
Straight-line rent adjustment	(78)	2,671	17,025	20,758	22,406	1,585	1,585	1,585	1,585	1,585
Non-controlling interest	(1,663)	(1,925)	(5,511)	(6,333)	(1,076)	0	0	0	0	0
Income tax	(2,837)	(88)	(2,837)	(88)	0	0	0	0	0	0
Net Income before Extraordinary Items	21,039	21,409	80,409	80,537	89,892	86,188	82,617	86,188	82,617	67,899
Discontinued operations	(1,795)	(1,866)	0	0	(35)	0	0	0	0	0
Extraordinary items	20	3,939	6,028	6,116	(1,076)	4,365	1,405	4,365	1,405	795
Reported Net Income	19,264	23,482	86,437	86,653	88,781	90,553	84,022	90,553	84,022	68,694
Distributions declared	(39,384)	(35,689)	(155,374)	(135,205)	(112,698)	(92,499)	(84,318)	(92,499)	(84,318)	(67,770)
Net Remaining	(20,120)	(12,207)	(68,937)	(48,552)	(23,917)	(1,946)	(296)	(1,946)	(296)	924

Earnings per Trust Unit (Basic)

Weighted-average trust units (basic) (thousands)	121,618	107,865	116,362	102,404	89,591	74,676	70,289	74,676	70,289	58,242
Cash available for distribution per unit (\$)	0.32	0.30	1.42	1.21	1.38	1.36	1.28	1.36	1.28	1.18
Net income before extras. per unit (\$)	0.16	0.18	0.69	0.79	1.00	1.15	1.18	1.15	1.18	1.17
Reported net income per unit (\$)	0.16	0.22	0.74	0.85	0.99	1.21	1.20	1.21	1.20	1.18
Gross cash distributions per unit (\$)	0.32	0.33	1.34	1.32	1.26	1.24	1.20	1.24	1.20	1.16
Declared distributions per unit (\$)	0.33	0.33	1.33	1.30	1.24	1.22	1.20	1.22	1.20	1.16

Earnings per Trust Unit (Diluted)

Weighted-average trust units (diluted) (thousands)	122,481	108,521	117,146	103,055	90,198	75,232	70,810	75,232	70,810	58,606
Cash available for distribution per unit (\$)	0.32	0.30	1.41	1.20	1.38	1.35	1.27	1.35	1.27	1.17
Gross cash distributions per unit (\$)	0.37	0.37	1.56	1.53	1.51	1.45	1.43	1.45	1.43	1.37

Payout Ratio

Declared distributions/cash avail. for distribution	100.5%	109.9%	93.8%	109.3%	90.9%	91.2%	93.9%	91.2%	93.9%	98.6%
Declared distributions/cash flow from operations	86.8%	89.5%	85.4%	86.3%	83.4%	85.3%	83.9%	85.3%	83.9%	84.7%



Notes:

All figures are in Canadian dollars unless otherwise noted.

DBRS ratings are not a recommendation to buy, sell, or hold Fund units.

Copyright © 2007, DBRS Limited, DBRS, Inc. and DBRS (Europe) Limited (collectively, DBRS). All rights reserved. The information upon which DBRS ratings and reports are based is obtained by DBRS from sources believed by DBRS to be accurate and reliable. DBRS does not perform any audit and does not independently verify the accuracy of the information provided to it. DBRS ratings, reports and any other information provided by DBRS are provided “as is” and without warranty of any kind. DBRS hereby disclaims any representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability, fitness for any particular purpose or non-infringement of any of such information. In no event shall DBRS or its directors, officers, employees, independent contractors, agents and representatives (collectively, DBRS Representatives) be liable (1) for any inaccuracy, delay, interruption in service, error or omission or for any resulting damages or (2) for any direct, indirect, incidental, special, compensatory or consequential damages with respect to any error (negligent or otherwise) or other circumstance or contingency within or outside the control of DBRS or any DBRS Representatives in connection with or related to obtaining, collecting, compiling, analyzing, interpreting, communicating, publishing or delivering any information. Ratings and other opinions issued by DBRS are, and must be construed solely as, statements of opinion and not statements of fact as to credit worthiness or recommendations to purchase, sell or hold any securities. DBRS receives compensation, ranging from US\$1,000 to US\$750,000 (or the applicable currency equivalent) from issuers, insurers, guarantors and/or underwriters of debt securities for assigning ratings. This publication may not be reproduced, retransmitted or distributed in any form without the prior written consent of DBRS.