Fundamental Research Corp.
Investment Analysis for Intelligent Investors

October 7, 2021

Yorkton Equity Group Inc. (TSXV: YEG)

Completes Previously Announced Acquisitions; Expecting Strong Q3

N/A
Current Price: $0.22
Fair Value: N/A
Risk*: 3

Sector / Industry: Real Estate

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Highlights

- Since our initiating report in June 2021, YEG closed the previously announced acquisitions of Larson Place (Kelowna), and Langford Apartments (Victoria), and entered into an agreement to divest its 25% interest in the Yorkton 108 development in Surrey.
- Larson Place ($0.35M in Net Operating Income/NOI) was acquired for $8.89M. Langford ($0.22M in NOI) was acquired for $5.73M, **reflecting cap rates of 3.8%-3.9%.** We note that these are attractive cap rates as multi-family properties in Vancouver currently have cap rates of 2.75% to 4.00%.
- We were **pleased to see YEG's plans to divest its interest in Yorkton 108,** as it is a non-cash flowing project, and does not fit with mangement's mandate to build a portfolio of cash-flowing multi-family properties. Sale price is yet to be disclosed. As YEG made this investment in April, we are not expecting significant upside from this sale. YEG will be able to use the funds from this divestiture to fund acquisitons.
- In total, the company has five projects. **These projects have combined appraised values of approximately $57M, and $24M in net asset value.**
- Q2 revenue (net operating income) was flat QoQ, but below expectations. We were expecting additional revenue to kick-in from the acquisition of Riviera Gardens in April. Since renovations commenced quickly after the acquisition, the company is unlikely to generate a positive NOI from this project this year. Management indicated that Riviera Gardens will be fully operating starting early 2022. We are **expecting a significant improvement in NOI** from renovations.
- Q2 revenue declined YoY due to increased vacancy rates at its commercial building in Edmonton, amid the pandemic. YEG has not disclosed segmented results, or operating metrics.
- Management is actively seeking/evaluating equity financing options to pursue multiple acquisitions in the near-term.
- As interest rates are low, market conditions are conducive to obtaining long-term mortgages. A recent webinar with the company's team can be viewed here.
- We continue to believe that the multi-family residential rental market is one of the **most attractive markets in Canadian real estate** in the near-term. Although the Delta variant has induced some market uncertainty, **we are starting to see an increase in new immigrants and students.** Note that Canada is one of the most highly vaccinated countries in the world, and remains one of the top destinations in the world for immigrants/students.

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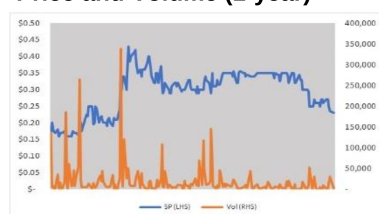
Price and Volume (1-year)



	YTD	12m
Ret.	-10%	29%
TSX	-2%	23%

Company Data

52 Week Range	$0.15 - $0.45
Shares O/S	113M
Market Cap.	$25M
Yield (forward)	N/A
P/E (forward)	N/A
P/B	1.1x

Key Financials (FYE - Dec 31) (C$)	2020	2021E	2022E
Cash	$1,059,018	$498,713	$665,929
Working Capital	-$1,517,319	$407,916	$537,299
Debt to Capital	20%	47%	46%
Assets	$14,944,188	$57,546,391	$57,789,274
Revenue	$443,597	$670,833	$1,427,500
Net Income	-$422,355	-$398,044	$129,383
EPS	$0.00	$0.00	$0.00

*See last page of this report for important disclosures, rating and risk definitions. All figures in C$ unless otherwise specified.

Financials

Net revenue (NOI) remained flat QoQ, but declined YoY due to increased vacancies at Pacific Mall (the only operating building in the company's portfolio at that time)

Income Statement YE - December 31	Q2-2020	Q2-2021	YoY	H1-2020	H1-2021	YoY
Net Revenue	**$168,492**	**$89,214**	-47%	**$294,970**	**$181,915**	-38%
Expenses						
G&A	$73,038	$135,738		$140,927	$318,696	
Management Fee	$0					
Interest	$20,354	$98,904		$48,605	$119,824	
Total Expenses	**93,392**	**234,642**	151%	**189,532**	**438,520**	131%
Depreciation	405	638		810	968	
EBT	**75,100**	**-145,428**		**105,438**	**-256,605**	
FV Changes and Others						
Tax	$4,537	$4,247		$9,074	$9,383	
Net Income	**$70,158**	**-$150,313**		**$95,554**	**-$266,956**	
EPS	$0.00	-$0.00		$0.00	-$0.00	

	2018	2019	2020	Q1-2020	Q1-2021	H1-2020	H1-2021
Funds from Operations	$12,746	$104,942	-$5,747	$35,346	-$81,787	$144,969	-$170,285
CFO	$45,436	$121,651	-$222,453	$43,874	-$203,722	$52,422	-$1,065,992
CFI	-$48,081	-$94,649	$72,573	-$48,821	-$80,483	-$176,294	$12,402
CFF	-$145,398	-$122,206	$1,169,409	$45,433	-$118,683	$173,442	$1,991,375
FCF	-$2,645	$27,002	-$149,880	-$4,947	-$284,205	-$123,872	-$1,053,590

Debt to capital of 22% at the end of Q2-2021; we expect debt to capital to increase to 47% from recent acquisitions; we note that REITs typically have a debt/capital of 40% to 60%

	2020	Q1-2021	Q2-2021
Investments	$13,360,000	$13,440,483	$26,497,665
Cash	$1,059,018	$656,130	$1,996,803
Working Capital	-$1,517,319	-$1,660,509	-$3,197,693
LT debt	-	-	-
Debt	$2,759,421	$2,661,474	$6,074,077
Debt to Capital	20.3%	19.8%	21.9%
EBIT/ Interest expense	3.2	-4.6	-0.5

Source: FRC / Company

Subsequent to Q2, the company raised $0.37M at $0.30 per unit. Each unit consisted of a common share and one full warrant (exercise price of $0.45 per share for two years).

Stock Options and Warrants – 1.13M options (weighted average exercise price of $0.21), and 20.38M warrants ($0.36) outstanding. 1.08M options are in-the-money, implying a potential to raise up to $0.24M.

Management remains focused on building a portfolio of cash-flowing properties

Combined NOI of $1.4M, and net asset value of $24M

Portfolio Summary

Project	Pacific Mall (acquired in Nov 2020)	Yorkton 108 (acquired in Apr 2021/divesting in Oct 2020)	Riviera Gardens (acquired in Apr 2021)	Larson Place (acquired in July 2021)	Langford (acquired in Sept 2021)	Total
Location	Edmonton, AB	Surrey, B.C.	Edmonton, AB	Kelowna, B.C.	Langford, B.C. (Victoria)	
Type	Two storey retail/commercial building	Residential development	62-unit condo building	19-unit townhouse development	4-storey building with 15 two-bed/three-bed units & one commercial unit	
Appraised Value/Purchase Price	$13.36M	$21.3M ($81.1M upon completion)	$8.1M	$8.9M	$5.7M	$57.4M
Status	100% equity	25% equity interest	100% equity	100% equity	100% equity	
NOI (Stabilized)	$0.44M	n/a	$0.41M	$0.35M	$0.22M	$1.42M
Cap Rate	3.29%	n/a	5.06%	3.93%	3.84%	4.05%
Mortgage	$2.7M	$2.6M	$3.5M	$6.6M	$4.4M	$19.8M
YEG's Equity	$10.66M	$4.68M	$4.60M	$2.30M	$1.30M	$23.5M

FRC Projections and Valuation

Due to renovations at Riviera Gardens, we are lowering our 2021 revenue and EPS forecasts

	Previous Forecasts		New Forecasts	
	2021	2022	2021	2022
Revenue	$930,000	$1,420,000	$670,833	$1,427,500
Net Income	-$87,044	$120,383	-$398,044	$129,383
EPS	-$0.00	$0.00	-$0.00	$0.00

Source: FRC / Company

As the company is in acquisition-mode, we continue not assigning a valuation at this time. Market conditions are conducive to obtaining long-term mortgages at low-rates. We believe management's 30+ year track record in real estate is YEG's key strength.

Risks

We believe the company is exposed to the following key risks:

Maintaining a risk rating of 3 (Average)

- Longer than expected impact of COVID-19.
- Investments in real estate are typically affected by macroeconomic conditions, and health of local markets.
- Like all real estate companies, YEG takes on leverage.
- Interest rate risks.
- A downturn in the real estate sector will impact the company's portfolio.

APPENDIX

Income Statement	2020	2021E	2022E
YE - December 31			
Net Revenue	**$443,597**	**$670,833**	**$1,427,500**
Expenses			
G&A	$151,436	$706,590	$727,788
Management Fee			
Interest	$92,403	$295,947	$591,893
Total Expenses	**243,839**	**1,002,537**	**1,319,681**
Depreciation			
EBT	**199,758**	**-331,703**	**107,819**
FV Changes and Others	-$1,811,786		
Tax	$1,189,673	-$66,341	$21,564
Net Income	**-$422,355**	**-$398,044**	**$129,383**
EPS	-$0.01	-$0.00	$0.00

Balance Sheet	2020	2021E	2022E
YE - December 31			
Assets			
Cash	$1,059,018	$498,713	$665,929
Receivables and Prepaid	$479,575	$67,083	$142,750
Investments			
Current Assets	**$1,538,593**	**$565,796**	**$808,679**
Equipment	$45,595	$45,595	$45,595
Investments	$13,360,000	$56,935,000	$56,935,000
Total Asset	**$14,944,188**	**$57,546,391**	**$57,789,274**
Liabilities			
Account payable and accrued liabilities	$239,236	$100,625	$214,125
Mortgages	$2,629,779	$19,729,779	$19,729,779
Loans			
Related Party	$129,642		
Security Deposits	$57,255	$57,255	$57,255
Current Liabilities	**$3,055,912**	**$19,887,659**	**$20,001,159**
Non-Current Liabilites	$1,026,802	$1,026,802	$1,026,802
Non-Controlling		$14,025,000	$14,025,000
Total Shareholders Equity	**$10,861,474**	**$22,606,930**	**$22,736,313**
Total Shareholders Equity+Liabilities	**$14,944,188**	**$57,546,391**	**$57,789,274**

Cash Flow Statement YE - December 31	2020	2021	2022
Operating Activities			
Net Income	-$422,355	-$398,044	$129,383
Adjustments	$416,608	$0	$0
FFO	**-$5,747**	**-$398,044**	**$129,383**
Change in WC	-$216,706	$144,239	$37,833
Cash From Operating Activities	**-$222,453**	**-$253,805**	**$167,216**
Investing Activities			
Investing Activities	-$205,260	-$4,000,000	
Others	$277,833		
Cash used Investing Activities	**$72,573**	**-$4,000,000**	**$0**
Financing Activities			
Equity	$1,134,888	$3,693,500	
Debt	$34,521		
Cash used in Financing Activities	**$1,169,409**	**$3,693,500**	**$0**
Net Increase(Decrease) in Cash	$1,019,529	-$560,305	$167,216

Fundamental Research Corp. Equity Rating Scale:
Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk
Hold – Annual expected rate of return is between 5% and 12%
Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk
Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

Fundamental Research Corp. Risk Rating Scale:
1 (Low Risk) - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues and may rely on external funding. These stocks are considered highly speculative.

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