



Condensed Interim Consolidated Financial Statements

For the three and nine months ended September 30, 2019

(Unaudited, in thousands of Canadian dollars)

Condensed Interim Consolidated Statement of Income

Unaudited (\$000s)	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Revenue (note 7)	53,946	60,245	129,915	147,452
Cost of sales	(30,486)	(32,194)	(65,620)	(75,713)
Gross profit	23,460	28,051	64,295	71,739
General and administrative expense	(5,497)	(5,917)	(16,616)	(17,755)
Fair value adjustment on investment properties (note 5 and 11)	3,300	(25)	1,359	258
Adjustments related to REIT units (note 10)	(3,398)	(643)	(10,351)	(2,778)
Gain on sale of assets	61	1	83	6
Operating earnings	17,926	21,467	38,770	51,470
Interest income	427	349	1,081	1,050
Finance costs	(7,333)	(6,539)	(21,399)	(18,176)
Net finance costs	(6,906)	(6,190)	(20,318)	(17,126)
Income before income taxes	11,020	15,277	18,452	34,344
Income tax recovery (expense)	5,048	(3,808)	2,343	(6,597)
Net income for the period	16,068	11,469	20,795	27,747
Income per share:				
Basic earnings per share	0.48	0.34	0.62	0.83
Diluted earnings per share	0.48	0.34	0.62	0.83

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Comprehensive Income

Unaudited (\$000s)	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Net income for the period	16,068	11,469	20,795	27,747
Other comprehensive income				
Items that may be reclassified subsequently to net income:				
Currency translation differences	1,923	(2,490)	(4,341)	4,302
Comprehensive income	17,991	8,979	16,454	32,049

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Financial Position

Unaudited (\$000s)	September 30, 2019	December 31, 2018
ASSETS		
Cash and cash equivalents	31,420	26,727
Accounts receivable	8,924	10,849
Income taxes recoverable	9,100	—
Agreements receivable	75,522	126,490
Land inventory (note 4)	777,791	758,940
Investment properties (note 5 and 11)	1,072,884	1,032,687
Property and equipment	13,670	14,020
Other assets	55,653	53,363
	2,044,964	2,023,076
LIABILITIES		
Accounts payable and accrued liabilities	51,396	44,825
Income taxes payable	—	8,605
Provision for land development costs	60,505	77,658
General debt (note 6)	702,437	659,556
Deferred income tax liabilities	58,115	66,493
REIT units (note 10 and 11)	101,697	98,374
	974,150	955,511
SHAREHOLDERS' EQUITY		
Share capital (note 8)	72,630	72,821
Contributed surplus	3,914	3,366
Accumulated other comprehensive income (AOCI)	24,788	29,129
Retained earnings	969,482	962,249
	1,070,814	1,067,565
	2,044,964	2,023,076

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Cash Flows

Unaudited (\$000's)	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
CASH FLOWS FROM (USED IN)				
OPERATING ACTIVITIES				
Net income for the period	16,068	11,469	20,795	27,747
Non cash items:				
Amortization of tenant incentives	3,161	1,752	5,919	5,007
Depreciation of property and equipment	525	518	1,153	1,170
Stock based compensation expense	189	111	548	323
Non-cash finance costs	611	491	1,973	1,698
Straight-line rent adjustment	(262)	(434)	(1,465)	(1,652)
Fair value adjustment on investment properties (note 5 and 11)	(3,300)	25	(1,359)	(258)
Fair value adjustment on REIT units (note 10 and 11)	1,180	(1,582)	3,685	(5,386)
Gain on sale of assets	(61)	(1)	(83)	(6)
Deferred income taxes	(7,677)	58	(8,283)	(4,839)
	10,434	12,407	22,883	23,804
Agreements receivable	14,773	9,906	50,968	30,943
Development activities	(10,992)	(22,549)	(22,687)	(43,581)
Purchase of land inventory (note 4)	(4,000)	(1,075)	(12,496)	(2,141)
Payment of tenant lease incentives and direct leasing costs	(4,623)	(2,604)	(9,107)	(6,342)
Operating assets and liabilities	15,799	7,838	(8,842)	(504)
	21,391	3,923	20,719	2,179
INVESTING ACTIVITIES				
Purchase of investment properties (note 5)	(1,050)	(24,532)	(13,528)	(24,532)
Additions to investment properties (note 5)	(5,431)	(4,885)	(15,633)	(17,218)
Net proceeds from disposal of investment properties (note 5)	—	—	314	516
Net proceeds from disposal of asset held for sale	—	—	—	16,459
Purchase of property and equipment	(477)	(338)	(883)	(743)
Proceeds on disposal of property and equipment	134	2	162	26
	(6,824)	(29,753)	(29,568)	(25,492)
FINANCING ACTIVITIES				
Proceeds from issuance of trust units	—	—	—	17,302
Revolving credit facilities	(9,441)	4,082	34,545	(22,317)
Proceeds from general debt	17,714	65,807	51,223	107,913
Repayment of general debt	(16,213)	(32,959)	(57,967)	(71,346)
Repurchase of REIT units	(216)	—	(361)	—
Dividends paid	(3,992)	(4,343)	(12,646)	(13,026)
Common shares repurchased (note 8)	(280)	—	(1,107)	—
Share capital issued	—	—	—	194
	(12,428)	32,587	13,687	18,720
FOREIGN EXCHANGE (LOSS) GAIN ON CASH HELD IN A FOREIGN CURRENCY				
	(179)	(73)	(145)	392
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS DURING THE PERIOD				
	1,960	6,684	4,693	(4,201)
CASH AND CASH EQUIVALENTS, BEGINNING OF THE PERIOD				
	29,460	31,620	26,727	42,505
CASH AND CASH EQUIVALENTS, END OF THE PERIOD				
	31,420	38,304	31,420	38,304
Total income taxes paid	13,874	2,944	22,508	4,088
Total interest paid	8,144	6,628	23,532	18,290

See accompanying notes to these condensed interim consolidated financial statements.

1. DESCRIPTION OF THE BUSINESS

We are a real estate development company with community development, property development, investment properties, REIT and recreational property divisions. We develop, manage, and own mixed-use residential communities, business and industrial parks, office buildings, retail commercial centres, and golf courses.

Melcor Developments Ltd. ("Melcor" or "we") is incorporated in Canada. The registered office is located at Suite 900, 10310 Jasper Avenue Edmonton, AB T5J 1Y8. We operate in Canada and the United States ("US"). Our shares are traded on the Toronto Stock Exchange under the symbol "MRD". As at September 30, 2019 Melton Holdings Ltd. holds approximately 47.1% of the outstanding shares and pursuant to IAS 24, Related party disclosures, is the ultimate controlling shareholder of Melcor.

As at November 6, 2019, Melcor through an affiliate, holds an approximate 53.1% effective interest in Melcor REIT ("REIT" or "the REIT") through ownership of all Class B LP Units of the Partnership and is the ultimate controlling party. Melcor continues to manage, administer and operate the REIT and its properties under an asset management agreement and property management agreement. Trust units of the REIT are traded on the Toronto Stock Exchange under the symbol "MR.UN".

Our quarterly results are impacted by the cyclical nature of our business environment. Income can fluctuate significantly from period to period due to the timing of plan registrations, the cyclical nature of real estate and construction markets, and the mix of lot sales and product types.

2. BASIS OF PRESENTATION

We prepare our condensed interim consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting.

These condensed interim consolidated financial statements should be read in conjunction with our annual consolidated financial statements for the year ended December 31, 2018, which have been prepared in accordance with IFRS as issued by the IASB.

These condensed interim consolidated financial statements were approved for issue by the Board of Directors on November 6, 2019.

3. SIGNIFICANT ACCOUNTING POLICIES AND NEW STANDARDS ADOPTED

The accounting policies followed in these condensed interim consolidated financial statements are consistent with those of the previous financial year, except as described below.

We have adopted the following new IFRS standards effective January 1, 2019

a) IFRS 16, Leases was issued in January 2016 by the IASB to replace IAS 17. IFRS 16 includes several changes in the method of accounting for operating leases including:

- i. All leases will be on the balance sheet of the lessees, except those that meet the limited exception criteria;
- ii. Rent expense for the leases on the balance sheet will be recorded as depreciation and finance expenses;
- iii. Timing of expenses will change as the finance lease model results in an accelerated recognition of expenses compared to a straight-line operating lease model.

Impact of Adoption

As the changes implemented through IFRS 16 are directed mainly towards lessees, the adoption of IFRS 16 did not result in any adjustments upon transition, change in recognition, or changes to our accounting policy as Melcor is a lessor. Adoption does require additional disclosures to the year end financial statements to show variable lease revenues earned and minimum lease payments under non-cancellable operating leases of investment properties for each year for up to 5 years. This standard was adopted through the modified retrospective approach.

b) IFRIC 23, Uncertainty over income tax treatments clarifies the application of the recognition and measurement requirements in IAS 12, "Income Taxes" ("IAS 12"), for situations where there is uncertainty over income tax treatments, IFRIC 23 specifically addresses whether;

- i. an entity considers income tax treatments separately;

- ii. assumptions that an entity makes regarding the examination of tax treatments by taxation authorities;
- iii. how an entity considers changes in facts and circumstances.

IFRIC 23 does not apply to taxes or levies outside the scope of IAS 12. IFRIC 23 is effective for annual periods beginning on or after January 1, 2019.

Impact of Adoption

The adoption of IFRIC 23 did not result in any adjustments upon transition, change in recognition, additional disclosures or changes to our accounting policy.

The following standards are effective January 1, 2020 and have not yet been adopted

- a) **IFRS 3, Business combinations** amendments were made to IFRS 3, Business combinations in order to clarify that obtaining control of a business that is a joint operation is a business combination achieved in stages. Amendments to IFRS 3 are effective for annual period beginning on or after January 1, 2020.

We are currently evaluating the impact of adopting the amendments to this standard to the consolidated financial statements.

4. LAND INVENTORY

	September 30, 2019	December 31, 2018
Raw land held	402,143	387,356
Land under development	169,369	136,534
Developed land	206,279	235,050
	777,791	758,940

During the nine month period ended September 30, 2019, we purchased 470.60 acres of land at a cost of \$28,608 and received vendor financing of \$16,112.

During the comparative nine month period ended September 30, 2018, we purchased 131.13 acres of land at a cost of \$4,766 and received vendor financing of \$2,625.

5. INVESTMENT PROPERTIES

Investment properties consists of the following:

	September 30, 2019	December 31, 2018
Investment properties	987,089	965,339
Properties under development	85,795	67,348
Total	1,072,884	1,032,687

The following table summarizes the change in investment properties during the period:

	Nine months ended September 30, 2019		
	Investment Properties	Properties under Development	Total
Balance - beginning of period	965,339	67,348	1,032,687
Additions			
Direct acquisition	12,478	1,050	13,528
Transfer from land inventory	—	12,305	12,305
Direct leasing costs	1,517	283	1,800
Property improvements	2,522	—	2,522
Development costs	—	12,837	12,837
Capitalized borrowing costs	—	274	274
Disposals	(314)	—	(314)
Transfers	13,018	(13,018)	—
Fair value adjustment on investment properties	(3,357)	4,716	1,359
Foreign currency translation (included in OCI)	(4,114)	—	(4,114)
Balance - end of period	987,089	85,795	1,072,884

	Year ended December 31, 2018		
	Investment Properties	Properties under Development	Total
Balance - beginning of year	907,310	68,546	975,856
Additions			
Direct acquisition	33,541	—	33,541
Transfer from land inventory	—	2,070	2,070
Direct leasing costs	1,054	803	1,857
Property improvements	3,897	—	3,897
Development costs	3	16,574	16,577
Capitalized borrowing costs	—	943	943
Disposals	(13,321)	—	(13,321)
Transfers	29,959	(29,959)	—
Fair value adjustment on investment properties	(7,508)	8,371	863
Foreign currency translation (included in OCI)	10,404	—	10,404
Balance - end of year	965,339	67,348	1,032,687

In accordance with our policy we record our investment properties at fair value. Fair value adjustments on investment properties are primarily driven by changes in capitalization rates and stabilized net operating income ("NOI"). Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 11.

Acquisitions

On August 1, 2019 Melcor acquired land for property development in Calgary, Alberta at a purchase price of \$1,050.

During the nine-month period ended September 30, 2019, the REIT acquired a retail investment property in Calgary, Alberta for a purchase price of \$12,478 (including transaction costs). This purchase was accounted for as an asset acquisition in accordance with our policy.

Disposals

During the nine-month period ended September 30, 2019, we disposed of one residential unit in Arizona for a sales price of \$314 (US \$235) (net of transaction costs). The sale price was settled through cash.

6. GENERAL DEBT

	September 30, 2019	December 31, 2018
Melcor - revolving credit facilities	59,319	46,529
REIT - revolving credit facility	21,756	—
Project specific financing	66,554	62,639
Secured vendor take back debt on land inventory	43,874	40,842
Debt on investment properties and golf course assets	454,955	454,342
REIT - convertible debentures	55,979	55,204
General debt	702,437	659,556

The change in project specific financing during the period is summarized as follows:

	September 30, 2019	December 31, 2018
Balance - beginning of period	62,639	20,926
Cash movements		
Loan repayments	(3,192)	(11,629)
New project financing	7,676	52,319
Non-cash movements		
Foreign currency translation included in OCI	(569)	1,023
Balance end of year	66,554	62,639

The change in secured vendor take back debt on land inventory during the period is summarized as follows:

	September 30, 2019	December 31, 2018
Balance - beginning of period	40,842	64,891
Cash movements		
Principal repayments		
Scheduled amortization on debt	(12,955)	(26,742)
Non-cash movements		
New secured vendor take back debt	16,112	2,625
Amortization of non-cash interest	(125)	(280)
Foreign currency translation included in OCI	—	348
Balance end of year	43,874	40,842

The change in debt on investment properties and golf course assets during the period is as follows:

	September 30, 2019	December 31, 2018
Balance - beginning of period	454,342	444,807
Cash movements		
Principal repayments		
Scheduled amortization on debt	(11,452)	(15,964)
Mortgage repayments	(30,368)	(51,909)
New mortgages	43,547	75,918
Non-cash movements		
Mortgage payable disposed through sale during the period	—	(3,662)
Deferred financing fees capitalized	(362)	(627)
Amortization of deferred financing fees	328	341
Change in derivative fair value swap	998	254
Foreign currency translation included in OCI	(2,078)	5,184
Balance end of year	454,955	454,342

7. REVENUE

Total Revenues	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Revenue from contracts	33,865	40,456	67,756	88,681
Revenue from other sources	20,081	19,789	62,159	58,771
	53,946	60,245	129,915	147,452

Timing of contract revenue recognition	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
At a point in time	29,032	35,868	52,566	74,570
Over time	4,833	4,588	15,190	14,111
	33,865	40,456	67,756	88,681

8. SHARE CAPITAL

Issued and outstanding common shares at September 30, 2019 are 33,259,243 (December 31, 2018 – 33,346,495). During the three and nine months ended September 30, 2019, there were no options exercised (Q3-2018 – nil and 14,200).

During the first quarter there were 64,352 common shares purchased for cancellation by Melcor pursuant to the Normal Course Issuer Bid (NCIB) at a cost of \$827 (December 31, 2018 - 57,156 common shares purchased at a cost of \$761). The NCIB commenced March 31, 2018 and ended March 30, 2019.

On April 1, 2019 Melcor commenced a new NCIB which allows Melcor to purchase up to 1,665,080 common shares for cancellation, representing approximately 5% of the issued and outstanding common shares. The common shares may be repurchased up to a maximum daily limit of 1,000. The price which Melcor will pay for common shares repurchased under the plan will be the market price at the time of acquisition. The NCIB ends one year from commencement, on March 31, 2020.

In connection with the commencement of the NCIB, Melcor also entered into an automatic purchase plan agreement with a broker to allow for the purchase of common shares under the NCIB at times when Melcor ordinarily would not be active in the market due to regulatory restrictions or self-imposed trading blackout periods.

As of September 30, 2019, there were 22,900 common shares purchased for cancellation by Melcor pursuant to the new NCIB at a cost of \$280, for a total of 87,252 shares purchase year-to-date between both NCIBs at a total cost of \$1,107.

9. SEGMENTED INFORMATION

Geographic Analysis

A reconciliation of our revenues and assets by geographic location is as follows:

External Revenues	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
United States	7,508	7,827	19,124	19,594
Canada	46,438	52,418	110,791	127,858
Total	53,946	60,245	129,915	147,452

Total Assets

As at	September 30, 2019	December 31, 2018
United States	268,870	272,537
Canada	1,776,094	1,750,539
Total	2,044,964	2,023,076

9. SEGMENTED INFORMATION (continued)

Divisional Analysis

Our divisions reported the following results:

For the three months ended September 30, 2019	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Segment revenue	25,897	13,559	9,589	17,468	3,854	—	70,367	(16,421)	53,946
Cost of sales	(17,800)	(13,500)	(4,100)	(6,782)	(2,579)	—	(44,761)	14,275	(30,486)
Gross profit	8,097	59	5,489	10,686	1,275	—	25,606	(2,146)	23,460
General and administrative expense	(2,068)	(561)	(607)	(697)	(723)	(1,707)	(6,363)	866	(5,497)
Fair value adjustment on investment properties	—	2,931	(1,373)	462	—	—	2,020	1,280	3,300
Gain on sale of assets	—	—	—	—	61	—	61	—	61
Interest income	326	7	11	28	—	55	427	—	427
Segment Earnings (Loss)	6,355	2,436	3,520	10,479	613	(1,652)	21,751	—	21,751
Finance costs									(7,333)
Adjustments related to REIT units									(3,398)
Income before tax									11,020
Income tax recovery									5,048
Net income for the period									16,068

For the three months ended September 30, 2018	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Segment revenue	33,469	131	7,899	17,283	3,779	—	62,561	(2,316)	60,245
Cost of sales	(20,471)	—	(3,198)	(6,855)	(2,405)	—	(32,929)	735	(32,194)
Gross profit	12,998	131	4,701	10,428	1,374	—	29,632	(1,581)	28,051
General and administrative expense	(2,216)	(578)	(639)	(702)	(744)	(1,852)	(6,731)	814	(5,917)
Fair value adjustment on investment properties	—	1,567	(613)	(1,746)	—	—	(792)	767	(25)
Gain on sale of assets	—	—	—	—	2	(1)	1	—	1
Interest income	242	8	2	40	—	57	349	—	349
Segment Earnings (Loss)	11,024	1,128	3,451	8,020	632	(1,796)	22,459	—	22,459
Finance costs									(6,539)
Adjustments related to REIT units									(643)
Income before tax									15,277
Income tax expense									(3,808)
Net loss for the period									11,469

9. SEGMENTED INFORMATION (continued)

For the nine months ended	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
September 30, 2019									
Segment revenue	60,241	13,595	28,985	52,886	7,856	—	163,563	(33,648)	129,915
Cost of sales	(41,561)	(13,500)	(12,097)	(21,228)	(5,210)	—	(93,596)	27,976	(65,620)
Gross profit	18,680	95	16,888	31,658	2,646	—	69,967	(5,672)	64,295
General and administrative expense	(6,088)	(1,765)	(1,727)	(2,161)	(1,913)	(5,205)	(18,859)	2,243	(16,616)
Fair value adjustment on investment properties	—	3,541	(5,353)	(258)	—	—	(2,070)	3,429	1,359
Gain on sale of assets	—	—	—	—	83	—	83	—	83
Interest income	782	21	28	89	—	161	1,081	—	1,081
Segment Earnings (Loss)	13,374	1,892	9,836	29,328	816	(5,044)	50,202	—	50,202
Finance costs									(21,399)
Adjustments related to REIT units									(10,351)
Income before tax									18,452
Income tax recovery									2,343
Net income for the period									20,795

For the nine months ended	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
September 30, 2018									
Segment revenue	72,910	20,174	23,632	52,837	7,714	—	177,267	(29,815)	147,452
Cost of sales	(44,279)	(19,850)	(9,530)	(21,117)	(4,995)	—	(99,771)	24,058	(75,713)
Gross profit	28,631	324	14,102	31,720	2,719	—	77,496	(5,757)	71,739
General and administrative expense	(7,009)	(1,784)	(1,819)	(2,157)	(1,947)	(5,403)	(20,119)	2,364	(17,755)
Fair value adjustment on investment properties	—	6,370	(4,344)	(5,161)	—	—	(3,135)	3,393	258
Gain on sale of assets	—	—	—	—	14	(8)	6	—	6
Interest income	758	19	6	104	—	163	1,050	—	1,050
Segment Earnings (Loss)	22,380	4,929	7,945	24,506	786	(5,248)	55,298	—	55,298
Finance costs									(18,176)
Adjustments related to REIT units									(2,778)
Income before tax									34,344
Income tax expense									(6,597)
Net loss for the period									27,747

10. NON-CONTROLLING INTEREST IN MELCOR REIT

In accordance with our policy, we account for the remaining 46.9% publicly held interest in the REIT as a financial liability measured at fair value through profit or loss (“FVTPL”). As at September 30, 2019 the REIT units had a fair value of \$101,697. We recorded adjustments related to REIT units for the three and nine months ended September 30, 2019 of \$3,398 and \$10,351 (Q3-2018 - \$643 and \$2,778).

On April 1, 2019 the REIT commenced a normal course issuer bid (“REIT NCIB”) which allows the REIT to purchase up to 659,339 trust units for cancellation, representing approximately 5% of the REIT’s issued and outstanding trust units. The trust units may be repurchased up to a maximum daily limit of 2,908. The price which the REIT will pay for trust units repurchased under the plan will be the market price at the time of acquisition. The REIT NCIB ends one year from commencement on March 31, 2020.

During the nine month period, there were 47,688 share purchased for cancellation by the REIT pursuant to the REIT NCIB at a cost of \$361, which is recorded as reduction in the balance of REIT units on the consolidated statement of financial position.

As illustrated in the table below, the adjustment is comprised of:

	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Fair value adjustment on REIT units (note 11)	(1,180)	1,582	(3,685)	5,386
Capitalized against REIT trust units	—	—	—	(1,190)
Capitalized to investment properties	—	—	—	(298)
Distributions to REIT unitholders	(2,218)	(2,225)	(6,666)	(6,676)
Adjustments related to REIT units	(3,398)	(643)	(10,351)	(2,778)

The following tables summarize the financial information relating to Melcor’s subsidiary, the REIT, that has material non-controlling interest (NCI), before intra-group eliminations.

As at	September 30, 2019	December 31, 2018
Assets	726,724	709,603
Liabilities	415,338	400,094
Net assets	311,386	309,509
Cost of NCI	103,959	103,959
Fair value of NCI	101,697	98,374

	For the three months ended		For the nine months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Rental Revenue	17,468	17,283	52,886	52,837
Net income and comprehensive income	2,310	3,097	4,732	10,873
Cash flows from operating activities	2,979	2,815	6,842	8,287
Cash flows used in investing activities	(403)	(683)	(14,611)	(19,719)
Cash flows from (used in) financing activities, before distributions to REIT unitholders	(695)	10,584	14,277	19,535
Cash flows used in financing activities - cash distributions to REIT unitholders	(2,218)	(2,225)	(6,666)	(6,564)
Net increase (decrease) in cash and cash equivalents	(337)	10,491	(158)	1,539

11. FAIR VALUE MEASUREMENT

Fair value is the price that market participants would be willing to pay for an asset or liability in an orderly transaction under current market conditions at the measurement date.

The fair value of Melcor's financial instruments are determined as follows:

- the carrying amounts of cash and cash equivalents, accounts receivables, agreements receivable and accounts payable and accrued liabilities approximate their fair values based on the short term maturities of these financial instruments.
- fair values of general debt are estimated by discounting the future cash flows associated with the debt at market interest rates (Level 2).
- fair value of derivative financial liabilities, which is the conversion feature on the REIT convertible debenture, and our floating for fixed interest rate swap, are estimated based upon unobservable inputs, including volatility and credit spread (Level 3).
- fair value of REIT units are estimated based on the closing trading price of the REIT's trust units and the fair value of the convertible debenture is estimated based on the closing trading price of the REIT's debenture (Level 1).

In addition, Melcor carries its investment properties at fair value, which is determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows (Level 3).

The fair value hierarchy categorizes fair value measurement into three levels based upon the inputs to valuation technique, which are defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: unobservable inputs for the asset or liability.

There were no transfers between the levels of the fair value hierarchy during the period.

The following table summarizes Melcor's assets and liabilities carried at fair value and its financial assets and liabilities where carrying value does not approximate fair value.

	September 30, 2019					December 31, 2018	
	Fair Value Hierarchy	Fair Value	Amortized Cost	Total Carrying Value	Total Fair Value	Total Carrying Value	Total Fair Value
Non-financial assets							
Investment properties	Level 3	1,072,884	—	1,072,884	1,072,884	1,032,687	1,032,687
Financial liabilities							
General debt, excluding convertible debentures and derivative financial liability	Level 3	—	646,265	646,265	666,394	604,352	589,890
Convertible debentures	Level 2	—	55,792	55,792	58,150	55,017	56,738
Derivative financial liability							
Interest rate swaps	Level 3	193	—	193	193	(803)	(803)
Conversion feature on convertible debentures	Level 3	187	—	187	187	187	187
REIT units	Level 1	101,697	—	101,697	101,697	98,374	98,374

Investment properties

Investment properties are remeasured to fair value on a recurring basis, determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows. The application of these valuation methods results in these measurements being classified as level 3 in the fair value hierarchy.

Under the discounted future cash flows method, fair values are determined by discounting the forecasted future cash flows over ten years plus a terminal value determined by applying a terminal capitalization rate to forecasted year eleven cash flows.

Under the direct income capitalization method, fair values are determined by dividing the stabilized net operating income of the property by a property specific capitalization rate.

The significant unobservable inputs in the Level 3 valuations are as follows:

- Capitalization rate - based on actual location, size and quality of the property and taking into consideration available market data as at the valuation date;
- Stabilized net operating income - revenue less direct operating expenses adjusted for items such as average lease up costs, vacancies, non-recoverable capital expenditures, management fees, straight-line rents and other non-recurring items;
- Discount rate - reflecting current market assessments of the uncertainty in the amount and timing of cash flows;
- Terminal capitalization rate - taking into account assumptions regarding vacancy rates and market rents;
- Estimated costs to complete for properties under development - based on expected completion dates considering development and leasing risks specific to each property and the status of approvals and/or permits; and
- Cash flows - based on the physical location, type and quality of the property and supported by the terms of existing leases, other contracts or external evidence such as current market rents for similar properties.

An increase in the cash flows or stabilized net operating income results in an increase in fair value of investment property whereas an increase in the capitalization rate, discount rate or terminal capitalization rate decreases the fair value of the investment property.

In determining the fair value of our investment properties judgment is required in assessing the 'highest and best use' as required under IFRS 13, *Fair value measurement*. We have determined that the current uses of our investment properties are their 'highest and best use'.

Melcor's executive management team is responsible for determining fair value measurements on a quarterly basis, including verifying all major inputs included in the valuation and reviewing the results. Melcor's management, along with the Audit Committee, discuss the valuation process and key inputs on a quarterly basis. At least once every two years, the valuations are performed by qualified external valuers who hold recognized and relevant professional qualifications and have recent experience in the location and category of the investment property being valued.

Investment properties were valued by Melcor's internal valuation team as at September 30, 2019 of which 30 investment properties (of 91 legal phases) with a fair value of \$367,955 were valued by qualified independent external valuation professionals during the period. Valuations performed during the period resulted in net fair value gains of \$1,359. As at December 31, 2018 Melcor's internal valuation team valued investment properties of which 32 investment properties (of 82 legal phases valued) with a fair value of \$420,145 were valued by qualified independent external valuation professionals during the year. Valuations performed during 2018 resulted in net fair value gains of \$863.

The following table summarizes the valuation approach, significant unobservable inputs, and the relationship between the inputs and the fair value:

Asset	Valuation approach	Significant unobservable inputs	Relationship between inputs and fair value
Investment properties	Direct capitalization or discounted cash flows	- Capitalization rate - Discount rate - Terminal rate - Stabilized NOI - Cash flows	Inverse relationship between capitalization, discount and terminal rates and fair value (higher rates result in decreased fair value); whereas higher stabilized NOI or cash flows results in increased fair value.
Properties under development	Direct capitalization less cost to complete	- Capitalization rate - Stabilized NOI - Costs to complete	Inverse relationship between capitalization rate and fair value (higher capitalization rate results in lower fair value); whereas higher stabilized NOI results in increased fair value.
Properties under development - undeveloped land	Direct comparison	- Comparison to market transactions for similar assets	Land value reflects market value.

Weighted average annual stabilized net operating income for investment properties as at September 30, 2019 is \$1,503 (December 31, 2018 - \$1,506) per property. Other significant valuation metrics and unobservable inputs are set out in the following table. Fair values are most sensitive to changes in capitalization rates.

September 30, 2019	Investment Properties			Properties under Development		
	Min	Max	Weighted Average	Min	Max	Weighted Average
Capitalization rate	5.50%	10.50%	6.67%	5.75%	6.50%	6.06%
Terminal capitalization rate	5.75%	9.00%	6.76%	6.00%	6.25%	6.15%
Discount rate	6.50%	9.50%	7.66%	6.75%	7.00%	6.96%

December 31, 2018	Investment Properties			Properties under Development		
	Min	Max	Weighted Average	Min	Max	Weighted Average
Capitalization rate	5.50%	10.50%	6.66%	6.00%	6.50%	6.23%
Terminal capitalization rate	5.75%	9.00%	6.76%	6.25%	6.25%	6.25%
Discount rate	6.50%	9.75%	7.66%	7.00%	7.00%	7.00%

An increase in capitalization rates by 50 basis points would decrease the fair value and carrying amount of investment properties by \$57,242 (December 31, 2018 - \$56,215). A decrease in capitalization rates by 50 basis points would increase the fair value and carrying amount of investment properties by \$66,520 (December 31, 2018 - \$65,343).

General debt, excluding derivative financial liabilities

The fair value of revolving credit facilities approximates the carrying value excluding unamortized financing costs. The facilities bear interest, at our option, at a rate per annum equal to either the bank's prime lending rate plus 0.75% to 2.25% or at the bank's then prevailing banker's acceptance rate plus a stamping fee of 2.25% to 3.00%.

The fair value of project specific financing, secured vendor take back debt on land inventory and debt on investment properties and golf course assets and convertible debenture have been calculated by discounting the expected cash flows of each loan using a discount rate specific to each individual loan. The discount rate is determined using the bond yield for similar instruments of similar maturity adjusted for each individual project's specific credit risk. In determining the adjustment for credit risk, we consider current market conditions and other indicators of credit worthiness.

Derivative financial liabilities

Our derivative financial liabilities are comprised of floating for fixed interest rate swaps on mortgages (level 3) and the conversion feature on our REIT convertible debentures (level 3).

The fair value of the interest rate swaps are calculated as the net present value of the future cash flows expected to arise on the variable and fixed portion, determined using applicable yield curves at the measurement date. As at September 30, 2019, the fair value of interest rate swap contracts was \$193 (December 31, 2018 - \$803).

The significant unobservable inputs used in the fair value measurement of the conversion feature on the REIT convertible debenture as at September 30, 2019 are as follows:

- Volatility - expected volatility as at September 30, 2019 was derived from the historical prices of the REIT's trust units. As the REIT was formed on May 1, 2013, we have used the entire historical data up until September 30, 2019. Volatility was 17.80% (December 31, 2018 - 17.80%).
- Credit spread - the credit spread of the convertible debenture was imputed from the traded price of the convertible debenture as at September 30, 2019. The credit spread used was 3.92% (December 31, 2018 - 3.92%).

REIT units

REIT units are remeasured to fair value on a recurring basis and categorized as level 1 in the fair value hierarchy. The units are fair valued based on the trading price of the REIT units at the period end date. At September 30, 2019 the fair value of the REIT units was \$101,697, resulting in a fair value loss during the three and nine months ended of \$1,180 and \$3,685 (2018 - gain of \$1,582 and \$5,386) in the statement of income and comprehensive income for the period ended ended September 30, 2019 (note 10).

12. CREDIT RISK

Agreements receivable are collateralized by specific real estate sold. Agreements receivable relate primarily to land sales in Alberta and, accordingly, collection risk is related to the economic conditions of that region. We manage credit risk by selling to certain qualified registered builders.

13. EVENTS AFTER THE REPORTING PERIOD

Distributions on REIT trust units

On October 15, 2019 the REIT declared a distribution of \$0.05625 per unit for the months of October, November and December 2019. The distributions will be payable as follows:

Month	Record Date	Distribution Date	Distribution Amount
October 2019	October 31, 2019	November 15, 2019	\$0.05625 per unit
November 2019	November 29, 2019	December 16, 2019	\$0.05625 per unit
December 2019	December 31, 2019	January 15, 2020	\$0.05625 per unit

REIT Convertible Debenture

On October 29, 2019, the REIT issued a 5.10% convertible unsecured subordinated debenture (the "2019 Debentures") to the public for gross proceeds of \$46,000, including \$6,000 issued pursuant to the exercise of an over-allotment option. The 2019 Debentures bear interest at an annual rate of 5.10% payable semi-annually in arrears on June 30 and December 31 each year, commencing December 31, 2019. The 2019 Debentures mature on December 31, 2024 and can be converted into trust units at the holders' options at any point prior to the maturity date at a conversion rate of 112.3596 trust units per one thousand principal amount of convertible debenture (the "Conversion Price"). On and from December 31, 2022, and prior to December 31, 2023, the 2019 Debentures may be redeemed by the REIT, in whole at any time, or in part from time to time, at a price equal to the principal amount thereof plus accrued and unpaid interest, provided that the volume weighted-average trading price of the trust units for a specified period preceding (the "Current Market Price") the date on which notice of redemption is given is not less than 125% of the Conversion Price. On and from December 31, 2023, and prior to the maturity date, the 2019 Debentures may be redeemed by the REIT, in whole at any time or in part from time to time, at a price equal to the principal amount thereof plus accrued and unpaid interest. Subject to regulatory approval and other conditions, the REIT may, at its option, elect to satisfy its obligation to pay the principal amount of the convertible debenture on redemption or at maturity, in whole or in part, by delivering that number of freely tradeable trust units obtained by dividing the principal amount of the 2019 Debentures being repaid by 95% of the Current Market Price on the date of redemption or maturity.

REIT Acquisition

The REIT has a commitment to acquire a 283,235 sf regional shopping centre in Grande Prairie, Alberta from a third-party for \$54.8 million. The purchase price will be partially satisfied through the 2019 Debentures described above, and the acquisition is expected to close in November 2019.

Dividends declared

On November 6, 2019 our board of directors declared a dividend of \$0.12 per share payable on December 31, 2019 to shareholders of record on December 16, 2019.