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MNR - Q1 2017 Monmouth Real Estate Investment Corp Earnings Call

EVENT DATE/TIME: FEBRUARY 09, 2017 / 3:00PM GMT

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PRESENTATION

Operator

Good morning and welcome to Monmouth Real Estate Investment Corporation's first-quarter 2017 earnings conference call.

(Operator Instructions)

Please note this event is being recorded. It is now my pleasure to introduce your host, Ms. Susan Jordan, Vice President of Investor Relations. Thank you, Ms. Jordan, you may begin.

Susan Jordan - *Monmouth Real Estate Investment Corporation - VP of IR*

Thank you very much, operator. In addition to the 10-Q that we filed with the SEC yesterday, we have filed an unaudited first-quarter supplemental information presentation. This supplemental information presentation, along with our 10-Q, are available on the Company's website at mreic.reit.

I would like to remind everyone that certain statements made during this conference call which are not historical facts may be deemed forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The forward-looking statements that we make on this call are based on our current expectations and involve various risks and uncertainties. Although the Company believes the expectations reflected in any forward-looking statements are based on reasonable assumptions, the Company can provide no assurance that its expectations will be achieved.

The risks and uncertainties that could cause actual results to differ materially from expectations are detailed in the Company's first-quarter 2017 earnings release and filings with the Securities and Exchange Commission. The Company disclaims any obligation to update its forward-looking statements.

Having said that, I would like to introduce Management with us today. Eugene Landy, Chairman; Kevin Miller, Chief Financial Officer, and Michael Landy, President and Chief Executive Officer. It is now my pleasure to turn the call over to Monmouth's President and Chief Executive Officer, Michael Landy.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Thanks, Susan. Good morning, everyone, and thank you for joining us. We're pleased to report our results for the first quarter ended December 31, 2016.

Our property portfolio is 100% occupied, representing a 120 basis point increase over the prior-year period and a 40 basis point increase over the prior quarter. In terms of per share earnings, it was another record quarter for Monmouth and represents an excellent start for FY17. Kevin will have more to say on our financial results later.

During the quarter, we acquired two brand-new class A build-to-suit properties. These acquisitions contained a total of 552,000 square feet and were purchased for an aggregate cost of $56.1 million.

Both properties are leased to FedEx Ground with a weighted-average lease term of 13.1 years. The cap rates for these two acquisitions average 6.6%. From a run rate standpoint, we expect these two properties to generate a combined total of approximately $3.7 million in annual rent.

We financed these two acquisitions with a total of $38 million in fixed-rate, 15-year fully-amortizing mortgage debt with an average interest rate of 4%. Also during the quarter, we completed a 51,000 square-foot expansion at our FedEx building in Edinburgh, Texas. This expansion was completed for a cost of approximately $4.8 million and resulted in a $500,000 increase in annual rent effective from the date of completion.

This expansion also resulted in a new 10 year lease which extended the prior lease expiration date from September, 2021, to September, 2026. At the end of the first quarter our gross leasable area was approximately 16.6 million square feet, representing a 15% increase over the prior-year period. Our portfolio now consists of 100 properties geographically diversified across 30 states.

Our weighted-average lease maturity at quarter and increased to 7.4 years from 7.1 years in the prior-year period. From a leasing standpoint in FY17, approximately 9% of our gross leasable area, representing 13 leases totaling approximately 1.5 million square feet, was scheduled to expire.

I'm pleased to report that thus far 6 of the 13 leases have been renewed. As reported last quarter our 87,500 square foot building, leased to FedEx in Fort Myers, renewed for only eight months because they're in the process of moving their operations to our newly constructed 214,000 square foot building at the Southwest Florida International Airport.

Excluding the eight month lease renewal, which we are already working on backfilling, the five leases that have renewed thus far represent approximately 719,000 square feet, or 47% of the expiring square footage, and have a weighted-average lease term of 5.9 years. These five renewals have a weighted-average lease rate of $5.34 per square foot on a GAAP basis and an initial rent of $5.16 per square foot on a cash basis. This represents an increase in the weighted average lease rate of 2.7% on a GAAP basis and a decrease in the weighted average lease rate of 2.8% on a cash basis.

The seven remaining leases that are set to expire this fiscal year are currently under discussion and we expect to have more to share with you in the ensuing quarters. We are very excited about our exceptional acquisition pipeline, which continued to grow over the quarter. We have entered into agreements to acquire a total of nine new build-to-suit properties containing 2.3 million total square feet, representing $250.5 million in acquisitions scheduled to close over the next several quarters.

In keeping with our business model, all of these future acquisitions consist of well located, brand-new build-to-suit projects currently under construction. Six of the nine properties are leased to investment-grade tenants, representing approximately 72% of the total $250.5 million current pipeline.

These nine properties are situated near major airports, major transportation hubs and manufacturing plants that are integral to the tenants' operations. The cap rates on these nine new build-to-suit deals average 6.6% and have a weighted-average lease maturity of 13.5 years.

Subject to satisfactory due diligence, we anticipate closing these transactions upon completion and occupancy. To date, we have already secured $100 million in financing for five of the properties. This new mortgage debt will have a weighted average interest rate of 3.86% and a maturity of 15 years and are all fully-amortizing loans.

Based on the average cap rates and the debt financing that we've already locked in, these five acquisitions are expected to generate a levered return-on-equity of approximately 15%. In this protracted low interest rate environment we have continuously enhanced our strong balance sheet. Our weighted-average debt maturity on our fixed-rate debt at quarter end is a very healthy 10.7 years as compared to 9.3 years in the prior year period.

Our weighted-average interest rate on our fixed-rate debt at quarter end is at a record low of 4.4%. Additionally, during the quarter we used approximately $54 million in net proceeds from our recent $135 million, 6.125% Series C Preferred Offering to redeem all of our 7.625% Series A Preferred Stock. This 150 basis point cost reduction results in approximately $800,000 in annual savings going forward.

These substantial improvements in our capital structure will benefit Monmouth for many years to come, regardless of what interest rates may do in the future. With regards to the US industrial property market, 2016 marked one of the strongest years ever. Fourth-quarter net absorption came in at 46 million square feet, marking the 27th consecutive quarter of positive net absorption and continuing the longest winning streak on record.

In total, the industrial sector absorbed 283 million square feet in 2016. The national average vacancy rate continues to come down and is currently 4.9%, representing an all-time low. National average asking rents are now $5.75 per square foot, which is up 5.5% year-over-year.

New industrial development has been increasing the past three years with 180 million square feet delivered in 2016, marking the largest amount since 2008. However, demand continues to outpace supply by a healthy margin. With the rise of e-commerce, which once again achieved new all-time records this past holiday season, each of our FedEx locations has become a highly coveted foothold for large businesses.

Major retailers are drawn to our FedEx locations so they can get their goods delivered to their customers as fast as possible. Our FedEx Ground locations have become the nucleus of today's logistics clusters that are so vital in supplying online consumption, which is projected to reach $2.4 trillion worldwide by 2018. We have focused our investments on assets that we feel are mission-critical to our strong tenant base.

Our modern industrial property portfolio is 100% occupied because our buildings are integral to our tenants operations. And now Kevin will provide you with greater detail on our financial results for the first quarter of FY17.

Kevin Miller - *Monmouth Real Estate Investment Corporation - CFO*

Thank you, Michael. Core funds from operations for the first quarter of FY17 were $13.9 million, or $0.20 per diluted share. This compares to core FFO for the same period one year ago of $11 million, or $0.17 per diluted share, representing an 18% increase.

Adjusted funds from operations, or AFFO, which excludes net realized gains on our securities investments was $12.9 million, or $0.19 per diluted share for the quarter, compared to $10.7 million or $0.17 per diluted share in the prior year period, representing a 12% increase. On a sequential basis, AFFO per share increased 6% over the prior quarter. As a result of our recent acquisition and expansion activity and our large acquisition pipeline, we anticipate continuing to meaningfully grow our per-share earnings going forward.

Rental and reimbursement revenues for the quarter were $27.2 million, compared to $22.3 million, or an increase of 22% from the previous year's quarter. Net operating income, or NOI, which we define as recurring rental and reimbursement revenues, less property taxes and operating expenses, were $23 million for the quarter, reflecting a 23% increase from the comparable period a year ago. Net income was $9.9 million for the first quarter, compared to $6.9 million in the previous year's first quarter, representing a 42% increase.

As Michael mentioned earlier, during the quarter we acquired two newly constructed industrial properties for a total of $56.1 million. One of the acquisitions, a 339,000 square foot distribution center leased to FedEx Ground for 15 years in the Buffalo, New York MSA, was for $35.1 million. We financed this transaction with a 15-year, fully-amortizing mortgage loan in the amount of $23.5 million at a fixed interest rate of 4.03%.

The other acquisition, a 214,000 square foot distribution center leased to FedEx Ground in Fort Myers, Florida, for 10 years was for $21 million. We financed this transaction with a 15-year, fully-amortizing mortgage loan in the amount of $14.5 million at a fixed interest rate of 3.97%. While most of our growth is attributable to our acquisitions and expansions, we have been able to grow organically as well.

Same property NOI increased 2.4% on a GAAP basis over the prior-year period and increased 3.1% on a cash basis. Our average lease maturity, as of the end of the quarter, increased to 7.4 years as compared to 7.1 years in the prior-year period. Our average annual rent per-square-foot increased 4.9% to $5.80 as of the quarter end as compared to $5.53 one year ago.

As of the end of the quarter, our capital structure consisted of approximately $582 million in debt, of which $506 million was property level fixed-rate mortgage debt and $76 million were loans payable. 87% of our debt is fixed-rate with a weighted-average interest rate of 4.4% as compared to 4.8% in the prior year period. We also had $193 million in perpetual preferred equity at quarter end.

Combined with an equity market capitalization of $1.1 billion, our total market capitalization was approximately $1.8 billion at quarter end. From a credit standpoint, we continue to be conservatively capitalized with net debt to total market capitalization at 29.8%, fixed charge coverage at 2.3 times and our net debt to EBITDA at six times for the quarter.

From a liquidity standpoint, we ended the quarter with $30.7 million in cash and cash equivalents. We also had $124 million available from our credit facility, as well as an additional $100 million potentially available from the accordion feature. In addition, we held $74.3 million in marketable REIT securities, representing 5.4% of our undepreciated assets with an unrealized gain of $10.2 million at quarter end, in addition to the $806,000 in net realized gains generated during the quarter.

And now let me turn it back to Michael before we open up the call for questions.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Thanks, Kevin. To quickly summarize, following the substantial growth achieved in FY16, our first quarter represents an excellent start to the new year. We have generated double-digit AFFO per share growth in each of the prior three years and with our first quarter AFFO per share up 12% from the prior year, FY17 is on track to continue this very favorable trend.

Our new annual report is something that we're very proud of and it is now available on our website. Or, if you prefer to receive a hard copy, please contact us directly and we'll be more than happy to FedEx it out. We'd now be happy to open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Rob Stevenson, Janney.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Good morning, guys. Mike, the seven remaining lease expirations in 2017, how many of those are FedEx?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Let's see here Rob, we have four.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

And do they have other locations close by or other options because it seems like, FedEx, for them to move is a multi-year planning strategy. What's really their option other than if they decide to abandon that specific market?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Right well actually there's five. Sorry. There's five. Correct, Kevin?

Kevin Miller - *Monmouth Real Estate Investment Corporation - CFO*

Yes, that's correct.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

No, I'm very confident to cut to the chase that all five of those FedExs will be renewing. The terms have been agreed to. We're just waiting on signed leases before we announce the specific terms, but we've come to agreement and they're pretty much signed and sealed just not delivered.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Okay, and then the other two, are there major -- do either of those have any major tenant-paid-for improvements that they would be loathe to leave behind?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

So the other two are looking like there won't be -- they are likely going to renew. I think what it's looking like right now for 2017 renewals, we announced 47% retention. We know the Fort Myers facility they are moving into -- they moved into our larger facility at the airport so that one is just an eight month renewal.

We know a tiny building in Urbandale, Iowa won't be renewing, that's Keystone Automotive. So we'll probably get 92% retention is what it's looking like, to probably answer your questions on what 2017 expirations are shaping up like. I will share more as the leases get signed but those are the only two -- the eight month renewal and the non-renewal on Keystone are the only two that we know won't be renewing and the others are pretty much just waiting for signature.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Okay. And then when you look at the $250 million of pipeline today plus the shadow pipeline, whatever you're working on behind that, is it still 55%-60% FedEx or are you bringing some new tenants in there?

I assume that the three non-investment-grade are not FedEx, in the current pipeline, but just wanted to get a feel for, as we look down the road, whether or not the FedEx exposure increases, decreases or basically stays the same when we fast forward a year or a year and a half from now.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Right. The pipeline is 2.3 million square feet. In square footage terms, FedEx is a good percentage. I would say FedEx is 60% in square footage terms, 40% tenants other than FedEx, including International Paper and some smaller non-investment-grade deals. As far as that $250.5 million total purchase price, 80% is investment-grade.

FedEx has been ramping up their network because the demand from e-commerce has been growing exponentially so the FedEx exposure in Monmouth's portfolio is going to go up. We will continue to do non-FedEx deals but we're not going to turn down these great FedEx deals. Our pipeline, as you heard in the prepared remarks, is an average cap rate of 6.6%.

These are brand-new class A facilities with an average lease term of 13.5 years. And just this week, a large portfolio transacted at a cap rate of 6.5%, older buildings, shorter leases, multi-tenant and so that wasn't a bad deal. I'm sure the buyer will do quite well over the long term with it, but it's a good indication of the investments we're making and I feel really good about this pipeline.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Okay. Then just last question, you have been very proactive in terms of lining up your debt financing well in advance of the close of some of these transactions at some very favorable terms. Given where the stock price has been, how do you think about funding the equity portion in advance.

Does the DRIP provide you enough? Do you think about, with the stocks -- as the stock gets at $15-ish, that pre-funding your equity requirements for the rest of the year, at least a part of it, through an offering and lowering debt in the near term? How are you balancing that ball as you think about 2017?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Well, don't forget we raised $135 million recently in perpetual preferred at 6.125%. Our DRIP run rate, last year we raised about $72 million through the dividend reinvestment plan and first quarter came in at $21 million. So the run rate is about $84 million in equity coming in through our dividend reinvestment plan. So we feel that's fine.

We have the Series B Preferred -- I cringe every time I see it on our balance sheet or say it, but it's 7.875% and that comes due in May and we'll be able to clean that up. So ideally, we replace that with Preferred Equity but the pipeline will be funded -- the equity portion, at this point, through our DRIP and the proceeds from our recent preferred offering. Kevin, you want to add to that at all?

Kevin Miller - *Monmouth Real Estate Investment Corporation - CFO*

I'd just like -- just a comment about how we are funding our pipeline and how we have been successful. And I just wanted to point out that we've locked in financing of those nine deals, five of them already. All 15-year, fully-amortizing loans with a weighted-average interest rate of 3.86%.

There's a few left to be locked in, and I know rates have gone up lately, the last few weeks, last month or two. But we're still -- maybe we're not seeing deals with rates in the 3%s anymore, now they are in the low 4%s, maybe 4.25%, and that type of rate, which is still giving us great double-digit levered returns on the deals that we have in the pipeline.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Okay. And then one more. Are you seeing any -- at this point, any upward movement in cap rates on the deals that you're doing or looking at for -- that haven't been consummated yet?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Yes, but the spreads are clearly tightening. As Kevin just said, the spreads, based on our pipeline of 6.6% and his borrowings at 3.86%, that is 274 basis point spread right there. And today, given interest rates have gone up 40, 50 bps and cap rates have maybe gone up 10, 15 bps so the spreads are in the low 200 bps, as opposed to the high 200 basis point spreads.

I do think cap rates are going to need to trend higher but so far not in a meaningful way because industrial is the favored property type and a lot of foreign capital continues to come in seeking industrial assets and that foreign capital has a lower cost of capital and a deteriorating currency that wants to be in a stable currency.

Rob Stevenson - *Janney Montgomery Scott - Analyst*

Okay. Thanks very much, guys.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Thank you, Robert.

Operator

Barry Oxford, D.A. Davidson.

Barry Oxford - *D.A. Davidson & Co. - Analyst*

Great. Hey, guys. Great numbers, also I guess I can't complain about your occupancy rate. But just to piggyback on Rob's question, how many bidders are you getting when you guys are going after these acquisition properties? The number of bids that you are getting versus maybe six months ago?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Are you talking about on the acquisition side or the financing side?

Barry Oxford - *D.A. Davidson & Co. - Analyst*

The acquisition side. So when you guys come in, how many other people are coming in to bid?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

How great is the competition? Numerically, I'm hard-pressed to answer that. I will tell you this, our pipeline's nine acquisitions are with seven different merchant builders. And those merchant builders we have long-term relationships with them and so the relationship is tried and true and while the amount of competition continues to increase, we continue to be able to source deals.

But how much competition numerically, I can't answer it. I will tell you the competition is fierce. I will tell you, we go back with FedEx to 1992 and FedEx did about 10 million to 11 million square feet in growth, FedEx Ground, in 2016, and we did about 15%, 20% of their expansion of their FedEx Ground network.

So I'm very happy with the deals we're getting and I think we're in a good position to continue to grow 15% to 25% growth in GLA year-over-year but, yes, it's a very competitive environment.

Barry Oxford - *D.A. Davidson & Co. - Analyst*

Right. Thanks for that color. Second question on the leasing, I think we have beaten 2017 and gotten that clear but is it too early for you to have conversations about 2018 or have you had some conversations or do you know of any major move out in 2018.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Off the top of my head I don't know any major move outs in 2018. I know some renewals in 2018. And, yes, it's not too early for our team to start proactively looking at 2018.

Barry Oxford - *D.A. Davidson & Co. - Analyst*

You got to give them something to do, Mike, right?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

(Laughter) We're busy. (Laughter)

Barry Oxford - *D.A. Davidson & Co. - Analyst*

All right, guys, I will yield the floor. Thank you.

Operator

Paul Adornato, BMO Capital Markets.

Paul Adornato - *BMO Capital Markets - Analyst*

Yes, hi. I was wondering if you foresaw any implications to the -- or spillover, if 1031 disappears in a tax reform?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Well, yes, the repercussions would be vast and detrimental. There's so much capital that comes in through the 1031 vehicle so we'll have to wait and see if that happens. But it would be a game changer, no question.

Paul Adornato - *BMO Capital Markets - Analyst*

Still on the same topic of the new administration, I see Trump is talking right now about infrastructure. If there are changes in infrastructure could that change the distribution patterns? And how do you think you're positioned over the long term?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Well, I think if you're referring to the stimulus of investing in modernizing the US infrastructure, I know that Fred Smith has been in front of Capital Hill several times and it's much needed and that would be stimulative for the economy.

So it's a long time coming and we have a new Transportation Secretary and so many goods are being shipped B2C, direct to your house, that there's a lot of things that need to be changed because the current infrastructure didn't contemplate e-commerce. But that's very good for industrial and it's pretty encouraging, as far as demand for industrial and growth for the broad economy at large, the rhetoric I've been reading and hearing.

Paul Adornato - *BMO Capital Markets - Analyst*

Okay and finally the marketable securities portfolio, I think you mentioned was about 5% of total assets. Will you cap it at a certain number? Was it 10% or is it -- or do you look at it on an absolute basis?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Absolutely, we have a self-imposed ceiling of approximately 10% of assets and we have a self-imposed floor of approximately 5% of assets because we want to have some liquid real estate on our balance sheet. So we're in the low range of the bandwidth right now, about 5% of assets are in liquid real estate. But a year ago there was a great arbitrage situation to invest in liquid real estate, the ten year was at 1.9% and many REITs were yielding 8% or greater.

Today, the ten year is hovering around 2.5% and it's hard to find really largely discounted REITs, so we increase our portfolio when there's compelling opportunity to do so and there is today only on a case-by-case basis. But the REITs are largely correlated and you will find opportunities to buy real estate cheaper on Wall Street and we will increase our portfolio when those opportunities arise.

Paul Adornato - *BMO Capital Markets - Analyst*

Okay, great. Thanks so much.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Thanks, Paul.

Operator

Craig Kucera, Wunderlich.

Craig Kucera - *Wunderlich Securities, Inc. - Analyst*

Hey, good morning, guys. I want to start first on your balance sheet, I think you got about $50 million of debt maturing this year. Can you talk about your plans to handle this year, whether you're going to refinance that as fixed-rate debt or maybe pay it down and put it on the line and what your thoughts are there?

Kevin Miller - *Monmouth Real Estate Investment Corporation - CFO*

Yes, sure. I will take that. That's true there is about $50 million of amortization next year and it's pretty much that every year going forward. And of that, there's probably about 10 more loans that we are -- well, actually about 13 more loans that we plan on paying off for the remainder of the fiscal year. Three of those loans we actually paid recently subsequent to the quarter. And our plan is to just keep those properties unencumbered which increases our availability on our line.

So thus far, through today, we've paid off four loans in this fiscal year, about $10.8 million of loans that'll generate about $2.6 million in NOI and they'll free up about $41 million in properties. And then for the remainder of the year, we'll probably pay off about 10 more properties or properties with loans that generate about $7 million in NOI and that will free up about $105 million in property.

So our plan is use fixed-rate debt on the new acquisitions and then continue to pay off the amortizing debt on the legacy acquisitions, which frees up our unencumbered assets and helps us have more liquidity.

Craig Kucera - *Wunderlich Securities, Inc. - Analyst*

Got it. When you think about spreads on investment maybe being a little tighter than they have if cap rates are necessarily backing up in tandem or certainly as much as where interest rates have moved, does that make you think you might want to maybe do a little bit of floating-rate debt or are you still dedicated to having longer-term, amortizing fixed-rate debt on the acquisitions even beyond those, as you look forward in the future?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

No, don't get us wrong, Craig, the spreads are still very wide. 200 basis points is our rule of thumb over our 50 year history and the average is 6% interest rate, 8% cap rate, and we've gone lower than that and we're still getting well in excess of that.

So they're just not historically wide spreads, I think the high watermark was in the mid-300 basis point range. We were doing deals at 340, 350 basis point spreads but those were anomalies and we did a lot of deals in the high 200, 280 basis point spread. Kevin's locked in 274 basis point spreads, which is very accretive,15% levered returns on equity. But even with rising rates, we're still getting well in excess of 200 basis point spreads.

Craig Kucera - *Wunderlich Securities, Inc. - Analyst*

Okay. And one more from me, just on your redevelopment pipeline. I know you announced one this quarter and I didn't see any in the disclosure, but as you're talking to your tenants do you anticipate that you'll see some incremental expansion opportunities this year or is that taking up a bit of a breather?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

No, an exciting part of our portfolio is that we have plentiful amount of land. Our pipeline has a land-to-building ratio of nearly 7 to 1. Our portfolio at large has nearly 6 to 1 land-to-building. So in our new annual report, which in my prepared remarks I referenced that we encourage all our investors to take a look at it, we show this year three case studies.

And in all three case studies there's ample land for expansion and these tenants likely, over the mid-term, will need additional space and we can accommodate that. Their businesses are strong and getting stronger and growing. So I would look at those three case studies in our annual report as just an illustration of our portfolio at large and the expansion capacity that we have.

Craig Kucera - *Wunderlich Securities, Inc. - Analyst*

Okay. Thank you.

Operator

(Operator Instructions)

Michael Boulegeris, Boulegeris Investments.

Michael Boulegeris - *Boulegeris Investments, Inc. - Analyst*

Thank you and congratulations on the continued, sustained qualitative growth at Monmouth. Michael, you noted that as of the new FedEx Ground deals, Monmouth is securing greater percentage of those new acquisition in recent years. I think you said in the 20% range. What do you attribute that to?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Our long-term relationship. Our first deal with FedEx was in 1992. They're still in the building. They certainly know that we're a great landlord and one of their preferred landlords and we work well together. We view them as a partner.

We view our shareholders as partners, our banking relationships as partners, all down the line. So it's just a matter of treating them -- looking at the long-term, looking for a mutually satisfactory outcome and we've always been willing, whether it's FedEx or Coca-Cola or any of our strong tenant base, to give up growth for quality. And one of the things I think the market maybe doesn't value to the correct extent is the stability that our cash flows derive.

They are very stable, predictable income streams. And so in our new letter to shareholders, we talk about how a $5 per square foot rent could actually be greater than a $6 rent and I think part of that is who's paying the rent and the longevity, durability, predictability of the cash flows that Monmouth generates.

Michael Boulegeris - *Boulegeris Investments, Inc. - Analyst*

Thank you for that clarity. May I ask, Gene, you, in a recent interview talked about expecting the unexpected and what might be some of the unexpecteds as you look into the next decade that may be impactful to the business -- to the Monmouth business. For example, I think you discussed inflation as it comes up on you real quick before you know it. But in general, what are some of the unexpecteds that Monmouth is preparing for in the coming years?

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Look, Gene's with us telephonically, so while Susan gears up his phone to come on the line, the thing about the world is nobody knows what the world will look like 10 years from now. And the trick is to build a business model that performs well throughout the economic cycles, so I think part of what Gene is saying is that in these black -- the whole definition of a black swan is something that was unforeseen.

But when you have long-term leases to strong investment grade tenants that are mission-critical to their business, that you tend to really put some space on your competition during the weak economic cycles because, while they're on their heels playing defense, your business is still very stable. But, Susan, you want to bring Gene on? Okay, so let's turn it over to Gene so he can answer that more fully.

Eugene Landy - *Monmouth Real Estate Investment Corporation - Chairman*

Mike, I'm always glad to come on the line. I hope everyone can hear me. The future is very, very bright. The economy is strong. We're not advocates of inflation.

We think inflation is bad but we don't control that and it looks to us that we're going to have inflation, that the labor market is tightening and there's a lot of other indications. And when you have a portfolio of leveraged real estate and you take a long-term view, the value of your properties go up dramatically and we see our portfolio values 10, 15 years from now to be substantially higher.

We started buying buildings at much lower prices per foot and now we're over $100 a foot and we have a portfolio of over $1 billion. So in terms of inflated dollars, we see that Monmouth REIT can be an excellent investment. And when we make these so-called long-term investments, we think 10 or 15 years is short-term, and if you look forward 10, 15 years and you look at inflation at 3%, 4% for that period, those increases in values will be very positive for our shareholders.

So we're going to have a -- create a terrific portfolio of valuable buildings in a good business, needed by our tenants and the values of them will not only be the current return. The important point is that everybody looks at FFO and current dividend but you really have to look at appreciation. When you buy real estate there are two components.

The first component is your current return but the second component is your long-term return, which includes appreciation and we think that Monmouth REIT has a terrific future in terms of potential appreciation.

Michael Boulegeris - *Boulegeris Investments, Inc. - Analyst*

Well, thank you for that -- those comments, Gene. Michael, if I could ask you one question and then one for Kevin. Last quarter it seemed like you took some incremental profits in your outstanding REIT portfolio.

Is your bias to continue to lean in that direction in support of the fledgling pipeline that you have? And just an administrative -- or question for Kevin on the -- it seems like reimbursements ticked up almost $1 million. Is there anything that was driving that this last quarter? Thank you.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Yes, so on the gains, we have $10.2 million unrealized gains at the end of the quarter so there's a lot of fruit on the vine, so to speak. Over the last seven years we've generated approximately $28 million in net realized gains on our portfolio. I don't have big plans to buy or sell at the moment. The portfolio's only 5% of gross assets, as we said earlier, and it's generating good income.

But, yes, it's good to have liquid real estate because the money is there. It's an unencumbered portfolio, we could borrow at a very low rate, approximately $40 million against the portfolio. So no big plans to harvest that fruit but we'll keep a watchful eye.

But again, a year ago there was a great arbitrage situation and we took advantage of it and that's why in FY16 you saw us realize $4.4 million and that's why in the first quarter you saw us realize another $800,000. But right now we're kind of in watch and wait mode. Kevin, you want to take the other half?

Kevin Miller - *Monmouth Real Estate Investment Corporation - CFO*

So on the question about the bump in the reimbursement revenues this quarter. If you look at it on a percentage basis, it is not that much of an increase. We were reimbursed about 92% of our operating expenses versus last year about 89%. But, yes, there was a slight bump this quarter.

I believe there was a pretty big, major -- not major, but there was a parking lot repair that this particular quarter, we were able to bill back for. So it could be lumpy depending on what the tenants need and what kind of repairs are needed that we bill back. But in general, our leases are net leases and the only thing that usually we have to cover are the roof and structure and usually the other type of expenses are borne by the tenant that are billed back, so that's is the reason for the slight increase this particular quarter.

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Michael Boulegeris - *Boulegeris Investments, Inc. - Analyst*

Great. Thank you.

Operator

This concludes our question and answer session. I would like to turn the conference back over to Michael Landy for any closing remarks.

Michael Landy - *Monmouth Real Estate Investment Corporation - President and CEO*

Well, thank you, Laura. I'd like to thank everyone for joining us on this call and for their continued support and interest in Monmouth. As always, Kevin, Gene and I are available for any follow-up questions.

We look forward to reporting back to you after our second-quarter. Thank you.

Operator

The conference is now concluded. Thank you for attending today's presentation. The teleconference replay will be available in approximately one hour. To access this replay, please dial US toll-free 1-877-344-7529 or international 1-412-317-0088. The conference ID number is 10097752. Thank you and please disconnect your lines at this time.
