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# Monmouth Real Estate Investment Corporation

NYSE:MNR

## FQ2 2018 Earnings Call Transcripts

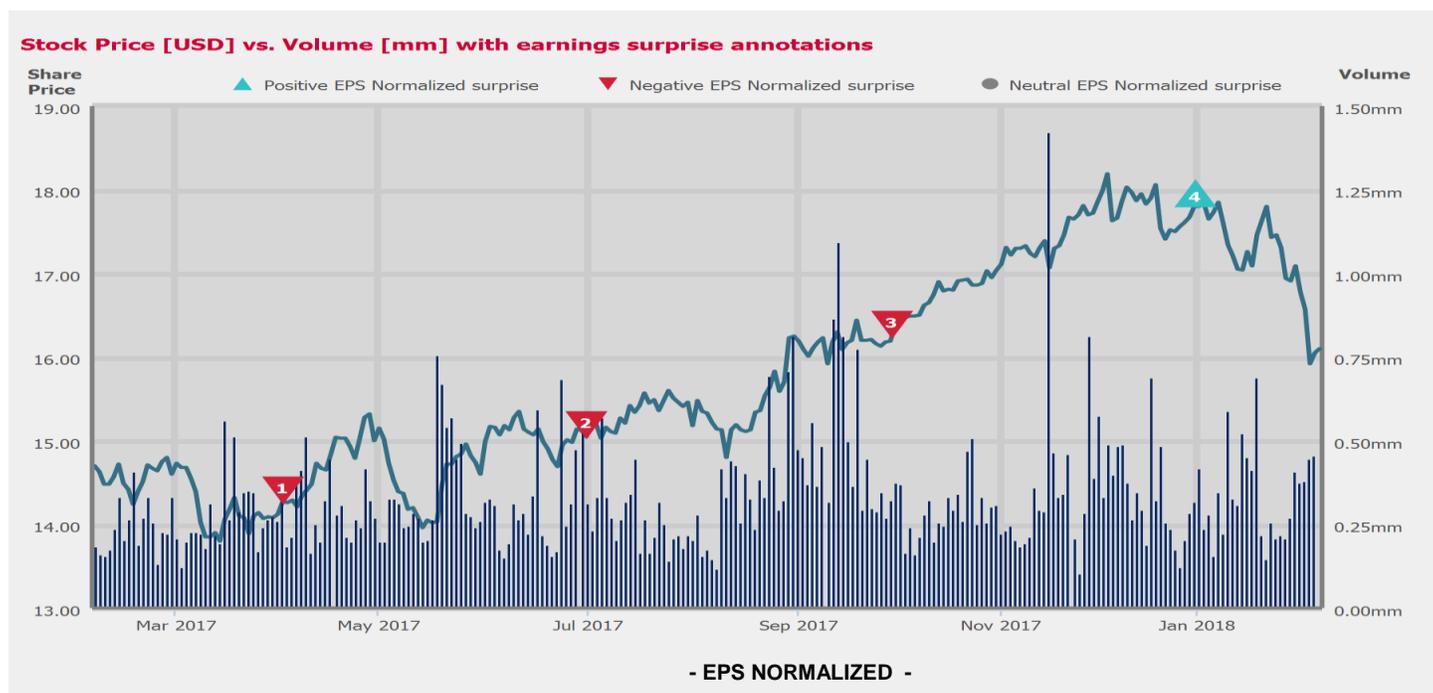
Wednesday, May 09, 2018 2:00 PM GMT

### S&P Capital IQ Estimates

	-FQ2 2018-			-FQ3 2018-	-FY 2018-	-FY 2019-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.13	0.10	▼ (23.08 %)	0.12	0.55	0.48
Revenue	-	-	▼ (1.03 %)	-	-	-
Revenue (mm)	33.97	33.62	-	35.10	137.90	145.90

Currency: USD

Consensus as of Apr-13-2018 6:36 PM GMT



	CONSENSUS	ACTUAL	SURPRISE
FQ2 2017	0.08	0.07	▼ <sup>1</sup> (22.22 %)
FQ3 2017	0.08	0.07	▼ <sup>2</sup> (22.22 %)
FQ4 2017	0.11	0.09	▼ <sup>3</sup> (18.18 %)
FQ1 2018	0.10	0.17	▲ <sup>4</sup> 70.00 %

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# Call Participants

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## EXECUTIVES

**Eugene W. Landy**  
*Founder & Chairman*

**Kevin S. Miller**  
*CFO, Chief Accounting Officer,  
Treasurer & Executive Director*

**Michael P. Landy**  
*CEO, President & Executive Director*

**Richard P. Molke**  
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**Susan M. Jordan**  
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# Presentation

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## Operator

Good morning, and welcome to Monmouth Real Estate Investment Corporation's Second Quarter 2018 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 now begin.

## Susan M. Jordan

*Vice President of Investor Relations*

Thank you very much, operator.

In addition to the 10-Q that we have filed with the SEC yesterday, we filed an unaudited quarterly supplemental information presentation. This supplemental information presentation, along with the 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 second quarter 2018 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'd like to introduce management with us today, Eugene Landy, Chairman; Michael Landy, President and Chief Executive Officer; Kevin Miller, Chief Financial Officer; and Richard Molke, Vice President of Asset Management.

It is now my pleasure to turn the call over to Monmouth's President and Chief Executive Officer, Michael Landy.

## Michael P. Landy

*CEO, President & Executive Director*

Thanks, Susan. Good morning, everyone, and thank you for joining us. We are pleased to discuss our results for the second quarter ended March 31.

As of the quarter-end, our portfolio consisted of 109 properties, geographically diversified across 30 states. At quarter-end, Monmouth's property portfolio was 99.2% occupied, representing our 9th consecutive quarter with an occupancy rate of 99% or greater.

During the quarter, we acquired one brand-new Class A built-to-suit property. This acquisition was purchased for a cost of \$57.5 million and contains a total of 832,000 square feet. This property located in Savannah, Georgia is leased for 10 years to Shaw Industries, one of the largest-flooring manufacturers and suppliers in the world. It is situated on 62 acres near the Port of Savannah, which is the fourth largest port in the U.S. and is the fastest-growing port in North America.

We expect this property to generate annual rent of approximately \$3.6 million. We are very pleased to add Shaw Industries, a wholly owned subsidiary of Berkshire Hathaway to our high-quality tenant roster.

The recently expanded Panama Canal has been surpassing all projections with over 400 million tons in shipments last year. This has helped propel shipping container growth on the East Coast ports to outpace that of the Western ports.

In Savannah, shipping container volume grew at a multiple of 4x that of the West Coast ports. In a similar manner to building our large e-commerce presence, we have strategically assembled a portfolio that is very well situated to benefit from these long-term trends.

Subsequent to quarter-end, we acquired a brand-new 399,000 square foot facility for \$30.8 million, leased for 10 years to B. Braun Medical in Daytona Beach, Florida. This property is situated on 28 acres located one mile east of Interstate 95 and is near the Daytona Beach International Airport.

From a run rate standpoint, we expect this property to generate annual rent of approximately \$2.1 million.

Following last year's 17% increase in our gross leasable area, thus far in fiscal 2018, we've increased our GLA by 1.5 million square feet, representing a 20% increase over the prior year period. This year-over-year growth has been achieved through the acquisition of 12 brand-new Class A properties at an aggregate cost of \$370.8 million.

Our gross leasable area now stands at 20.3 million square feet and consists of 110 properties geographically diversified across 30 states.

Our weighted average building age as of the quarter-end was 9.2 years, representing the youngest portfolio in the industrial REIT sector.

As I've stated in the past, building age is an increasingly important metric for our property type, as demand for modern industrial space, driven by the rapid growth in e-commerce continues to be the primary driver of the sustained positive net absorption trends the industrial sector has been experiencing.

Modern industrial buildings are similar to 20th-century industrial buildings in name only. These omnichannel assets involve substantial infrastructure investments made by our tenants and contain ample acreage. Our portfolio currently contains a land-to-building ratio of 5:1. Our weighted average lease maturity at quarter-end was 7.8 years as compared with 7.4 years in the prior year period, representing a 5% increase.

From a leasing standpoint, in fiscal 2018, 16 leases totaling approximately 1.5 million square feet or approximately 8% of our gross leasable area are scheduled to expire. I am pleased to report that thus far, 7 of the 16 leases have been renewed. One of the 7 leases, which is with FedEx Ground for a property located in Charleston, South Carolina, renewed for only 4 months because the tenant plans to move its operations from our 92,000-square foot facility to a new 261,000-square foot facility that we are currently under contract to acquire upon completion.

This property will be leased to FedEx Ground pursuant to a new 15-year lease. The other 6 lease renewals to date represent approximately 569,000 square feet or 37% of the expiring GLA. These 6 lease renewals have a weighted average lease term of 6.1 years and result in an increase in the weighted average lease rate of 3.9% on a GAAP basis and 1.5% on a cash basis. Of the 9 remaining leases, originally set to expire during fiscal 2018, two of the properties were sold and one of the properties is under contract to be sold. These 3 properties represent 12% of the expiring GLA for fiscal 2018.

Additionally, 1 property, representing 15% of the expiring square footage was retenanted for 3 years. The remaining 5 properties, of which, only 1 is vacant, are currently under discussion. We expect to have more to report on these

properties in the ensuing quarters.

Looking at our balance sheet, our weighted average debt maturity on our fixed-rate debt at quarter-end is a very strong 11.5 years as compared to 10.7 years in the prior year period, representing one of the longest debt maturity schedules in the entire REIT sector.

At quarter-end, 81% of our \$794.2 million in total debt was fixed rate. Our weighted average interest rate on our fixed-rate debt at quarter-end was 4.1% as compared to 4.4% 1 year ago.

In addition, during the first half of fiscal 2018, we sold 1.26 million shares of our 6.125% Series C preferred stock through our ATM program at a weighted average price of \$25.09 per share, generating net proceeds of approximately \$31 million.

As of the end of the quarter, 11.1 million shares of our 6.125% Series C preferred stock were issued and outstanding, representing an aggregate liquidation value of \$277.4 million.

Because our Series C was trading below par throughout most of this recent quarter, only 216,000 shares were issued during the quarter.

During the first half of fiscal 2018, we raised approximately \$49 million in common equity through our dividend reinvestment plan at an average price of \$15.51 per share. Of this amount, a total of \$6 million in dividends were reinvested this quarter, representing a 23% participation rate in our dividend reinvestment plan.

The rising interest rate environment has resulted in a pronounced sell-off in REIT securities. Our securities portfolio went from \$4.1 million in unrealized losses at the end of last quarter to \$31.1 million in unrealized losses at the end of this quarter. Because real estate is priced simultaneously in 2 markets, public and private, arbitrage opportunities can present themselves. The public REIT market now represents a substantial discount to private market valuations, and we are confident that this discrepancy will be resolved over time.

We increased our securities holdings from \$123.8 million at the end of fiscal 2017 to \$144.6 million at the end of the current quarter, representing a 17% increase.

Over the prior year period, our dividend income increased by 101% from \$1.4 million in the second quarter of last year to \$2.9 million in the recent quarter.

Our securities portfolio currently represents approximately 8.3% of our undepreciated total assets. With regards to our property acquisition pipeline, which grew over the quarter, we currently have commitments to purchase 2 brand-new Class A built-to-suit industrial assets. One is a 363,000-square foot industrial building that is leased to Amazon, representing the second Amazon distribution center to be added to our high-quality portfolio. The other acquisition under contract is a 261,000-square foot industrial building leased to FedEx Ground. The total purchase price for these 2 properties is approximately \$80.9 million and they have a weighted average lease term of 12.3 years. We anticipate closing these transactions sometime during the remainder of fiscal 2018 and the first quarter of fiscal 2019.

To take advantage of today's attractive interest rate environment, we have already locked in very favorable financing for one of these acquisitions. The financing terms for this acquisition are \$29.9 million in proceeds, representing 63% of the total cost with an interest rate of 3.82%. This mortgage is a 15-year self amortizing loan and will result in a levered return on equity of approximately 12%.

With regards to the overall U.S. industrial market outlook, following last year's strong performance, 2018 is off to a very good start with approximately 41 million square feet of positive net absorption during the first quarter. This extends the

record streak of positive net absorption to 32 consecutive quarters or 8 straight years. The national average vacancy rate continues to show strength and is currently 4.5% unchanged over the quarter and representing a 90 basis point improvement from the prior year.

This marks the lowest vacancy level in over 30 years. This increased demand is driving rents higher to an average asking rent of \$5.99 per square foot, representing a 5.5% increase over the prior year period. Currently there is approximately 251 million square feet of new industrial construction taking place in the U.S, representing a 17% increase over the prior year. Approximately 2/3 of this new supply is speculative development.

Intermodal rail volume, which correlates closely to warehouse demand has been posting record numbers the past 2 months. E-commerce sales continue to grow at a 16% compound annual growth rate. All indicators are pointing towards strong demand for U.S. industrial space for the foreseeable future.

The U.S. economy continues to show strength with first quarter real GDP weighing in at an annualized rate of 2.3%, driven primarily by increased business spending. This follows 2.9% real GDP growth in the prior quarter. The U.S. unemployment rate in April fell to a record low of 3.9%, resulting in heightened inflation expectations.

Year-over-year private sector wages grew at 2.9% through March, representing the largest increase in nearly a decade. Despite the broad-based decline in public REIT valuations, industrial property cap rates have continued to compress lower and construction costs have continued to rise. This has resulted in a large disparity between public and private market valuations. Based upon recent transaction announcements, Monmouth's portfolio comprised of modern high-quality assets on long-term leases to investment grade tenants has appreciated in value substantially.

And now Kevin will provide you with greater detail on our financial results for the second quarter of fiscal 2018.

**Kevin S. Miller**

*CFO, Chief Accounting Officer, Treasurer & Executive Director*

Thank you, Michael. Core funds from operations for the second quarter of fiscal 2018 were \$16.8 million or \$0.22 per diluted share. This compares to core FFO for the same period 1 year ago of \$12.4 million or \$0.17 per diluted share, representing a 29% increase from the previous year.

Adjusted funds from operations, or AFFO, were \$0.22 per diluted share for the recent quarter as compared to \$0.18 per diluted share a year ago, also representing a 22% increase from the previous year.

Rental and reimbursement revenues for the quarter were \$33.6 million compared to \$27.3 million, representing an increase of 23% from the previous year.

Net operating income was \$28.4 million for the quarter, reflecting a 22% increase from the comparable period a year ago. This increase was due to the additional income related to the 11 industrial properties purchased since the prior year period.

Net income was \$11.6 million for the second quarter compared to \$8.4 million in the previous year's second quarter, representing a 38% increase.

As Michael mentioned, occupancy at quarter-end was 99.2% compared to 100% 1 year ago, representing an 80 basis point decrease. We are under contract to sell an 87,500 square foot vacant building located in Fort Myers, Florida, for \$6.4 million, which is approximately \$2.4 million above our U.S. GAAP net book carrying value. The sale is expected to close during the third quarter, at which time our occupancy rate is expected to increase to 99.6%.

Our average lease maturity, as of the end of the quarter, was 7.8 years as compared to 7.4 years a year ago, representing an increase of 5.4%.

Our average annual rent per square foot was \$5.91 as of the quarter-end as compared to \$5.79 a year ago, representing an increase of 2.1%. This average rent is 1.3% below the current national average asking rent of \$5.99 per square foot.

With regards to our same property metrics for the current 3-month period, our same property occupancy decreased 110 basis points to 98.9%, and our same property NOI increased 0.2% on a GAAP basis and 0.3% on a cash basis due to the increased rents.

As Michael mentioned earlier, during the quarter, we acquired a newly constructed 832,000 square foot distribution center leased to Shaw Industries, a wholly owned subsidiary of Berkshire Hathaway for 10 years in Savannah, Georgia. We financed this transaction with a 14-year fully amortizing mortgage loan in the amount of \$33.3 million, at a fixed interest rate of 3.53%.

Subsequent to the quarter-end, we purchased a newly constructed 399,000-square foot distribution center leased to B. Braun Medical for 10 years in Daytona Beach, Florida. We financed this transaction with a 15-year fully amortizing mortgage loan in the amount of \$19.5 million at a fixed interest rate of 4.25%.

Thus far, during fiscal 2018, we've acquired 4 newly constructed properties, totaling 1.7 million square feet for \$140.4 million with a weighted average lease maturity of 10.4 years.

These acquisitions were financed with \$86.6 million in fixed-rate mortgage debt with a weighted average interest rate of 3.83% and a weighted average debt maturity of 13.5 years.

As of the quarter-end, our capital structure consisted of approximately \$794 million in debt, of which \$640 million was property level fixed-rate mortgage debt and \$154 million were loans payable. 81% of our total debt is fixed rate with a weighted average interest rate of 4.1% as compared to 4.4% in the prior year period. We also had \$277 million in perpetual preferred equity at quarter-end.

Our total debt plus preferred equity, combined with an equity market capitalization of \$1.2 billion, results in a total market capitalization of approximately \$2.2 billion at quarter-end.

From a credit standpoint, we continue to be conservatively capitalized with our net debt to total market capitalization at 34.4%. Our net debt plus preferred equity to total market capitalization at 46.7%, our fixed charge coverage at 2.4x and our net debt to adjusted EBITDA at 6.7x.

From a liquidity standpoint, we ended the quarter with \$12.5 million in cash and cash equivalents. We also had \$90 million available from our credit facility as well as an additional \$100 million potentially available from the accordion feature.

In addition, we held \$144.6 million in marketable REIT securities at quarter-end, representing 8.3% of our total undepreciated assets.

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

**Michael P. Landy**  
*CEO, President & Executive Director*

Thanks, Kevin. In summary, Monmouth's strong performance has continued through this most recent quarter.

Our AFFO per share of \$0.22, represents a 22% improvement over the prior year period. With a very conservative 77% AFFO dividend payout ratio, we remain confident about continuing to provide our shareholders with the high-quality reliable income streams that we have delivered for over a quarter century.

Our 99.2% occupancy rate at quarter-end illustrates the mission-critical nature of our properties for our investment grade tenant base. This quarter marked our ninth consecutive quarter with an occupancy rate of 99% or greater. We have 2 exceptional assets currently in our acquisition pipeline, and we anticipate continued long-term qualitative growth for the remainder of fiscal 2018.

We'd now be happy to take your questions.

## Question and Answer

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### Operator

[Operator Instructions] And our first question will come from Jeremy Metz of BMO Capital Markets.

### Robert Jeremy Metz

*BMO Capital Markets Equity Research*

In terms of the remaining 2018 expirations, if we go back to the last call, I believe these are all still outstanding so it doesn't necessarily sound like there is a lot of progress necessarily made during the quarter and out of that short-term FedEx extension. So just given demand that we keep hearing about the intense focus your customers are putting on the supply chain, wondering just what is holding up some of these decisions here especially if the trends are only continuing to move higher. Then maybe as a follow-on to that, what's the longer-term plan for that building FedEx is vacating in a few months?

### Michael P. Landy

*CEO, President & Executive Director*

Okay, I'm going to turn it over to Rich. But before I do that, the premise that not a lot has happened, I don't disagree with you for making that premise, but it's erroneous. We've had a lot of movement. FedEx is likely to remain in the buildings, we just don't report until the lease is signed. But we have several letters of terms that have been agreed to. So I'll turn it over to Rich. And if you could just a little more granular on the progress we've made over the quarter.

### Richard P. Molke

*Vice President of Asset Management*

So the 4 leases that remained 403 square feet, that's representing 26% of expiring GLA. Of those 4, 3 of these are FedEx leases, totaling 300,000 square feet or 75% of the remaining GLA set to expire.

### Michael P. Landy

*CEO, President & Executive Director*

And of those 3, we have letters of terms...

### Richard P. Molke

*Vice President of Asset Management*

Which are 75% of the remaining 4 with a weighted average term of about 9 years.

### Michael P. Landy

*CEO, President & Executive Director*

So we've got a couple 10-year renewals coming, and I guess, one a little less. Go on, Rich.

### Richard P. Molke

*Vice President of Asset Management*

And for Charleston, that's a really good market, it's been on the market for a little while now, we've had good traffic and there's a few things we're working on. So we're really positive on backfilling that shortly.

**Robert Jeremy Metz**

*BMO Capital Markets Equity Research*

Yes. And sorry, in the longer-term plan for the FedEx one -- they are leaving in a few months it sounds like, right, and they are going to -- you're building another building for them?

**Richard P. Molke**

*Vice President of Asset Management*

Correct. That's the Charleston FedEx.

**Robert Jeremy Metz**

*BMO Capital Markets Equity Research*

I got you. Okay. And then in terms of the project you have under contract for Amazon. This is your second one, I think the first one was closed earlier this year. Just wondering if you can Mike maybe talk a little bit about the process here, I don't think you mentioned where it was located. And then what the yield looks like, as I imagine this would have been a pretty heavily sought after deal.

**Michael P. Landy**

*CEO, President & Executive Director*

Yes, Jeremy. I'm only at liberty to say so much on that acquisition. I'll tell you it's in a market that will be a direct beneficiary of the expanded Panama Canal. Certainly, Amazon assets are highly coveted and very competitively bid. We're being very disciplined. Our pipeline only has 2 acquisitions, but they're both Class A high-quality assets to investment grade tenants, brand-new buildings on long-term leases but industrial cap rates continue to compress and we feel really fortunate we were able to acquire both of these properties. So one is -- the FedEx is in a high 5% cap rate and Amazon has 2% bumps, that will get us a 6.2% average cap rate over the 10-year lease.

**Robert Jeremy Metz**

*BMO Capital Markets Equity Research*

Appreciate that. I just have one last one for Kevin here. Just including the preferred you're around, call it 8 to 9x net debt to EBITDA, depending on how you look at the securities book. I was wondering, what's the longer-term goal for leverage, and how should we think about the bridge and the timing to get there? And just your thoughts on using equity outside of the DRIP?

**Michael P. Landy**

*CEO, President & Executive Director*

Okay. I just want to take that first, Kevin. You think about that for a second. But Jeremy, when you say 8 to 9x depending on how you look at the securities portfolio. First, I think you got to look at the preferred equity. Monmouth has \$277 million in perpetual preferred equity, which you're treating as debt. And so that's about 26% of our total debt is in perpetual preferred equity, which never matures. So you're not looking at it apples-to-apples with other REITs that maybe didn't take advantage of this low-interest rate, flat yield curve environment, so we took advantage of it. We increased our capital stack for perpetual preferred equity to 26%. And that takes our weighted average maturities out eternally. And as Kevin mentioned in our prepared remarks, our weighted average debt maturity, not counting the perpetual preferred goes out 11.5 years. So we're not as highly levered as a net debt to EBITDA of 8x would make you think. You back out the preferred and you get 6.7x. You got to take into account that the cash flow that Monmouth derives is from long-term leases to investment grade tenants. And that certainly results in a capital structure that can support a lot more leverage than would otherwise be the case. You saw in the financial crisis our 100% payout ratio for our dividend was maintained. So I'll turn it over to you, Kevin, if you want to add anything to that. But I do think you should look apples-to-apples and treat preferred equity -- perpetual preferred equity different than short-term debt.

**Kevin S. Miller**

*CFO, Chief Accounting Officer, Treasurer & Executive Director*

Yes. Everything -- I think Michael covered all the main points. The only thing I'd like to add, and I think Mike mentioned this, our income stream is 85% investment grade. So I don't think you could just compare every other REIT with their income stream, with our income stream and then compare it to the debt. So I think we could support a little bit higher net debt to EBITDA than maybe some other REITs, based on our high-quality income stream. And just as far as going forward, we're just going to continue to do what we've been doing which is basically financing new acquisitions with long-term debt that's amortizing and is matched with the lease term. So that way our revenue is matched with our debt.

**Operator**

The next question comes from Barry Oxford of D.A. Davidson.

**Barry Paul Oxford**

*D.A. Davidson & Co., Research Division*

To build off of the preferred question, Mike, when the preferred is trading, let's say below par or at some point, at what point would you say look, I'm not going to issue the preferred, it just does doesn't make any sense at -- whether it's \$25 or \$24 or whatever number?

**Michael P. Landy**

*CEO, President & Executive Director*

Okay. So the money we've raised thus far has been above par, \$25.09. And if you look at \$24.25 results in a 6.3% yield. So I wouldn't be hesitant to take on capital at 6.3%, but I don't think I'd go much lower than that. It depends on the use of proceeds, and what sort of returns we can get so that's the other factor, in this quarter we issued very little preferred. So it's a good thing to have. We're big believers in matching long-term assets with long-term financing and perpetual preferred equity. I think we're going to look back and be very pleased with the \$277 million we've raised thus far. Gene, you want to add that at all?

**Eugene W. Landy**

*Founder & Chairman*

Well, that's our basic structure. We're great believers in having one pillar of our capital being preferred and anytime you can get capital at 6.25% perpetual capital. We think that's a very good investment. We -- and I believe the company follows this. People always keep looking at what the current return is in terms of FFO, and I look at total returns. And I think the total return is much higher over 10, 15-year period. So if you have investments that are yielding 5.75% or 6%, and you're paying 6.25% on preferred, then you still make a lot of money over 10 years, if you have the 5%, 6% inflation. So we really believe in issuing preferred and that the common shareholders will get very pleasant returns over a decade.

**Barry Paul Oxford**

*D.A. Davidson & Co., Research Division*

Great. Mike, just switching gears a little bit. When you look at your book of portfolios and you've grown it, I think the number you said was \$144 million. Where do you see that kind of capping out? And let's say the spread from Main Street to Wall Street even gets wider going forward and it becomes more attractive to buy securities, let's say, I hope that doesn't happen, but let's say that it does, where is your kind of cap no matter what the spread is, it's as high as I'm going to go?

**Michael P. Landy**

*CEO, President & Executive Director*

Sure. We've made a lot of money over the years investing in REIT securities, where -- we -- not by intention, but we've

never bought at the bottom, and we always sell too soon. But we've always done very well being conservative long-term value investors, and we cap it at 10% of gross assets. Gross assets are about \$1.8 billion, with our pipeline it will get a little higher over time. Right now, it's \$150 million as you mentioned, it's 8.3% of gross assets. So we have some headroom and no question the spreads have gotten better. We increased our portfolio year-over-year by 45%, but our dividend income's grown by 101%. So it's been a good adjunct. We see ourselves as capital allocators into real estate investments. There's 2 markets, the public market and the private market. The private market is 85% of the U.S. real estate. And so with only 15% publicly traded, you get inefficiencies. We watch it closely and nothing in the market is new. Everything that happens in the market has happened before and will likely happen again. So I'm hesitant to say things are different this time. But there are a couple of things that are different at the moment and that would be that the market is highly indexed today, there's more ETFs and index funds than there are total companies. And so that's created a hyper correlation within the sectors. And then real estate's now on its own sector, real estate used to be in the financial sector with insurance companies and banks, and I think ultimately, it's great that real estate's in its own sector. But by being out there alone in this highly indexed environment, and rising interest rate environment, we've become highly convex. And so you're seeing with every rise in the 10-year treasury rate, REIT's have just been selling entirely, the whole sector. So it's creating a real anomaly, a real discrepancy between what's happening in the larger private market and the public market, and I was excited about it last quarter, I'm excited about it today. And I don't mind if real estate gets cheaper. We like investing, most of the money you make on an investment is determined by your purchase price. And purchase pricing on a computer-traded real estate is a lot more advantageous than in the highly competitive private market at the moment.

**Barry Paul Oxford**

*D.A. Davidson & Co., Research Division*

Right, got you. One last question, Mike, again switching gears. When we look at your acquisition pipeline and you look out, I know you can't speak to any specific tenants, but when you're looking at the types of tenants, how many would you say are directly related to e-commerce? Is it 20% of the acquisition pipeline, is it 10%, 50%?

**Michael P. Landy**

*CEO, President & Executive Director*

Yes. It's a hard snapshot in time to give you because it's always growing. Every time we tour a property, the e-commerce section of that distribution center is growing by leaps and bounds. We were just at the Milwaukee Tool building in Memphis, and the amount of goods flowing via FedEx from e-commerce purchases from various e-tailers has grown since we were there last time, and it's probably grown since we were just there. I'll tell you because we own a big percentage of the FedEx Ground network and because e-commerce is growing exponentially, a lot of people are setting up their distribution centers as close to our FedEx buildings as possible. And if you look at our presentation, our company presentation, you'll see that. You'll see aerial photos of large retailers setting up shop right next to our buildings. So it's a growing percentage. I can't give you a fixed number, but having a big percentage of the FedEx Ground network, it's very advantageous and you're seeing the value of that.

**Barry Paul Oxford**

*D.A. Davidson & Co., Research Division*

Right. Do you think FedEx can ultimately be hurt Amazon, or there is enough room in the marketplace when it comes to delivering goods?

**Michael P. Landy**

*CEO, President & Executive Director*

Everybody talks about free shipping. Amazon spends about \$15 billion a year on shipping. And that's through FedEx and UPS and the U.S. Postal Service. And e-commerce is growing at a 16% CAGR since the turn of the century. And so Amazon wants to get into logistics. But Amazon is just B2C. FedEx, 85% of FedEx' business is business-to-business. So only 15% is the e-commerce B2C. It's the fastest-growing component. But the name of the game is delivery density. You want your trucks full, you want them to go to a zip code and have a lot of deliveries. If you're just doing B2C, the way Amazon is, it's not very profitable. That last mile is highly unprofitable and that's why there will be a brick-and-mortar

component to return goods, to pick up goods. It's just economically not feasible to deliver little packages to your house, multiple times a day. So FedEx is highly profitable, they're doing great. Amazon needs to get into logistics to augment the network, the growth of e-commerce as such that the networks have to be expended. FedEx has been investing billions of dollars a year in expanding their network. UPS has been a little late to the party, but they've announced multibillion dollar expansions recently. And that's just because demand is growing inordinately greater amount than supply has been growing. And supply needs to catch-up.

**Operator**

And our next question will come from James Gordon of Gordon Finance LLC.

**James Gordon**

Gentlemen, I have one question. As you have increased your positions as a percentage of undepreciated assets in market securities, it becomes more relevant from quarter-to-quarter, as to what REITs you're actually buying. You only report this at the end of the year in your 10-K, it's not in your 10-Q and it's not in your quarterly reports otherwise. Would you disclose what you are buying and why you can comment on why you feel that when interest rates rising, buying securities at this time is timely, and due to the fact that the increase in interest rate seems to be just starting?

**Michael P. Landy**

*CEO, President & Executive Director*

Sure, I'll take that. We do disclose our position in our 10-K, as you mentioned. We do not rotate in and out of holdings quarter-by-quarter. So we don't feel the need to bring you up to date. It hasn't really changed much since our 10-K. I'll tell you our portfolio is about 95% invested in REIT common stocks, 5% in REIT preferred stocks. We have 11 different common positions, 33% of that portfolio is in retail REITs, 28% is in office REITs, 11% is in UMH a manufactured housing REIT. Rising interest rates, you're right. Rates may continue. These algorithms have a set pattern that with rising rates you should not invest in REITs. As though they're fixed income investments but they are total return investments, REITs have historically done very well in rising interest rate environments. I can't time the exact bottom of the market but I'm very happy with the risk-adjusted returns today, and if it gets cheaper, I'll be even happier tomorrow.

**James Gordon**

In answering the previous question, you look at a target of 10%. Can we rely on the fact that you fellows are not going to go higher than 10% of your undepreciated assets? Even as opportunities may grow as interest rates rise or is this simply a hope or a prayer that you won't go beyond 10%?

**Michael P. Landy**

*CEO, President & Executive Director*

Well, it's a target, and the market is very volatile. So the market's on some days up 5% the portfolio, on others down 5%. We limit it because our core business is investing in real estate on Main Street. But we do allocate 10% of gross assets to liquid real estate. It enhances our liquidity, and it enhances our diversity. So the market could go up to the point where we'd have over 10%. We would stop buying, but we wouldn't sell just because the appreciation took us over 10%. So 10% is a guideline, we would certainly slow down in our buying. We would come to a halt. But if the market's taking it higher, and we feel the values have more appreciation in front of them, we're not going to sell just to maintain the 10%. It's a guideline, we're going to adhere to those parameters. Same with we try to set a floor at 5%. That's not to say we won't go lower than 5%, but we try to keep it within that bandwidth.

**James Gordon**

Well, I think what's troubling to me, as a significant manager of investments in your company, is trying to figure out what advantages you guys have picking stocks in the open market as opposed to ETFs or mutual funds. You have tremendous advantages in building warehouses and in dealing with your tenants, and I think you're one of the best managers out there in the United States. But I'm puzzled as to why I should think of you as the -- as efficient or good

operators of an REIT mutual fund, a small one, albeit but still a mutual fund?

**Michael P. Landy**

*CEO, President & Executive Director*

I think you're framing the concept too narrowly. In the broad context, we're real estate investors. We underwrite real estate the same way, if it's trading on Main Street or if it's trading on Wall Street. And we have an empirically proven track record that we're very good at that. So we're going to continue to do it. It's not -- in the short term, you're right. REIT stocks behave like stocks, but in the long term, REIT securities perform like the underlying real estate. So I wouldn't worry too much about a 90-day swing from \$4 million in unrealized losses to \$31 million in unrealized losses. Today, if I marked it to market, it's less than that. It's improved, but that's the market and the private real estate we own is moving around in values too, you're just not seeing it, so maybe it's not causing you concern, but it gives us liquidity, a lot of REITs are taking advantage of the discrepancy between Wall Street and Main Street by selling their Main Street assets and buying back their own shares. When you buy back your own shares, you're shrinking the company, you're reducing your liquidity, and that's one step towards doing what we're doing, but we think taking that extra step and investing in other liquid real estate, enhances your liquidity, increases your diversity, and there's REITs trading at bigger discounts than our currency is trading. So there's ample arguments to be made why investing in REIT securities is a good adjunct to our concept and often delivers much better total returns than investing in hard assets.

**Operator**

The next question comes from John Benda of National Securities Corporation.

**John Richard Benda**

*National Securities Corporation, Research Division*

So just quickly on overall company strategy. Can you elaborate a little more on why you guys haven't really bought much in the California, the West Coast markets where the 2 largest ports are in the country. I mean, is it -- I think that there would be some tenants that would fit your profile there. Can you just talk about that a little bit?

**Michael P. Landy**

*CEO, President & Executive Director*

Sure. We're forward-looking. We want to invest where the future path to progress is going. 70% of the U.S. population resides east of the Mississippi. You're right, the largest ports are on the West Coast. But Southeast ports increased shipping container growth 3x that of the West Coast ports last year. So you have 27% growth in the Southeast ports versus a very modest rounding up 8% growth on the West Coast ports. So you can't be backwards looking. I think when we first invested in the digital revolution, ramping up with FedEx, seeing that e-commerce was going to eat into retail spending, people were burying their heads in the sand. They didn't think that it was going to be a significant amount of traditional brick-and-mortar. It's only less than 1%, it's only 3%, 5%. Today it's going on 20%. And nobody's got their head in the sand now. The retailers were slow to realize that and they're scrambling to embrace e-commerce. Well the same with the Panama Canal. It's been expanded. It gives you a 29 day shortcut. It saves you \$4,000 per shipping container to go through the canal. And so now everybody is looking at California with the lowest cap rates, the highest regulation, net population and companies moving to more business-friendly climates. We've been way ahead of that, way ahead before the canal expansion even came online.

**Operator**

The next question comes from Craig Kucera of B. Riley FBR.

**Craig Gerald Kucera**

*B. Riley FBR, Inc., Research Division*

Kevin, you mentioned that you locked in debt on one acquisition, and I think right around 3.8%. Can you tell us when you locked that in? And how that will compare with where current quotes perhaps are?

**Kevin S. Miller***CFO, Chief Accounting Officer, Treasurer & Executive Director*

Sure. We locked that in prior to the huge increase in interest rate -- the significant increase in interest rates a few months ago. And I would -- I haven't locked in the other one yet, we should be locking it in soon. And based on what I'm hearing, it's going to be anywhere from 110 basis points over the 10 year or somewhere around there. So while rates has risen, the spreads over the 10 year have come down. So it's not going to be significantly more than we've gotten in the past. And we'll still have I think a decent spread between the cap rate and the interest rate where it will make sense to continue to grow our acquisition pipeline if the asset is of quality and nature that we feel is worth it.

**Craig Gerald Kucera***B. Riley FBR, Inc., Research Division*

Got it. So Mike, I feel like in the past your historic average has maybe been 200 basis points of your cost to debt. Is that correct? And I guess, how low would you go for the right asset, maybe whether it has embedded lease increase or rent increases or just some color on that?

**Michael P. Landy***CEO, President & Executive Director*

Yes. No, you're absolutely right. The historic is at 8% cap rate and a 6% borrowing rate. 60-year treasury average is a 6% 10-year treasury and the world is coming to an end because it's 50% of that today. So interest rates by historic standards are tremendously low. Cap rates are at historic lows, the deals we've locked in, the spread was less than 200 on the FedEx. Amazon, we haven't locked in financing yet, so I can't report on that. But we've gone historically as low as 125 basis points spread. And that gets to be too tight where we're not interested in growing the company at tighter spreads than that. I will tell you we've seen cap rates invert, where you were borrowing at 6% and investing at 5%. That was in 2006, 2007 when everybody was very pollyannaish and underwriting the most optimistic aggressive assumptions on rent increases and occupancy gains, et cetera. We had none of that, and then when the Great Recession ensued, we were able to put money to work and invest at 9.25% cap rates. So the spreads weren't as wide as they got subsequent to that. But we were the only ones out there acquiring assets when everybody was back into reequitizing pretend and extend mode when the tide went out.

**Craig Gerald Kucera***B. Riley FBR, Inc., Research Division*

Got it. And just looking longer term and obviously the cost of your margin debt on your securities portfolio is significantly lower. When you go through underwriting process, I would imagine you're going to consistently look at sort of these 15 years self-amortizing, long-term fixed-rate mortgages as sort of your base line for underwriting, correct? Versus maybe some short-term debt that's lower cost?

**Michael P. Landy***CEO, President & Executive Director*

Absolutely correct. It's so important in real estate to match your assets with your liabilities. And a lot of people are focused on these 90-day cycles. So they could borrow short and invest long and generate tremendous accretion and beat the targets, et cetera, et cetera. But in the long run, that's a real mismatch, it's very dangerous to do that. So we have a weighted average lease maturity that goes out 7.8 years. We have a weighted average debt maturity that goes out 11.5 years. And although interest rates are rising, they're still 50% of what the normal historic 10-year treasury rate is. So we're sitting here in a great position, rates could rise as much as they want. And we'll sleep very well at night and the company will perform very well.

**Craig Gerald Kucera***B. Riley FBR, Inc., Research Division*

Right. A few years ago, you guys were fairly active in redeveloping some assets, expanding some of your FedExs, and you have a lot of land that gives you that capacity today. But I guess, since they've been quiet, are you getting inbound calls today, given the tightness in the markets that we might see some expansions here over the next several quarters or is that still pretty quiet?

**Michael P. Landy**

*CEO, President & Executive Director*

It's not quiet, but nothing to really report. But you're right in that where are people going to go with less than 5% vacancy. Where are they going to go, there's not a lot of options. And fortunately, we have a lot of land so they don't have to go anywhere in many cases, we could just expand their building and they could stay right where they are. But markets are very tight and the economy is picking up and so we do anticipate increased expansions to report at some point.

**Kevin S. Miller**

*CFO, Chief Accounting Officer, Treasurer & Executive Director*

But we do have one expansion. We have one expansion right now that we do disclose. It's a FedEx parking lot expansion. And as Mike said, there's a bunch of calls that we're speaking with other tenants and FedEx about other expansions that we just can't report right now.

**Craig Gerald Kucera**

*B. Riley FBR, Inc., Research Division*

Okay. One more for me and I'll jump back in the queue. I know you raised the dividend back in October but even on that higher dividend your AFFO payout is the lowest it's been since I followed you here, right around 77%. Can you remind us how the board looks at dividend payouts that maybe a floor for that payout ratio?

**Michael P. Landy**

*CEO, President & Executive Director*

We don't have a set floor, but you're absolutely right from a historic standpoint, the cushion's never been greater. And our projections or the cushions is only going to increase in the ensuing quarters. So we feel good about that and we did raise our dividend 2 times in the last 3 years for a total 13% dividend increases. We've maintained our dividend for how many years now?

**Kevin S. Miller**

*CFO, Chief Accounting Officer, Treasurer & Executive Director*

26.

**Michael P. Landy**

*CEO, President & Executive Director*

26 consecutive years of maintaining or increasing our dividend, so we're going to be very conservative about it and we look at what are the uses of proceeds. Is the best use of proceeds to return capital to our shareholder base or is it to retain that precious cheapest cost of capital and grow our earnings through reinvestment? So that's the broad context in which the discussion is held but we want to stay on the course of raising the dividend. We're big shareholders, we like nothing more than to increase our payout, but it depends on use of proceeds, depends on the cushion. We don't have any vacancy. So we don't have an operating leverage component to say, if we fill the space, we can grow earnings even more. We're 99.2% occupied. So that's a factor we look at as well.

**Operator**

And our next question comes from Michael Boulegeris of Boulegeris Investments.

**Michael G. Boulegeris**  
*Boulegeris Investments, Inc.*

With the announced large ProLogis, DCT merger, what are your thoughts on further industry consolidation? And do the metrics of that deal confirm that Monmouth's underlined strategic real estate assets represent compelling value?

**Michael P. Landy**  
*CEO, President & Executive Director*

Well, certainly, it represents how hard it is to acquire a portfolio of quality assets. We've been at this a long time. I don't really want to date myself, but there were industrial REITs named Cabot, Keystone, AMB, CenterPoint, they all got acquired over the years. And in the last 2 weeks, 2 more are disappearing. DCT, as you mentioned, is getting acquired in an all stock transaction with ProLogis, and the announcement earlier this week was Gramercy's being acquired by Blackstone, who's been a big aggregator of industrial portfolios. And to purchase a portfolio in mass, of course, you have to pay a premium, and based on the valuations that portfolios have been going for our stock is at a big discount. There is no -- in our opinion, admittedly biased opinion, there is no portfolio of our quality where 85% of the cash flow is derived by long-term leases to investment grade tenants and the other 15% is investment grade quality tenants. So we have a very high caliber portfolio, we have the youngest portfolio, as I mentioned. We have ample land, but in the long term, when a company disappears, that's the end of it. This was my father's lifelong project, he ran the company for decades and that's what we want to do. So you could sell the company in the short term and pick up a big premium, but we're not interested in that. We're interested in growing the company. It's a very cyclical asset class, and just because the peak at this cycle maybe near, doesn't mean it's a higher peak than the peak of next cycle. Gene, you want to add to that?

**Eugene W. Landy**  
*Founder & Chairman*

Long-term, the prospects of the company are very, very good. The inflation in this country is running much more than the 2% that's reported.

Home values are going up 8% a year. The economy is booming, FedEx expects a tremendous final quarter this year. The cost of building buildings, land is up 40%, steel, aluminum is up, labor is up. You won't be able to build the kind of buildings we have 5, 10 years from now for the prices that we pay for them. So the prospects for the company are really, really good. So -- and there is no pressure on us to look short term. Everyone always cheers when a company that's selling at one price, sells out for 15% more, and everybody is so happy, but does anybody ever looked back at all those transactions that occurred 5, 8, 10 years ago and see how much money the shareholders lost? The values today are far higher than the companies that sold out 5, 10 years ago from now. And 5, 10 years from now, you'll be talking about values for Monmouth REIT that are far above what we see today. There are now -- nothing goes on forever, and we as shareholders, and major shareholders and we as directors of the company have to listen to any proposals that come and we do take them seriously. And we will consider what's in the best interest of the shareholders but you have to realize when you say a term like best interest of the shareholders, are you talking about over the next 6 months or you're talking about over the next 10 years? And I can tell you that in the United States, where the growth has been excellent, the leaders of the country say the future is just so good that probably we would lean to continuing to run the company. But we listen to proposals of people and have them, because that's our duty as directors.

**Michael G. Boulegeris**  
*Boulegeris Investments, Inc.*

We appreciate your long-term vision. And just a follow-on, Michael, your comments on the dividend that you highlighted in the press release. Is it likely that the board may assess the potential for a dividend increase in let's say the first half of fiscal 2019?

**Michael P. Landy**

*CEO, President & Executive Director*

I can't answer that definitively. I'll go back to my remarks to the prior question. We have an ample cushion to do so. If that's the path we want to pursue, we certainly have that option. But there's too many other variables. We did just raise it on October 1, and let's just see what the ensuing quarters brings. But it certainly -- we have the free cash flow we have the ability to do so. I would just want to be conservative and I did not want to lock myself into anything definitive.

**Michael G. Boulegeris**

*Boulegeris Investments, Inc.*

Fair enough and lastly, Gene, you've commented in the past about the Panama Canal, and I think in Monmouth's most recent investor presentation, you have additional material as far as the East Coast ports and is the growth you're seeing on the East Coast perhaps exceeding, even your very optimistic projections of a couple of years ago, it really appears that there's been quite a bit of acceleration.

**Eugene W. Landy**

*Founder & Chairman*

There is so much opportunity, it's amazing. And if we improve the infrastructure in the United States, if we dredge the ports and enlarge the airports and fix the railroads and fix the highways, and the international situation as far as the other countries of the world, they're growing and it's just an immense improvement in the economy, and so that as far as logistics are concerned, it's a nice path forward. And we want to invest in not only buildings, but infrastructure in these ports. And we think there's a great future as the U.S. economy continues to grow. I'm always amazed, the population now is 320 million, when I started it was 150 million. And we continue to grow by 1 million, 2 million people a year, and we continue to go ahead 2%, 3%, 4% a year. So the future continues to be bright, and we are just a leader of the world in our economy. And we try and I think we've succeeded over the past years. In building a company sticking to certain basic principles, and it's working. And we're so proud of the fact that we saw FedEx and we decided that we wouldn't limit the amount of FedEx's we own. And now 50% of our portfolio is FedEx, and we will continue that policy. So we're very optimistic and the problem will be is making -- continue to make things work. Transporting how -- if the Internet sales keep going up, how are you going to deliver all that merchandise? And how you're going to store it? We're running out of land in certain areas. So it's -- we who have the portfolio such as ours we're very, very proud of it and it's going to be very valuable.

**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 P. Landy**

*CEO, President & Executive Director*

Well, thanks, Laura. I'd like to mention as we did last quarter, our new annual report is available. We're very proud of our new addition and feel it's an essential read for all investors and prospective investors. So please contact Susan Jordan, our Vice President of Investor Relations, and we'll be happy to FedEx you out a copy. I'd like to thank everyone for joining us on this call and for their continued support and interest in Monmouth. Kevin, Gene and I are available for any follow-up questions. And as always, we will be presenting at NAREIT's REITWeek Conference next month in New York and hope to see you there. We look forward to reporting back to you after our third quarter. Thank you.

**Operator**

The conference has now concluded. Thank you for attending today's presentation. The teleconference replay will be available in approximately 1 hour. To access this replay, please dial U.S. toll-free (877) 344-7529, or international toll, 1 (412) 317-0088. The conference ID number is 10117592.

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