Management's Discussion & Analysis

August 10, 2016

The following discussion of Melcor Developments Ltd.'s (Melcor's) financial condition and results of operations should be read in conjunction with the condensed interim consolidated financial statements and related notes for the quarter ended June 30, 2016 and the management's discussion & analysis (MD&A) and consolidated financial statements for the fiscal year ended December 31, 2015.

The financial statements underlying this MD&A, including 2015 comparative information, have been prepared in accordance with International Financial Reporting Standards (IFRS) unless otherwise noted. All dollar amounts included in this MD&A are Canadian dollars unless otherwise specified.

Melcor's Board of Directors, on the recommendation of the Audit Committee, approved the content of this MD&A on August 10, 2016.

Other Information

Additional information about Melcor, including our annual information form, information circular and annual and quarterly reports, is available on SEDAR at www.sedar.com.

Non-standard Measures

We refer to terms that are not specifically defined in the CPA Handbook and do not have any standardized meaning prescribed by IFRS. These non-standard measures may not be comparable to similar measures presented by other companies. We believe that these non-standard measures are useful in assisting investors in understanding components of our financial results.

For a definition of these measures, refer to the section "Non-standard Measures" at the end of the MD&A.

Forward-looking Statements

In order to provide our investors with an understanding of our current results and future prospects, our public communications often include written or verbal forward-looking statements.

Forward-looking statements are disclosures regarding possible events, conditions, or results of operations that are based on assumptions about future economic conditions, courses of action and include future-oriented financial information.

This MD&A and other materials filed with the Canadian securities regulators contain statements that are forward-looking. These statements represent Melcor's intentions, plans, expectations, and beliefs and are based on our experience and our assessment of historical and future trends, and the application of key assumptions relating to future events and circumstances. Forward-looking statements may involve, but are not limited to, comments with respect to our strategic initiatives for 2016 and beyond, future development plans and objectives, targets, expectations of the real estate, financing and economic environments, our financial condition or the results of or outlook of our operations.

By their nature, forward-looking statements require assumptions and involve risks and uncertainties related to the business and general economic environment, many beyond our control. There is significant risk that the predictions, forecasts, valuations, conclusions or projections we make will not prove to be accurate and that our actual results will be materially different from targets, expectations, estimates or intentions expressed in forward-looking statements. We caution readers of this document not to place undue reliance on forward-looking statements. Assumptions about the performance of the Canadian and US economies and how this performance will affect Melcor's business are material factors we consider in determining our forward-looking statements. For additional information regarding material risks and assumptions, please see the discussion under Business Environment and Risks in our annual MD&A.

Readers should carefully consider these factors, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. Except as may be required by law, we do not undertake to update any forward-looking statement, whether written or oral, made by Melcor or on its behalf.

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Our Business

Melcor is a diversified real estate development and asset management company. We transform real estate from raw land to high-quality residential communities and commercial developments. We develop and manage mixed-use residential communities, business and industrial parks, office buildings, retail commercial centres and golf courses.

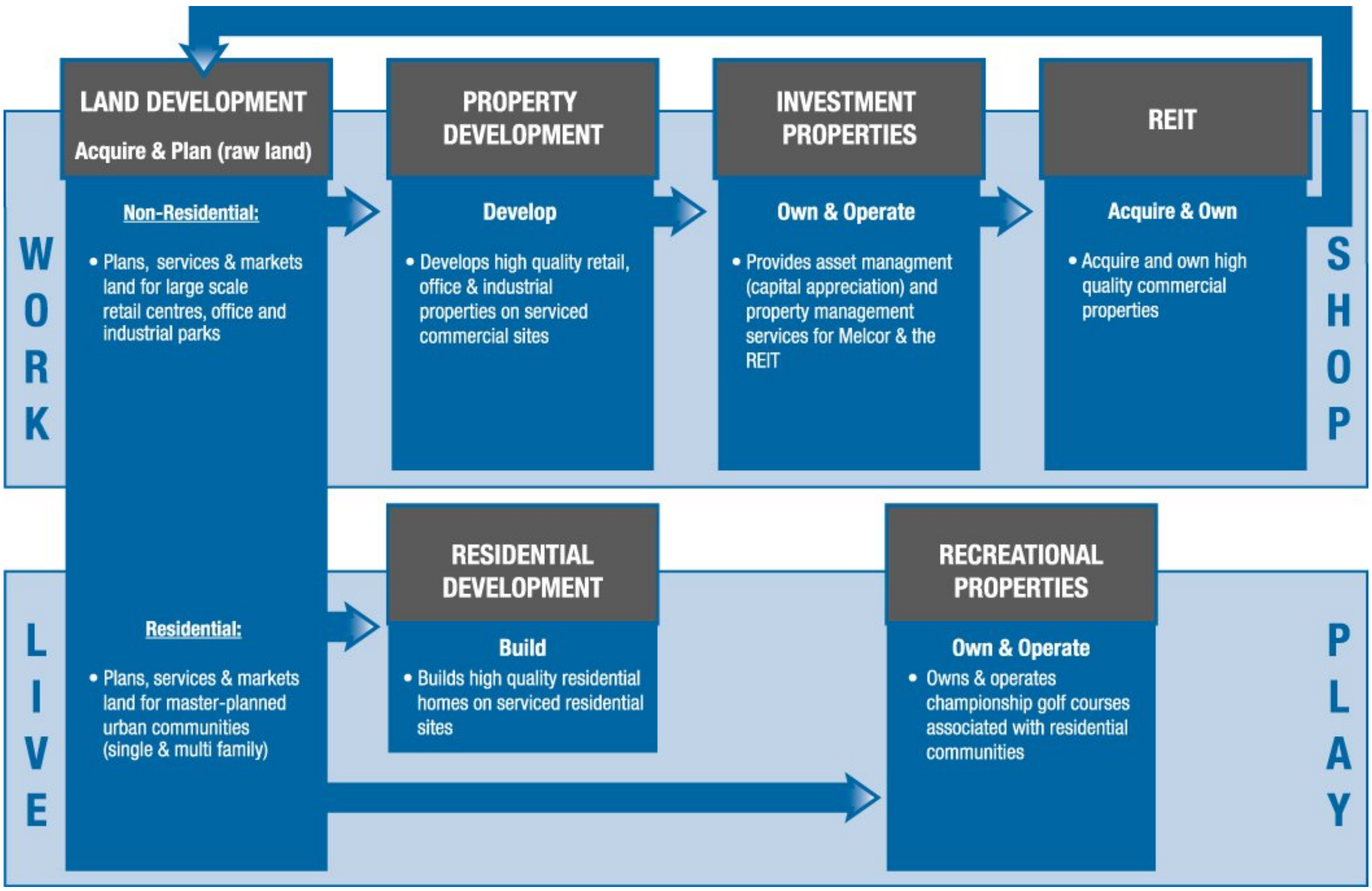
We are committed to building communities that enrich quality of life - communities where people live, work, shop and play.

We operate four integrated divisions that together manage the full life cycle of real estate development:

- acquiring raw land and planning residential communities and commercial developments (Community Development)
- project managing development, leasing and construction of commercial properties (Property Development)
- operating a portfolio of commercial and residential properties, focused on property improvements and capital appreciation of owned properties and property management of REIT owned properties (Investment Properties)
- acquiring and owning high quality leasable commercial and residential sites (the REIT)

In addition, we own and operate championship golf courses associated with our residential communities in our fifth division, Recreational Properties.

The diagram below illustrates how each of our operating divisions complements one another to create and enhance value from our real estate assets.



In addition to extending the value of our asset base, these diversified operating divisions enable us to manage our business through real estate cycles (both general market conditions and the seasonality associated with construction and development) and diversify our revenue base.

Our headquarters are in Edmonton, Alberta, with regional offices across Alberta, British Columbia, and in Phoenix, Arizona. Our developments span western Canada and the southwestern US.

We have been publicly traded since 1968 (TSX:**MRD**).

Second Quarter Highlights

($000s except as noted)	For the three months ended			For the six months ended		
	June 30, 2016	June 30, 2015	Change	**June 30, 2016**	June 30, 2015	Change
Revenue	**42,084**	46,113	(8.7)%	**72,638**	83,667	(13.2)%
Gross margin (%) *	**48.4%**	46.0%	2.4 %	**49.9 %**	46.6%	3.3 %
Net income (loss)	**1,778**	3,917	(54.6)%	**(5,936)**	18,477	(132.1)%
Net Margin (%) *	**4.2%**	8.5%	(4.3)%	**(8.2)%**	22.1%	(30.3)%
Funds from operations *	**8,388**	8,578	(2.2)%	**12,578**	14,791	(15.0)%
Per Share Data ($)						
Basic earnings (loss)	**0.05**	0.12	(58.3)%	**(0.18)**	0.56	(132.1)%
Diluted earnings (loss)	**0.05**	0.12	(58.3)%	**(0.18)**	0.56	(132.1)%
Funds from operations *	**0.25**	0.26	(3.8)%	**0.38**	0.45	(15.6)%

As at ($000s except as noted)	**June 30, 2016**	December 31, 2015	Change
Shareholders' equity	**957,359**	977,970	(2.1)%
Total assets	**1,892,038**	1,891,969	— %
Per Share Data ($)			
Book value *	**28.80**	29.43	(2.1)%

**See non-standard measures for calculation.*

All divisions remained active in Q2-2016; however the pace of sales in the Community Development division is slower than it has been over the past few years. We continue to see interest and steady activity in select regions and asset classes. In other regions builders have excess inventory and sales of single-family lots have softened significantly.

Our strategy of managing our business for the long-term has resulted in a strong and stable balance sheet that enables us to seek out and take advantage of opportunities to grow our business via opportunistic raw land and commercial income-producing property acquisitions.

Our strategy of growing and diversifying our investment property portfolio has contributed to a more stable and diverse revenue profile that is less sensitive to rapid changes in the economy. Our income producing commercial properties have increased by 477,874 sf since Q2-2015.

In the second quarter:

- Revenue declined 9% to $42.08 million compared to Q2-2015 primarily due to decreased lot sales in the Community Development division.
- Revenue from income-producing assets (Investment Properties and the REIT) grew by 5% over Q2-2015. This is consistent with our long-term diversification strategy to increase the portion of revenues earned from income-producing assets, which represented 61% of total revenue during the quarter, up from 53% in Q2-2015.
- Funds from operations was $8.39 million compared to $8.58 million in Q2-2015. Funds from operations eliminates the elements that have no cash impact on our business from net income (loss) and we view it as a better indicator of our operating business than net income.
- We continue to acquire new land when opportunities arise. During the quarter, we acquired:
  - 54.35 acres in Lethbridge for $2.67 million; and
  - 39.91 acres in Edmonton for $0.78 million.
- We continue to invest in and grow our portfolio of income-producing assets and completed the construction of two buildings valued at $3.3 million which added 14,534 sf to our portfolio.
- We paid a quarterly dividend of $0.12 per share on June 30, 2016. The REIT paid distributions of $0.05625 per trust unit in April, May and June for a quarterly payout ratio of 77%.
- On August 10, 2016 we declared a quarterly dividend of $0.12 per share, payable on September 30, 2016 to shareholders of record on September 15, 2016. The dividend is an eligible dividend for Canadian tax purposes.
- On August 10, 2016, the board of directors appointed Naomi Stefura as Chief Financial Officer.

Revenue & Margins:

Revenue from income-producing assets grew by 5% compared to Q2-2015. This growth is consistent with our long-term diversification strategy to increase the portion of revenues earned from income-producing assets and has had a positive impact on our results over the past few years. Community Development division revenue decreased by 25% compared to Q2-2015, contributing to the overall revenue decrease of 9% compared to Q2-2015. While we continue to see residential sales activity, the pace has slowed and there is softer demand in some asset classes and regions compared to the prior year.

Gross margin was 48% compared to 46% in Q2-2015 and is impacted by the mix in revenue produced by our operating divisions. Our Investment Properties and REIT divisions contributed to a larger proportion of revenue in the current year, and generally operate at margins in excess of 60%.

Net fair value gains on investment properties of $2.44 million were recognized in Q2-2016. Gains in Property Development were $1.95 million during the quarter as we continue to actively develop commercial properties. These gains were offset by losses in our Investment Properties and REIT divisions primarily driven by capital and tenant incentive spending that did not result in a significant change in the fair value of the related property.

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

Funds From Operations (FFO)

Funds From Operations (FFO) is a non-standard measure used in the real estate industry to measure operating performance. We believe that FFO is an important measure of the performance of our real estate assets. FFO adjusts for certain non-cash earnings items included in income such as fair value adjustments on investment properties and REIT units.

Below is a reconciliation of net income (loss) to FFO:

($000s)				
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Net income (loss) for the period	**1,778**	3,917	**(5,936)**	18,477
Amortization of operating lease incentives	**1,516**	1,517	**3,093**	2,777
Fair value adjustment on investment properties	**(2,436)**	(6,359)	**(1,417)**	(7,002)
Depreciation on property and equipment	**495**	541	**739**	799
Stock based compensation expense	**69**	74	**157**	170
Non-cash interest	**1,220**	246	**1,585**	485
Gain on sale of asset	**(3)**	(58)	**(3)**	(58)
Deferred income taxes	**173**	7,685	**(25)**	7,374
Fair value adjustment on REIT units	**5,576**	1,015	**14,385**	(8,231)
FFO	**8,388**	8,578	**12,578**	14,791
FFO per share	**0.25**	0.26	**0.38**	0.45

FFO during the quarter decreased to $8.39 million compared to $8.58 million in Q2-2015. FFO was impacted by lower sales in the Community Development division (54% decrease in lots sold and 25% decrease in divisional revenue). The growth in revenue from income-producing assets has helped stabilize overall income.

Melcor's net loss during the quarter was the result of fair value losses reported on our REIT units (loss of $5.58 million). Income before taxes for the quarter, prior to fair value adjustments was steady at $7.33 million compared with $7.44 million during Q2-2015.

Divisional Results

Our business is comprised of five integrated and complementary operating divisions:

- Community Development, which acquires raw land for future commercial and residential community development;
- Property Development, which develops high-quality retail, office and industrial income-producing properties on serviced commercial sites developed by Community Development;
- Investment Properties, which manages and leases the commercial developments produced by the Property Development division and an externally purchased portfolio of assets, as well as assets held in the REIT;
- The REIT, which owns and holds 38 income-producing properties; and
- Recreational Properties, which owns and operates championship golf courses associated with Melcor residential communities.

Our Corporate division carries out support functions including accounting, treasury, information technology, administration, legal and human resources.

The following tables summarize the results of our operating divisions:

	Community Development		Property Development		Investment Properties		REIT		Recreational Properties	
	Three months ended June 30		Three months ended June 30		Three months ended June 30		Three months ended June 30		Three months ended June 30	
($000s except as noted)	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015
Revenue	**15,591**	20,679	**3,304**	7,375	**8,885**	8,083	**16,807**	16,323	**4,256**	4,273
Portion of total revenue	**37%**	45%	**8%**	16%	**21%**	18%	**40%**	35%	**10%**	9%
Cost of sales	**(10,813)**	(14,206)	**(3,300)**	(7,350)	**(3,423)**	(2,861)	**(6,522)**	(6,442)	**(2,188)**	(2,183)
Gross margin	**4,778**	6,473	**4**	25	**5,462**	5,222	**10,285**	9,881	**2,068**	2,090
Gross margin %	**31%**	31%	**—%**	—%	**61%**	65%	**61%**	61%	**49%**	49%
Portion of total margin	**23%**	31%	**—%**	—%	**27%**	25%	**51%**	47%	**10%**	10%
General and administrative expense	**(2,020)**	(2,497)	**(364)**	(331)	**(588)**	(956)	**(652)**	(516)	**(872)**	(816)
Fair value adjustment on investment properties	**—**	—	**1,948**	3,963	**(705)**	2,898	**(174)**	(1,899)	**—**	—
Gain on sale of assets	**—**	—	**—**	—	**—**	—	**—**	—	**3**	58
Interest income	**152**	674	**1**	—	**—**	3	**8**	18	**—**	—
Divisional income before tax	**2,910**	4,650	**1,589**	3,657	**4,169**	7,167	**9,467**	7,484	**1,199**	1,332

	Community Development		Property Development		Investment Properties		REIT		Recreational Properties	
	Six months ended June 30		Six months ended June 30		Six months ended June 30		Six months ended June 30		Six months ended June 30	
($000s except as noted)	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015	**2016**	2015
Revenue	**23,530**	35,900	**3,310**	7,427	**16,773**	15,827	**33,433**	32,581	**4,474**	4,462
Portion of total revenue	**32%**	43%	**5%**	9%	**23%**	19%	**46%**	39%	**6%**	5%
Cost of sales	**(15,925)**	(24,684)	**(3,300)**	(7,350)	**(6,281)**	(5,657)	**(13,015)**	(12,825)	**(2,749)**	(2,682)
Gross margin	**7,605**	11,216	**10**	77	**10,492**	10,170	**20,418**	19,756	**1,725**	1,780
Gross margin %	**32%**	31%	**—%**	1%	**63%**	64%	**61%**	61%	**39%**	40%
Portion of total margin	**21%**	29%	**—%**	—%	**29%**	26%	**56%**	50%	**5%**	5%
General and administrative expense	**(4,193)**	(4,467)	**(844)**	(775)	**(1,273)**	(2,087)	**(1,393)**	(1,293)	**(1,223)**	(1,145)
Fair value adjustment on investment properties	**—**	—	**4,031**	6,157	**(2,820)**	2,725	**(1,999)**	(3,708)	**—**	—
Gain on sale of assets	**—**	—	**—**	—	**—**	—	**—**	—	**3**	58
Interest income	**479**	1,375	**2**	—	**2**	6	**17**	36	**—**	—
Divisional income before tax	**3,891**	8,124	**3,199**	5,459	**6,401**	10,814	**17,043**	14,791	**505**	693

Divisional results are shown before inter-segment eliminations and exclude corporate division.

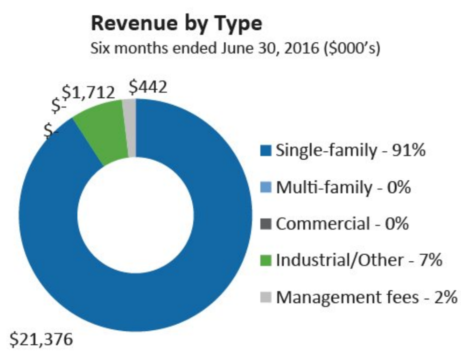
Community Development

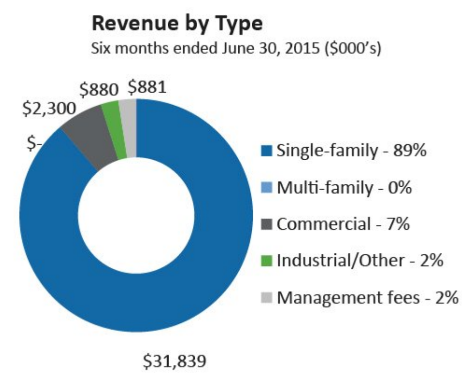
Our Community Development division acquires raw land in strategic urban corridors and subsequently plans, develops and markets this land as builder-ready urban communities and large-scale commercial and industrial centres. This process includes identifying and evaluating land acquisitions, site planning, obtaining approvals from municipalities, developing the land, construction, marketing and ultimately selling the lots to home builders (for residential communities) or developers (for commercial/industrial centres). The division also sells sites to our Property Development division, who in turn develops commercial properties on the land.

Master-planned mixed-use residential communities comprise the majority of Community Development's portfolio. We create efficient and sustainable urban communities by establishing an overall vision for each community and the amenities that will make it a desirable place to live. Residential lots and multi-family parcels are sold to home builders who share our passion for quality and with whom we have long-standing relationships.

Our focus is to grow market share and income levels by ensuring that we have an appropriate land mix and the right inventory in high demand areas in growing regions. We proactively manage our agreement receivables by maintaining an exclusive builder clientele and working closely with those builders.

Sales Activity





Revenue and income can fluctuate significantly from period to period due to the timing of plan registrations, the cyclical nature of real estate markets and the mix of land sold.

Consolidated	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Sales data: (including joint ventures at 100%)				
Single family sales (number of lots)	**92**	202	**135**	285
Gross average revenue per single-family lot ($)	**178,800**	153,300	**195,400**	159,800
Commercial sales (acres)	**2.11**	—	**2.11**	2.90
Gross average revenue per commercial land acre ($)	**817,600**	—	**817,600**	793,100
Industrial sales (acres)	**—**	1.76	**0.95**	1.76
Gross average revenue per industrial land acre ($)	**—**	500,000	**510,000**	500,000
Financial results: (including joint ventures at Melcor's interest)				
Revenue ($000s)	**15,591**	20,679	**23,530**	35,900
Earnings ($000s)	**2,910**	4,650	**3,891**	8,124

Note: The number of lots in the table above includes joint ventures at 100%; however, revenue is reported at Melcor's interest.

The Community Development division remained active in the quarter with development continuing in communities and phases that met pre-sales targets. We remain committed to managing our risk in this uncertain environment by ensuring that market demand is in place prior to proceeding with development. In regions where demand is soft, we are taking advantage of this opportunity to progress land use through the municipal approvals process to ensure we have "shovel-ready", developable land ready when market demand improves.

Single-family lot sales were down but the average revenue per lot was up by 22%. The mix of land sold for commercial, industrial and multi-family development also contributed to lower overall revenue of $15.59 million in Q2-2016, a decrease of $5.09 million from $20.68 million in Q2-2015.

Our primary market is Alberta. Market conditions have remained stable in the Edmonton and Lethbridge regions, while the Calgary and Red Deer regions have more sluggish markets.

Regional Sales Analysis

A summary of our lot and acre sales by region is as follows:

Regional Sales Analysis	**Three months ended June 30, 2016**			Three months ended June 30, 2015		
(including joint ventures at 100%)	**Single- family (Lots)**	**Multi-family (Acres)**	**Non-Residential (Acres)**	Single- family (Lots)	Multi-family (Acres)	Non-Residential (Acres)
Edmonton Region	**72**	**—**	**—**	101	—	1.76
Red Deer Region	**8**	**—**	**—**	46	—	—
Calgary Region	**5**	**—**	**2.11**	29	—	—
Lethbridge	**4**	**—**	**—**	23	—	—
Kelowna	**3**	**—**	**—**	3	—	—
United States	**—**	**—**	**—**	—	—	—
	92	**—**	**2.11**	202	—	1.76

Regional Sales Analysis	**Six months ended June 30, 2016**			Six months ended June 30, 2015		
(including joint ventures at 100%)	**Single- family (Lots)**	**Multi-family (Acres)**	**Non-Residential (Acres)**	Single- family (Lots)	Multi-family (Acres)	Non-Residential (Acres)
Edmonton Region	**84**	**—**	**—**	171	—	1.76
Red Deer	**10**	**—**	**0.95**	50	—	—
Calgary Region	**6**	**—**	**2.11**	33	—	2.90
Lethbridge	**25**	**—**	**—**	27	—	—
Kelowna	**10**	**—**	**—**	4	—	—
United States	**—**	**—**	**—**	—	—	—
	135	**—**	**3.06**	285	—	4.66

The Edmonton region had lower sales volume in Q2-2016, but continued to experience steady activity in certain communities. Successful lot draws were conducted in two communities and we expect sales to close when plan registrations are completed.

Year-to-date, Lethbridge and Kelowna results are on par or up from the same period in 2015. These results are trending with expectations as these regions are more insulated from the impact of the oil and gas industry.

The Red Deer region remains sluggish, but has shown improvement compared to Q1-2016 as a result of promotional programs designed to move inventory. The 8 single-family lots sold in Q2-2016 compares with 2 lots in Q1-2016.

Single-family lot sales in the Calgary region also remain sluggish compared to the prior period. Commercial land was sold to the Property Development division for continued development of Chestermere Station.

Inventory

A summary of the movement in our developed lot inventory is as follows:

Developed Inventory	**Six months ended June 30, 2016**			Six months ended June 30, 2015		
(including joint ventures at 100%)	**Single- family (Lots)**	**Multi-family (Acres)**	**Non-Residential (Acres)**	Single- family (Lots)	Multi-family (Acres)	Non-Residential (Acres)
Open	**1,433**	**63.10**	**144.41**	1,144	67.61	139.65
Purchases	**—**	**—**	**—**	—	—	—
New developments	**66**	**—**	**15.43**	474	6.83	—
Internal sales	**—**	**—**	**—**	—	—	—
Sales	**(135)**	**—**	**(3.06)**	(285)	—	(4.66)
	1,364	**63.10**	**156.78**	1,333	74.44	134.99

Raw land inventory

To support future growth, we acquire land in strategic growth corridors and maintain an inventory of land for future development in our primary markets. During the quarter, we purchased 54 acres in the Lethbridge region and 40 acres in the Edmonton region for future residential development. In Q2-2015, we purchased 147 acres in the Red Deer region.

We continue to monitor our land holdings to secure our position in our target markets.

Property Development

Our Property Development division develops, manages construction, markets and initially leases high-quality retail, office and industrial revenue-producing properties on prime commercial sites. The division currently operates solely in Alberta.

The Property Development division supports Melcor's strategic objectives of asset diversification, income growth and value creation by constructing income-producing commercial developments, primarily on land acquired at fair market value from the Community Development division.

The Property Development division increases the value of land assets and delivers long-term sustainable returns with high profile anchor tenants such as ATB, Bank of Montreal, Canadian Tire, Canadian Western Bank, Cara, CIBC, Home Depot, Loblaws, McDonald's, Rexall Drugs, Rona, Royal Bank, Save-on Foods, Scotiabank, Shoppers Drug Mart, Staples, Starbucks, Subway, TD Canada Trust, Tim Hortons, Wal-Mart, Winners and many others.

Completed buildings are transferred from Property Development to Investment Properties at fair market value (based on third party appraisals) once construction and leasing activities near completion. The transfer revenue and related costs are eliminated on consolidation and do not impact overall earnings.

Management fee revenue is comprised of fees paid by joint arrangement partners and is a percentage of total development costs incurred, which fluctuate period to period depending on the development stage of active projects.

The Property Development division realizes fair value gains resulting from development and leasing activities as construction is in progress. We generally expect to see the majority of fair value increases in the third and fourth quarters as construction and leasing are completed.

Division Highlights

($000s except as noted)	**Three months ended**		**Six months ended**	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Total revenue	**3,304**	7,375	**3,310**	7,427
Revenue from property transfers	**3,300**	7,350	**3,300**	7,350
Management fees	**4**	25	**10**	77
Gross margin (%) on property transfers	**37%**	24%	**37%**	24%
Square footage transferred (sf, at 100%)	**14,534**	19,930	**14,534**	19,930
Number of buildings transferred	**2**	2	**2**	2
Fair value adjustment on investment properties	**1,948**	3,963	**4,031**	6,157

The Property Development division has approximately 100,000 sf of development planned for the 2016 construction season. During the quarter, the division completed and transferred 2 buildings (14,534 sf) to Investment Properties. Construction on additional phases of existing retail and industrial projects is underway.

This division continues to focus on the planning and design of future projects, including new product types, following the completion of several major multi-year projects in recent years. New projects must meet specific pre-lease thresholds before we begin development and we discontinued speculative development in 2015.

Regional Highlights

($000s except as noted)	Three months ended		Six months ended	
Fair value adjustments by region	**June 30, 2016**	June 30, 2015	**June 30, 2016**	June 30, 2015
Northern Alberta	**960**	3,613	**1,823**	3,613
Southern Alberta	**988**	350	**2,208**	2,544
	1,948	3,963	**4,031**	6,157

Year-to-date fair value adjustments are a result of continued development on some of our multi-year developments including gains of $2.04 million at Kingsview Market. Development continues on a 15-acre site for the Northern Alberta Institute of Technology (NAIT) in Spruce Grove. Construction on that site is expected to be completed in 2016 and transferred to our Investment Properties division for long term holding.

Future development opportunities

We continually identify parcels of land from our land inventory that are well suited for commercial development. We also work with municipalities to gain approvals to commence development on new projects. The following tables illustrate our current and future project expectations.

Current Projects

Project	Location	Type	Total SF *	Developed to Date	SF Under Development
The Village at Blackmud Creek	South Edmonton	*Regional business park*	607,000	57,364	—
Telford Industrial	Leduc	*Industrial Park*	385,000	98,790	44,000
West Henday Promenade	West Edmonton	*Regional mixed use centre*	726,000	96,627	—
Kingsview Market	Airdrie	*Regional shopping centre*	331,000	126,851	18,300
Chestermere Station	Chestermere	*Neighbourhood shopping centre*	308,000	236,219	20,600
Clearview Market	Red Deer	*Neighbourhood shopping centre*	151,120	141,120	10,000
The District at North Deerfoot	North Calgary	*Regional business / industrial park*	2,250,000	23,155	—
Campsite Business park	Spruce Grove	*Industrial Park*	170,000	—	13,654

Expected Future Projects

Project	Location	Type	Total SF *	Ownership Interest	Expected Start (year)
The Shoppes at Jagare Ridge	South Edmonton	*Neighbourhood shopping centre*	105,000	50%	2016
The Shoppes at Canyons	Lethbridge	*Neighbourhood shopping centre*	105,000	100%	2017
Greenwich	West Calgary	*Regional mixed use centre*	395,000	100%	2017
Jensen Crossing	St. Albert	*Regional mixed use centre*	148,000	100%	2017
Rollyview	Leduc	*Neighbourhood shopping centre*	150,000	100%	2017
West Pointe Marketplace	Lethbridge	*Regional power centre*	750,000	100%	2018
Keystone Common	North Calgary	*Regional power centre*	775,000	100%	2020
West Calgary Marketplace	West Calgary	*Regional power centre*	800,000	100%	2020

** Size represents the estimated total square footage projected for full build-out. This includes sites that may be individually sold to retailers or end-users.*

Investment Properties

Our Investment Properties division manages and leases our portfolio of high-quality office, retail, industrial and residential properties, which are located across western Canada and the US, including the properties owned by the REIT.

Our Investment Properties division manages 3.87 million sf of income-producing commercial GLA and 781 residential units.

Our commercial property portfolio is primarily comprised of properties developed and transferred from our Property Development division. Our goal is to improve the operating efficiency of each property for stable and growing cash flows making them attractive assets for the REIT to purchase under its Right of First Offer (ROFO) option. In our management capacity, we are committed to efficient property management for optimized operating costs, occupancy and rental rates, providing the REIT and our joint venture partners with best in class management services. We focus on client retention through continuous customer contact and ongoing service evaluations. We also enhance our portfolio by upgrading the appearance, functionality and desirability of our properties, thereby increasing their rental potential.

Our growing US properties portfolio is part of a strategic initiative to reduce our exposure to the western Canadian resource sector. We also own 7 parking lots and other assets which are held for the long-term, providing current stable income and future re-development opportunities.

Our portfolio under management has high occupancy rates with long-term tenancies from high-quality retail and commercial clients.

Operating results

The following table summarizes the division's key performance measures:

($000s except as noted)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Commercial properties GLA under management (sf, total)	**3,870,922**	3,393,048	**3,870,922**	3,393,048
Properties owned and managed (sf)	**745,596**	369,592	**745,596**	369,592
Properties managed (sf)	**3,125,326**	3,023,456	**3,125,326**	3,023,456
Revenue (total)	**8,885**	8,083	**16,773**	15,827
Commercial properties	**2,825**	2,276	**5,753**	4,450
US properties	**4,556**	4,333	**8,020**	8,426
Management fees	**1,161**	1,110	**2,312**	2,227
Parking lots and other assets	**343**	364	**688**	724
Net operating income (NOI) *	**5,348**	5,277	**9,974**	10,115
Funds from operations *	**4,965**	4,393	**9,423**	8,282
Funds from operations per share *	**0.15**	0.13	**0.28**	0.25

** See non-standard measures for definition and calculation.*

Commercial properties

Over the past twelve months, Property Development transferred 5 buildings (46,144 sf, at 100%) which generated a significant increase in commercial properties revenue and NOI over 2015. Revenues generated on assets acquired from Property Development and were held through the period were $1.10 million in the second quarter and $2.16 million year to date (2015 - $0.26 million and $0.53 million respectively). During Q2-2016 Property Development transferred two buildings, adding 14,534 to owned and managed GLA. With 100,000 sf of GLA under active development in the 2016 construction season, we expect continued growth. During Q2-2016 we completed re-development of a mixed use retail/office property in downtown Edmonton. The property, acquired in June 2015, added 12,000 sf (at 100%) to our portfolio. Same asset revenue remained steady over Q2-2015.

Occupancy on properties owned by Investment Properties was 91% at June 30, 2016 compared to 90% at year end. Stability in occupancy reflects the slower pace of development over the past twelve months and a larger proportion of the portfolio being comprised of mature properties.

The following is a reconciliation of commercial properties same asset net operating income (NOI) to NOI:

($000s except as noted)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Same asset NOI *	**1,319**	1,188	**2,568**	2,601
Properties transferred from PD	**878**	226	**1,782**	437
Properties transferred to REIT	**6**	198	**35**	196
NOI before adjustments	**2,203**	1,612	**4,385**	3,234
Amortization of operating lease incentives	**71**	124	**172**	193
Straight-line rent adjustment	**(94)**	(68)	**(560)**	(247)
NOI *	**2,180**	1,668	**3,997**	3,180

** See non-standard measures for definition.*

Divisional NOI is defined as rental revenue less property operating costs plus amortization of operating lease incentives plus/minus straight-line rent adjustment. Same asset NOI increased over Q2-2015 due to changes in non-cash items, partially offset by higher property taxes and recoverable costs on buildings which have lower recovery ratios. Year to date same-asset NOI was steady over 2015.

US properties

We saw significant growth in our commercial portfolio through the first half of 2016 with three properties purchased during the first quarter with a total GLA of 306,169 sf. Details of acquisitions completed to date in 2016 are as follows:

	Date	Type	Area	Price ($ millions)
Offices at Promenade, Greater Denver Area, Colorado	Feb 2016	Office	128,383 sf / 8.74 ac	$20.07 (US$17.03)
Offices at Inverness, Greater Denver Area, Colorado	Mar 2016	Office	95,127 sf / 6.85 ac	$13.07 (US$9.75)
Syracuse Hill One, Greater Denver Area, Colorado	Mar 2016	Office	82,659 sf / 4.56 ac	$13.22 (US$10.19)

Over the past twelve months, the US property portfolio has seen significant activity. We divested three residential assets and acquired four commercial properties. We have also reduced our investments in Texas and increased investments in Phoenix and Denver, reflecting our commitment to increasing our US commercial portfolio in regions which hedge our exposure to resource economies.

We recognized a full quarter of revenue on commercial assets acquired in Q1-2016, driving a $0.22 million or 5% increase in revenue over Q2-2015. Year to date revenue was down $0.41 million or 5% due to the lag time of reinvesting funds following the sale of residential assets in 2015. Revenue from residential assets sold during 2015 were $2.06 million (US$1.67 million) in Q2-2015 and $4.06 million (US$3.28 million) for the first six months of 2015. Comparatively, revenue from newly acquired commercial assets in Q2-2016 was $2.27 million (US$1.74 million) and $3.33 million (US$2.51 million) year to date (2015 - $0.22 million (US$0.18 million)) in the comparative three and six month periods). Same asset revenue was steady over 2015 with stable occupancy and rental rates.

The following is a reconciliation of US properties same asset net operating income (NOI) to NOI:

($000s except as noted)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Same asset NOI	**930**	882	**1,743**	1,696
Third party acquisitions	**860**	92	**1,270**	92
Third party disposition	**(1)**	958	**(72)**	1,928
NOI before adjustments	**1,789**	1,932	**2,941**	3,716
Foreign current translation	**442**	441	**892**	882
Amortization of operating lease incentives	**20**	—	**30**	—
Straight-line rent adjustment	**(111)**	(1)	**(160)**	(1)
NOI *	**2,140**	2,372	**3,703**	4,597

** See non-standard measures for definition.*

Divisional NOI is defined as rental revenue less property operating costs plus amortization of operating lease incentives plus/minus straight-line rent adjustment. Same asset NOI was steady over 2015.

Management fees & other

We earn management fees under the asset management and property management agreements with the REIT and under other joint venture agreements where Melcor acts as the manager. Management fees were stable over Q2-2015 at $1.16 million ($2.31 million year to date). Growth in property management and asset management fees was offset by a decrease in leasing fees which fluctuate based on the timing of leasing activity by the REIT.

During Q2-2016, we recognized $0.34 million in revenue on our 516 parking stalls and other assets (Q2-2015- $0.36 million). This revenue can fluctuate from period to period.

Funds from operations (FFO) increased by $0.57 million or 13% over Q2-2015 as a result of higher NOI on re-cycling of our US investment properties and lower general & administrative expense. The decrease in general & administrative expense relates to payments made to the REIT under Head and Bridge Lease Agreements entered into for property acquisitions from Investment Properties completed during 2014. These amounts are eliminated on consolidation.

REIT

The REIT owns 38 income-producing office, retail and industrial properties, comprising 2,775,723 square feet of GLA and a land lease community at June 30, 2016. The REIT's portfolio has a diversified tenant profile, with a mix of national, regional and local tenants operating in a variety of industries.

We have a controlling 56.7% effective interest in the REIT through ownership of all Class B LP Units (December 31, 2015 - 56.7%). As Melcor controls the REIT, we consolidate 100% of the REIT's revenues, expenses, assets and liabilities.

Operating results

The following table summarizes the REIT's key performance measures:

($000s except as noted)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Rental revenue	**16,807**	16,323	**33,433**	32,581
Net operating income (NOI) *	**10,773**	10,382	**21,386**	20,587
Same asset NOI * *(see calculation following)*	**9,976**	9,877	**19,846**	19,752
Fair value adjustment on investment properties	**(174)**	(1,899)	**(1,999)**	(3,708)
Gross leasable area (GLA) (sf)	**2,775,723**	2,738,212	**2,775,723**	2,738,212
Occupancy % (weighted by GLA)	**93.2%**	92.1%	**93.2%**	92.1%
Fair value of portfolio	**661,451**	644,139	**661,451**	644,139
Funds from operations *	**10,426**	10,279	**20,652**	20,117
Funds from operations per share *	**0.31**	0.31	**0.62**	0.61

** See non-standard measures for definition and calculation.*

Rental revenue increased by 3% or $0.48 million in Q2-2016 ($0.85 million year to date) as a result of 43,231 sf of additional GLA brought online over the past twelve months. We acquired additional phases at two existing properties and densified two existing retail properties with new commercial retail units (CRUs). Rental revenue from the newly acquired/constructed GLA was $0.38 million and $0.71 million during the three and six-months ended June 30, 2016 (2015 - $0.01 million and $0.01 million respectively). On a same-asset basis, base rent grew 2% as a result of an increase in average base rent as rent-steps on escalating leases kicked in and there were fewer tenants on rent-free periods. Positive movement in base rents was offset by lower recoveries and straight-line rent adjustment, resulting in flat same-asset rental revenue over 2015.

Weighted average base rent was $15.65, up 1% compared to December 31, 2015. Increases in base rents correlated with a decrease in straight-line rent adjustments.

Direct operating expenses increased $0.08 million and $0.19 million or 1% over the comparative three and six-month period. Excluding the impact of newly acquired/constructed properties, direct operating expenses were steady over 2015. On a same-asset basis, property taxes increased 7% over 2015 as a result of recently constructed suburban retail properties converting from a land based valuation to an income based approach. Mill rates and appraised values across the rest of the portfolio remained relatively stable over 2015. These increases were offset by an 8% reduction in utility costs as a result of lower energy consumption combined with cost savings on utility contracts. Same-asset operating expenses were flat over 2015.

GLA added in the past twelve months via property acquisitions and the construction of two CRUs in existing properties led to a 4% increase in NOI over 2015. On a same-asset basis, NOI was steady.

The following is a reconciliation of same asset net operating income (NOI) to NOI:

($000s except as noted)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Same asset NOI *	**9,976**	9,877	**19,846**	19,752
Acquisitions	**309**	4	**572**	4
NOI before adjustments	**10,285**	9,881	**20,418**	19,756
Amortization of operating lease incentives	**785**	896	**1,610**	1,618
Straight-line rent adjustment	**(297)**	(395)	**(642)**	(787)
Divisional NOI	**10,773**	10,382	**21,386**	20,587

** See non-standard measures for definition and calculation.*

Funds from operations

Funds from operations (FFO) increased by $0.15 million or 1% over Q2-2015 as a result of higher NOI, partially offset by increased general and administrative expenses.

Recreational Properties

Our Recreational Properties division owns and manages championship golf courses built to add value to Melcor residential communities.

Our golf courses aspire to achieve consistent course conditions and quality, and to be recognized as championship public golf courses with state of the art clubhouses that contribute to our ability to attract tournaments and events. Achieving these goals enables us to find the appropriate balance between the revenue levers of course fees, number of rounds played and customer satisfaction and enjoyment.

		2016		2015	
	Ownership interest	**Season opened**	**Rounds of Golf**	**Season opened**	**Rounds of Golf**
Managed by Melcor:					
Lewis Estates (Edmonton)	60%	**March 31**	**14,796**	**April 9**	14,722
The Links (Spruce Grove)	100%	**April 1**	**12,006**	**April 10**	12,607
Black Mountain (Kelowna)	100%	**March 11**	**15,320**	**March 13**	13,220
Managed by a Third Party:					
Jagare Ridge (Edmonton)	50%	**April 8**	**10,593**	**April 17**	10,741

Favourable spring conditions resulted in an early season start for our golf courses. This was offset by unfavorable weather conditions in June. Rounds of golf played increased 3% over Q2-2015.

General and Administrative Expense

Cost management strategies implemented across the company contributed to an overall 19% reduction in G&A expense over Q2-2015.

Liquidity & Capital Resources

The following table represents selected information as at June 30, 2016, compared to December 31, 2015.

As at ($000s except as noted)	**June 30, 2016**	31-Dec-15
Cash & cash equivalents	**35,178**	48,674
Restricted cash	**—**	2,288
Accounts receivable	**13,489**	18,744
Agreements receivable	**107,706**	152,183
Revolving credit facilities	**91,034**	104,071
Accounts payable and accrued liabilities	**26,380**	40,534
Total assets	**1,892,038**	1,891,969
Total liabilities	**934,679**	913,999
Debt to equity ratio*	**0.98**	0.93

**See non-standard measures for definition and calculation.*

We employ a range of strategies to maintain operations and facilitate growth. Our principal liquidity needs are to:

- Fund recurring expenses;
- Meet debt service requirements;
- Make dividend payments;
- Make distributions to unitholders of the REIT;
- Fund land development; and
- Fund investing activities such as the discretionary purchase of land inventory and/or investment property purchases.

We are able to meet our capital needs through a number of sources, including cash generated from operations, long and short-term borrowings from our syndicated credit facility, mortgage financings, convertible debentures, and the issuance of common shares or trust units. Our primary use of capital includes paying operating expenses, sustaining capital requirements on land and property development projects, completing real estate acquisitions, debt principal and interest payments, paying distributions on the REIT units and paying dividends when declared by our board of directors.

We believe that internally generated cash flows, supplemented by borrowings through our credit facility and mortgage financings, where required, will be sufficient to cover our normal operating and capital expenditures. We regularly review our credit facility limits and manage our capital requirements accordingly.

We do not currently have plans to raise additional capital through the issuance of common shares, trust units, preferred shares or convertible debentures; however, under certain circumstances, we would consider these means to facilitate growth through acquisition or to reduce the utilized level on our credit facility.

Financing

As at June 30, 2016, our total general debt outstanding was $657.56 million. This compares to $631.01 million at December 31, 2015. A summary of our debt is as follows:

As at ($000s)	**June 30, 2016**	December 31, 2015
Melcor - revolving credit facilities	**74,707**	84,813
REIT - revolving credit facility	**16,327**	19,258
Project specific financing	**21,298**	25,280
Secured vendor take back debt on land inventory	**72,598**	76,092
Debt on investment properties and golf course assets	**441,435**	395,006
REIT - convertible debenture	**32,493**	32,251
Derivative financial liabilities - interest rate swaps	**983**	318
Unamortized deferred financing fees	**(2,281)**	(2,010)
	657,560	631,008

We are subject to financial covenants on our revolving credit facility. We were in compliance with these covenants at June 30, 2016.

	Covenant	June 30, 2016
Maximum debt to total capital	1.25	0.76
Minimum interest coverage ratio	3.00	3.50
Minimum net book value of shareholders' equity	$ 300,000	$ 957,359

We are also subject to financial covenants on the REIT's $35.00 million revolving credit facility. The covenants include a maximum debt to total capital ratio of 60% (excluding convertible debenture), a minimum debt service coverage ratio of 1.50, and a minimum adjusted unitholders' equity of $140.00 million. As at June 30, 2016, and throughout the period, we were in compliance with our financial covenants.

These metrics are non-standard measures used to assess compliance with our lending agreements and are not specifically defined in the CPA Handbook or in IFRS. These non-standard measures may not be comparable to similar measures presented by other companies.

Sources and uses of cash

The following table summarizes our cash flows from (used in) operating, investing and financing activities, as reflected in our consolidated statement of cash flows:

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Cash flows from (used in) operating activities	**2,350**	8,261	**25,292**	**(1,418)**
Cash flows used in investing activities	**(3,667)**	(14,311)	**(42,322)**	**(24,350)**
Cash flows from (used in) financing activities	**10,577**	(27)	**5,859**	**14,578**

Cash flows from operating activities were $25.29 million in the first half of 2016, an increase of $26.71 million over the same period of 2015. Timing of collections on accounts receivable and agreements receivable, combined with settlement of liabilities resulted in net inflows of $25.91 million compared with $2.30 million during the same period in the prior year. Cash expended on purchase of land inventory and development reflect the slow down in the Community Development division, with $9.44 million in spending year to date, down $5.37 million from 2015.

Cash flows used in investing activities was $42.32 million, an increase of $17.97 million over 2015. During 2016, we continued to re-invest US funds with the purchase of three suburban office properties in the Greater Denver area for total cash consideration of $33.74 million (US $25.46 million) - net of assumed mortgage of $15.62 million (US $11.53 million). We also invested $9.07 million in the construction of new commercial properties as well as enhancements to existing commercial properties.

Cash flows used in financing activities were $5.86 million, a change of $8.72 million over the first half of 2015. Proceeds from general debt of $55.60 million were partially offset by repayments on our credit facilities of $13.04 million and repayments on general debt of $30.13 million. During the first half of 2016 we paid $0.24 per share dividend for a total of $7.98 million, a decrease of $1.97 million over 2015 as the dividend was reduced by $0.06 per share.

Share Data

Melcor has been a public company since 1968 and trades under the symbol “MRD” on the Toronto Stock Exchange. As at June 30, 2016 there were 33,246,562 common shares issued and outstanding and 760,767 options, each convertible to one common share upon exercise or exchange. There is only one class of common shares issued.

Off Balance Sheet Arrangements, Contractual Obligations, Business Environment & Risks, Critical Accounting Estimates, Changes in Accounting Policies

There are no material changes to the above titled sections at June 30, 2016 in comparison to the December 31, 2015 annual MD&A.

Normal Course Issuer Bid

On March 29, 2016 we announced a new Normal Course Issuer bid commencing March 31, 2016 and ending March 30, 2017. Under the bid, we may acquire up to 1,661,810 common shares in total (approximately 5% of our issued and outstanding common shares) with a daily repurchase restriction of 1,433 common shares. As at June 30, 2016, we did not repurchase any common shares.

Quarterly Results

The following table presents a summary of our unaudited operating results for the past eight quarters. This information should be read in conjunction with the related financial statements, notes to the financial statements and management's discussion and analysis.

	Three Months Ended							
($000s)	**30-Jun-16**	31-Mar-16	31-Dec-15	30-Sept-15	30-Jun-15	31-Mar-15	31-Dec-14	30-Sept-14
Revenue	**42,084**	30,554	91,721	87,921	46,113	37,554	121,452	93,484
Net income (loss)	**1,778**	(7,714)	32,658	24,823	3,917	14,560	50,077	26,193
Per Share								
Basic earnings	**0.05**	(0.23)	0.98	0.75	0.12	0.44	1.56	0.83
Diluted earnings	**0.05**	(0.23)	0.99	0.74	0.12	0.44	1.46	0.83
Book value	**28.80**	28.86	29.43	28.47	27.67	27.76	27.22	25.96

We have historically experienced variability in our results of operations from quarter to quarter due to the seasonal nature of the development business and the timing of plan registrations with the municipalities. We typically experience the highest sales in our Community Development division in the fourth quarter, as this is when the majority of plans register. The fair value gains in our Property Development division are also seasonally affected, as the majority of construction in Alberta takes place during the spring and summer months. Growth in our income-producing assets serves to offset this cyclicality.

Subsequent Events

Refer to note 11 of the interim consolidated financial statements for information pertaining to subsequent events.

Internal Control over Financial Reporting & Disclosure Controls

The Chief Executive Officer and the Chief Financial Officer have evaluated whether there were material changes to internal control over financial reporting during the quarter ended June 30, 2016 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting. No such changes were identified.

Non-standard Measures

Throughout this MD&A, we refer to terms that are not specifically defined in the CICA Handbook and do not have any standardized meaning prescribed by IFRS. These non-standard measures may not be comparable to similar measures presented by other companies.

We believe that these non-standard measures are useful in assisting investors in understanding components of our financial results.

The non-standard terms that we refer to in this MD&A are defined below.

Net operating income (NOI): this is a measure of revenue less direct operating expenses.

Same asset NOI: this measure compares the NOI on assets that have been owned for the entire current and comparative period.

Funds from operations (FFO): this measure is commonly used to measure the performance of real estate operations.

Calculations

We use the following calculations in measuring our performance.

Book value per share = (shareholders' equity) / (number of common shares outstanding)

Gross margin (%) = (gross profit) / (revenue) This measure indicates the relative efficiency with which we earn revenue

Net margin (%) = (net income (loss)) / (revenue) This measure indicates the relative efficiency with which we earn income

Debt to equity ratio = (total debt) / (total equity)

Net operating income (NOI) = (net income (loss)) +/– (fair value adjustments on investment properties) + (general and administrative expenses) – (interest income) + (amortization of operating lease incentives) +/- (straight-line rent adjustment). A reconciliation of NOI to the most comparable IFRS measure, net income (loss), is as follows:

Investment Properties

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Segment Earnings	**4,169**	7,167	**6,401**	10,814
Fair value adjustment on investment properties	**705**	(2,898)	**2,820**	(2,725)
General and administrative expenses	**588**	956	**1,273**	2,087
Interest income	**—**	(3)	**(2)**	(6)
Amortization of operating lease incentives	**91**	124	**202**	193
Straight-line rent adjustment	**(205)**	(69)	**(720)**	(248)
Divisional NOI	**5,348**	5,277	**9,974**	10,115

REIT

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Segment Earnings	**9,467**	7,484	**17,043**	14,791
Fair value adjustment on investment properties	**174**	1,899	**1,999**	3,708
General and administrative expenses	**652**	516	**1,393**	1,293
Interest income	**(8)**	(18)	**(17)**	(36)
Amortization of operating lease incentives	**785**	896	**1,610**	1,618
Straight-line rent adjustment	**(297)**	(395)	**(642)**	(787)
Divisional NOI	**10,773**	10,382	**21,386**	20,587

Funds from operations (FFO) = (net income (loss)) + (amortization of operating lease incentives) +/– (fair value adjustment on investment properties) + (depreciation of property and equipment) + (stock based compensation expense) + (non-cash interest) +/- (gain (loss) on sale of asset) + (deferred income taxes) +/– (fair value adjustment on REIT Units). A reconciliation of NOI to the most comparable IFRS measure, net income (loss), is as follows:

Consolidated

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Net income (loss) for the period	**1,778**	3,917	**(5,936)**	18,477
Amortization of operating lease incentives	**1,516**	1,517	**3,093**	2,777
Fair value adjustment on investment properties	**(2,436)**	(6,359)	**(1,417)**	(7,002)
Depreciation on property and equipment	**495**	541	**739**	799
Stock based compensation expense	**69**	74	**157**	170
Non-cash interest	**1,220**	246	**1,585**	485
Gain on sale of asset	**(3)**	(58)	**(3)**	(58)
Deferred income taxes	**173**	7,685	**(25)**	7,374
Fair value adjustment on REIT units	**5,576**	1,015	**14,385**	(8,231)
FFO	**8,388**	8,578	**12,578**	14,791

Investment Properties

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Segment Earnings	**4,169**	7,167	**6,401**	10,814
Fair value adjustment on investment properties	**705**	(2,898)	**2,820**	(2,725)
Amortization of operating lease incentives	**91**	124	**202**	193
Divisional FFO	**4,965**	4,393	**9,423**	8,282

REIT

($000s)	Three months ended		Six months ended	
	June 30, 2016	June 30, 2015	June 30, 2016	June 30, 2015
Segment Earnings	**9,467**	7,484	**17,043**	14,791
Fair value adjustment on investment properties	**174**	1,899	**1,999**	3,708
Amortization of operating lease incentives	**785**	896	**1,610**	1,618
Divisional FFO	**10,426**	10,279	**20,652**	20,117

FFO per share = (FFO) / (basic weighted average common shares outstanding)

Condensed Interim Consolidated Financial Statements

For the three and six months ended June 30, 2016

(Unaudited, in thousands of Canadian dollars)

Condensed Interim Consolidated Statement of Income (Loss)

	For the three months ended		For the six months ended	
(Unaudited)	**June 30, 2016**	June 30, 2015	**June 30, 2016**	June 30, 2015
Revenue	**42,084**	46,113	**72,638**	83,667
Cost of sales	**(21,733)**	(24,899)	**(36,369)**	(44,674)
Gross profit	**20,351**	21,214	**36,269**	38,993
General and administrative expense	**(4,807)**	(5,964)	**(9,649)**	(10,973)
Fair value adjustment on investment properties (note 5 and 10)	**2,436**	6,359	**1,417**	7,002
Adjustments related to REIT units (note 9)	**(7,459)**	(2,917)	**(18,149)**	4,426
Gain on sale of asset	**3**	58	**3**	58
Operating earnings	**10,524**	18,750	**9,891**	39,506
Interest income	**162**	696	**501**	1,418
Finance costs	**(6,492)**	(6,664)	**(12,881)**	(11,860)
Net finance costs	**(6,330)**	(5,968)	**(12,380)**	(10,442)
Income (loss) before income taxes	**4,194**	12,782	**(2,489)**	29,064
Income tax expense	**(2,416)**	(8,865)	**(3,447)**	(10,587)
Net income (loss) for the period	**1,778**	3,917	**(5,936)**	18,477
Earnings (loss) per share:				
Basic earnings (loss) per share	**0.05**	0.12	**(0.18)**	0.56
Diluted earnings (loss) per share	**0.05**	0.12	**(0.18)**	0.56

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Comprehensive Income (Loss)

	For the three months ended		For the six months ended	
(Unaudited)	**June 30, 2016**	June 30, 2015	**June 30, 2016**	June 30, 2015
Net income (loss) for the period	**1,778**	3,917	**(5,936)**	18,477
Other comprehensive income (loss)				
Items that may be reclassified subsequently to net income (loss):				
Currency translation differences	**319**	(1,282)	**(7,016)**	7,443
Comprehensive income (loss)	**2,097**	2,635	**(12,952)**	25,920

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Financial Position

(Unaudited)	June 30, 2016	December 31, 2015
ASSETS		
Cash and cash equivalents	35,178	48,674
Restricted cash (note 3)	—	2,288
Accounts receivable	13,489	18,744
Income taxes recoverable	12,354	2,455
Agreements receivable	107,706	152,183
Land inventory (note 4)	700,388	696,802
Investment properties (note 5 and 10)	958,295	904,348
Property and equipment	16,090	16,269
Other assets	48,538	50,206
	1,892,038	1,891,969
LIABILITIES		
Accounts payable and accrued liabilities	26,380	40,534
Income taxes payable	—	1,342
Provision for land development costs	89,258	93,839
General debt (note 6)	657,560	631,008
Deferred income tax liabilities	66,695	66,875
REIT units (note 9 and 10)	94,786	80,401
	934,679	913,999
SHAREHOLDERS' EQUITY		
Share capital (note 7)	70,269	70,061
Contributed surplus	2,854	2,743
Accumulated other comprehensive income (AOCI)	21,689	28,705
Retained earnings	862,547	876,461
	957,359	977,970
	1,892,038	1,891,969

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Changes in Equity

(Unaudited)	Equity attributable to Melcor's shareholders Share capital	Contributed surplus	AOCI	Retained earnings	Total equity
Balance at January 1, 2016	**70,061**	**2,743**	**28,705**	**876,461**	**977,970**
Net loss for the period	—	—	—	(5,936)	(5,936)
Cumulative translation adjustment	—	—	(7,016)	—	(7,016)
Transactions with equity holders					
Dividends	—	—	—	(7,978)	(7,978)
Employee share options					
Value of services recognized	—	157	—	—	157
Share issuance	208	(46)	—	—	162
Balance at June 30, 2016	**70,269**	**2,854**	**21,689**	**862,547**	**957,359**

(Unaudited)	Equity attributable to Melcor's shareholders Share capital	Contributed surplus	AOCI	Retained earnings	Total equity
Balance at January 1, 2015	67,767	2,947	10,023	820,598	901,335
Net income for the period	—	—	—	18,477	18,477
Cumulative translation adjustment	—	—	7,443	—	7,443
Transactions with equity holders					
Dividends	—	—	—	(9,947)	(9,947)
Employee share options					
Value of services recognized	—	170	—	—	170
Share issuance	1,179	(268)	—	—	911
Balance at June 30, 2015	68,946	2,849	17,466	829,128	918,389

See accompanying notes to these condensed interim consolidated financial statements.

Condensed Interim Consolidated Statement of Cash Flows

	For the three months ended		For the six months ended	
Unaudited ($000s)	**June 30, 2016**	June 30, 2015	**June 30, 2016**	June 30, 2015
CASH FLOWS FROM (USED IN)		(note 12)		(note 12)
OPERATING ACTIVITIES				
Net income (loss) for the period	**1,778**	3,917	**(5,936)**	18,477
Non cash items:				
Amortization of tenant incentives	**1,516**	1,517	**3,093**	2,777
Depreciation of property and equipment	**495**	541	**739**	799
Stock based compensation expense	**69**	74	**157**	170
Non cash interest	**1,220**	246	**1,585**	485
Straight-line rent adjustment	**(473)**	(128)	**(1,188)**	(894)
Fair value adjustment on investment properties (note 5 and 10)	**(2,436)**	(6,359)	**(1,417)**	(7,002)
Fair value adjustment on REIT units (note 9 and 10)	**5,576**	1,015	**14,385**	(8,231)
Gain on sale of asset	**(3)**	(58)	**(3)**	(58)
Deferred income taxes	**173**	7,685	**(25)**	7,374
	7,915	8,450	**11,390**	13,897
Agreements receivable	**16,838**	16,360	**44,477**	31,129
Development activities	**(7,282)**	(11,376)	**(8,127)**	(12,309)
Purchase of land inventory (note 4)	**(1,309)**	—	**(1,309)**	(2,500)
Payment of tenant lease incentives and direct leasing costs	**(1,330)**	(1,284)	**(2,570)**	(2,873)
Change in restricted cash (note 3)	**—**	—	**—**	63
Operating assets and liabilities	**(12,482)**	(3,889)	**(18,569)**	(28,825)
	2,350	8,261	**25,292**	(1,418)
INVESTING ACTIVITIES				
Purchase of investment properties	**—**	(7,128)	**(33,738)**	(10,146)
Additions to investment properties	**(4,224)**	(6,551)	**(9,068)**	(13,315)
Change in restricted cash (note 3)	**1,041**	—	**1,041**	—
Purchase of property and equipment	**(493)**	(702)	**(566)**	(959)
Proceeds on disposal of property and equipment	**9**	70	**9**	70
	(3,667)	(14,311)	**(42,322)**	(24,350)
FINANCING ACTIVITIES				
Revolving credit facilities	**4,719**	(7,043)	**(13,037)**	15,506
Proceeds from general debt	**13,268**	17,045	**55,598**	19,976
Repayment of general debt	**(4,698)**	(5,716)	**(30,133)**	(12,229)
Change in restricted cash (note 3)	**1,146**	168	**1,247**	361
Dividends paid	**(3,990)**	(4,976)	**(7,978)**	(9,947)
Share capital issued	**132**	495	**162**	911
	10,577	(27)	**5,859**	14,578
FOREIGN EXCHANGE GAIN (LOSS) ON CASH HELD IN A FOREIGN CURRENCY	**107**	(39)	**(2,325)**	174
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS DURING THE PERIOD	**9,367**	(6,116)	**(13,496)**	(11,016)
CASH AND CASH EQUIVALENTS, BEGINNING OF THE PERIOD	**25,811**	14,111	**48,674**	19,011
CASH AND CASH EQUIVALENTS, END OF THE PERIOD	**35,178**	7,995	**35,178**	7,995
Total income taxes paid	**6,350**	4,470	**14,892**	17,240
Total interest paid	**6,248**	4,684	**13,271**	13,891

See accompanying notes to these condensed interim consolidated financial statements.

(Unaudited – in $000s except per share, share and acre amounts)

1. CORPORATE INFORMATION

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

The parent company is Melcor Developments Ltd. (“Melcor” or “we”) and is incorporated in Canada. The registered office is located at Suite 900, 10310 Jasper Avenue Edmonton, AB T5J 1Y8. We operate in Canada and the United States (“US”). Our shares are traded on the Toronto Stock Exchange under the symbol “MRD”. As at June 30, 2016 Melton Holdings Ltd. holds 47.2% of the outstanding shares and pursuant to IAS 24, Related party disclosures, is the ultimate controlling shareholder of Melcor.

As at August 10, 2016, Melcor through an affiliate, holds an approximate 56.7% effective interest in Melcor REIT ("REIT" or "the REIT") through ownership of all Class B LP Units of the Partnership and is the ultimate controlling party. Melcor continues to manage, administer and operate the REIT and its properties under an asset management agreement and property management agreement. Trust units of the REIT are traded on the Toronto Stock Exchange under the symbol "MR.UN".

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

2. BASIS OF PRESENTATION

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

These condensed interim consolidated financial statements should be read in conjunction with our annual consolidated financial statements for the year ended December 31, 2015, which have been prepared in accordance with IFRS as issued by the IASB.

These condensed interim consolidated financial statements were approved for issue by the Board of Directors on August 10, 2016.

3. RESTRICTED CASH

Restricted cash represents subsidies funded by Melcor as part of the REIT's Initial Public Offering to subsidize finance costs on assumed debt and Class C LP Units, and to fund capital expenditures, environmental expenditures, tenant incentives and lease costs. The cash was required to be presented as restricted pursuant to a covenant in the underwriting agreement. On May 1, 2016 the term of the covenant elapsed, at which point the remaining restricted cash was re-classified to cash and cash equivalents.

4. LAND INVENTORY

	June 30, 2016	December 31, 2015
Raw land held	**343,740**	353,809
Land under development	**140,370**	134,200
Developed land	**216,278**	208,793
	700,388	696,802

During the six month period ended June 30, 2016, we purchased 94 acres of land at a cost of $3,443 and received vendor financing of $2,134.

During the comparative six month period ended June 30, 2015 we purchased 147 acres of land at a cost of $14,000 and received vendor financing of $11,500.

5. INVESTMENT PROPERTIES

Investment properties consists of the following:

	June 30, 2016	December 31, 2015
Investment properties	**893,408**	847,387
Properties under development	**64,887**	56,961
Total	**958,295**	904,348

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

			Six months ended June 30, 2016
	Investment Properties	**Properties under Development**	**Total**
Balance - beginning of period	847,387	56,961	**904,348**
Additions			
Direct acquisition	49,356	—	**49,356**
Transfer from land inventory	—	254	**254**
Direct leasing costs	293	189	**482**
Property improvements	1,247	—	**1,247**
Development costs	1,885	5,833	**7,718**
Capitalized borrowing costs	—	103	**103**
Transfers	3,050	(3,050)	**—**
Fair value adjustment on investment properties	(3,180)	4,597	**1,417**
Foreign currency translation (included in OCI)	(6,630)	—	**(6,630)**
Balance - end of period	**893,408**	**64,887**	**958,295**

			Year ended December 31, 2015
	Investment Properties	Properties under Development	**Total**
Balance - beginning of year	863,966	37,138	**901,104**
Additions			
Direct acquisition	983	3,018	**4,001**
Acquisition through business combination	14,619	—	**14,619**
Transfer from land inventory	—	4,211	**4,211**
Direct leasing costs	587	424	**1,011**
Property improvements	5,024	—	**5,024**
Development costs	439	25,533	**25,972**
Capitalized borrowing costs	—	258	**258**
Disposals	(81,153)	(3,088)	**(84,241)**
Transfers	20,067	(20,067)	**—**
Fair value adjustment on investment properties	40	9,534	**9,574**
Foreign currency translation (included in OCI)	22,815	—	**22,815**
Balance - end of year	**847,387**	**56,961**	**904,348**

In accordance with our policy we record our investment properties at fair value. Fair value adjustments on investment properties are primarily driven by changes in capitalization rates and stabilized net operating income ("NOI"). Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 10.

During the six months ended June 30, 2016, we completed the acquisition of three suburban office properties in the greater Denver area:

- On February 26 - the Offices at Promenade for $23,073 (US$17,032) (including transaction costs). As part of the purchase Melcor also assumed a mortgage on the property with a carrying value of $15,618 (US$11,529). As at financial liability we recorded the assumed mortgage at its fair value on initial recognition. The fair value of the mortgage was calculated using a market interest rate for an equivalent mortgage;
- On March 3 - the Offices at Inverness for $13,067 (US$9,746) (including transaction costs); and
- On March 31 - Syracuse Hill One for $13,216 (US$10,188) (including transaction costs).

These acquisitions were funded through available cash and were accounted for as direct acquisitions.

Supplemental information on fair value measurement, including valuation techniques and key inputs, is included in note 10.

6. GENERAL DEBT

	June 30, 2016	December 31, 2015
Melcor - revolving credit facilities	**74,707**	84,813
REIT - revolving credit facility	**16,327**	19,258
Project specific financing	**21,298**	25,280
Secured vendor take back debt on land inventory	**72,598**	76,092
Debt on investment properties and golf course assets	**441,435**	395,006
REIT - convertible debenture	**32,493**	32,251
Derivative financial liabilities - interest rate swaps	**983**	318
Unamortized deferred financing fees	**(2,281)**	(2,010)
	657,560	631,008

7. SHARE CAPITAL

Issued and outstanding common shares at June 30, 2016 are 33,246,562 (December 31, 2015 – 33,233,712). During the three and six months ended June 30, 2016, there were 10,350 and 12,850 options exercised (Q2-2015 – 37,466 and 69,566).

8. SEGMENTED INFORMATION

Geographic Analysis

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

External Revenues	**For the three months ended**		**For the six months ended**	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
United States	**4,793**	4,334	**8,477**	8,426
Canada	**37,291**	41,779	**64,161**	75,241
Total	**42,084**	46,113	**72,638**	83,667

Total Assets

As at	**June 30, 2016**	December 31, 2015
United States	**205,685**	184,908
Canada	**1,686,353**	1,707,061
Total	**1,892,038**	1,891,969

(Unaudited – in $000s except per share, share and acre amounts)

8. SEGMENTED INFORMATION (continued)

Divisional Analysis

Our divisions reported the following results:

For the three months ended June 30, 2016	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Segment revenue	15,591	3,304	8,885	16,807	4,256	—	48,843	(6,759)	42,084
Cost of sales	(10,813)	(3,300)	(3,423)	(6,522)	(2,188)	(131)	(26,377)	4,644	(21,733)
Gross profit	4,778	4	5,462	10,285	2,068	(131)	22,466	(2,115)	20,351
General and administrative expense	(2,020)	(364)	(588)	(652)	(872)	(1,059)	(5,555)	748	(4,807)
Fair value adjustment on investment properties	—	1,948	(705)	(174)	—	—	1,069	1,367	2,436
Gain on sale of assets	—	—	—	—	3	—	3	—	3
Interest income	152	1	—	8	—	1	162	—	162
	2,910	1,589	4,169	9,467	1,199	(1,189)	18,145	—	18,145
Finance costs									(6,492)
Adjustments related to REIT units									(7,459)
Income before tax									4,194
Income tax expense									(2,416)
Net income									1,778

For the three months ended June 30, 2015	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Segment revenue	20,679	7,375	8,083	16,323	4,273	—	56,733	(10,620)	46,113
Cost of sales	(14,206)	(7,350)	(2,861)	(6,442)	(2,183)	(154)	(33,196)	8,297	(24,899)
Gross profit	6,473	25	5,222	9,881	2,090	(154)	23,537	(2,323)	21,214
General and administrative expense	(2,497)	(331)	(956)	(516)	(816)	(1,774)	(6,890)	926	(5,964)
Fair value adjustment on investment properties	—	3,963	2,898	(1,899)	—	—	4,962	1,397	6,359
Gain on sale of assets	—	—	—	—	58	—	58	—	58
Interest income	674	—	3	18	—	1	696	—	696
	4,650	3,657	7,167	7,484	1,332	(1,927)	22,363	—	22,363
Finance costs									(6,664)
Adjustments related to REIT units									(2,917)
Income before tax									12,782
Income tax expense									(8,865)
Net income									3,917

(Unaudited – in $000s except per share, share and acre amounts)

Six months ended June 30, 2016 June 30, 2016	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Segment revenue	23,530	3,310	16,773	33,433	4,474	—	81,520	(8,882)	72,638
Cost of sales	(15,925)	(3,300)	(6,281)	(13,015)	(2,749)	(270)	(41,540)	5,171	(36,369)
Gross Profit	7,605	10	10,492	20,418	1,725	(270)	39,980	(3,711)	36,269
General and administrative expense	(4,193)	(844)	(1,273)	(1,393)	(1,223)	(2,229)	(11,155)	1,506	(9,649)
Fair value adjustment on investment properties	—	4,031	(2,820)	(1,999)	—	—	(788)	2,205	1,417
Gain on sale of assets	—	—	—	—	3	—	3	—	3
Interest Income	479	2	2	17	—	1	501	—	501
	3,891	3,199	6,401	17,043	505	(2,498)	28,541	—	28,541
Finance costs									(12,881)
Adjustment related to REIT units									(18,149)
Loss before tax									(2,489)
Income tax expense									(3,447)
Net loss									(5,936)

Six months ended June 30, 2015	Community Development	Property Development	Investment Properties	REIT	Recreational Properties	Corporate	Subtotal	Intersegment Elimination	Total
Revenue	35,900	7,427	15,827	32,581	4,462	—	96,197	(12,530)	83,667
Cost of sales	(24,684)	(7,350)	(5,657)	(12,825)	(2,682)	(308)	(53,506)	8,832	(44,674)
Gross profit	11,216	77	10,170	19,756	1,780	(308)	42,691	(3,698)	38,993
General and administrative expense	(4,467)	(775)	(2,087)	(1,293)	(1,145)	(3,076)	(12,843)	1,870	(10,973)
Fair value adjustment on investment properties	—	6,157	2,725	(3,708)	—	—	5,174	1,828	7,002
Gain on sale of assets	—	—	—	—	58	—	58	—	58
Interest Income	1,375	—	6	36	—	1	1,418	—	1,418
	8,124	5,459	10,814	14,791	693	(3,383)	36,498	—	36,498
Finance costs									(11,860)
Adjustment related to REIT units									4,426
Income before tax									29,064
Income tax expense									(10,587)
Net income									18,477

(Unaudited – in $000s except per share, share and acre amounts)

9. NON-CONTROLLING INTEREST IN MELCOR REIT

In accordance with our policy, we account for the remaining 43.3% publicly held interest in the REIT as a financial liability measured at fair value through profit or loss ("FVTPL"). As at June 30, 2016 the REIT units had a fair value of $94,786. We recorded fair value losses related to REIT units for the three and six months ended June 30, 2016 of $7,459 and $18,149 (Q2-2015 - fair value loss of $2,917 and fair value gain of $4,426, respectively for each comparative period).

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

	For the three months ended		For the six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Fair value adjustment on REIT units (note 10)	**(5,576)**	(1,015)	**(14,385)**	8,231
Distributions to REIT unitholders	**(1,883)**	(1,902)	**(3,764)**	(3,805)
Adjustments related to REIT units	**(7,459)**	(2,917)	**(18,149)**	4,426

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

As at	**June 30, 2016**	December 31, 2015
Assets	**665,845**	666,458
Liabilities	**360,544**	362,129
Net assets	**305,301**	304,329
Cost of NCI	**102,707**	102,707
Fair value of NCI	**94,786**	80,401

	For the three months ended		For the six months ended	
	June 30, 2016	June 30, 2015	**June 30, 2016**	June 30, 2015
Revenue	**16,807**	16,323	**33,433**	32,581
Net income (loss) and comprehensive income (loss)	**(4,153)**	111	**(14,119)**	13,402
Cash flows from operating activities	**2,937**	324	**5,546**	2,919
Cash flows from (used in) investing activities	**564**	(771)	**(917)**	(1,064)
Cash flows from (used in) financing activities, before distributions to REIT unitholders	**(3,292)**	4,378	**352**	(2,717)
Cash flows used in financing activities - cash distributions to REIT unitholders	**(1,883)**	(1,902)	**(3,764)**	(3,805)
Net increase (decrease) in cash and cash equivalents	**(1,674)**	2,029	**1,217**	(4,667)

10. FAIR VALUE MEASUREMENT

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

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

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

(Unaudited – in $000s except per share, share and acre amounts)

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

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

	June 30, 2016				December 31, 2015	
	Fair Value	**Amortized Cost**	**Total Carrying Value**	**Total Fair Value**	Total Carrying Value	Total Fair Value
Non-financial assets						
Investment properties	**958,295**	**—**	**958,295**	**958,295**	904,348	904,348
Financial liabilities						
General debt, excluding derivative financial liabilities	**—**	**656,572**	**656,572**	**663,986**	631,003	638,297
Derivative financial liabilities						
Interest rate swaps	**983**	**—**	**983**	**983**	318	318
Conversion feature on convertible debenture	**5**	**—**	**5**	**5**	5	5
REIT units	**94,786**	**—**	**94,786**	**94,786**	80,401	80,401

The table below analyzes assets and liabilities carried at fair value in the consolidated statement of financial position, by the levels in the fair value hierarchy. The fair hierarchy categorizes fair value measurement into three levels based upon the inputs to valuation technique, which are defined as follows:

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

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

	Level 1	**Level 2**	**Level 3**	**Total**
Non-financial assets				
Investment properties	—	—	958,295	958,295
Financial liabilities				
REIT units	94,786	—	—	94,786
Derivative financial liabilities				
Interest rate swaps	—	983	—	983
Conversion feature on convertible debenture	—	—	5	5

Investment properties

Investment properties are remeasured to fair value on a recurring basis, determined based on the accepted valuation methods of direct income capitalization or discounted future cash flows.

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

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

(Unaudited – in $000s except per share, share and acre amounts)

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

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

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

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

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

Investment properties were reviewed by qualified external valuators at June 30, 2016, which resulted in fair value gains of $1,417 recorded as fair value adjustment on investment properties in the interim condensed consolidated statements of income and comprehensive income.

For the year ended December 31, 2015, Melcor Development Ltd.'s internal valuation team performed the valuation assessment. Of 76 legal phases assessed, 37 properties with a fair value of $586,298 were valued by qualified independent external valuation professionals during the year, which resulted in fair value gains of $9,574.

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

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

Weighted average annual stabilized net operating income for investment properties as at June 30, 2016 is $1,499 (December 31, 2015 - $1,488). Other significant valuation metrics and unobservable inputs are set out in the following table. Fair values are most sensitive to changes in capitalization rates.

(Unaudited – in $000s except per share, share and acre amounts)

	Investment Properties			**Properties under Development**		
June 30, 2016	**Min**	**Max**	**Weighted Average**	**Min**	**Max**	**Weighted Average**
Capitalization rate	**5.50%**	**8.75%**	**6.58%**	**6.00%**	**6.75%**	**6.44%**
Terminal capitalization rate	**5.75%**	**9.00%**	**6.81%**	**6.00%**	**7.25%**	**6.83%**
Discount rate	**6.50%**	**9.75%**	**7.67%**	**7.00%**	**7.75%**	**7.38%**

	Investment Properties			Properties under Development		
December 31, 2015	Min	Max	Weighted Average	Min	Max	Weighted Average
Capitalization rate	5.50%	9.00%	6.54%	5.75%	6.75%	6.58%
Terminal capitalization rate	5.75%	9.25%	6.80%	6.00%	7.25%	7.03%
Discount rate	6.50%	10.00%	7.68%	7.00%	7.75%	7.47%

An increase in capitalization rates by 50 basis points would decrease the fair value and carrying amount of investment properties by $55,480 (December 31, 2015 - $55,349). A decrease in capitalization rates by 50 basis points would increase the fair value and carrying amount of investment properties by $64,599 (December 31, 2015 - $64,573).

REIT units

REIT units are remeasured to fair value on a recurring basis. The units are fair valued based on the trading price of the REIT units at the period end date. At June 30, 2016 the fair value of the REIT units was $94,786, resulting in a fair value loss for the six month period of $14,385 (December 31, 2015 - gain of $25,261) recorded in the statement of income and comprehensive income (note 9).

Derivative financial liabilities

Our derivative financial liabilities are comprised of floating for fixed interest rate swaps on mortgages (level 2) and the conversion feature on our convertible debenture (level 3).

The fair value of the interest rate swaps are calculated as the net present value of the future cash flows expected to arise on the variable and fixed portion, determined using applicable yield curves at the measurement date. As at June 30, 2016 the fair value of interest rate swap contracts was $983.

The significant unobservable inputs used in the fair value measurement of the conversion feature on the convertible debenture as at June 30, 2016 are as follows:

- Volatility - expected volatility as at June 30, 2016 was derived from the historical prices of our trust units. As the REIT was formed on May 1, 2013, price history is limited and we use the entire historical data up until June 30, 2016. Volatility was 15.86% (December 31, 2015 - 15.86%).
- Credit spread - the credit spread of the convertible debenture was imputed from the traded price of the convertible debenture as at June 30, 2016. The credit spread used was 4.60% (December 31, 2015 - 4.60%).

11. EVENTS AFTER THE REPORTING PERIOD

Distributions on REIT trust units

On July 15, 2016 we declared a distribution of $0.05625 per unit for the months of July, August and September 2016. The distributions will be payable as follows:

Month	**Record Date**	**Distribution Date**	**Distribution Amount**
July 2016	July 29, 2016	August 15, 2016	$0.05625 per unit
August 2016	August 31, 2016	September 15, 2016	$0.05625 per unit
September 2016	September 30, 2016	October 17, 2016	$0.05625 per unit

Dividends declared

On August 10, 2016 our board of directors declared a dividend of $0.12 per share payable on September 30, 2016 to shareholders of record on September 15, 2016.

12. COMPARATIVE FIGURES

The three and six month comparative 2015 balances of payment of tenant incentives and direct leasing costs of $1,284 and $2,873, change in restricted cash of $0 and $63, and purchase of land inventory of $0 and $2,500 have been reclassified from investing activities to operating activities in the consolidated statement of cash flows to reflect better presentation of the underlying nature of the cash flows.