Killam Properties Inc.
Annual Report 2012

Our Business

Killam Properties Inc. is a growing Canadian real estate company. We own, manage and develop multi-family residential properties in Atlantic Canada and Ontario. Since the first acquisition in 2002, our portfolio has grown to $1.4 billion in apartments and manufactured home communities (MHCs).

We have a strong operating platform and diverse portfolio of quality assets. We are maximizing Killam's value and long-term profitability by concentrating on three key areas of growth:

Increasing the earnings from our existing properties,

Expanding our portfolio and diversifying geographically through accretive acquisitions, with an emphasis on newer assets, and

Developing high-quality apartments in our core markets.

We are committed to this strategy and made advancements in each area during 2012. We believe that this strategy will distinguish Killam as having one of the highest quality multi-family residential portfolios in Canada.

Our Mission

To have a team of caring staff deliver clean, safe, quality housing to tenants who are proud to call our properties home, and to be a fiscally responsible company that is recognized as a community leader.

Our Apartment Portfolio

We own and manage a portfolio of 11,620 apartment units in Atlantic Canada and Ontario. Halifax accounted for 46% of apartment revenue in 2012. We expanded into Ontario in 2010 and our portfolio now includes 1,078 units in Ottawa, London, Cambridge and Mississauga.

Our MHC Portfolio

We own and manage 7,407 sites in 44 MHCs in Atlantic Canada and Ontario. MHCs are a strong complement to our apartment business, offering stable cash flows and occupancy of 98%.

The James, Halifax, NS

2012 Highlights

Increased funds from operations per share by 2.9%.

Achieved 2.0% growth in net operating income from same store properties.

Completed $85 million in acquisitions.

Expanded geographically with acquisitions in Ottawa and Mississauga.

Strengthened the balance sheet, reducing total debt as a percent of total assets to 51.6%.

Invested $40 million in four apartment developments opening in 2013.

12.7% total annual return for shareholders.

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2012 Performance Summary

Objective	2012 Target	2012 Performance
Consolidation of the Multi-family Residential Real Estate Market	To complete approximately $100 million in acquisitions.	Completed $85 million in acquisitions, including $78 million in apartment acquisitions and $7 million for the acquisition of three parcels of land for future development.
Increase Investment in New Properties	Acquire new properties as part of the acquisition program in 2012.	Acquired two new buildings in 2012, including 1175 Maritime Way, a 146-unit building in Ottawa, built in 2012, and Chapter House, a 41-unit building in downtown Halifax, built in 2004.
	Continue with four apartment developments, on time and on budget.	The four developments were 75% complete at December 31, 2012, on track for completion in early 2013. The first building, Brighton House in Charlottetown, opened in February 2013, and the remaining projects are expected to be ready for occupancy in April and May 2013. The developments are expected to be completed within 6% of their original budgets.
Geographic Diversification	Acquisitions in 2012 to include investments in Ontario.	53% of acquisitions completed in 2012 were in Ontario. Killam entered both the Ottawa market, with the purchase of five buildings, and the Greater Toronto Area market, with the acquisition of a 199-unit building in Mississauga.
Growth in Same Store Net Operating Income	Grow the net operating income of the existing portfolio by 2% to 4%.	Achieved same store net operating income growth of 2%.
Maximize Value of Excess Land	Complete 25 to 30 home sales in 2012 and gain approval for additional developments on excess land.	Completed 26 home sales. Killam also completed site expansions at its Greenhill MHC in Nova Scotia.

Richmond Hill, London, ON

Financial & Operating Highlights

(in thousands, except per share amounts)

As at and for the years ended December 31,	**2012**	2011	% Change
Operations			
Property revenue	**$133,641**	$126,089	6.0%
Net rental income	**$80,444**	$76,352	5.4%
Funds from operations (FFO)	**$36,096**	$31,757	13.7%
FFO per share (basic)	**$0.72**	$0.70	2.9%
Dividends declared per share [1]	**$0.58**	$0.57	1.8%
AFFO payout ratio	**96.7%**	98.3%	(160 bps)
Financial Position			
Total assets	**$1,443,128**	$1,329,531	8.5%
Total liabilities	**$854,692**	$816,988	4.6%
Total equity	**$588,436**	$512,543	14.8%
Shares outstanding (weighted average)	**50,227**	45,523	10.3%
Shares outstanding (at Dec 31)	**53,802**	49,291	9.2%
Total debt as a percent of total assets	**51.6%**	55.2%	(360 bps)
Interest coverage ratio	**2.09**	1.98	5.6%
Portfolio Information			
Apartment units	**11,620**	10,638	9.2%
MHC sites	**7,407**	9,441	(21.5%)
Total units	**19,027**	20,079	(5.2%)

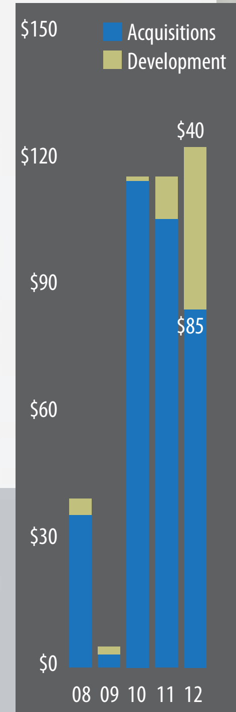
(1) Killam increased its annual dividend from $0.56 per share to $0.58 per share in 2011. The increase became effective for the June 2011 dividend.

Killam by the Numbers

Expanding Annually Through Acquisitions and Development

Annual Investment in Acquisitions and Development in $ Millions

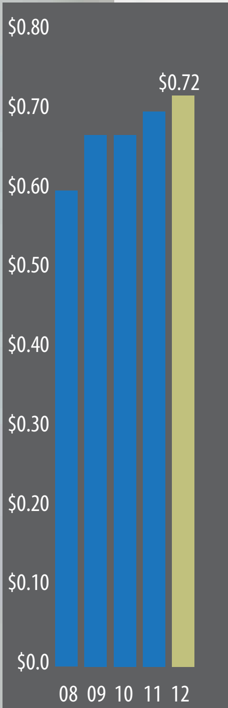
Killam completed $85 million in acquisitions in 2012, which included the Company's first properties in Mississauga and Ottawa. Development was also an important focus for growth in 2012, with $40 million invested in four development projects. Combining acquisitions and the development of apartments increases Killam's growth potential in today's competitive acquisition environment, and expands the portfolio of new, high-quality properties.



Growing FFO per Share

FFO per Share

FFO per share increased 2.9% in 2012 to $0.72 per share, compared to $0.70 in 2011. The growth was primarily attributable to increased earnings from Killam's existing portfolio, up 2% year-over-year, and contributions from acquisitions. These gains were partially offset by the decrease in NOI resulting from the MHC disposition in May 2012, increased shares outstanding and the investment in uncompleted developments. Four development projects underway in 2012 are expected to contribute positively to FFO per share growth in 2013.

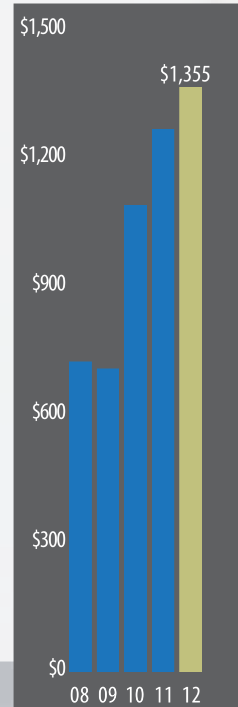


Increasing Value of Real Estate Assets

Value of Investment Properties in $ Millions (1)

Killam's investment properties were valued at $1.4 billion at December 31, 2012. The increase from 2011 was attributable to $85 million in acquisitions, $40 million invested in development projects and fair value appreciation of the existing portfolio. These increases were partially offset by the sale of 12 MHC properties for $73 million in May 2012.

(1) Values reflect the fair market value of assets for 2010-2012 as presented under International Financial Reporting Standards (IFRS). 2008 and 2009 values reflect the gross book value of assets as reported under previous Canadian GAAP.

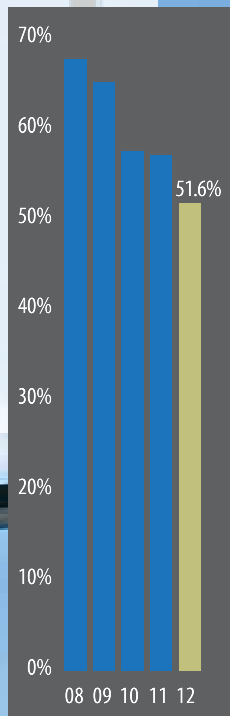


The Plaza Development, Fredericton, NB

Strengthening the Balance Sheet

Total Debt as a Percentage of Total Assets

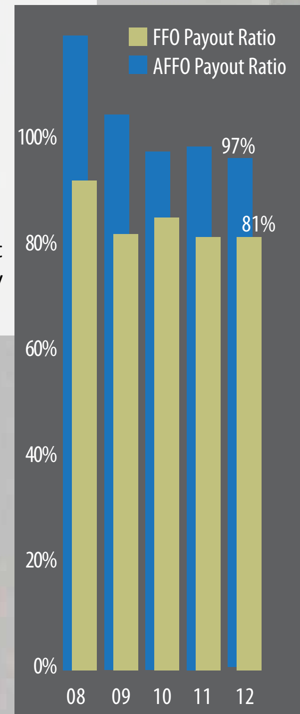
Killam strengthened its balance sheet in 2012, decreasing debt as a percent of total assets to 51.6% at December 31, 2012, down from 55.2% at December 31, 2011. The reduction reflects higher property values and an increase in cash on hand. Killam targets to maintain a debt ratio of between 55% and 65% of total assets.



Improving Payout Ratios

Dividends as a Percentage of FFO and AFFO

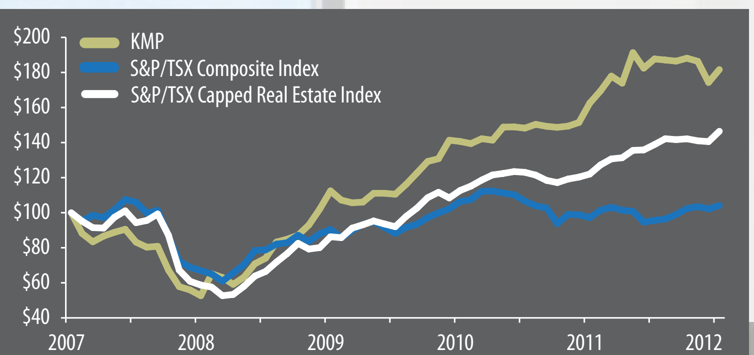
Killam's FFO and AFFO payout ratios improved in 2012. AFFO, adjusted funds from operations, represents FFO less capital requirements to maintain the portfolio. These payout ratios highlight the stability of Killam's dividend.

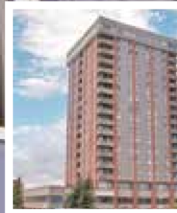


Strong Relative Performance

Total Cumulative Return Comparison Based on a $100 Investment

Killam has outperformed both the S&P/TSX Composite Index and the S&P/TSX Capped Real Estate Index over the last five years. Earnings growth, strong investor demand for yield and strength of the multi-family real estate asset class has contributed to Killam's performance.





Chapter House, Halifax, NS

Advancing the Plan

Portfolio

We have a diverse portfolio of quality properties and we are focused on increasing the value of these assets by maximizing revenue and operational efficiencies, and through capital investment. One of our key performance indicators is same store net operating income (NOI) growth, representing the increased operating profits of properties that we've owned for equivalent periods. This takes out the impact of acquisitions and measures the growth of the same portfolio year-over-year. We expect to grow same store NOI an average of 2% to 4% on an annual basis. In 2012 we increased same store NOI by 2%, and over Killam's history we have achieved an average annual growth rate of 3.5%.

1355 Silver Spear Road, Mississauga, ON

Advancing the Plan

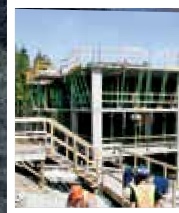
Acquisitions

Acquisitions are an important growth area for Killam. Since our first apartment purchase in 2002, we've completed $1 billion in acquisitions. Killam's portfolio of 193 properties has been accumulated over eleven years, often one building or MHC at a time. During 2012, we completed $85 million in acquisitions, including eight apartment buildings located in Halifax, Ottawa and Mississauga. Growth will continue in 2013; we've targeted $75 million to $125 million in acquisitions for the year.

We're acquiring a combination of new and older properties in central locations in our core markets. Geographically, our acquisitions are split between Atlantic Canada and Ontario. In 2012, 14% of our earnings were generated outside of Atlantic Canada. We're working to increase that number to 50% through our acquisition program.

Advancing the Plan

New Developments



S2 Development, Halifax, NS

We're enhancing our growth opportunities by developing new properties. We recognize the benefits of owning new buildings and believe one of the best ways to grow our portfolio with the highest-quality new buildings is to build them. We're investing in energy-efficient systems and extensive amenities, which will set our new apartments apart from others. We're designing buildings for people seeking the convenience and flexibility of renting, but with the space, quality and amenities associated with ownership.

We started our development program in 2010 and completed our first development, a 49-unit building, in 2011. During 2012 we made significant progress on four new properties. The new buildings, totaling an investment of $63 million, will be completed during the first half 2013. We plan to continue to invest in new developments on an annual basis, including two new projects scheduled to start in 2013.

Management Team

Philip Fraser
President &
Chief Executive Officer

Robert Richardson
Executive Vice President
& Chief Financial Officer

Ruth Buckle
Vice President
Property Management

Erin Cleveland
Vice President
Finance

Pamela Crowell
Vice President
Property Management
(MHC)

Jeremy Jackson
Vice President
Marketing

Dale Noseworthy
Vice President
Investor Relations and
Corporate Planning

Michael McLean
Vice President
Development

S2 Development, Halifax, NS

President's Letter

Dear Fellow Shareholders,

I am pleased to report on Killam's results for 2012 and to discuss the Company's plans going forward. This past year, Killam's eleventh year of operation, was another eventful one. We made progress in each of our three key growth areas: increasing the value of our existing portfolio, growing through acquisitions and enhancing our portfolio with developments. This year's annual report theme is "Advancing the Plan" and highlights that we're staying on course with each of these three important components of Killam's growth strategy.

Increasing the Earnings from Our Properties

Growing the operating cash flow from our properties on an annual basis is paramount to Killam's success. Our existing portfolio of $1.4 billion in assets is the real fuel for growth per share. We expect to increase operating earnings from our same store assets by an average of 2% to 4% per year, and have been successful in doing so over our history. To continue to achieve these numbers, we need to grow the top line, maximize operational efficiencies and manage expenses.

In 2012, we achieved 2% same store NOI growth. We were successful in achieving rental rate increases, up 3.6% in the year, which more than offset a decrease in occupancy rates in certain apartment markets due to new rental supply. Overall, same store rental revenue increased by 1.9%, including 1.5% for the apartment portfolio and 3.5% for the MHC portfolio.

Halifax, Nova Scotia, home to 41% of our apartment units, has seen an increase in new rental construction over the past two years. The construction is being fuelled by an expectation of increased demand from an aging population of baby boomers, plus population growth from the $25 billion, 25-year Irving Shipbuilding contract which is scheduled to start in 2015. The new rental supply is coming to market a few years ahead of this demand growth, resulting in a slight uptick in vacancy rates in Halifax in 2012. As Atlantic Canada's economic hub, we are confident in the long-term strength of Halifax. Killam is well positioned to face increased competition in Halifax, with a diverse portfolio of well-maintained and centrally located assets.

St. John's, Newfoundland, led our same store growth in 2012. The offshore oil activity in Newfoundland has transformed St. John's. We've seen the benefit of owning in this market with year after year rental growth above the average for our portfolio, and the average increase for the country, as measured by Canada Mortgage and Housing Corporation. In 2012, our average rent increased by 7.4% in St. John's. Occupancy levels remain strong in the city, and are among the highest in our portfolio. We are optimistic about the St. John's market, and look to expand our ownership in the city.

Saint John, New Brunswick and Charlottetown, PEI, proved to be our two most challenging markets in 2012. Saint John, representing only 7% of Killam's apartment NOI, experienced softness over the last couple of years as economic growth slowed, following completion of several energy projects in the city. While we've seen our occupancy in this market stabilize, we do not anticipate strong rental growth over the near term.

Following three years of strong occupancy, Charlottetown experienced a recent spike in vacancy due to new construction and a decrease in international immigration. After ending the year with the highest vacancy in our portfolio, we've seen improvements in leasing in Charlottetown in the first quarter of 2013. In addition, we are experiencing strong demand for our new development, Brighton House, which recently opened in Charlottetown.

As in Halifax, we've seen above-average development in Moncton, resulting in increased competition. We experienced a dip in occupancy in Moncton during the first half of 2012, but we successfully increased occupancy in the third quarter, ending the year at 96.3%. We expanded our capital investment in Moncton in 2012 to better compete with new product, and have also added rental incentives as required.

With more moderate levels of new construction in recent years, Fredericton has not experienced increased competition and has proven to be our most stable market in New Brunswick over the last year. We expect this trend to continue in 2013.

Finally, in Ontario, we've seen a mix of results. Killam's occupancy was down in Ontario year-over-year due to turnover in a portfolio of properties in Ottawa acquired in September 2012 and a short-term spike in vacancy in Cambridge. We are actively leasing units in both Ottawa and Cambridge and we expect to show improvement in 2013. On the positive front, we've seen strong demand for units in our London assets, with both buildings currently fully leased. As well, 1175 Maritime Way, a new 146-unit building in Ottawa, is also fully leased.

Competitive Acquisition Market in 2012

The acquisition environment was competitive this past year as low interest rates and strong demand for yield continued to push capitalization rates lower. We completed $85 million in acquisitions in 2012. Although we weren't able to purchase all the buildings we would have liked due to the competitive market, we are pleased with the additions we did make and the capitalization rates at which we were able to transact.

We acquired two properties in Halifax, which we believe will outperform the market over the long-term. Ottawa is a market that we've been looking to expand in for the last five years and we were pleased to have purchased five properties there in 2012. Subsequent to year-end, we added a sixth building, increasing our presence in Ottawa. We're expanding our management platform in Ottawa and are confident in the opportunities for growth in the city. Finally, we completed our first acquisition in the GTA. We're optimistic about the potential of the Toronto area and over time expect to expand our presence in this key Canadian market.

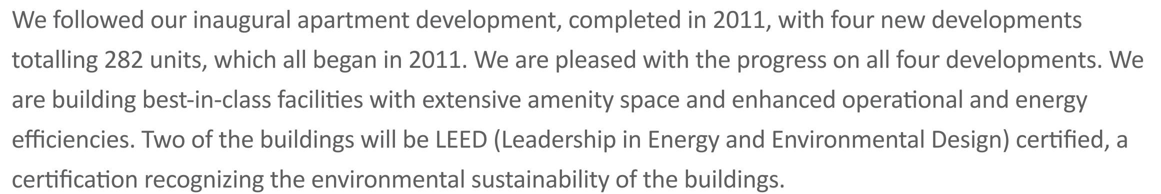
Portfolio of Non-core MHCs Sold in 2012

We sold twelve manufactured home communities during the second quarter of 2012. This sale represents our first asset divestiture. The properties were sold for a total price of $72.3 million and included five communities in Western Canada and seven communities in Ontario. The net proceeds, after the assumption of existing mortgages, were $33.9 million.

While we continue to value the MHC business and its stable contribution to funds from operations, this sale crystallized the appreciation in value for a portion of our MHC portfolio that was geographically dispersed and not considered core to our operations. In addition, a transaction associated with this sale allowed us to acquire our first asset in the GTA.

New Developments to Open in 2013

Our third area of growth is development, which was an important focus in 2012. We believe that investing in new assets will result in improved long-term shareholder returns given the higher growth potential realized through a quality tenant base, low operating costs, and significantly reduced capital requirements.



We followed our inaugural apartment development, completed in 2011, with four new developments totalling 282 units, which all began in 2011. We are pleased with the progress on all four developments. We are building best-in-class facilities with extensive amenity space and enhanced operational and energy efficiencies. Two of the buildings will be LEED (Leadership in Energy and Environmental Design) certified, a certification recognizing the environmental sustainability of the buildings.

The first of the four buildings completed was Brighton House in Charlottetown, which opened its doors in February 2013 and was 50% leased by the end of that month. The other buildings are scheduled to open in April and May of this year. We look forward to having these properties contribute positively to our FFO growth in the second half of 2013.

We expect to invest in developments on an annual basis, complementing our acquisition program. We will manage the developments responsibly, and expect to limit the annual development spending to within 5% of Killam's asset base.

Looking Forward

Our plan for the year ahead is to continue to stay the course, making progress in our three core areas of growth.

We are targeting between 2% and 4% earnings growth from our existing portfolio. New construction in certain markets in Atlantic Canada may impact occupancy levels in 2013; however, we are able to adjust our leasing and marketing strategies to react quickly. We believe that our diversified portfolio of quality assets will mitigate the impact of higher levels of competition in the market.

We expect to benefit from the continued low interest rate environment in 2013. We have $85 million of mortgage debt rolling with interest rates at 4.36% on the apartment debt and 6.24% on the MHC debt, between 100 and 150 basis points higher than what we can borrow at today. With interest rates projected to stay low in 2013, we expect to refinance at more attractive rates and decrease our interest costs.

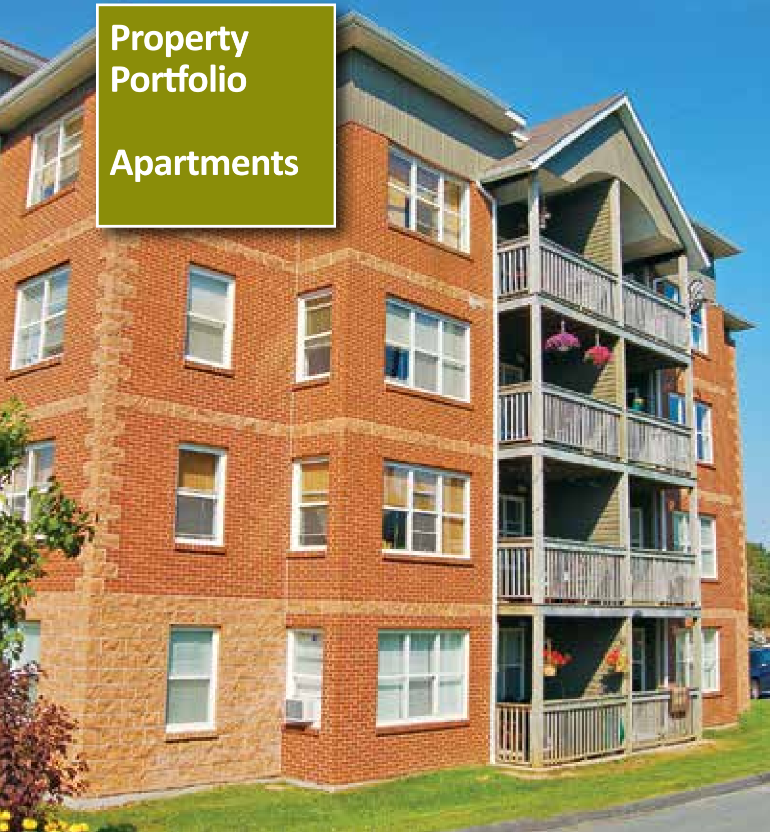
Low interest rates are also expected to keep the acquisition market competitive and capitalization rates low. We've targeted $75 million to $125 million in acquisitions in 2013, which will include new and older buildings, as well as a mix of locations between Atlantic Canada and Ontario. Our ability to meet our acquisition target for the year will depend on the ability to purchase properties at accretive levels.

On the development front, we expect to complete and lease-up our four new developments as well as commence two new development projects.

I would like to thank all Killam employees for their contributions and continued commitment, and the board of directors for their governance throughout 2012. In addition, I would like to thank you, our shareholders, for your support and interest in Killam. I invite you to attend Killam's annual meeting on May 8, 2013 at 2pm Atlantic Time at the Halifax Marriott Harbourfront Hotel, either in person or via webcast. I look forward to providing updates on our progress in 2013 over the coming months.

Yours truly,

Philip Fraser



Property Portfolio

Apartments

NOVA SCOTIA	Units	Year Built	Average Rent	
HALIFAX			**Dec-12**	**Dec-11**
1 Oak Street	146	1969	$878	$838
10-214 Harlington Crescent	60	1978	791	765
19 Plateau Crescent	81	1974	776	754
159 Radcliffe Drive	25	1995	983	952
175-211 Harlington Crescent	60	1978	793	768
1540 Carlton Street	1	n/a	2,000	n/a
21 Parkland Drive	98	2002	1,118	1,070
26 Alton/36 Kelly Street	80	1969	686	665
294-300 Main Street	58	1969	806	771
3 Veronica Drive	70	1983	863	831
31 Carrington Place	38	1998	1,239	1,191
3565 Connaught Avenue	19	1958	789	771
50 Barkton Lane	63	1991	844	814
5206 Tobin Street	47	1993	1,078	1,040
57 Westgrove Place	41	1969	762	743
59 Glenforest/21 Plateau	153	1978	758	735
6 Jamieson Street	24	1965	748	726
6087 South Street	9	1999	1,411	1,366
6101 South Street	30	2002	1,525	1,479
67-141 Harlington Crescent	60	1978	772	743
75 Knightsridge Drive	41	1986	864	839
85-127 Harlington Crescent	60	1978	784	758
9 Bruce Street	60	1974	631	604
9 Sybyl Court	22	1975	703	683
95 Knightsridge Drive	46	1984	950	913
Bedford Apartments	53	1987	746	713
Brentwood Apartments	240	1968	769	n/a
Chapter House	41	2004	1,853	n/a
Dillman Place	60	1970s	734	708
Garden Park Apartments (1)	246	1980	869	845
Glenforest Apartments	80	1969	866	849
Glenbourne Gate	67	2000	982	928
Glenmoir Terrace	28	1972	738	706
Hillcrest Apartments	50	1980	799	773
Kent Street Properties	139	1950s	867	843
Lakefront Apartments	396	1954	723	697
Linden Lea/Pleasant Street	28	1950s	682	651
Maplehurst Apartments	268	1965	796	765
Maplehurst Houses	15	1965	1,003	981
Parker Street Apartments	239	1960/75	749	719
Parkridge Place	76	2002	1,009	970
Paxton Place	67	2000	980	929
Quinpool Court	198	1978	1,044	1,000
Quinpool Towers	233	1978	1,069	1,023
Shaunslieve Apartments	154	1978	803	797
Sheradon Place	82	1979	910	864
Spring Garden Terrace	201	1964	1,139	1,099
The James	108	2008	1,325	1,297
The Linden	81	2011	1,489	1,493
Victoria Gardens	198	1954	742	722
Waterview Place	82	1971	797	768
HALIFAX TOTAL	**4,822**			
SYDNEY				
Cabot House	88	1974	940	922
Moxham Court	51	1998	1,019	964
SYDNEY TOTAL	**139**			
NS TOTAL	**4,961**			

(1) Killam has a 47% ownership interest in the 246-unit Garden Park Apartments.

NEW BRUNSWICK	Units	Year Built	Average Rent	
MONCTON			**Dec-12**	**Dec-11**
100 Archibald Street	60	2003	$809	$782
101 Archibald Street	60	1993	755	737
115 Kedgewick Drive	25	2009	886	847
133 Kedgewick Drive	23	2010	891	863
135 Gould Street	69	2011	929	960
155 Canaan Drive	48	2008	984	994
1111 Main Street	16	1957	1,476	1,476
276-350 Gauvin Road	84	1991/96	719	690
303 Normandie Street	70	1994	814	783
316 Acadie Avenue	48	1996	742	721
360 Acadie Avenue	60	1998	720	699
364-368 Gauvin Road	80	1995	741	729
Belmar Plaza	50	2005	902	882
Buckingham Place	55	1998	828	806
Cambridge Court	45	1994	885	855
Cambridge Place	63	1995	1,064	1,025
Cameron Street	81	1966/67	694	653
Eagles Ridge Estates	59	1994	814	799
Gordon/Bonaccord Street	41	1984/40s	704	677
Hestor & Church Street	64	1993	725	678
Lakeview Estates	48	1980/81	681	657
Lorentz Apartments	101	1969	751	733
Lutz & Kendra Street	40	1950/75	722	708
Pine Glen Apartments	54	1974	713	703
Suffolk Street	80	2000	741	718
MONCTON TOTAL	**1,424**			
FREDERICTON				
25 McKnight Street	64	2001	$943	$927
110 McKnight Street	45	1996	783	763
116 & 126 Wilsey Avenue	48	1975	764	728
120 McKnight Street	45	1998	846	830
127 & 157 Biggs Street	46	1985/92	800	769
200 Reynolds Street	52	2001	990	965
260 Wetmore Road	38	1978	762	747
300 Reynolds Street	52	2006	997	970
305 Reynolds Street	52	2010	1,029	1,004
50,60 Greenfield/190 Parkside	72	1977/86	718	691
75 Greensfield Drive	44	1980	685	674
969 Regent Street	62	1997/01	890	866
Carrington House	41	2002	913	906
Elroy Apartments	194	1973	808	793
Forest Hill Towers	151	1968/79	890	859
Princess Place	141	1968/79	776	749
Southgate Apartments	47	2003	960	933
Venus Apartments	54	1965	904	873
Westwood Apartment	45	1975	723	667
FREDERICTON TOTAL	**1,293**			
SAINT JOHN				
37 Somerset Place	21	2007	$1,067	$1,070
53 Somerset Place	16	1973	697	680
115 Woodhaven Drive	24	1977	634	600
Blue Rock Estates	60	2007	826	804
Carleton Towers	60	1968	697	675
Cedar Glen Apartments	204	1977	713	681
Ellerdale Apartments	154	1975	674	642
Fort Howe Apartments	153	1970	798	782
Parkwood Apartments	205	1947	660	645
Rocky Hill Apartments	42	2004	957	937
Sydney Arms	54	1961	748	733
The Anchorage	51	2003	970	937
Woodward Gardens	99	1962	780	770
SAINT JOHN TOTAL	**1,143**			
MIRAMICHI				
Edward Court	96	1993	$687	$662
NB TOTAL	**3,956**			

ONTARIO	Units	Year Built	Average Rent	
OTTAWA			**Dec-12**	**Dec-11**
1425 Rosenthal Avenue	54	1962	$861	n/a
1440 Mayview Avenue	103	1960s	868	n/a
266 Bronson Avenue	43	1968	845	n/a
621 Cummings Avenue	44	1950s	781	n/a
1175 Maritime Way (2)	146	2012	1,670	n/a
OTTAWA TOTAL	**390**			
LONDON				
180 Mill Street (2)	127	2011	$1,672	n/a
Richmond Hill Apartments	137	2009	1,609	1,571
LONDON TOTAL	**264**			
CAMBRIDGE				
100 Eagle Street	119	2008	$1,542	$1,517
200 Eagle Street	106	2004	1,383	1,350
CAMBRIDGE TOTAL	**225**			
MISSISSAUGA				
1355 Silver Spear Road (2)	199	1968	$1,115	n/a
ON TOTAL	**1,078**			

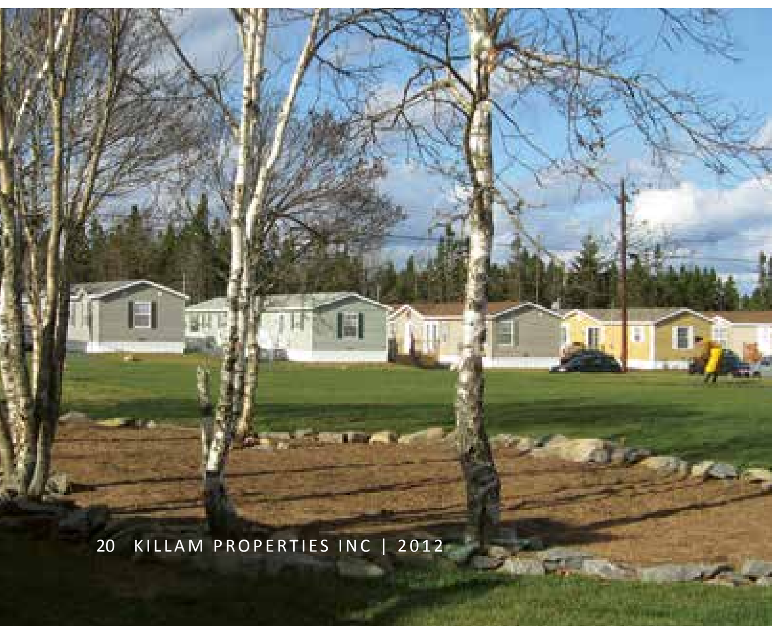
NEWFOUNDLAND	Units	Year Built	Average Rent	
ST. JOHN'S			**Dec-12**	**Dec-11**
Blackshire Court	69	1981	$868	$786
Cornwall Manor	31	1976	713	669
Freshwater Road Apartments	159	1972	790	735
Forest Manor	65	1978	749	687
Meadowland Apartments	105	1976	720	694
Mount Pleasant Manor	100	1976	701	646
Pleasantview Manor	36	1979	714	678
Rutledge Manor	53	1983	1,036	1,018
Torbay Road Apartments	84	1972	760	699
Village Manor	40	1978	730	693
ST. JOHN'S TOTAL	**742**			
GRAND FALLS				
Ridgeview Terrace Apartments	59	1975	$542	$536
Terrace Apartments	89	1970/90	752	738
GRAND FALLS TOTAL	**148**			
NL TOTAL	**890**			

PEI	Units	Year Built	Average Rent	
CHARLOTTETOWN			**Dec-12**	**Dec-11**
198 Spring Park Road	32	2006	$1,046	$1,001
27 Longworth Avenue	24	1983	689	667
319-323 Shakespeare Drive	22	2004	853	846
505-525 University Avenue	35	2003	1,164	1,139
Bridlewood Apartments	66	1998/99	872	846
Browns Court	52	1997	1,058	1,014
Burns/University	95	2003	1,017	982
Charlotte Court	49	2011	830	830
Country Place	39	1998/02	881	862
DesBarres House	51	1978	617	594
Horton Park	69	1987	812	792
Kensington Court	105	1990	807	793
Queen Street	48	1978	674	649
CHARLOTTETOWN TOTAL	**687**			
SUMMERSIDE				
Nevada Court	48	1995	$724	$714
PE TOTAL	**735**			
APARTMENT TOTAL	**11,620**			

(2) 180 Mill Street, 1175 Maritime Way and 1355 Silver Spear Road are owned through a joint venture - Killam has a 25% interest in each property.

Property Portfolio

MHC



NOVA SCOTIA	Sites	Acres	Average Rent	
			Dec-12	Dec-11
Amherst MHC	300	67	$193	$162
Birch Hill Estates	216	73	234	233
Birchlee Estates	222	42	235	230
Cairdeil Estates	160	37	175	176
Cowan Place	56	50	184	188
Enfield Estates	56	10	217	216
Fairview Estates	131	131	326	326
Glen Aire Estates	265	130	195	194
Greenhill Estates	115	30	221	223
Heather Estates	217	72	219	219
Kent Drive Estates	50	10	183	151
Maple Ridge Park	160	160	264	264
Mountainview Estates	353	168	227	227
Silver Birch Estates	64	16	199	199
Valley View Hills	196	50	200	200
NS TOTAL	**2,561**			

NEW BRUNSWICK	Sites	Acres	Average Rent	
			Dec-12	Dec-11
Burton Estates	91	32	$227	$227
Camper's City (3)	224	61	151	153
Crown & Currie Estates	176	140	251	249
Kent & Bayview	148	123	151	150
Milford Estates	152	22	293	293
Park P'Tiso Estates	79	18	172	172
Pine Tree Village	828	260	280	260
Parkside Estates	94	15	225	225
River East Estates	109	72	220	220
Tamarack Estates	419	75	240	238
White Frost Estates	212	51	224	209
NB TOTAL	**2,532**			

ONTARIO	Sites	Acres	Average Rent	
			Dec-12	Dec-11
Cedardale (3)	204	25	$167	$156
Domaine le Village	70	36	290	274
Family Paradise (3)	214	50	174	159
Holiday Harbour (3)	143	15	142	141
Holiday Park (3)	289	35	158	147
Lakewood Estates	60	13	282	272
Lynnwood Gardens	64	54	301	305
Millcreek	73	35	401	386
Paradise Valley (3)	392	109	174	169
Pine Tree Village	70	38	371	359
Pinehurst Estates	82	16	244	232
Rockdale Ridge	69	96	259	248
Stanley Park	107	76	302	279
The Village at Listowel	87	53	332	285
Westhill Estates	94	8	295	281
Wood Haven (3)	126	50	175	172
ON TOTAL	**2,144**			

NEWFOUNDLAND	Sites	Acres	Average Rent	
			Dec-12	Dec-11
Lakeview Court	86	13	$185	$173
Sunset Parkway	84	43	175	164
NL TOTAL	**170**			
MHC TOTAL	**7,407**			

(3) Properties are seasonal. Average monthly rent shown equal to annual rent divided by 12.

Making a Difference

2012 Highlights

Killam Scholarship Program

In 2012, Killam introduced a Scholarship Program, awarding three $3,000 scholarships to the children of employees. After a competitive application process, three students were selected for demonstrating an outstanding combination of academic excellence and community involvement.

Photo left to right: Bradley Price, Hayley Gillis and Mauresa Godbout

Supporting the YMCA

The Halifax North End Community YMCA reopened its gymnasium in September 2012 to unveil its newly renovated facility to the community. The renovation was helped in part by a $100,000 contribution from the board of directors of Killam Properties Inc.

Photo left to right: Bette Watson-Borg, YMCA President & CEO; Maureen MacDonald, Minister of Health for Nova Scotia; Peter Green, Community YMCA Campaign Chair and Robert Richardson, EVP & CFO, Killam Properties Inc.

Home Away From Home

On an annual basis, Killam donates six fully furnished apartments to hospitals in Halifax, Saint John, Moncton, Fredericton and Charlottetown. These units are used by families of patients who need to travel away from home for health care.

Red Cross

Killam has partnered with the Red Cross in many of its communities in Canada. The Red Cross is on hand to help when emergencies and disasters impact communities. Over the last five years, Killam has provided the Red Cross with financial assistance to fund their operations. In response, the Red Cross has provided emergency training to Killam staff, helping us react to emergencies effectively when required.

Management's Discussion & Analysis

Dollar amounts in thousands (except as noted)

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PART I

Basis of Presentation

The following management discussion and analysis ("MD&A") has been prepared by Management and focuses on key statistics from the consolidated financial statements and pertains to known risks and uncertainties. To ensure that the reader is obtaining the best overall perspective, this MD&A should be read in conjunction with material contained in the Company's audited consolidated financial statements for the years ended December 31, 2012 and 2011. The consolidated financial statements for the years ended December 31, 2012 and 2011 have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). These documents, along with the Company's 2012 Annual Information Form, are available on SEDAR at www.sedar.com. The discussions in this MD&A are based on information available as at March 5, 2013.

Forward-looking Statements

Certain statements in this MD&A constitute "forward-looking statements". In some cases, forward-looking statements can be identified by the use of words such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "potential", "continue" or the negative of these terms or other comparable terminology, and by discussions of strategies that involve risks and uncertainties. Readers should be aware that these statements are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from those anticipated or implied, or those suggested by any forward looking statements, including: competition, national and regional economic conditions and the availability of capital to fund further investments in Killam's business. Further information regarding these risks, uncertainties and other factors may be found under the heading "Risk Management" in this MD&A and in the Company's most recent Annual Information Form. Given these uncertainties, readers are cautioned not to place undue reliance on any forward-looking statements contained, or incorporated by reference, in this MD&A.

By their nature, forward-looking statements involve numerous assumptions, inherent risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and various future events may not occur. Although Management believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that future results, levels of activity, performance or achievements will occur as anticipated. Neither Killam nor any other person assumes responsibility for the accuracy and completeness of any forward-looking statements, and no one has any obligation to update or revise any forward-looking statement, whether as a result of new information, future events, circumstances, or such other factors which affect this information, except as required by law. The forward-looking statements in this document are provided for the limited purpose of enabling current and potential investors to evaluate an investment in the Company. Readers are cautioned that such statements may not be appropriate and should not be used for any other purpose.

Non-IFRS Measures

There are measures included in this MD&A that do not have a standardized meaning under IFRS and therefore may not be comparable to similarly titled measures presented by other publicly traded companies. The Company includes these measures as a means of measuring financial performance.

- Net operating income ("NOI") is calculated by the Company as income from property operations. The use of NOI when referring to a particular segment is calculated as revenue less operating costs for that segment.
- Funds from operations ("FFO") are calculated by the Company as net income plus deferred tax expense, loss on disposition and depreciation on owner-occupied property, less fair value gains, gain on disposition and non-controlling interest. Killam's definition of FFO is calculated in accordance with the REALpac definition.
- Adjusted funds from operations ("AFFO") are calculated by the Company as FFO less the industry standard of $450 per apartment unit for "maintenance" related capital costs and $100 per Manufactured Home Community ("MHC") site, although the MHC industry does not have a standard amount for "maintenance" related capital costs.
- Same store results in relation to the Company are revenues and property operating expenses for stabilized properties the Company has owned for equivalent periods in 2012 and 2011 (89% of the portfolio based on unit count).
- Capitalization Rate ("Cap-Rate") is the rate calculated by dividing the forecasted NOI from a property by the property's purchase price.
- Interest coverage is calculated by dividing the earnings before interest, tax, depreciation, and fair value adjustments by interest expense.
- Debt service coverage is calculated by dividing the earnings before interest, tax, depreciation, and fair value adjustments by interest expense and principal mortgage repayments.

PART II

Key Performance Indicators (KPIs)

Management measures Killam's performance based on the following key performance indicators (KPI):

1. FFO per Share – A standard measure of earnings for real estate entities. Management is focused on growing FFO per share on an annual basis.
2. Rental Increases – Management expects to achieve increases in average rental rates on an annual basis and measures the average rental increases achieved.
3. Occupancy – Management is focused on maximizing occupancy levels while also managing the impact of higher rents. This measure considers units rented as a percentage of total stabilized units at a point in time.
4. Same Store NOI Growth – This measure considers the Company's ability to increase the NOI of properties that it has owned for equivalent periods year-over-year, removing the impact of acquisitions, dispositions and developments.
5. Weighted Average Cost of Debt – Killam monitors the weighted average cost of its mortgage debt, and total debt.
6. Debt to Total Assets – Killam measures its debt levels as a percentage of total assets and works to ensure that the debt remains at a conservative level.
7. Term to Maturity – Management monitors the average number of years to maturity on its debt.
8. Interest Coverage Ratio – A common measure of credit risk used by lenders, this measure considers Killam's ability to pay interest on outstanding debt. Generally, the higher the interest coverage ratio, the lower the credit risk.
9. Debt Service Coverage Ratio – A common measure of credit risk used by lenders, this measure considers Killam's ability to pay interest and principal on outstanding debt. Generally, the higher the debt service coverage ratio, the lower the credit risk.

Business Overview

Killam Properties Inc., based in Halifax, Nova Scotia, is one of Canada's largest residential landlords, owning, operating, managing and developing multi-family residential and Manufactured Home Community ("MHC") properties. Killam's 149 apartment properties are located in Atlantic Canada's six largest urban centres and in Ontario. The Company's 44 MHCs are located in Ontario and Atlantic Canada. The value of Killam's real estate assets at December 31, 2012, was $1.4 billion. Killam is focused on growing its portfolio, maximizing the value of its properties and increasing FFO per share.

Killam was founded in 2000, based on the recognition of an opportunity to create value through the consolidation of apartments in Atlantic Canada and MHCs across Canada. Killam's first apartment was purchased in 2002 and its first MHC was purchased in 2003. From 2002 to 2009, Killam's apartment portfolio grew through the acquisition of properties in Atlantic Canada's six largest cities, including Halifax, Moncton, Saint John, Fredericton, St. John's and Charlottetown. Killam is now Atlantic Canada's largest residential landlord, with a 13% market share of the multi-family rental units in these core markets. Killam entered the Ontario apartment market in 2010, and today owns 10 properties in the Province, including assets in Mississauga, Ottawa, London and Cambridge. Killam plans to expand its presence in Ontario with additional acquisitions and developments. The apartment business is Killam's largest business segment, accounting for 82% of the Company's NOI from property operations in 2012. At December 31, 2012, Killam's apartment portfolio consisted of 11,620 units.

Killam has been complementing its acquisition program with the construction of apartment buildings since 2010. The Company's first development project, a 49-unit building, was completed in 2011. The other development projects, totaling 282 units, are currently underway, with the first building completed in February and the remaining three expected to be completed in the first half of 2013. The aggregate cost of the development projects is $63.1 million, representing approximately 4% of Killam's asset base.

The Company's multi-family rental portfolio is distinguishable from the majority of other residential rental companies through its ownership in MHCs, also known as land-lease communities or trailer parks. Killam owns the land and infrastructure supporting each community and leases the lots to tenants, who own their own homes and pay Killam a monthly site rent. With 44 communities, Killam owns the largest portfolio of MHCs of any publicly traded company, and is the second largest owner of MHCs in Canada. The portfolio includes MHCs in Ontario and Atlantic Canada. The MHC business accounted for 18% of Killam's NOI in 2012.

Financial and Operational Highlights

The following table presents a summary of Killam's financial and operating performance for the year ended December 31, 2012 compared to 2011:

Results of Operations

	2012	2011	Change
Property revenue	**$ 133,641**	$ 126,089	6.0%
NOI	**$ 80,444**	$ 76,352	5.4%
Income before fair value gains, loss on disposition and income taxes	**$ 37,023**	$ 32,671	13.3%
Net income applicable to common shareholders	**$ 51,727**	$ 65,965	(21.6)%
Earnings per share (basic)	**$ 1.03**	$ 1.45	(29.0)%
FFO	**$ 36,096**	$ 31,757	13.7%
FFO per share (basic)	**$ 0.72**	$ 0.70	2.9%
Shares outstanding (December 31st)	**53,801,809**	49,290,571	9.2%
Weighted average shares outstanding (basic)	**50,226,973**	45,523,031	10.3%

Same Store Results

	2012	2011	Change
Same store revenue	**$ 112,466**	$ 110,404	1.9%
Same store expenses	**$ (45,366)**	$(44,644)	1.6%
Same store NOI	**$ 67,100**	$ 65,760	2.0%

Balance Sheet (as at December 31)

	2012	2011	Change
Investment properties	**$ 1,354,665**	$ 1,258,219	7.7%
Total assets	**$ 1,443,128**	$ 1,329,531	8.5%
Total liabilities	**$ 854,692**	$ 816,988	4.6%
Total equity	**$ 588,436**	$ 512,543	14.8%

Ratios

	2012	2011	Change
Total debt to total assets	**51.6%**	55.2%	(360) bps
Weighted average mortgage interest rate	**4.48%**	4.63%	(15) bps
Weighted average years to maturity	**3.40**	3.80	(0.4) years
Interest coverage	**2.09x**	1.98x	5.6%
Debt service coverage	**1.35x**	1.34x	0.7%

Summary of 2012 Results and Operations

FFO Growth

Killam earned FFO of $36.1 million, or $0.72 per share, during 2012 compared to $31.8 million or $0.70 per share in 2011. The 2.9% growth in FFO per share was primarily attributable to positive FFO contributions from acquisitions and same store property growth, partially offset by increased interest costs associated with the convertible debentures, higher administrative costs, and the impact of additional shares outstanding.

Same Store NOI Increased by 2.0%

Killam's same store portfolio posted a 2.0% increase in NOI compared to 2011. Total revenue increased by 1.9% following higher rental rates, partially offset by higher vacancy. Expenses increased by 1.6% from the same period last year driven by higher property taxes which increased by 3.0% and general property operating expenses which increased by 1.8%.

Revenue Growth Despite Decreased Occupancy

Killam posted revenue growth, driven by increased rental rates, despite market pressure on occupancy. The change in occupancy during the year was primarily attributable to a short-term over-supply of new apartments in Halifax and Moncton, and a decrease in demand for rental units in Saint John and Charlottetown. Killam has responded to the occupancy demand pressure by offering rental incentives and implementing new marketing strategies at specific properties. The Company expects to see increased rental demand in its core Halifax market following population growth driven by the $25 billion Irving Shipbuilding Contract, expected to start in 2015.

Benefiting from Lower Interest Costs

Killam has been renewing maturing mortgages at lower interest rates. During 2012, Killam successfully refinanced $21.6 million in maturing apartment mortgages at a weighted average interest rate of 2.89%, 194 basis points lower than the weighted average interest rate of 4.83% on the debt prior to refinancing. Killam also refinanced $10.2 million in maturing MHC mortgages at a weighted average interest rate of 4.22%, 166 basis points lower than the weighted average interest rate of 5.88% prior to refinancing. Killam took advantage of lower long-term interest rates and renewed five apartment mortgages with 10-year terms in 2012, at a weighted average interest rate of 3.15%.

Positive Earnings Impact from Acquisitions Partially Offset by Disposition of 12 MHCs

Killam acquired a total of $84.8 million in acquisitions for 2012. In addition to properties acquired in Ontario, Killam purchased two properties in Halifax for $34.1 million, representing 281 units. $103 million in acquisitions completed in 2011 also contributed positively to year-over-year earning's growth. This NOI growth was partially tempered by the NOI forgone with the sale of 12 non-core MHCs during the second quarter of 2012.

Expansion of Ontario Apartment Portfolio

Killam acquired six buildings in Ontario during 2012, totaling $43.8 million. Killam acquired a four-building, 244-unit apartment portfolio in Ottawa for $24.5 million. As well, two acquisitions were made through Killam's partnership with Kuwait Finance House ("KFH") for $19.4 million, representing Killam's 25% interest in the properties. These acquisitions included a new 146-unit building in Ottawa and a 199-unit building in Mississauga.

Construction Continued on Development Projects

Killam's development projects, representing 282 units, have total budgeted costs of $63.1 million. The first building was completed in February 2013 and the remaining projects are expected to be completed during the first half of 2013, and will contribute positively to FFO per share during the balance of the year. Killam also acquired additional parcels of land in Nova Scotia and Newfoundland during 2012 for future development. The investment of $34 million in the development projects and acquisition of land resulted in a short-term dilutive impact on FFO per share in 2012.

Rise in Real Estate Valuations

Killam recorded $37.7 million in fair value gains in 2012, as compressed Cap-Rates increased the fair value of the Company's apartment and MHC portfolios. The continued low interest rate environment and the stability of the real estate sector in Canada have resulted in higher valuations for real estate assets. The gain in real estate valuations does not impact the Company's FFO per share, its key measure of performance.

Business Overview - Apartments

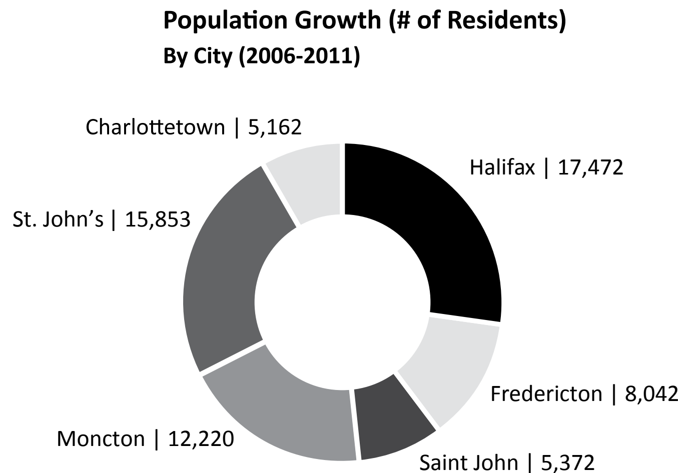
The following table summarizes Killam's apartment portfolio by market as at December 31, 2012:

	Units[1]	Number of Properties	% of Apartment NOI and Equity Income
Nova Scotia			
Halifax[2]	4,822	50	49.0%
Sydney	139	2	1.1%
	4,961	52	50.1%
New Brunswick			
Moncton	1,424	28	10.0%
Fredericton	1,293	19	10.7%
Saint John	1,143	13	7.0%
Mirimichi	96	1	0.7%
	3,956	61	28.4%
Ontario[3]			
Ottawa	390	5	1.2%
London	264	2	2.5%
Cambridge	225	2	3.3%
Mississauga	199	1	0.5%
	1,078	10	7.5%
Newfoundland			
St. John's	742	10	6.8%
Grand Falls	148	2	0.8%
	890	12	7.6%
Prince Edward Island			
Charlottetown	687	13	6.1%
Summerside	48	1	0.3%
	735	14	6.4%
Total	**11,620**	**149**	100.0%

(1) Unit count includes properties held through Killam's partnerships and joint ventures.
(2) Killam owns a 47% interest in and manages Garden Park Apartments, a 246-unit building located in Halifax, NS. Killam's 47% ownership interest represents 116 of the 246 units related to this property.
(3) Killam owns three buildings located in Ontario through a joint venture, with Killam having 25% ownership interest and managing the properties. Killam's 25% ownership interest represents 118 of the 472 units related to these properties.

Growing Population in Atlantic Canadian Cities

Atlantic Canada is home to 2.3 million people, approximately 43% of whom live in the six largest cities. The urbanization trend is strong across Atlantic Canada. The net change in population in Killam's core markets as measured by Statistics Canada in the 2011 Census, is shown in the following graph. Over the last five years these cities have experienced increased population growth, driven by urbanization and immigration.



Looking forward, Killam expects to see continued population and economic growth in its core Atlantic Canadian markets. Management expects Halifax and St. John's to lead the Atlantic Canadian market over the next few years. As the largest city in Atlantic Canada, Halifax continues to attract a diverse population, both from rural areas of Nova Scotia, and internationally. Irving Shipyard's award of the $25 billion, 25-year shipbuilding contract will have positive growth implications for Halifax, and Atlantic Canada. The contract is expected to generate an average of 8,500 direct and indirect jobs, and up to 11,500 jobs during its peak year in 2020. The shipyard is scheduled to begin to cut steel in 2015. In the meantime, Irving has started work on $350 million in infrastructure upgrades to facilitate the work. With 49% of Killam's apartment NOI earned from its centrally located properties in Halifax, Killam expects to benefit from the increased demand for housing.

St. John's, Newfoundland has been transformed by offshore investments, with exceptionally strong economic growth in recent years. The St. John's economy has grown by approximately 11% over the past three years and continued growth is expected. The decreased affordability of home ownership, coupled with an absence of new construction for rental units for the last twenty years, is generating strong demand for rental units in St. John's. Killam's new 71-unit property in St. John's is scheduled to open in April 2013. This property has experienced very strong pre-leasing and is evidence of the pent-up demand for multi-family housing.

Decreasing Capitalization Rates

Prior to Killam's consolidation of apartments in Atlantic Canada, the largest apartment owner had approximately 1,200 units, representing less than 2% of the market. The fragmented ownership in Atlantic Canada's major centres enabled Killam to purchase apartment buildings at attractive yields given comparable assets in Canada's other major cities. Since 2005 there has been Cap-Rate compression in Killam's core markets, a trend experienced throughout Canada. Low interest rates, access to Canadian Mortgage and Housing Corporation ("CMHC") insured financing and demand for multi-family residential properties have all contributed to decreased Cap-Rates. The Ontario market saw continued compression throughout 2012 with sub 5.0% Cap-Rates for premium product. The Halifax market appears to be trading at Cap-Rates in-line with many of Canada's larger cities while Cap-Rates in other Atlantic Canadian cities are marginally higher.

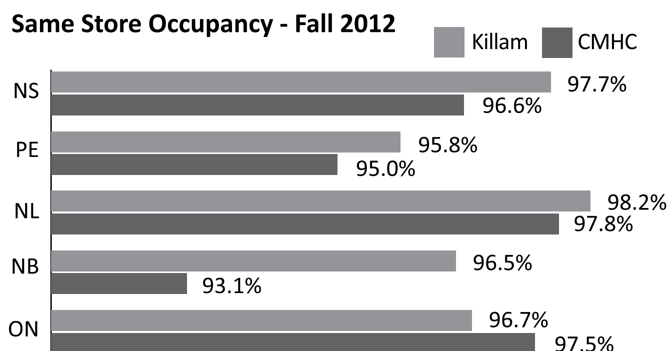
Killam's Solid Infrastructure Supports Geographic Expansion

Killam's operational platform can support a larger and more geographically diverse portfolio. In addition to its head office in Halifax, Killam has regional offices in Saint John, Fredericton, Moncton, Charlottetown and Cambridge. Property management is handled internally for all apartment locations, with the exception of Newfoundland, where properties are managed by an arm's length, third-party management firm.

Management continues to see opportunities to acquire apartment properties in Atlantic Canada, as well as expanding ownership in the Ontario market. During 2012, 7.5% of Killam's consolidated NOI from apartment rental operations was generated outside Atlantic Canada as the Company continued to invest in the Ontario market. Management expects to further increase this percentage by continuing to acquire apartments in Ottawa, the Greater Toronto Area ("GTA"), and South Western Ontario. Further comments on plans to increase the Company's investment outside Atlantic Canada are provided in the strategy section of the MD&A.

Increasing the Value of the Apartment Portfolio through NOI Growth

To achieve NOI growth, Killam must address three critical factors; occupancy, rental rates, and operating costs. Killam has been able to show growth despite pressure on operating costs (approximately 60% of operating costs are related to heating, water, and realty taxes) and occupancy. In fact, in 2012, strong revenue growth was achieved, despite the pressure on occupancy, with Killam beating CMHC occupancy statistics in its core Atlantic Canadian markets.



Source: CMHC 2012 Fall Rental Market Report

Regarding operating costs, Killam has made investments to convert its heating systems to natural gas where possible to lessen the impact of volatile oil prices and has also implemented water saving measures to control this cost. This work is paying off and today Killam heats 92% of its portfolio with heating systems other than oil and has decreased water usage at properties where water refits are complete.

Limited Exposure to Rent Control

Killam is generally able to move rents to market on an annual basis. PEI is the one province in Atlantic Canada with rent control for apartments, and this represents only 6.4% of Killam's apartment units. The Company analyzes each property on a regular basis, considering its location, tenant base and vacancy, to evaluate the ability to increase rents for both existing tenants and on turnover. The ability to increase revenue is important in generating NOI growth. Over the last three years, Killam has increased rents by an average of 2.2%, 2.8% and 3.6% in 2010, 2011 and 2012, respectively.

Managing Costs

Management is able to directly control approximately 40% of operating expenses, including labour costs, repairs and maintenance and property general and administrative expenses. The remaining operating costs, including utilities and property taxes, are less controllable. Utility and fuel costs represented approximately 30% of Killam's apartment operating costs in 2012. Killam's apartments are currently heated with a combination of natural gas, electricity and oil. Heating costs for electrically heated units are generally paid by the tenant directly. Volatile oil and natural gas prices have an impact on Killam's ability to control these expenses. To mitigate this volatility, the Company is active in energy conservation initiatives, natural gas conversions in Halifax and New Brunswick and monitoring its energy usage.

CMHC Insured Debt Available

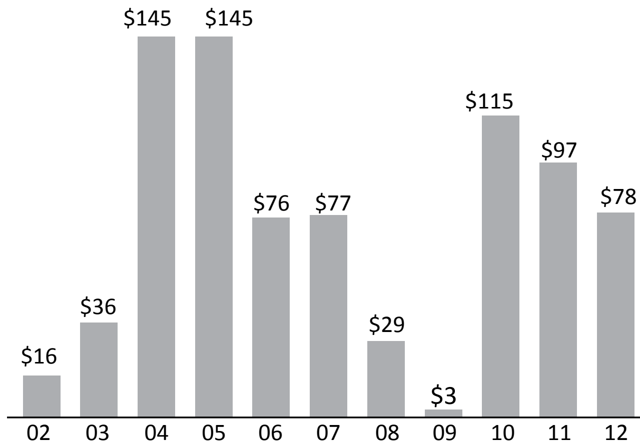
Killam's apartments and MHCs are financed with mortgages. At the time of acquisition, mortgage debt typically represents between 65% and 75% of the value of the asset. The mortgage term on the debt varies, but typically has been a five-year term. Over the last two years, Killam has increased the amount of 10-year debt, taking advantage of the low interest rate environment.

Canadian apartment owners can apply for CMHC mortgage loan insurance. The mortgage insurance guarantees the repayment of the loan to the lender, eliminating default risk to the lender which results in lower interest rates for the borrower than with conventional mortgages. Killam has utilized CMHC insurance and has 61.0% of its apartments financed with CMHC insured debt. As mortgages are renewed or new properties are financed, Killam will use CMHC insurance and increase the percentage of insured debt. CMHC insurance is not available for the owners of MHCs, however, it is available for the individual home owners.

Portfolio Growth through Acquisitions

Killam has been an active consolidator in Canada for the last 10 years. The graph below summarizes the total invested in apartment acquisitions since Killam's first acquisition in 2002.

Apartment Acquisition History
($ millions)



Portfolio Growth through Development

Demand for newly constructed rental apartments is strong in Atlantic Canada, with high occupancy rates and above average rents. CMHC's Fall 2012 Halifax Rental Market Report reported 98.7% occupancy for properties built in 2000 or later, compared to 97.0% for all rental markets in the city. The average rent for a two-bedroom unit in these newer buildings was $1,266 per month, compared to an average two-bedroom rent of $954. Killam's apartment portfolio includes buildings of newer construction, with approximately 20% of Killam's apartment units built in 2000 or later. These properties have high occupancy and lower than average capital requirements.

Management believes that developing new rental properties will enable the Company to increase its percentage of newer product at more advantageous pricing than relying solely on the acquisition of new product. Direct involvement in the development also gives Killam control of decision making, planning, and the quality and features of the buildings.

Killam completed its first development in 2011. The Company has four new developments, with a total estimated cost of $63.1 million, representing approximately 4% of Killam's total asset base. One project was completed in February 2013 and the remaining projects are expected to be completed in the first half of 2013. Please see page 29 of the MD&A for further discussion on the development projects.

Business Overview - Manufactured Home Communities

Offering Diversification and Stability to the Apartment Portfolio

In addition to acquiring apartments, Killam has built a portfolio of MHCs. Killam acquired its first community in 2003, and as at December 31, 2012, owned 44 communities across four provinces, with a total of 7,407 rentable sites.

The following table summarizes Killam's MHC investment by province as at December 31, 2012:

	Sites	Number of Communities	% of MHC NOI
Nova Scotia	2,561	15	31.5%
New Brunswick	2,532	11	31.7%
Ontario	2,144	16	34.9%
Newfoundland	170	2	1.9%
Total	7,407	44	100.0%

How the MHC Business Works

With MHCs, Killam owns the land and infrastructure supporting each community and leases the sites to the tenants, who own their own homes and pay Killam a monthly rent. In addition to site rent, the tenant may have a mortgage payment to a financial institution for their home. The average rent in Killam's MHC portfolio is $224/month, which offers value and affordability to tenants. The home owner is responsible for property taxes based on the assessed value of their home and Killam is responsible for the property tax on the land.

MHCs require less recurring capital investment and deliver a more predictable and stable cash flow than apartments. MHC home owners are responsible for the repair, maintenance and operating costs of their homes, which removes significant variable costs that are typically borne by Killam for apartments. The operating profit margin in Killam's MHC business averaged 63.9% over the last two years, compared to 59.6% for apartments.

The most significant costs to operate MHCs are water, land property tax and general repairs and maintenance to the water and sewer infrastructure. Killam's experience with MHCs has shown that the largest variable expenses are costs related to the water and sewer infrastructure. The majority of other costs have little variability.

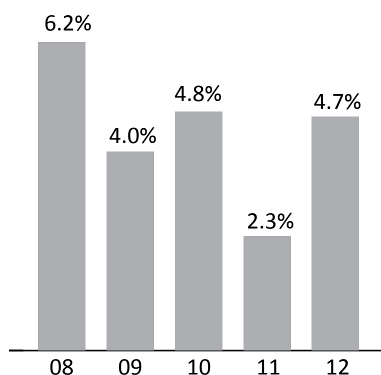
Killam's MHCs enjoy a stable tenant base, with consistently strong occupancy of approximately 98%. Should a tenant choose to leave a community, they sell their home, with the home typically remaining on the site and rent collection continuing uninterrupted from the new homeowner, who Killam approves as part of the sale process.

Increasing the Value of the MHC Portfolio through NOI Growth

As with apartments, Management is focused on improving the performance of the current MHC portfolio through annual rental increases, expansion opportunities, and managing expenses. Improving the profitability of the portfolio will lead to higher valuations for the properties in a stable Cap-Rate environment.

Management measures success in improving profitability through same store NOI growth. MHCs have little exposure to energy costs, resulting in stable operating costs, even in an environment of volatile natural gas and oil prices. Same store NOI growth for MHCs over the last five years is shown below.

MHC Same Store NOI Growth



More Exposure to Rent Control for MHCs

Ontario and Nova Scotia both have rent control for MHCs. In all other provinces where Killam owns MHCs, Management can increase rents to market. Rent control for MHCs in Nova Scotia was introduced in 2012 and the allowable rental increase was set at 3.0% for 2013. The allowable rent increase for renewing MHC tenants in Ontario in 2012 was 3.1%, which is the same as the allowable rental increase for apartments. The allowable rent increase in Ontario for 2013 is 2.5%. In both Ontario and Nova Scotia, owners may apply for above-guideline increases to offset significant capital expenditures. Higher rent increases are also allowed for new tenants entering the communities.

Expansion Opportunities for MHCs

Killam began MHC expansions at some of its communities in 2007 and since then has developed an additional 249 sites in eight communities and has sold 189 homes into those expansions. Future expansion potential has been identified at 9 of the Company's MHCs, totaling up to 583 new site developments. Killam expects to develop new sites as demand for new homes in the communities supports expansion costs.

Home Sales

Killam acts as a retailer for home manufacturers to supply homes to Killam's communities, both at existing and expanded sites. The houses are built in a manufacturing facility and delivered by road to the sites. Homes are available in a variety of sizes and layouts and typically sell for between $90 thousand and $185 thousand, with the higher sales prices usually in Ontario. Management expects to net $12 thousand to $20 thousand profit per home sale, which, as noted earlier, offsets a portion of the capital investment to expand the new sites. Annual new home sale levels are dependent on Killam's site expansion program and the overall economic environment.

Business Strategy

Killam's overall business objectives are:

1. To own a high-quality, geographically diverse multi-family apartment and MHC portfolio in Canada.
2. To generate annual increases in FFO per share, and
3. To increase the underlying net asset value of its investment properties.

Consolidation of the Multi-family Residential Real Estate Market

Management plans to continue to grow the apartment portfolio through accretive acquisitions, with an increased focus in Ottawa, the GTA and South Western Ontario. During 2012, Killam completed $84.8 million in acquisitions, including newly constructed buildings in Ottawa and Halifax. Killam's acquisition goal for 2013 is $75 - $125 million.

Increased Investment in New Properties

The average age of Killam's apartments is 31 years, which is relatively young compared to the apartment market in Canada. Our experience has shown that the amount of capital spent on a property is strongly correlated to its age. Generally, the amount of annual capital to maintain a property increases as the building ages.

In addition to the capital requirements, experience in our core markets has highlighted that demand is strong for new properties, and renters are willing to pay a premium for modern properties. The new properties added to our portfolio are condo quality, providing tenants with features and amenities traditionally associated with ownership. We believe that demand for this type of rental accommodation will grow given an increasing number of homeowners reaching retirement age and looking for alternatives to home ownership.

With strong demand for acquisition of apartments over the last three years, Cap-Rates have declined, and the pricing differential between older and newer buildings has reduced. This enables Killam to increase the amount of newer apartments in its portfolio without paying a significant premium for quality assets. In addition to purchasing more new properties, Killam's development program will also increase the number of new properties over time.

Management believes that increasing Killam's ownership in new, high-quality buildings will result in above-market and long-term demand for the Company's assets from an aging population, reduce annual capital requirements for deferred maintenance, and transform Killam's portfolio, over time, into one of the highest quality portfolios in Canada. The Company will continue to own older properties, knowing that older properties that are well located and well maintained can also perform well over the long-term.

Geographic Diversification

Geographic diversification in the apartment segment is a priority for Killam. With a 13% market share in its core markets in Atlantic Canada, Killam is the region's largest residential landlord. The maximum market share Management foresees Killam reaching in Atlantic Canada is between 15%-18%. With Atlantic Canada representing only 4.9% of the Canadian rental market, Killam's growth opportunities increase significantly when considering assets outside Atlantic Canada.

With its strong operating platform, Killam can support a larger and more geographically diverse portfolio. The Company is now building a portfolio in key markets in the Greater Toronto Area, and the South Western Ontario. The Ontario market is core to the Canadian rental market, with 36% of the Canadian rental universe.

To accelerate its entrance into the Ontario rental market, Killam formed a partnership with KFH in 2010 with the objective of acquiring multi-family residential properties in Ontario. Under the partnership, the partners may contribute equity up to $100 million, with 75% of the equity from KFH and 25% from Killam, to purchase up to $250 million in apartments. Killam manages all properties purchased in the partnership. The partnership agreement gives Killam the opportunity to acquire larger properties than it would otherwise without a partner. The term of the partnership agreement is 5 years, plus the option of two one-year extensions. At the end of the term, KFH is expected to exit the investment, providing Killam the option to acquire 100% of the asset or share in sale proceeds. The partnership now holds three properties, with total acquisition costs of $111.8 million. The buildings held through the partnership are located in Ottawa, Mississauga and London.

Management has set a target to have 50% of its NOI generated outside of Atlantic Canada by 2015-2016. During 2012, following the sale of 12 MHCs in Ontario and Western Canada, the percentage of NOI and equity income generated outside of Atlantic Canada was reduced by approximately 3% to 14%. The overall percentage of NOI generated outside of Atlantic Canada is expected to grow as additional acquisitions are completed in Ontario.

Growth in Same Store NOI

Killam is focused on improving the performance of its current portfolio through annual increases to rents, stability of occupancy and expense management. Improving the profitability of the portfolio is expected to lead to higher valuations for the assets in a stable Cap-Rate environment. The Company expects same store NOI growth between 2% and 4% annually.

Performance Compared to 2012 Key Objectives

Consolidation of Multi-family Residential Real Estate Market	
2012 Target	Complete approximately $100 million in acquisitions.
2012 Performance	Killam's acquisitions totaled $84.8 million in 2012 as follows: - $78.0 million in apartment acquisitions (including $19.4 million accounted for as equity investments). - $6.8 million for the acquisition of land for future development.
Increase Investment in New Properties	
2012 Target	Acquire new properties as part of the acquisition program in 2012. Continue with Killam's four developments, on schedule and on budget.
2012 Performance	Killam acquired two new buildings in 2012, Chapter House, which was built in 2004 and the Kanata Lakes Apartments which was completed in 2012. Killam's four development projects have progressed on schedule throughout 2012. Brighton House was completed in early February 2013 and the remaining projects are all expected to be completed by April and May 2013. The total cost of development increased from original budgets by 6%, the result of higher than expected pricing for trades and suite enhancements.
Geographic Diversification	
2012 Target	2012 acquisition program to include investments in Ontario.
2012 Performance	The Company acquired a four-building, 244-unit portfolio of apartments in Ottawa, as well as a 146-unit property in Ottawa and a 199-unit property in Mississauga, through its joint venture.

Growth in Same Store Net Operating Income	
2012 Target	Same Store NOI growth of 2% to 4%.
2012 Performance	The Company achieved consolidated same store NOI growth of 2.0% for 2012.
Maximize the Value of Excess Land	
2012 Target	Complete 30 to 40 home sales and gain approval for additional developments on excess land. Following the sale of 12 MHCs during the second quarter, Killam adjusted its home sale target for 2012 to between 25 and 30 homes.
2012 Performance	Completed 26 sales, including 18 home sales and 8 home placements in 2012.

2013 Targets

Consolidation of Multi-family Residential Real Estate Market	Complete $75-$125 million in acquisitions.
Increase Investment in New Properties	Acquire new properties as part of the acquisition program in 2013. Complete and lease-up Killam's four developments, and commence two new development projects.
Geographic Diversification	2013 acquisition program to include investments in Ontario.
Growth in Same Store Net Operating Income	Same Store NOI growth of 2% to 4%.

2013 Outlook

Competitive Acquisition Environment

With continued low interest rates, access to CMHC insured financing for apartments and strong demand for yield, we expect to see the competitive acquisition environment continue for 2013. Throughout 2013, the Company will continue to seek new buildings and focus on the Ontario market to build its geographic diversification.

Low Interest Rates

The low interest rate environment enables Killam to renew its maturing debt at lower interest rates, and makes 10-year term mortgages more attractive. Killam has $85.2 million of mortgage debt maturing in 2013, having a weighted average interest rate of 4.36% on apartment debt and 6.24% on MHC debt. With interest rates expected to stay low in 2013, Killam expects to refinance its apartment debt at between 3.0% and 3.5% and MHC debt at between 5.0% and 5.5%.

High Levels of Multi-Family Construction May Impact Vacancy

Killam experienced a decrease in occupancy in 2012, partially attributable to increased rental supply in Halifax and Moncton. In Halifax, new construction may place upward pressure on the vacancy rate. However, population growth in Halifax will gain significant momentum in 2014/2015 as the $25 Billion shipbuilding program ramps up.

High Natural Gas Prices in Nova Scotia and New Brunswick

A short-term decrease in the natural gas supply off the coast of Nova Scotia has resulted in a temporary spike in natural gas costs in Atlantic Canada. Prices approximately doubled year-over-year in December 2012 and have remained high during the first quarter of 2013. The cost of gas in Nova Scotia, excluding delivery charges, averaged $10.40 per GJ in January and February 2013, compared to $5.08 per GJ in January and February, 2012. A similar trend has been seen in New Brunswick. The unusual spike in prices reflects a decline in production from the offshore Sable Island gas field, the relatively high cost of gas in neighbouring New England markets, and a delay in production from Encana's Deep Panuke project off Nova Scotia's coast. Prices are expected to come down once production levels increase in the spring of 2013.

Development Projects

Killam expects to see positive NOI and FFO earnings from its development projects in 2013. Brighton House was completed during the month of February, 2013 and is 53% leased. The remaining developments are expected to be ready for occupancy during April and May 2013. The new buildings should experience lower operating expenses as a result of the quality construction and LEED features.

PART III

2012 Financial Overview

Property Revenue

For the years ended December 31,

	2012	2011	% Change
Same store revenue	**$ 112,466**	$ 110,404	1.9%
Other properties	**21,175**	15,685	35.0%
Total operating revenues	**$ 133,641**	$ 126,089	6.0%

Same store property revenue reflects the 164 stabilized properties that Killam has owned for equivalent periods in 2012 and 2011. The same store analysis includes 16,850 units, or 89% of Killam's portfolio. Home sales are excluded from the analysis. Other properties revenue includes properties acquired in 2012 and 2011, developments, MHC properties which were sold during Q2-12 and other non-stabilized properties. Details of properties acquired in 2012 are found on page 28.

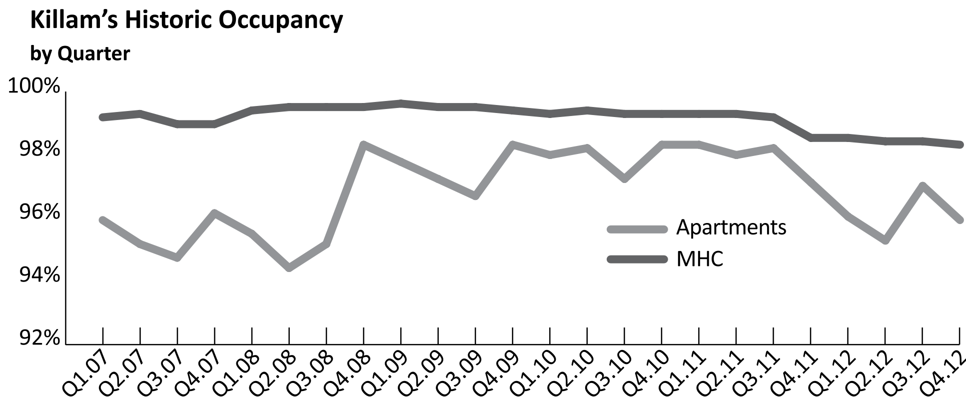
Total property operating revenue, excluding the properties held through its joint venture, is $133.6 million. The 6.0% revenue increase from 2011 was generated though acquisitions and increased rental rates, partially offset by an increase in vacancy. Killam, like all real estate rental operators, is sensitive to vacancy rates, however, Killam believes its portfolio is quite defensive given its geographic diversification and two distinct asset types, apartments and MHCs. Based on current rents, an annualized 1% change in apartment vacancy rates would impact the annualized rental revenue by $1.1 million.

Occupancy by Core Market

Apartments

	December 31, 2012			December 31, 2011		
	Units	**Occupancy (1)**	**Average Rent**	Units	Occupancy (1)	Average Rent
Halifax, NS	**4,822**	**96.6%**	**$ 889**	4,410	97.3%	$ 856
Moncton, NB	**1,424**	**96.3%**	**800**	1,426	94.1%	779
Fredericton,NB	**1,293**	**97.8%**	**846**	1,293	97.9%	822
Saint John, NB	**1,143**	**93.6%**	**747**	1,143	97.0%	725
St. John's, NL	**742**	**97.8%**	**776**	742	98.7%	726
Charlottetown, PE	**687**	**91.6%**	**871**	687	98.3%	847
Ontario	**1,078**	**93.1%**	**1,331**	489	96.7%	1,489
Other Atlantic	**431**	**96.1%**	**776**	448	94.9%	752
Total apartments	**11,620**	**95.9%**	**$ 888**	10,638	97.0%	$ 843
MHCs	**7,407**	**98.1%**	**$ 224**	9,441	98.3%	$ 237
Total portfolio	**19,027**	**96.6%**		20,079	97.6%	

(1) Occupancy of stabilized properties



As highlighted in the table and chart above, Killam's apartment occupancy levels declined in 2012 from highs maintained throughout much of 2010 and 2011, ending the year with 95.9% occupancy, compared to 97.0% at December 31, 2011. Despite the decline, Killam was successful in implementing rent increases across the portfolio and achieving same store revenue growth of 1.5% in 2012 by implementing average rent increases of 3.6%.

CMHC has reported increased vacancy levels in certain markets in Atlantic Canada following the introduction of higher than normal levels of new rental supply, specifically in Halifax, Moncton and Charlottetown. Softness in the Saint John, New Brunswick economy has resulted in decreased rental demand in that market. Offsetting these negative trends, is continued strong demand for rental product in St. John's, Newfoundland, a stable rental market in Fredericton, and an overall aging population with an increased tendency to rent. Killam is strengthening its position in the tighter rental market with new marketing initiatives, rental incentives where required, and a continued focus on best-in-class service. Killam measures its performance against CMHC vacancy statistics, and out-performed the market in each of its core cities in Atlantic Canada when measured against CMHC's Fall 2012 Market Rental Reports, as shown on Page 7.

Halifax, Killam's most significant market, ended the year at 96.6% occupancy. Halifax has seen an increase in new rental supply in recent months, with rental construction levels above the 10 year annual average of approximately 800 units per year. This new supply, along with other construction projects anticipated to come to market in 2013, is expected to lead to continued competitive market conditions in the short-term. Looking to 2014 and beyond, an increase in population growth, fueled in part by the start of the $25 billion, 25-year, Irving Shipbuilding Contract, is predicted to increase demand for rental product, absorbing the new supply.

In New Brunswick, Fredericton outperformed Moncton and Saint John in 2012, and a similar story is expected in 2013. Killam made occupancy gains in Moncton during the second half of 2012 and ended the year with 96.3% occupancy. Rental incentives and increased capital investment in unit renovations have contributed to gains in Moncton. Saint John, representing 7.0% of Killam's apartment NOI, has experienced softness over the last two years, as economic growth in the City has slowed following the completion of investments in energy projects in the market. Killam has responded to the slow-down in demand by increasing marketing and rental incentives, where required.

Following three years of near-full occupancy, Killam's Charlottetown portfolio has experienced a recent increase in vacancy, impacted by new supply introduced in the market, and a slowdown in the number of international immigrants coming to Charlottetown as part of PEI's Provincial Nominee Program. Despite a decline in occupancy, Killam's new development in Charlottetown, Brighton House, is leasing up quickly, with 53% of units leased for April 2013.

St. John's, Newfoundland remains Killam's strongest market, with the Company's apartment portfolio 97.8% occupied at December 2012, and average same store rental rates up 7.4% year-over-year. Killam remains optimistic about the long-term NOI growth opportunities in the St. John's market, where, despite above average rental rate growth over the last four years, monthly rents remain affordable, averaging $776 per month.

Killam's occupancy was down in Ontario year-over-year due primarily to Killam's growing portfolio. The Company is stabilizing a portfolio of older properties acquired in Q3 2012 in Ottawa and experienced a short-term rise in vacancy in Cambridge. Killam's London and Mississauga assets were near full occupancy at year-end, and the lease-up on the newly developed properties in both Ottawa and London has been very strong.

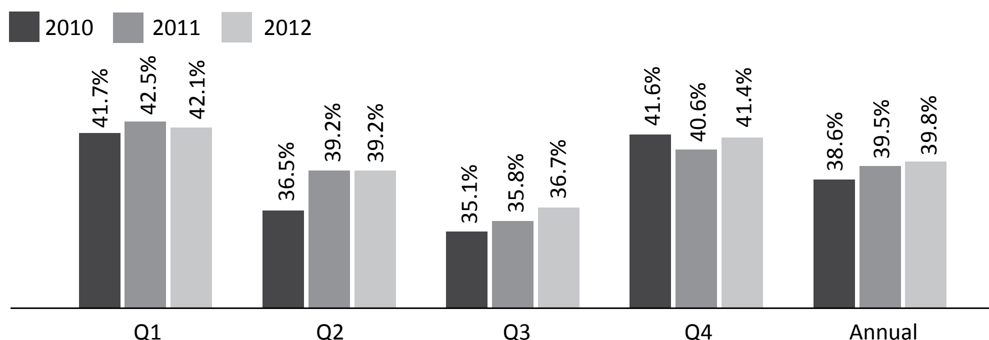
Property Operating Expenses

For the years ended December 31,

	2012	2011	% Change
Same store properties	**$45,366**	$44,644	1.6%
Other properties	**7,831**	5,093	53.8%
	$53,197	$49,737	1.6%

Total Property Operating Expense

As a Percentage of Property Revenue



Killam's property operating expenses as a percentage of operating revenues for 2012 increased 30 bps to 39.8% from 39.5% in 2011. The increase can be attributed to higher property tax expense and operating costs partially mitigated by rental increases. These variances are discussed in more detail in the same-store results sections of the MD&A.

Consolidated Same Store Results[1]

For the years ended December 31,

		2012		2011	% Change
Property revenue		**$ 112,466**		$110,404	1.9%
Property expenses					
Operating expenses	17.3%	**19,503**	17.4%	19,164	1.8%
Utility and fuel expenses	12.2%	**13,734**	12.4%	13,705	0.2%
Property taxes	10.8%	**12,129**	10.7%	11,775	3.0%
Total property expenses	40.3%	**45,366**	40.5%	44,644	1.6%
Net operating income		**$ 67,100**		$ 65,760	2.0%

(1) Same store results reflect the operations for 164 stabilized properties that Killam has owned for equivalent period in 2012 and 2011. The same store analysis includes 16,850 units (89%) of Killam 's portfolio (based on unit count). Home sales are excluded from this analysis.

Same store property NOI increased 2.0% year-over-year. Total revenues increased 1.9% as a result of the positive impact of rental increases of $3.9 million (3.6% increase in rental rates) offset by increased vacancy of $1.8 million (100 bps increase in vacancy rates). Total property operating expenses increased 1.6%, which was driven by a 3.0% increase in property taxes as a result of higher assessments in 2012 and a 1.8% increase in operating expenses, partially offset by relatively flat net utility and fuel costs. Property operating expenses include salaries and benefits, repairs and maintenance, contract services, insurance, property administration and advertising expenses. The increase year-over-year can be attributed to higher repairs and maintenance costs, which includes painting costs, to prepare units for leasing.

Segment & Same Store Review

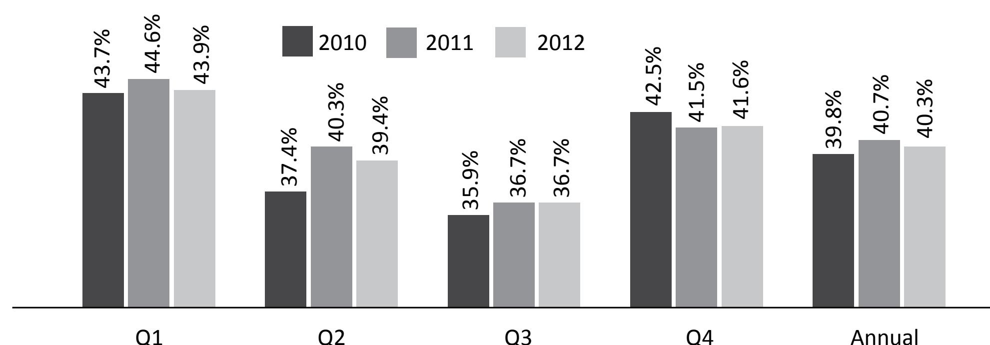
Apartment Segment

For the years ended December 31,

		2012		2011	% Change
Property revenue		**$110,464**		$100,301	10.1%
Property expenses					
Operating expenses	16.0%	**17,655**	16.1%	16,101	9.7%
Utility and fuel expenses	12.2%	**13,463**	12.7%	12,703	6.0%
Property taxes	12.1%	**13,392**	11.9%	11,887	12.7%
Total property expenses	40.3%	**44,510**	40.7%	40,691	9.4%
Net operating income		**$ 65,954**		$ 59,610	10.6%

Apartments Operating Expense

As a Percentage of Property Revenue



Killam's apartment business accounted for 82% of income from property operations for the year ended December 31, 2012, compared to 78% in 2011. The apartment portfolio generated total revenue growth of 10.1% in 2012 compared to 2011. The increase is attributed to increased rental revenue for the same store assets and revenues from acquisitions completed in 2011 and 2012.

Total property expenses were 40 basis points lower in 2012 compared to 2011, as a percentage of total property revenue. A more detailed analysis of property expenses is presented in the same store results, which follow.

Apartments - Same Store Results

For the years ended December 31,

		2012		2011	% Change
Property revenue		**$ 93,488**		$ 92,074	1.5%
Property expenses					
Operating expenses	16.0%	**15,241**	16.2%	14,875	2.5%
Utility and fuel expenses	12.0%	**11,858**	13.0%	11,954	(0.8)%
Property taxes	12.0%	**11,187**	11.8%	10,850	3.1%
Total property expenses	40.0%	**38,286**	41.0%	37,679	1.6%
Net operating income		**$ 55,202**		$ 54,395	1.5%
Weighted average rent per unit		**$ 855**		$ 832	2.8%

Apartment Same Store NOI by City

For the years ended December 31,

	2012	2011	$ Change	% Change
Halifax	**$ 26,447**	$ 25,470	$ 977	3.8%
Moncton	**5,159**	5,157	2	- %
Fredericton	**4,656**	4,733	(77)	(1.6)%
Saint John	**4,617**	4,872	(255)	(5.2)%
Ontario	**4,276**	4,198	78	1.9%
St. John's	**4,087**	3,773	314	8.3%
Charlottetown	**3,700**	3,821	(121)	(3.2)%
Other Atlantic locations	**2,260**	2,371	(111)	(4.7)%
	$ 55,202	$ 54,395	$ 807	1.5%

Revenue growth of 1.5% year-over-year was primarily attributable to increased average rents of 3.6%, partially offset by an increase in vacancy, as discussed on page 15.

Killam's apartment same store utility and fuel costs decreased year-over-year as a result of the Company's recent natural gas conversions in Halifax and a weighted average decrease in natural gas prices in 2012, even including the spike in pricing in December. The breakdown of the utility and fuel expenses in 2012 compared to 2011 are as follows:

Utility and Fuel Expense

For the years ended December 31,

	2012	2011	% Change
Natural gas	**$ 2,546**	$ 2,310	10.2%
Oil	**1,985**	2,919	(32.0)%
Electricity	**4,223**	3,807	10.9%
Water	**3,076**	2,885	6.6%
Other	**28**	33	(15.2)%
Total utility and fuel expenses	**$ 11,858**	$ 11,954	(0.8)%

Natural gas and oil costs represented 23% of total utility and fuel costs in 2012, and 6% of total property operating expenses. Killam's apartment properties are heated with a combination of natural gas (55%), electricity (36%), oil (8%) and other sources (1%).

Killam benefited from recent natural gas conversions in 2012, reflected in lower total oil and natural gas costs than 2011. The average cost of oil in 2012 was $0.87 per litre, compared to an average per litre equivalent of $0.32 for gas in Nova Scotia and $0.63 for gas in New Brunswick, highlighting the incentive for conversion.

Killam's weighted average cost of natural gas, on a per GJ basis, decreased approximately 6.3% in 2012, compared to 2011 pricing. The savings where highest in New Brunswick, where rates decreased 10.7% in the year, compared to Nova Scotia, where rates decreased 3.2%. The savings in New Brunswick were due primarily to a change in Enbridge Gas New Brunswick's pricing system introduced in October 2012. Killam benefited from a reallocation of rate classes, and a decrease in the delivery charges.

The positive impact of these delivery cost savings is expected to be more than offset by high natural gas costs in both Nova Scotia and New Brunswick during the first half of 2013 due to a decline in gas supply off the coast of Nova Scotia and high prices in New England.

Although not as significant a variable as it was two years ago, Killam continues to be exposed to fluctuations in the cost of heating oil, the weighted average cost of which increased by 7.0% in 2012 compared to 2011.

Killam's electricity costs increased by 10.9% in 2012 compared to 2011 due to higher electrical rates and Killam's decision to offer electricity included in monthly rents in some markets as a rental incentive to remain competitive with market incentives.

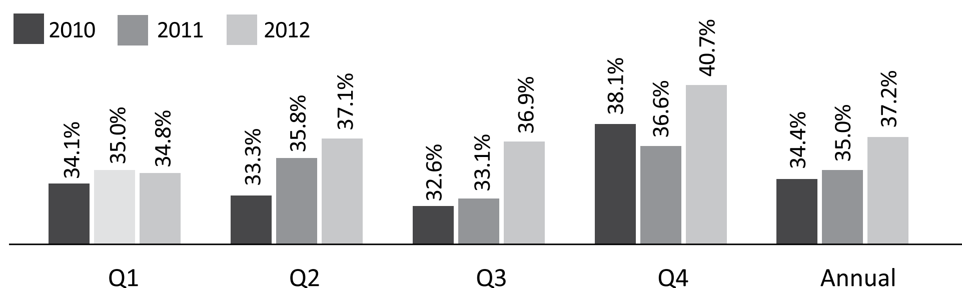
Water charges increased 6.6% year-over-year, mostly due to an 11.7% increase in Halifax Water Commission rates effective June 25, 2012. During suite renovations in both 2012 and 2011, Killam upgraded showers and toilets in many of its building to reduce water consumption to mitigate rising water rates.

Killam continues to maximize its energy efficiency programs to lessen its carbon footprint and mitigate pressure from rising utility prices.

MHC Segment

For the years ended December 31,

		2012		2011	% Change
Property revenue		**$ 22,653**		$ 25,709	(11.9)%
Property expenses					
Operating expenses	21.7%	**4,921**	20.9%	5,384	(8.6)%
Utility and fuel expenses	10.7%	**2,418**	9.5%	2,435	(0.7)%
Property taxes	4.8%	**1,082**	4.6%	1,185	(8.7)%
Total property expenses	37.2%	**8,421**	35.0%	9,004	(6.5)%
Net operating income		**$ 14,232**		$ 16,705	(14.8)%



Killam's MHC business accounted for 18% of earnings from property operations during 2012 compared to 22.0% in 2011. Revenue from the MHCs decreased by $3.1 million, down 11.9% compared to 2011 due to the sale of twelve MHC properties in May 2012. The impact of the sale was partially offset by increased revenue at same store properties and an MHC acquisition completed in December 2011. Expenses as a percentage of property revenue increased by 220 basis points in 2012 compared to 2011 as the MHC portfolio sold in May 2012 included higher margin properties. For a more detailed analysis please see the MHC Same Store section below.

Same Store Results - MHCs

For the years ended December 31,

		2012		2011	% Change
Property revenue		**$ 18,978**		$ 18,330	3.5%
Property expenses					
Operating expenses	22.5%	**4,263**	23.4%	4,289	(0.6)%
Utility and fuel expenses	9.9%	**1,875**	9.6%	1,751	7.1%
Property taxes	5.0%	**942**	5.0%	925	1.8%
Total property expenses	37.4%	**7,080**	38.0%	6,965	1.7%
Net operating income		**$ 11,898**		$ 11,365	4.7%
Weighted average rent per unit		**$ 223**		$ 215	3.7%

Same store property revenue increased 3.5% in 2012 compared to 2011 as a result of an increase of 3.7% in the weighted average rent per unit. Total same store property expenses increased 1.7% year-over-year as a result of a reduction in operating expenses offset by an increase of 7.1% in utility and fuel expenses, which is mostly driven by increased water rates and consumption.

PART IV

Other Income

Home Sales

For the years ended December 31,

	2012	2011	%Change
Home sale revenue	**$ 2,241**	$ 4,229	(47.0)%
Cost of home sales	**(1,789)**	(3,705)	(51.7)%
New home placement fees	**98**	560	75.0%
Operating expenses	**(81)**	(94)	(13.8)%
Income from home sales	**$ 469**	$ 486	(3.5)%

Killam completed 18 home sale and 8 home sale placements during 2012, compared to 38 home sales and 7 home sale placement in 2011. The decreased number of home sales in 2012 was as a result of the immediate need for housing following the forest fires in Slave Lake Alberta, which accounted for 11 of 38 sales in 2011. The sale by Killam of 12 MHCs in May 2012 also decreased the opportunity for home sales.

Home sale operating expenses include all costs associated with marketing homes, including open houses, advertising costs, etc.

Equity Income

Equity income represents Killam's 25% interest in the net income of the joint ventures that own 180 Mill Street, Kanata Lakes and Silver Spear apartments, all of which are located in Ontario. A summary of the performance of the three properties is included below. The properties were originally acquired without debt, however, mortgages were placed on all three properties during 2012. The timing of the placement of the mortgages resulted in lower than normal annual interest expense compared to the remainder of Killam's real estate portfolio.

For the years ended December 31,

	2012	2011	% Change
Property revenue	**$ 6,708**	$ 52	128.0%
Property operating expenses	**(2,936)**	(1)	N/A
Net operating income	**3,772**	51	73.0%
Interest and deferred financing expense	**(857)**	-	N/A
Fair value gains	**120**	-	N/A
Net income	**3,035**	51	58.5%
Killam's 25% interest	**$ 758**	$ 13	57.3%

Corporate Income

For the years ended December 31,

	2012	2011	% Change
Property management fees	**$ 363**	$ 81	348.1%
Interest and other revenue	**599**	13	N/A
	$ 962	$ 94	923.4%

Corporate income includes property management fees, interest on bank accounts, and transaction fees related to the joint venture partnership. The increase in Corporate income year-over-year is related to an increase in property management fees of $0.3 million plus $0.2 million in transaction fees earned related to the joint venture acquisitions in 2012. Interest and other revenue is higher in 2012 compared to 2011 due to $0.4 million in expense related to the remediation of an oil spill at one of the Company's MHC's in Ontario being netted against interest and other revenue expenses in the 2011. This lawsuit is still ongoing and any proceeds from the lawsuit will be recorded in other revenue when received.

Fair Value Gains

For the years ended December 31,

	2012	2011	% Change
Apartments	**$ 31,593**	$ 42,968	(26.5)%
MHCs	**6,133**	9,102	(32.6)%
	$ 37,726	$ 52,070	(27.6)%

The effective weighted average Cap-Rate used to value the apartment properties decreased by 17 basis points to 6.02% year-over-year, reflecting an increased valuation for some properties.

The effective weighted average Cap-Rate used to value the MHCs decreased year-over-year by 24 basis points as a result of Cap-Rate compression in the fourth quarter of 2012. See further discussion on Cap-Rates in the "Investment Properties" section of the MD&A.

Other Expenses

Financing Costs

For the years ended December 31,

	2012	2011	% Change
Mortgage and loan interest	**$ 28,590**	$ 29,038	(1.5)%
Amortization on fair value adjustments on assumed debt	**(229)**	-	N/A
Convertible debenture interest	**6,632**	5,357	23.8%
Subordinated debenture interest	**703**	688	2.2%
Capitalized interest	**(1,063)**	(192)	453.6%
	$ 34,633	$ 34,891	(0.7)%

Mortgage and loan interest expense was lower during 2012, on a gross dollar basis, compared to 2011, due to the disposal of twelve MHC properties during the second quarter of 2012 and refinancings which occurred during the past twelve months at lower interest rates. These savings were partially offset by interest costs related to mortgages on new acquisitions.

Mortgage and loan interest expense on Killam's same store properties was $23.9 million in 2012, down from $25.0 million in 2011. As a percentage of property revenue, same store mortgage and loan interest expense was lower during 2012, at 21.3%, compared to 22.9% in 2011.

Killam manages interest rate risk by entering into fixed-rate mortgages and staggering the maturity dates of its mortgages. An annualized 1% change in the interest rate on Killam's mortgage and vendor debt at December 31, 2012 would affect financing costs by approximately $6.3 million per year. However, only $88.8 million of Killam's mortgage and vendor debt matures in the next twelve months and that same interest rate change would impact Killam by only $0.8 million per annum. The Company's credit facility is discussed on page 35 of the MD&A.

Convertible debenture interest was higher in 2012 compared to 2011 as the Company issued $46.0 million convertible debentures bearing interest at a rate of 5.45% on June 2, 2011 resulting a full year of related interest expense in 2012.

Capitalized interest increased year-over-year as a result of the interest costs associated with the development properties. Interest costs associated with the general corporate borrowings used to fund development have been capitalized to the respective developments throughout 2012 using the Company's weighted-average borrowing rate of 4.50% annualized.

Depreciation Expense

For the years ended December 31,

	2012	2011	% Change
	$ 540	$ 301	79.4%

Depreciation expense relates to the Company's head office building, vehicles, heavy equipment and administrative office furniture, fixtures and computer equipment. These assets do not form part of the Company's investment properties. Although the vehicles and equipment are used at various properties they are not considered part of investment properties and are depreciated for accounting purposes. The increase year-over-year is a result of the Company's acquisition of a 50% interest in its head office building in November 2011, offset by the sale of the MHC properties in the second quarter of 2012.

Amortization of Deferred Financing Costs

For the years ended December 31,

	2012	2011	% Change
	$ 1,605	$ 1,410	13.8%

Deferred financing amortization has increased by 13.8% in 2012 compared to 2011 as a result of refinancings and new debt associated with acquisitions. The deferred financing costs include mortgage assumption fees, application fees and legal costs related to obtaining financings and these costs are amortized over the term of the respective mortgage. CMHC insurance fees are amortized over the amortization period of the mortgage. The costs associated with the convertible and subordinated debentures are amortized over the terms of the debentures.

Administration

For the years ended December 31,

	2012	2011	% Change
	$ 8,832	$ 7,672	15.1%
As a percentage of total revenues	**6.6%**	6.1%	

Administration includes expenses which are not specific to an individual property. These expenses include TSX related costs, management and head office salaries and benefits, communication costs, office equipment leases, professional fees and other head office and regional office expenses.

Administrative expenses as a percentage of revenues were higher year-over-year as a result of increased incentive payments, severance costs and higher professional fees.

Loss on Disposition

During the second quarter of 2012, the Company disposed of twelve MHC properties located in Western Canada and Ontario. The loss on disposition of the investment property for the twelve months ended December 31, 2012 of $1.3 million represents the difference between the proceeds from disposition compared to the fair value of the properties less the carrying costs of the related mortgages.

Deferred Tax Expense

The Company has booked future income tax expense for the years ended December 31, 2012, and 2011. Killam is not currently cash taxable and does not expect to pay significant cash taxes in the near future. The Company has not claimed the maximum Capital Cost Allowance ("CCA") allowed over the past number of years and has the ability to reduce taxable income through increasing these claims along with the use of loss carry-forwards. Based on the assumption that the Company does not add to its asset base, Management estimates it would take approximately three to five years to fully utilize these deductions.

PART V

Funds from Operations

FFO is recognized as an industry-wide standard measure for real estate entities' operating performance, and Management considers FFO per share to be a key measure of operating performance. The calculation of FFO includes adjustments specific to the real estate industry applied against net income to calculate a supplementary measure of performance that can be compared with other real estate companies and real estate investment trusts. REALpac, Canada's senior national industry association for owners and managers of investment real estate, has recommended guidelines for a standard industry calculation of FFO based on IFRS. FFO does not have a standardized meaning under IFRS and therefore may not be comparable to similarly titled measures presented by other public companies. Killam calculates FFO in accordance with the REALpac definition as follows:

For the years ended December 31,

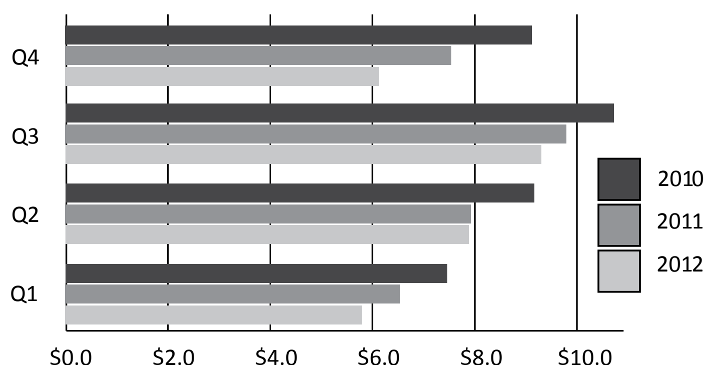
	2012	2011	% Change
Net income	**$ 54,229**	$ 66,821	(18.8)%
Fair value gains	**(37,726)**	(52,070)	(27.5)%
Fair value gains included in equity income	**(30)**	-	N/A
Non-controlling interest (before tax and gains)	**(951)**	(914)	4.0%
Deferred tax expense	**19,234**	17,920	7.3%
Loss on disposition	**1,286**	-	N/A
Depreciation on owner-occupied building	**54**	-	N/A
FFO	**$ 36,096**	$ 31,757	13.7%
FFO/share- basic	**$ 0.72**	$ 0.70	2.9%
FFO/share- diluted	**$ 0.71**	$ 0.69	2.9%
Weighted average shares- basic (000's)	**50,227**	45,523	10.3%
Weighted average shares- diluted (000's) (1)	**50,797**	45,961	10.5%

(1) The calculation of weighted average shares outstanding for diluted FFO and AFFO purposes excludes the convertible debentures as they are anti-dilutive.

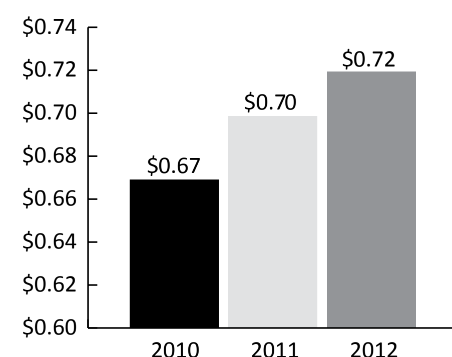
Killam earned FFO of $36.1 million, or $0.72 per share, during 2012 compared to $31.8 million or $0.70 per share during 2011. The increase of 2.9% in FFO per share year-over-year is primarily attributable to acquisitions, and increased earnings from same store properties. These positive impacts were offset by an increase in the weighted average number of shares outstanding associated with the December 2011 and 2012 equity raises, lost NOI related to the sale of the twelve MHC communities, and increased administrative costs.

During 2012, Killam also invested cash of approximately $27.2 million (net of construction financing), related to development projects which will become accretive once construction and lease-up are completed in 2013.

FFO (in $ millions)



FFO per share ($)



Reconciliation of FFO per share

FFO per share - 2011	$ 0.70
Net FFO increase from acquisitions, equity investments, divestitures and developments	0.07
Increase in FFO from same store properties	0.06
Other	0.01
Increase in weighted average shares outstanding	(0.08)
Increase in administrative costs	(0.03)
Increase in non-mortgage interest	(0.01)
FFO per share - 2012	$ 0.72

Adjusted Funds From Operations

Adjusted Funds From Operations ("AFFO") is a supplemental measure used by real estate analysts and some investors to represent FFO after taking into consideration the capital spend related to maintaining the earning capacity of a portfolio. AFFO is a non-IFRS measure and Management believes that significant judgment is required to determine the annual capital expenditures that relate to maintaining the earnings capacity of an asset compared to the capital expenditures that will lead to higher rents or more efficient operations.

In order to provide investors with information to assist in assessing the Company's payout ratio, Management has calculated AFFO using the industry standard of $450 per apartment unit. The MHC industry does not have a standard amount for "maintenance" related capital expenditures. Management has assumed $100 per MHC site as a reasonable estimate of non-NOI enhancing capital expenditures per MHC site. The weighted average number of rental units owned during the year was used to determine the capital adjustment applied to FFO to calculate AFFO.

For the years ended December 31,

	2012	2011	% Change
Funds from operations	**$ 36,096**	$ 31,757	13.7%
Maintenance Capital Expenditures			
Apartments	**(4,952)**	(4,538)	9.1%
MHCs	**(791)**	(929)	(14.9)%
Adjusted funds from operations	**$ 30,353**	$ 26,290	15.5%
AFFO/ share - basic	**$ 0.60**	$ 0.58	3.4%
AFFO/ share - diluted	**$ 0.59**	$ 0.57	3.5%
AFFO payout ratio - basic(1)	**96%**	99%	(3.0)%

(1) The 2012 AFFO payout ratio is based on Killam's annualized dividend of $0.58. The 2011 AFFO payout ratio is based on an annualized dividend of $0.56 for the period January to May and $0.58 for June - December.

PART VI

Investment Properties

As at December 31,

	2012	2011	% Change
(i) Investment properties	**$ 1,296,724**	$ 1,246,645	4.0%
(ii) Investment properties under construction ("IPUC")	**57,941**	11,574	400.6%
	$ 1,354,665	$ 1,258,219	7.7%

Continuity of Investment Properties

The following table summarizes the changes in value of Killam's investment properties for the years ended December 31, 2012 and 2011, highlighting the fair value adjustment that flows through the income statement for each period.

For the years ended December 31,

	2012	2011
Balance, beginning of the year	**$ 1,246,645**	$ 1,081,778
Acquisition of properties	**58,821**	95,970
Disposition of properties	**(72,889)**	-
Transfer to IPUC	**-**	(5,373)
Transfer from IPUC	-	4,691
Capital expenditures	**22,467**	17,509
Fair value adjustments - Apartments	**35,547**	42,968
Fair value adjustment - MHCs	**6,133**	9,102
Balance, end of year	**$ 1,296,724**	$ 1,246,645

The increase in the fair value of the investment properties is a result of acquisitions of $58.8 million in properties, capital investments of $22.5 million and a decrease in the weighted average Cap-Rates used to determine the fair market value of the apartment portfolio, resulting in a fair value adjustment of $42.1 million. This increase in investment properties was partially offset by the sale of twelve MHC properties during the second quarter of 2012.

The key valuation assumption used to determine the fair market value, using the direct capitalization method, is the Cap-Rate for each property. A summary of the Cap-Rates used for the December 31, 2012 and December 31, 2011 valuations as provided by Killam's independent appraiser, are as follows:

	December 31, 2012			December 31, 2011		
	Low	**High**	**Effective Weighted Average**	Low	High	Effective Weighted Average
Apartments	**4.50%**	**8.00%**	**6.02%**	5.50%	8.00%	6.19%
MHCs	**6.50%**	**8.50%**	**7.04%**	6.75%	9.40%	7.28%

As highlighted in the above chart, the effective weighted average Cap-Rate used to value the apartment properties decreased by 17 basis points year-over-year, generating an increased valuation for some properties. The effective weighted average Cap-Rates used to value the MHCs decreased 24 basis points from December 31, 2011.

The impact of a 10 basis point change in the Cap-Rate used to value the investment properties would affect the fair value as follows:

	December 31 , 2012			December 31, 2011		
	Weighted Average	**Increase**	**Decrease**	Weighted Average	Increase	Decrease
Apartments	**6.02%**	**$ 18,958**	**$ 18,338**	6.19%	$ 16,251	$ 16,785
MHCs	**7.04%**	**2,435**	**2,366**	7.28%	3,126	3,213
Total		**$ 21,393**	**$ 20,704**		$ 19,377	$ 19,998

The impact of a 1% change in net operating income used to value the investment properties would affect the fair value as follows:

	December 31, 2012 Increase/Decrease	December 31, 2011 Increase/Decrease
Apartments	**$ 11,220**	$ 10,215
MHCs	**1,688**	2,309
Total	**$ 12,908**	$ 12,524

2012 Acquisitions - Investment Properties

Property	Location	Acquisition Date	Year Built	Units	Total Purchase Price
Apartments					
Chapter House[(1)]	Halifax	26-Feb-12	2004	41	$ 14,029
Brentwood	Halifax	22-Mar-12	1968	240	20,074
Mayview, Rosenthal, Cummings, Bronson	Ottawa	30-Aug-12	1950's-60's	244	24,464
					$ 58,567
Land					
Land-Topsail Road	St. John's	16-Jul-12			3,290
Land- Pleasantville	St. John's	24-Sep-12			1,922
					$ 5,212
Other					
668 Forest Hills Road[(2)]					226
1540 and 1546 Carlton Street[(3)]					1,402
					$ 1,628
Investment Property Acquisitions					**$ 65,407**
Investment Property Acquisitions through Joint Ventures[(4)]					
Kanata Lakes	Ottawa	15-May-12	2012	146	$ 10,956
Silver Spear	Mississauga	31-May-12	1968	199	8,486
					$ 19,442
Total Acquisitions					**$ 84,849**

(1) Chapter House also has 14,500 square feet of commercial space.
(2) 668 Forest Hills Road is a residential dwelling adjacent the entrance of the Forest Hills apartment building purchased for future development.
(3) 1540 and 1546 Carlton Street are residential dwellings adjacent Spring Garden Terrace purchased in Q4 2012 for future development potential.
(4) The investment property acquired represents Killam's 25% interest in the properties. The acquisitions are recorded as part of the Killam's investments and are accounted for using the equity method.

In addition to apartment acquisitions, during 2012 Killam purchased three parcels of land for future development. Two parcels of land were purchased in St. John's, Newfoundland, which provides the Company with a total of three future development sites in the city. The lot located on Topsail Road is 4.8 acres and is zoned for 284 units, with the first phase of development expected to contain 125-150 units. The Pleasantville lot is a 2.3 acre lot located in close proximity to the Company's Bennett House development, and is zoned for 102 units. The Company also acquired 1540 and 1546 Carlton Street in Halifax, expected to be redeveloped in the future.

2012 Dispositions - Investment Properties

On May 31, 2012, Killam sold a portfolio of 12 MHCs. The sale allowed Killam to crystallize the increased value of five non-core MHCs in Western Canada and seven properties in Ontario, and to generate net proceeds of $33.9 million. As part of the sale transaction, Killam purchased a 25% interest in a 199-unit building in Mississauga with its joint venture partner. The properties that were disposed of are as follows:

Property	Location	Disposal Date	Sites	Acres	Fair Value at Disposition
MHCs					
The Poplars	British Columbia	31-May-12	130	36	$ 7,386
Lynwood Estates	Alberta	31-May-12	110	18	4,370
Evergreen Estates	Alberta	31-May-12	73	11	2,298
Hillpark Estates	Alberta	31-May-12	136	18	4,667
Sunset Estates	Saskatchewan	31-May-12	247	77	7,839
Bayview Estates	Ontario	31-May-12	146	60	4,030
Fergushill Estates	Ontario	31-May-12	152	49	5,971
Golden Horseshoe Estates	Ontario	31-May-12	267	33	8,806
Green Haven Estates	Ontario	31-May-12	230	45	9,120
Parkside Estates	Ontario	31-May-12	144	80	5,124
Silver Creek Estates	Ontario	31-May-12	237	80	10,519
Sunny Creek Estates	Ontario	31-May-12	160	53	2,759
					$72,889

Investment Properties Under Construction

For the years ended December 31,

	2012	2011
Balance, beginning of year	**$ 11,574**	$ 1,033
Capital expenditures[1]	**47,284**	9,667
Interest capitalized	**1,063**	192
Transfers from investment properties	**-**	5,373
Transfers to investment properties	**-**	(4,691)
Fair value losses	**(1,980)**	-
Balance, end of year	**$ 57,941**	$ 11,574

(1) Includes acquisition of land for future developments.

Killam's investment properties under construction are recorded at fair value. At December 31, 2012, there was a fair value write-down of $2.0 million. The write-down was related to land costs allocated to two of the development projects constructed on land adjacent to existing Killam properties. The allocation of land costs were estimated at the inception of the development and were deemed to be too high once the required site servicing was completed.

Killam's development projects at December 31, 2012 are summarized as follows:

Project Name	Location	Units	Start Date	Expected Completion	Projected Cost	Construction Costs to Date[1]	% Complete
					($millions)	($millions)	
S2	Halifax, NS	63	Q2 2011	Q2 2013	$15.8	$11.0	70%
The Plaza at Forest Hills	Fredericton, NB	101	Q2 2011	Q2 2013	23.8	18.5	78%
Brighton House	Charlottetown, PE	47	Q3 2011	Q1 2013	6.9	6.5	94%
Bennett House	St. John's, NL	71	Q4 2011	Q2 2013	16.6	11.3	68%
Total		282			$63.1	$47.3	

(1)Excludes all land costs

At December 31, 2012, Killam's development projects were between 68% and 94% complete based on the estimated total project costs compared to costs incurred to date. The total projected development costs increased slightly in the fourth quarter, by $0.1 million. This variance was driven by an increase in projected development costs for Bennett House of $0.9 million, offset by a decrease in the projected costs at S2 of $1.1 million. The increased costs for Bennett House relate to upgraded hardwood flooring and increased cladding costs. The reduction in costs associated with S2 are a result of a review of the final site development costs and the identification of approximately $1.0 million in costs related to improvements to Shaunslieve Apartments, the existing property adjacent to S2.

Brighton House was completed during the month of February 2013, and the Company expects all of the remaining developments to be ready for occupancy by April and May 2013. Final construction for all of the properties will be completed during Q2-13. At December 31, 2012, the Company had drawn down $14.1 million in construction financing which funded all of the construction costs incurred during the fourth quarter of 2012. The Company still has $23.4 million available in construction financing which will fund the remaining construction costs as well as construction holdback payments upon completion.

The Company had strong pre-leasing activity at both Brighton House and Bennett House. The Company expects these properties to reach full occupancy by late Q3-13. Bennett House has 55 of the 71 units pre-leased and the Company expects the remainder of the building to lease-up quickly given the limited availability of new apartment construction in St. John's.

S2 and The Plaza have less confirmed leases than the other developments, therefore Management has developed specific advertising and marketing strategies for the new buildings and is confident that lease-up will accelerate.

Management is anticipating a year-one return of between 5% and 6% on its developments, and minimal capital requirements for the next ten to fifteen years.

Capital Improvements

Killam invests capital to maintain and improve the operating performance of its properties. During 2012, Killam invested a total of $22.5 million, compared to $17.5 million in 2011. Capital investments in the year are added to the book value of the investment properties.

For the years ended December 31,

	2012	2011	% Change
Apartments	**$ 19,039**	$ 12,569	51.5%
MHCs	**3,345**	4,921	(65.4)%
Other	**84**	19	342.1%
	$ 22,468	$ 17,509	28.3%

Apartments

A summary of the capital spend on the apartment segment is included below:

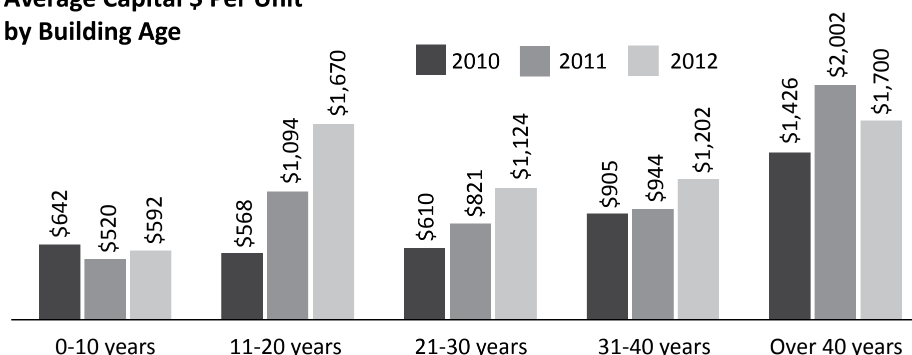
For the years end December 31,

	2012	2011	% Change
Building improvements	**$ 9,353**	$ 5,268	77.5%
Suite renovations	**4,945**	3,270	51.2%
Land improvements	**1,374**	1,369	0.4%
Boilers and heating equipment	**1,902**	1,268	50.0%
Appliances	**808**	542	49.1%
Parking lots	**211**	401	(47.4)%
Equipment	**237**	326	(27.3)%
Other	**209**	125	67.2%
Total capital spend - Apartments	**$ 19,039**	$ 12,569	51.5%
Average units outstanding	**11,312**	10,084	12.2%
Capital spend per unit	**$ 1,683**	$ 1,246	35.1%

Killam estimates that $450 per unit of the capital spending relates to maintenance capital, and the remainder relates to value enhancing upgrades. Maintenance capital varies with market conditions and relates to investments that are not expected to lead to an increase in the NOI, or increased efficiency, of a building; however, it may extend the life of a building. Examples of maintenance capital include roof and structural repairs and are in addition to regular repairs and maintenance costs that are expensed to NOI. Value enhancing upgrades are investments in the properties that are expected to result in higher rents and/or increased efficiencies. This includes unit and common area upgrades and energy investments, such as natural gas conversions.

Killam spent $1,683 per unit in 2012 compared to $1,246 per unit in 2011. Contributing to capital spend has been $1.0 million related to natural gas conversions at 14 buildings located in Halifax and Dartmouth, Nova Scotia over the last two years. Given the lower cost of natural gas compared to oil, the Company expects to see utility cost savings as a result of these recent conversions going forward. The Company also spent $3.9 million on capital work related to the properties adjacent to the development sites including site servicing costs, parking lot upgrades, lighting, balcony and roofing upgrades. These enhancements reposition the older properties in concert with the construction of the developments. Excluding these costs in 2012, the average spend per unit would be $1,273.
The timing of capital spending is influenced by tenant turnover, market conditions, and individual property requirements, causing annual variability in capital spending. In addition, the length of time that Killam has owned a property and the age of the property also influences the annual capital requirements.

The following chart shows the average capital spend per unit for same store properties for each of the last three years.



As the chart highlights, the capital spend per unit is less for newer properties, averaging $592 per unit in 2012, compared to $1,700 per unit for buildings over 40 years old. This analysis excludes capital spending on development and energy projects. Capital spending was higher than normal for properties in the 11 to 20 age group due to increased unit upgrades in Moncton to compete with new developments. Moncton properties represent 52% of the units included in the 11 to 20 age category in 2012. Excluding the Moncton properties, the average capital spend per unit for properties built between 1993 and 2002 would be $1,231.

The building improvements of $9.4 million in 2012 are comprised mainly of roofing, balcony, brick replacement and exterior upgrades. These projects represent upgrades at a number of Killam's older properties which will reduce future repair and maintenance costs.

The increase of $1.7 million related to suite renovations year-over-year is a result of the higher vacancy experienced in 2012. More unit upgrades were completed to compete with new rental product in certain markets. Many of the suite renovations have high-end upgrades, including laminate and hardwood flooring and stainless steel appliances. Killam expects to recover the renovation costs through increased rental rates.

Value-enhancing property capital improvements increase the operating effectiveness and profitability of the property portfolio. Killam expects to spend approximately $13 million to $15 million during 2013 on apartment portfolio capital investments.

MHCs

A summary of the capital spend on the MHC segment is included below:

For the years ended December 31,

	2012	2011	% Change
Water & sewer upgrades	**$ 1,812**	$ 3,077	(41.1)%
Roads and paving	**421**	905	(53.5)%
Equipment	**36**	110	(67.3)%
Other	**527**	574	(8.2)%
Site expansion and land improvements	**549**	255	115.3%
Total capital spend - MHCs	**$ 3,345**	$ 4,921	(32.0)%
Average units outstanding	**8,251**	9,290	(11.2)%
Capital spend per unit	**$ 405**	$ 530	(23.6)%

Management expects to spend between $300 and $400 in capital per MHC site on an annual basis. As with the apartment portfolio, a portion of the MHC capital is considered maintenance capital and a portion is value enhancing. Management estimates that $100 per unit is maintenance capital, including costs to support the existing infrastructure, and the remaining amount increases the value of the properties, with improved roadways, ability to accommodate future expansion, and community enhancements, such as the addition of playgrounds. The cost of some capital projects will be recovered through above guideline increases in the provinces with rent control, leading to increased NOI for the investment.

As with the apartment portfolio, the timing of capital spending changes based on requirements at each community. Per unit costs year-over-year are down primarily due to lower costs related to water and sewer infrastructure. In 2013, Killam expects to spend $2.5 million to $3.5 million on capital investments in the MHC portfolio.

Investments

For the years ended December 31,

	2012	2011
Balance, beginning of the year	**$ 8,420**	$ -
Additions	**19,563**	8,522
Share of net income	**758**	13
Distributions	**(18,452)**	(115)
Balance, end of period	**$ 10,289**	$ 8,420

Investments relate to Killam's 25% interest in three apartment buildings in Ontario acquired through a joint venture with Kuwait Finance House.

The joint venture acquired Kanata Lakes, a new 146-unit building in Ottawa, on May 15, 2012. The total purchase price, including soft costs, was $43.5 million, with Killam's 25% interest being $10.9 million. The purchase price was satisfied with cash and mortgage debt of $24.9 million and was placed on the property in July 2012. On May 31, 2012, the joint venture purchased Silver Spear, a 199-unit building in Toronto with 3.6 acres of surplus land, for a total purchase price, including soft costs, of $33.9 million, with Killam's 25% interest being $8.5 million. The purchase price was satisfied with cash, and mortgage debt of $25.2 million was placed on the property in December 2012. Killam also placed a mortgage on 180 Mill Street, acquired in December 2011, in the amount of $27.5 million in 2012. The distributions paid out relate primarily to the flow of funds back to Killam once mortgages were placed on the properties.

Liquidity and Capital Resources

The Company's primary sources of capital are cash generated from operating activities, credit facilities, mortgage financing and refinancing, and equity and debt issuances. The Company's primary use of capital include property acquisitions and developments, major property improvements, recurring property maintenance, debt principal and interest payments, and payment of dividends. The Company anticipates meeting all current and future obligations with current cash and cash equivalents, cash flow generated from operations and conventional mortgage refinancing assuming that occupancy levels remain strong and that the Company will be able to obtain financing on reasonable terms.

Killam's ability to grow through acquisitions and development will be dependent on the ability to access mortgage debt, construction financing and to raise equity in the capital markets. As at December 31, 2012, Killam had $56.7 million in available cash on-hand; however, $10.0 million was required for repayment of subordinated debentures in January 2013, leaving $46.7 million of cash on-hand available for acquisitions and development. Based on an assumed 60% mortgage debt on acquisitions, this capital is expected to support acquisitions and/or further developments of approximately $117 million.

Mortgages and Other Loans

Below are Killam's key debt metrics:

As at December 31,

	2012	2011	% Change
Weighted average years of maturity of mortgage and vendor debt	**3.4**	3.8	(0.4) years
Gross mortgage, loan and vendor debt as a percentage of total assets	**45.2%**	48.1%	(290) bps
Total debt as a percentage of total assets	**51.6%**	55.2%	(360) bps
Interest coverage ratio (rolling twelve months)	**2.09**	1.98	5.6%
Debt service coverage ratio (rolling twelve months)	**1.35**	1.34	0.7%
Weighted average interest rate of mortgage and vendor debt	**4.48%**	4.63%	(15) bps
Weighted average interest rate of total debt	**4.84%**	4.94%	(10) bps

The Company's long-term debt consists largely of fixed-rate, long-term mortgage financing. In certain cases the Company will also utilize vendor-take-back ("VTB") mortgages as part of an acquisition. As at December 31, 2012, the Company has only two VTB's, worth $0.8 million. Mortgages are secured by a first or second charge against the individual properties and the vendor financing is secured by a general corporate guarantee.

As at December 31, 2012, only the construction financing loans and two demand loans have floating interest rates. These loans have an interest rate of prime plus 1.0% - 1.5%. The construction financing has floating interest rates between prime and prime plus 1%.

Mortgages and vendor financings decreased by $5.1 million year-over-year due to the disposition of MHC properties and regular principal repayments. These reductions were partially offset by debt associated with acquisitions completed in 2012 ($34.7 million) and net proceeds on the refinancing of maturing mortgages ($10.9 million).

Killam's December 31, 2012 weighted average interest rate on mortgages improved to 4.48% compared to 4.63% as at December 31, 2011, as a result of refinancings during the period at lower interest rates as well as the retirement of debt associated with the sale of the twelve MHC properties. This trend is expected to lessen in 2014 when $150 million (24% of portfolio) of current mortgage balances will be refinanced. In the ensuing two years, $226 million of mortgages will also mature; by December 31, 2016, 74% of Killam's mortgages are expected to be refinanced and the weighted average years to maturity will increase and the average number of years to maturity lengthened.

Total debt as a percentage of total assets decreased to 51.6% at December 31, 2012, from 55.2% at December 31, 2011. Management expects to maintain the percentage of debt to total assets between 55% and 65%. This ratio is sensitive to changes in the fair value of investment properties, in particular Cap-Rate changes. A 10 basis point increase in the weighted average Cap-Rate at December 31, 2012, would have increased the ratio of debt as a percentage of assets by 80 basis points.

2012 Refinancings

During the year ended December 31, 2012, Killam refinanced the following mortgages:

	Mortgage Debt Maturities		Mortgage Debt on Refinancing		Weighted Avg. Term	Net Proceeds
Apartments[1]	$ 21,563	4.83%	$ 28,420	2.89%	7.4 years	$ 6,857
MHCs	10,254	5.88%	14,293	4.22%	5.0 years	4,039
	$ 31,817	5.17%	$ 42,713	3.33%		$ 10,896

(1) In addition, a $0.9 million VTB mortgage bearing interest at a rate of 5.0% was repaid in full.

The following table sets out the maturity dates and average interest rates of mortgage and vendor debt, and percentage of apartment mortgages that are CMHC insured by the year of maturity:

	Apartments			MHCs		**Total**	
Year of Maturity	Balance Dec 31,2012	Weighted Avg Int Rate %	% CMHC Insured	Balance Dec 31, 2012	Weighted Avg Int Rate %	**Balance Dec 31, 2012**	**Weighted Avg Int. Rate %**
2013	77,918	4.36	74.1	10,929	6.24	**88,847**[1]	**4.72**
2014	132,604	4.45	50.9	17,817	5.59	**150,421**	**4.59**
2015	88,021	4.51	47.0	16,799	5.53	**104,820**	**4.68**
2016	109,073	4.31	50.0	12,543	5.39	**121,616**	**4.42**
2017	23,478	3.26	88.4	20,426	4.60	**43,904**	**3.88**
2018	20,179	4.76	35.7	-	-	**20,179**	**4.76**
2019	20,555	4.86	100.0	-	-	**20,555**	**4.86**
2020	18,835	4.08	100.0	-	-	**18,835**	**4.08**
2021	24,385	3.79	88.8	-	-	**24,385**	**3.79**
2022	25,230	3.16	55.8	-	-	**25,230**	**3.16**
Thereafter	14,105	4.41	100.0	-	-	**14,105**	**4.41**
	$ 554,383	4.29	61.0	$ 78,514	5.38	**$ 632,897**	**4.45**

(1) Includes $2.1 million related to a demand loan classified as current.

As at December 31, 2012, approximately 61% of the Company's apartment mortgages were CMHC insured (53% of all mortgages) (December 31, 2011 – 61% and 51%, respectively). The weighted average interest rate on the CMHC insured mortgages was 3.98% as at December 31, 2012 (December 31, 2011– 4.13%).

Access to mortgage debt is essential in financing future acquisitions and in refinancing maturing debt. Management has intentionally diversified Killam's mortgages to avoid dependence on any one lending institution and has staggered the maturity dates of its mortgages to manage interest rate risk. Management anticipates continued access to mortgage debt for both new acquisitions and refinancings. Access to CMHC insured financing gives apartment owners an advantage over other asset classes as lenders are provided a government guarantee on the debt and therefore able to lend at more favourable rates.

The following table presents the NOI of properties that are available to Killam to refinance at debt maturity for 2013 and for 2014.

2013	**Number of Properties**	**NOI (last 12 months)**	**Principal Balance (at maturity)**
Apartments with debt maturing in 2013	20	$ 9,742	$ 74,455
MHCs with debt maturing in 2013	8	1,825	10,721
2013 Debt Maturities	28	$ 11,567	$ 85,176
2014			
Apartments with debt maturing in 2014	41	$ 17,126	$ 124,466
MHCs with debt maturing in 2014	9	2,980	16,638
2014 Debt Maturities	50	$ 20,106	$ 141,104

Future Contractual Debt Obligations

At December 31, 2012, the timing of the Company's future contractual debt obligations are as follows:

Year	Maturing Mortgage and Loans	Construction Financing	Convertible Debentures	Subordinated Debentures	December 31 Total
2013	$ 105,369	$ 14,062	$ -	$ 10,000	**$ 129,431**
2014	144,987	-	-	-	**144,987**
2015	112,501	-	-	-	**112,501**
2016	112,041	-	-	-	**112,041**
2017	46,311	-	57,500	-	**103,811**
Thereafter	111,688	-	46,000	-	**157,688**
	$ 632,897	**$ 14,062**	**$ 103,500**	**$ 10,000**	**$ 760,459**

Debentures

The Company's $57.5 million convertible unsecured subordinated debentures mature November 30, 2017, bear interest at 5.65% and are convertible, at the holders' option, to common shares at a price of $13.40. The Debentures are redeemable at the option of the Company after November 30, 2013, and on or before November 30, 2015, provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is not less than 125% of the conversion price. After November 30, 2015, the debentures are redeemable at face value. Upon maturity or redemption, the Company may elect to repay all or any portion of the debentures outstanding by issuing the number of common shares obtained by dividing the aggregate of the principal amount of the debentures that have matured or are being redeemed by 95% of the weighted average market price of the common shares for the preceding 20 days (ending 5 days preceding the fixed date for redemption or maturing).

The Company's $46.0 million convertible unsecured subordinated debentures mature June 30, 2018, bear interest at 5.45% and are convertible, at the holders' option, to common shares at a price of $14.60. The Debentures are redeemable at the option of the Company after June 30, 2014 and on or before June 30, 2016, provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is not less than 125% of the conversion price. After June 30, 2016, the debentures are redeemable at face value. Upon maturity or redemption, the Company may elect to repay all or any portion of the debentures outstanding by issuing the number of common shares obtained by dividing the aggregate of the principal amount of the debentures that have matured or are being redeemed by 95% of the weighted average market price of the common shares for the preceding 20 days (ending 5 days preceding the fixed date for redemption or maturing).

The Company's $10.0 million of unsecured subordinated debentures expired, and were repaid, on January 4, 2013 and consisted of three tranches of $2.5 million, $2.5 million, and $5.0 million, bearing interest at 5.92%, 6.06% and 6.33%, respectively. Related warrants associated with the subordinated debentures also expired on January 4, 2013.

Construction Loans

The Company has access to four floating rate, non-revolving, demand construction loans totaling $37.9 million for the purpose of financing the development of its investment properties under construction located in Halifax, Charlottetown, Fredericton, and St. John's. Payments are made monthly on an interest-only basis. The construction loans have interest rates ranging from prime to prime plus 1%. At December 31, 2012, a total of $14.1 million was drawn down at a weighted average interest rate of 3.68% (December 31, 2011 - $Nil).

Credit Facility

The Company has a credit facility with a major financial institution, which consists of a $2.0 million revolving demand facility that can be used for the Company's acquisition program and general business purposes. The interest rate on the debt is prime plus 125 basis points on prime rate advances or 225 basis points over Banker's Acceptances (BAs). Killam has the right to choose between prime rate advances and BAs based on available rates and timing requirements. As December 31, 2012, the Company had assets with a fair value of $1.6 million pledged to the line and had a balance outstanding of $Nil.

Shareholders' Equity

For the year ended December 31, 2012, 471,593 stock options were exercised for cash proceeds of $4.2 million. In addition, 816,992 warrants associated with the subordinated debentures were exercised for a total cash proceeds of $10.0 million.

On December 10, 2012, Killam completed a public share offering, on a bought deal basis, of 2.5 million shares, to the public at a price of $12.00 per share for gross proceeds of $30 million. On December 14, 2012, the Company closed the sale of an additional 375,000 common shares for gross proceeds of $4.5 million pursuant to an over-allotment option with the underwriters.

Killam pays a dividend of $0.04833 per share per month ($0.58 per share annualized). The monthly dividend was increased from $0.04668 per share effective for the June 2011 dividend.

The Company's Dividend Reinvestment Plan ("DRIP") allows shareholders to elect to have all cash dividends from the Company reinvested in additional common shares. Shareholders who participate in the DRIP receive an additional dividend of common shares equal to 3% of each cash dividend that was reinvested. The price per share is calculated by reference to the ten-day volume weighted average price of the Company's common shares on the Toronto Stock Exchange preceding the relevant dividend date, which typically is on or about the 15th day of the month following the dividend declaration. For the year ended December 31, 2012, the Company issued 347,473 common shares under the DRIP with a value of $4.4 million (2011 - 284,843 common shares with a value of $3.0 million). For the year ended December 31, 2012, the average DRIP participation rate was 15% (2011 - 12%).

PART VII

Quarterly Results & Discussion of Q4 Operations

Summary of Quarterly Results

An eight quarter trend highlighting key operating results is shown below:

	2012				2011			
	Q4	**Q3**	**Q2**	**Q1**	Q4	Q3	Q2	Q1
Property revenue	$ 33,360	$ 33,894	$ 33,679	$ 32,631	$ 32,484	$ 33,052	$ 30,267	$ 29,598
Operating expenses	$ 13,801	$ 12,452	$ 13,161	$ 13,781	$ 13,196	$ 11,857	$ 12,048	$ 12,636
Net rental income	$ 19,559	$ 21,442	$ 20,518	$ 18,850	$ 19,288	$ 21,195	$ 18,219	$ 16,962
Operating expense %	41.4%	36.7%	39.1%	42.2%	40.6%	35.9%	39.8%	42.7%
Home sale income	$ 101	$ 93	$ 231	$ 44	$ 179	$ 250	$ 121	$ (64)
Equity & other income (loss)	$ 527	$ 439	$ 508	$ 322	$ (126)	$ 214	$ 199	$ 148
Net income applicable to common shareholders	$ 10,425	$ 12,662	$ 18,558	$ 10,082	$ 12,608	$ 19,747	$ 18,043	$ 15,567
Per share basic	$ 0.20	$ 0.26	$ 0.37	$ 0.20	$ 0.27	$ 0.43	$ 0.40	$ 0.35
Funds from operations	$ 8,732	$ 10,721	$ 9,179	$ 7,463	$ 7,549	$ 9,784	$ 7,896	$ 6,528
Per share basic	$ 0.17	$ 0.21	$ 0.19	$ 0.15	$ 0.16	$ 0.22	$ 0.18	$ 0.15

Q4 - Consolidated Statements of Income

In thousands (except per share amounts)

For the three months ended December 31,	**2012**	2011
Property revenue	**$ 33,360**	$ 32,484
Property operating expenses	**(13,801)**	(13,196)
Home sales	**101**	179
Equity income	**240**	13
Other income	**287**	(139)
	20,187	19,328
Financing costs	**8,315**	9,083
Depreciation	**199**	53
Amortization of deferred financing costs	**366**	406
Administration	**2,361**	2,034
	11,241	11,576
Income before fair value gains, loss on disposition and income taxes	**8,946**	7,765
Fair value gains	**10,057**	8,918
Gain on disposition	**24**	-
Income before income tax expense	**19,027**	16,683
Deferred tax expense	**(7,357)**	(3,879)
Net income	**$ 11,670**	$ 12,804
Net income attributable to:		
Common shareholders	**$ 10,425**	$ 12,608
Non-controlling interests	**1,245**	196
	$ 11,670	$ 12,804

Q4 Apartments - Same Store

For the three months ended December 31,		**2012**		2011	% Change
Property revenue		**$ 23,744**		$ 23,349	1.7%
Property expenses					
Operating expenses	**16.7%**	**3,958**	17.1%	3,982	(0.6)%
Utility and fuel expenses	**13.6%**	**3,232**	13.2%	3,092	4.5%
Property taxes	**11.7%**	**2,787**	11.6%	2,714	2.7%
Total property expenses	**42.0%**	**9,977**	41.9%	9,788	1.9%
Net operating income		**$13,767**		$ 13,561	1.5%

Q4 MHCs - Same Store

For the three months ended December 31,		**2012**		2011	% Change
Property revenue		**$ 4,439**		$ 4,305	3.1%
Property expenses					
Operating expenses	**23.2%**	**1,028**	24.3%	1,048	(1.9)%
Utility and fuel expenses	**10.2%**	**453**	9.0%	386	17.4%
Property taxes	**5.3%**	**235**	5.4%	234	0.4%
Total property expenses	**38.7%**	**1,716**	38.7%	1,668	2.9%
Net operating income		**$ 2,723**		$ 2,637	3.3%

Q4 FFO

For the three months ended December 31,	**2012**	2011	% Change
Net income	**$ 11,670**	$ 12,804	
Fair value gains	**(10,087)**	(8,918)	
Non- controlling interest (before tax and gains)	**(238)**	(216)	
Depreciation on owner-occupied building	**54**		-
Loss on disposition	**(24)**		-
Deferred tax expense	**7,357**	3,879	
FFO	**$ 8,732**	$ 7,549	15.7%
FFO/share - basic	**$ 0.17**	$ 0.16	6.3%
FFO/share - diluted	**$ 0.17**	$ 0.16	6.3%
Weighted average shares - basic (000's)	**51,528**	46,728	10.3%
Weighted average shares - diluted (000's) (1)	**51,914**	47,153	10.1%

(1) The calculation of weighted average shares outstanding for diluted FFO purposes excludes the convertible debentures as they are anti-dilutive.

FFO was $8.7 million in the fourth quarter, up 15.7% from $7.5 million in the fourth quarter of 2011. FFO per share was $0.17, up from $0.16 earned in the same period in 2011. As the FFO reconciliation on page 39 highlights, contributions from same store properties contributed to the increase. Consolidated same store NOI increased by 1.8% in the quarter, with apartment NOI up 1.5% and MHC NOI up 3.3%.

Killam's apartment portfolio continued to generate quarter-over-quarter revenue growth, as increased rental rates, up 3.7% from Q4 2011, offset higher vacancy. As shown in the same store summary above, higher utility and fuel costs, up 4.5%, were the main driver of the 1.9% increase in total operating expenses. Increased electricity costs and a spike in natural gas costs in Nova Scotia (up 68% from December 2011, as discussed on page 19) more than offset the savings achieved from lower oil costs following natural gas conversions completed late in 2011 and early 2012.

The MHC portfolio continued to generate strong revenue growth, up 3.1% from Q4 2011, driven by increased rental rates. An increase in utility costs of 17.4% resulted in an increase of total operating expenses of 2.9%. A timing difference in electricity costs and recoveries is the primary reason for the increased utility costs; year-over-year utility costs increased 7.1%.

Acquisitions also contributed positively to FFO growth in the quarter, however, the positive impact was partially offset by a reduction in earnings from the twelve property MHC portfolio sold in May 2012 and an increase in the shares outstanding. Also impacting FFO per share growth in Q4 was the short-term dilutive impact of the development projects and a high cash balance in preparation for future acquisitions. The completion of the development projects in the first half of 2013 are expected to contribute to FFO per share growth during the second half of the year.

Killam recorded higher administrative costs during the fourth quarter of 2012 compared to the fourth quarter of 2011. This relates primarily to the timing of the compensation program for Killam's senior executives.

Q4 - FFO Reconciliation

FFO per share- Q4 2011	**$ 0.16**
Add:	
Increased FFO from same store properties - due to NOI growth and decrease in interest expense	**0.01**
Increased earnings associated with acquisitions and equity investments	**0.02**
Increase in other income - Q4 2011 other income was offset by $0.4 million in costs associated with the remediation of an environmental clean up	**0.01**
Decrease in non-mortgage interest due to increased capitalization of interest relating to development projects	**0.01**
Other	**0.01**
Less:	**(0.02)**
Divestiture of MHC portfolio	**(0.02)**
Increase in weighted average shares outstanding	**(0.01)**
Increase in administrative costs	
FFO per share - Q4 2012	**$ 0.17**

PART VIII

Risk Management

Killam faces a variety of risks, the majority of which are common to real estate entities. Real estate investments are generally subject to varying degrees of risk, depending on the nature of the property. These risks include (i) changes in general economic conditions, (ii) changes in local conditions (such as an oversupply of space or a reduction in demand for real estate in the area), (iii) changes to government regulations (such as new or revised residential tenant legislations), (iv) competition from others with available space, and (v) the ability of the landlord or owner to provide adequate maintenance economically.

Real estate is relatively illiquid. Such illiquidity will tend to limit Killam's ability to rebalance its portfolio promptly in response to changing economic or investment conditions. In addition, financial difficulties of other property owners, resulting in distress sales, may depress real estate values in the markets in which the Company operates.

Killam's exposure to general risks associated with real estate investments is mitigated with both its geographic diversification, and investments in both apartments and MHCs.

Killam is exposed to other risks, as outlined below:

Interest Rate Risk

Interest risk is the risk that the Company would experience lower returns as the result of its exposure to a higher interest rate environment. The Company is exposed to interest rate risk as a result of its mortgages and loans payable, however this risk is mitigated through the Company's strategy to have the majority of its mortgages payable in fixed-term arrangements. The Company also structures its financings so as to stagger the maturities of its debt, minimizing the Company's exposure to interest rates in any one year.

As at December 31, 2012, no mortgages or vendor debt had floating interest rates except for two demand loan for $2.8 million. These loans have an interest rate of prime plus 1.0-1.5% (December 31, 2011 - 1.5%). During 2012, Killam obtained construction loans of $14.1 million with floating interest rates ranging from prime to prime plus 1% and consequently, Killam is exposed to short-term interest rate risk on these loans.

Liquidity Risk

Liquidity risk is the risk that the Company may not have access to sufficient debt and equity capital to fund its growth program and/or refinance its debt obligations as they mature. Senior Management manages the Company's cash resources based on financial forecasts and anticipated cash flows. The maturities of the Company's long-term financial liabilities are set out in Notes 12 to 16 of the consolidated financial statements. The Company structures its financings so as to stagger the maturities of its debt, thereby minimizing the Company's exposure to liquidity risk in any one year. In addition, the Company's apartments qualify for CMHC insured debt, reducing the refinancing risk on mortgage maturities. The Company's MHCs do not qualify for CMHC insured debt, however, they continue to have access to mortgage debt.

Increased Supply Risk

Increased supply risk is the risk of loss from increased competition from the addition of new rental units in Killam's core markets. Numerous other residential developers and apartment owners compete for potential tenants. Although it is Killam's strategy to own multi-family residential properties in premier locations in each market in which it operates, some of the apartments or MHCs of Killam's competitors may be newer, better located or offer lower rents. An increase in alternative housing could have a material adverse effect on Killam's ability to lease units and in the rents charged and could adversely affect Killam's revenues and ability to meet its obligations. To mitigate against this risk Killam has a geographically diverse asset base. Management is expanding this diversification by increasing Killam's investment in apartment markets outside Atlantic Canada.

Credit Risk

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease term commitments. The Company mitigates the risk of credit loss through the diversification of its existing portfolio and limiting its exposure to any one tenant. Credit assessments are conducted with respect to all new leasing and the Company also obtains a security deposit to assist in potential recovery requirements. In addition, the receivable balances are monitored on an ongoing basis with the result that the Company's exposure to bad debt is not significant. The Company's bad debt expense experience has historically been less than 0.4% of revenues. None of Killam's tenants account for more than 1% of the tenant receivables as at each of the period-ends presented in these financial statements.

Development Risk

Development risk is the risk that costs of developments will exceed original estimates, unforeseen delays occur and/or units will not be leased in the timeframe and/or at rents anticipated. Killam minimizes its exposure to development risk my limiting the amount of development underway at any one time. To reduce the Company's exposure to price increases, Killam enters into fixed-rate contracts when possible. To reduce the lease-up risk, Killam does extensive market research in advance of each development to support expected rental rates, and pre-markets its properties early on in the process, to increase demand for the new developments.

Environmental Risk
As an owner of real estate, Killam is subject to federal, provincial and municipal environmental regulations. These regulations may require the Company to fund the costs of removal and remediation of certain hazardous substances on its properties or releases from its properties. The failure to remediate such properties, if any, could adversely affect the Company's ability to borrow using the property as collateral or to sell the real estate. Killam is not aware of any material non-compliance with environmental laws at any of its properties. The Company has made, and will continue to make, the necessary capital expenditures to comply with environmental laws and regulations. Environmental laws and regulations can change rapidly, and the Company may be subject to more stringent environmental laws and regulations in the future. The Company mitigates its risk of losses associated with oil tank leaks by enforcing the requirement for appropriate insurance, performing regular oil tank inspections, and enforcing the removal of oil tanks when homes are sold.

General Uninsured Losses
Killam carries comprehensive general liability, fire, flood, extended coverage and rental loss insurance with policy specifications, limits and deductibles customarily carried for similar companies. There are, however, certain types of risks (generally of a catastrophic nature) that are either uninsurable or would not be economically insurable.

Rent Control Risk
Rent control exists in some provinces in Canada, limiting the percentage of annual rental increases to existing tenants. Killam is exposed to the risk of the implementation of, or amendments to, existing legislative rent controls in the markets in which it operates, which may have an adverse impact on the Company's operations. In the provinces that Killam currently operates, Prince Edward Island, and Ontario have rent controls. As well, Nova Scotia introduced rent control for MHCs in 2012.

Utility and Property Tax Risk
Killam is exposed to volatile utility costs and increasing property taxes. Utility expenses, mainly consisting of oil, natural gas, water and electricity charges, have been subject to considerable price fluctuations over the past several years. Killam has the ability to raise rents on the anniversary date of its leases, subject to the overall rental market conditions, to offset rising energy and utility costs, however rental increases may be limited by market conditions. Killam invests in energy efficiency initiatives to reduce its reliance on utility costs; however Killam remains exposed to price volatility. The Company has the ability to fix rates through the use of SWAP contracts for a portion of its oil and natural gas consumption to reduce the impact of fluctuations in commodity prices. To address the risk of property tax increases, Killam, along with the assistance of outside consultants, reviews property tax assessments and, where warranted, appeals them.

Taxes
Killam is currently not cash-tax taxable due to its ability to reduce taxable income through unclaimed CCA, and does not expect to be cash taxable for at least the next three to five years. A change in circumstances that could result in the Company paying cash taxes in advance of this estimate may have a negative impact on Killam's liquidity. To mitigate against this risk, Killam is working with tax advisors to identify those issues that may impact a change in the Company's tax situation.

Dividend Payments
Dividend payments may exceed actual cash available from time to time because of items such as mortgage principal repayments, capital requirements, and redemption of shares, if any. The Company may be required to use part of its debt capacity, raise additional equity, or reduce dividends in order to accommodate such items, and there can be no assurance that funds from such sources will be available on favourable terms, or at all.

Significant Accounting Judgments, Estimates and Assumptions

In the application of Killam's accounting policies, which are described in Note 2 of the financial statements, Management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The judgments, estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements Other Than Estimates

In the process of applying the Company's accounting policies, Management has made the following judgments, which have the most significant effect on the amounts recognized in the consolidated financial statements:

Property Acquisitions
When investment properties are acquired, Management considers whether the acquisition represents the acquisition of an asset or a business. The Company accounts for an acquisition as a business combination where an integrated set of activities is acquired in addition to the property. More specifically, consideration is made of the extent to which significant processes are acquired and, in particular, the extent of ancillary services provided by the subsidiary (e.g., maintenance, cleaning, security, bookkeeping, leasing operations, etc.). The significance of any process is judged with reference to the guidance in IAS 40 about ancillary services.

Management believes that the majority of the Company's acquisitions will be classified as asset acquisitions. During the acquisition of most properties, Killam buys the asset itself and any short-term leases that are in-place. Generally, Killam does not purchase any business systems or processes with a property. Management would consider an acquisition to be a business combination if all the following criteria were met:

- The acquisition includes a property portfolio (multiple buildings),
- A significant staff complement is included, including a maintenance team, leasing representatives and property management personnel, and
- Systems are acquired and continue to be incorporated into operations.

Investment Properties
The Company's accounting policies relating to investment properties are described in Note 2(F). In applying this policy, judgment is applied in determining whether certain costs are additions to the carrying amount of the property and, for properties under development, identifying the point at which substantial completion of the property occurs and identifying the directly attributable borrowing costs to be included in the carrying value of the development property. Judgment is also applied in determining the extent and frequency of independent appraisals.

Leases
The Company has entered into residential property leases on its investment property portfolio. The Company has determined, based on an evaluation of the terms and conditions of the arrangements, that it retains all the significant risks and rewards of ownership of these properties and so accounts for the contracts with tenants as operating leases.

Financial Instruments
The Company's accounting policies relating to financial instruments are described in Note 2(K). The critical judgments inherent in these policies relate to applying the criteria set out in IAS 39 to designate financial instruments as fair value through profit and loss "FVTPL", assessment of the effectiveness of hedging relationships, determining whether the Company has significant influence over investees with which it has contractual relationships in addition to the financial instrument it holds and identification of embedded derivatives subject to fair value measurement in certain hybrid instruments.

Taxes
The Company is subject to income and capital gains taxes in numerous jurisdictions. Significant judgment is required to determine the total provision for current and deferred taxes. There are many transactions and calculations for which the ultimate tax determination and timing of payment is uncertain. In particular, when calculating deferred taxation, the effective tax rate applicable to the temporary differences in investment property depends on the method by which the carrying amount of investment property will be realised. The Company recognizes liabilities for current taxes based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income and deferred tax provisions in the period in which the determination is made. Deferred tax assets and liabilities are recognized on a net basis to the extent they are relating to the same fiscal entity and fall due in approximately the same period.

Estimates

Valuation of Investment Properties
The fair value of investment properties is partially determined by independent real estate valuation experts (the "external valuator") using recognized valuation techniques and partially by Management. The external valuator uses the capitalization of net income method to determine the fair market values. In some cases, the fair values are corroborated by recent real estate transactions with similar characteristics and location to those of the Company's assets. Management's internal valuation model is also based on a capitalization of NOI by property, using property specific quarterly Cap-Rates, provided by an the external valuator.

IPUC is also valued at fair value, except if such values cannot be reliably determined. In the case when a fair value cannot be reliably determined, such property is recorded at cost. The fair value of IPUC is determined using the capitalization of net income.

The determination of the fair value of investment property requires the use of estimates such as future cash flows from assets and Cap-Rates applicable to those assets. In addition, development risks (such as construction and leasing risks) are also taken into consideration when determining the fair value of IPUC. These estimates are based on local market conditions existing at the reporting date. In arriving at their estimates of market values, the external valuator uses their market knowledge and professional judgement and does not rely solely on historical transaction comparables. The critical estimates and assumptions underlying the valuation of investment properties and developments are set out in Note 5.

Fair Value of Financial Instruments
Where the fair value of financial assets and financial liabilities recorded in the consolidated balance sheet cannot be derived from active markets, they are determined using valuation techniques, including the discounted cash flow model. Inputs to these models are taken from observable markets where possible, but where this is not feasible a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Deferred Income Taxes
Uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to taxable income and expense already recorded.

Share Based Compensation
The compensation costs relating to the share based compensation are based on estimates of how many options or restricted units will actually vest and be exercised.

Future Accounting Policy Changes

IAS 1 Financial Statement Presentation — Presentation of Items of Other Comprehensive Income ("OCI")
The amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment becomes effective for annual periods beginning on or after July 1, 2012, and has no impact on the Company's financial position.

IFRS 9 Financial Instruments: Classification and Measurement ("IFRS 9")
IFRS 9 as issued reflects the first phase of the IASBs' work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard was initially effective for annual periods beginning on or after January 1, 2013, but Amendments to IFRS 9 Mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, moved the mandatory effective date to January 1, 2015. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Company's financial assets, but is not expected to have any impact on classification and measurements of financial liabilities.

IFRS 10 Consolidated Financial Statements ("IFRS 10")
IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements ("IAS 27") that addresses the accounting for consolidated financial statements. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require Management to exercise significant judgement to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27. This standard becomes effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of this amendment.

IFRS 11 Joint Arrangements ("IFRS 11")
IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities — Non-monetary Contributions by Venturers. IFRS 11 removes the option to account for jointly controlled entities using proportionate consolidation. Instead, joint arrangements that meet the definition of a joint venture must be accounted for using the equity method. Otherwise, joint arrangements are accounted for by recognizing the group's share of the arrangement's assets and liabilities. This standard becomes effective for annual periods beginning on or after January 1, 2013. The Company assessed the impact of the standard on its current joint ventures and does not anticipate any significant change to the current accounting on adoption of the standard.

IFRS 12 Disclosure of Involvement with Other Entities ("IFRS 12")
IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required, including:

- A requirement to disclose judgements made in determining if the Company controls, has joint control or significant influence over an entity, and
- A requirement to disclose judgements made in determining the type of joint arrangement in which the Company has an interest.

The Company will disclose its judgement in respect of the entities currently excluded from the consolidated financial statements that will be included due to the existence of potential voting rights held within the Company. This standard becomes effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of this amendment.

IFRS 13 Fair Value Measurement ("IFRS 13")
IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Company does not consider that the definition of fair value that is applied in IFRS 13 differs in a material way from its current approach and consequently anticipates there will not be any impact from this standard on its financial position. However, IFRS 13 does expand the disclosure requirements in respect of fair value measurement. In particular, the financial statements will in the future, as well as other disclosures, contain:

• An analysis of the fair value hierarchy for investment property (as well as for financial instruments — see Note 26 of the financial statements)
• Information about the sensitivity of fair value measurements to changes in unobservable estimation inputs, and,
• A detailed commentary on the Company's valuations methods and procedures
IFRS 13 becomes effective for annual periods beginning on or after January 1, 2013. The Company does not expect IFRS 13 to have a significant impact on its consolidated financial statements, but may result in more extensive disclosure in the financial statements.

Disclosure Controls and Procedures and Internal Controls

The Company's Management, including the Chief Executive Officer and the Chief Financial Officer, does not expect that the Company's Disclosure Controls and Procedures and Internal Controls will prevent or detect all error and all fraud. Because of the inherent limitations in all control systems, an evaluation of controls can provide only reasonable, not absolute, assurance that all control issues and instances of fraud or error, if any, within the Company have been detected.

Disclosure Controls and Procedures
As of December 31, 2012, the Company's Management evaluated the effectiveness of the operation of its disclosure controls and procedures ("Disclosure Controls"), as defined under rules adopted by the Canadian Securities Administrators. This evaluation was performed under the supervision of, and with the participation of, the Chief Executive Officer and the Chief Financial Officer.

Disclosure Controls and Procedures are designed to ensure that information required to be disclosed in documents filed with securities regulatory authorities is recorded, processed, summarized and reported on a timely basis, and is accumulated and communicated to the Company's Management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Based on the evaluation of Disclosure Controls, the Chief Executive Officer and the Chief Financial Officer have concluded that, subject to the inherent limitations noted above, the Company's Disclosure Controls are effective in ensuring that material information relating to the Company and its consolidated subsidiaries is made known to the Company's Management on a timely basis by others within those entities, and is included as appropriate in this MD&A.

Internal Controls over Financial Reporting
Internal controls over financial reporting ("ICFR") are designed to provide reasonable assurance regarding the reliability of the Company's financial reporting and its preparation of financial statements for external purposes in accordance with IFRS. Management's documentation and assessment of the effectiveness of the Company's ICFR continues as of the date of this MD&A with the focus on processes and controls in areas identified as being "key risks".

As of the financial year ended December 31, 2012, the certifying Officers have evaluated the design and effectiveness of such ICFR, or caused them to be designed and evaluated under their supervision. The certifying Officers have concluded that the design and effectiveness of ICFR were operating effectively as at December 31, 2012, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The certifying Officers have evaluated whether there were any changes to the Company's ICFR during the year ended December 31, 2012 that have materially affected, or are reasonably likely to materially affect its ICFR. No changes were identified through their evaluation.

Subsequent Events

On January 4, 2013, the Company repaid matured subordinated debentures, consisting of a $10 million payment.

On January 15, 2013, the Company acquired a 5.2 acre development site on Saginaw Parkway in Cambridge, Ontario. The purchase price of $4.1 million was satisfied with cash. The site is zoned for a maximum height of seven storeys and density of 180 units.

On January 18, 2013, and February 18, 2013, the Company announced dividends of $0.04833 per share, payable on February 15, 2013 and March 15, 2013, respectively, to shareholders of record on January 31, 2013 and February 28, 2013, respectively.

On January 25, 2013, the Company acquired a 102-unit apartment building in Ottawa, Ontario. The purchase price of $10.4 million was satisfied with cash.

On February 18, 2013, the Company acquired a 0.8 acre development site on St. George Blvd in Moncton, New Brunswick. The purchase price of $1.1 million was satisfied with cash.

On March 4, 2013, the Company acquired a new 83-unit luxury apartment building located at 200 Royale Boulevard in Halifax, Nova Scotia. The purchase price was $19.1 million and was satisfied with a new 10-year CMHC mortgage of $12.6 million at 3.03%, and the balance in cash.

Management's Responsibility for Financial Statements

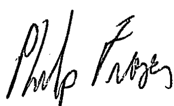
The accompanying consolidated financial statements and management's discussion and analysis of results of operations and financial condition (MD&A) have been prepared by the management of Killam Properties Inc. in accordance with International Financial Reporting Standards, and include amounts based on management's informed judgements and estimates. Management is responsible for the integrity and objectivity of these consolidated financial statements. The financial information presented in the MD&A is consistent with that in the consolidated financial statements in all material respects.

To assist management in the discharge of these responsibilities, management has established the necessary internal controls designed to ensure that our financial records are reliable for preparing financial statements and other financial information, transactions are properly authorized and recorded, and assets are safeguarded.

As at December 31, 2012, our Chief Executive Officer and Chief Financial Officer evaluated, or caused an evaluation under their direct supervision of, the design and operation of our internal controls over financial reporting (as defined in National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings) and, based on that assessment, determined that our internal controls over financial reporting were appropriately designed and operating effectively.

Ernst & Young LLP, the auditors appointed by the Shareholders, have examined the consolidated financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to the Shareholders their opinion on the consolidated financial statements. Their report as auditors is set forth below.

The consolidated financial statements have been further reviewed and approved by the Board of Directors and its Audit Committee. This committee meets regularly with management and the auditors, who have full and free access to the Audit Committee.



Philip Fraser
President and Chief Executive Officer
March 5, 2013

Robert Richardson
Chief Financial Officer

Independent Auditors' Report

To the Shareholders of Killam Properties Inc.

We have audited the accompanying consolidated financial statements of Killam Properties Inc., which comprise the consolidated statements of financial position as at December 31, 2012 and 2011 and the consolidated statements of income and comprehensive income, changes in equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

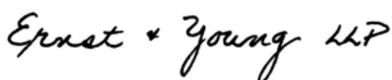
Management's responsibility for the consolidated financial statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Killam Properties Inc. as at December 31, 2012 and 2011 and its their financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.



Chartered Accountants

Halifax, Canada

March 5, 2013

Consolidated Statement of Financial Position

As at December 31,

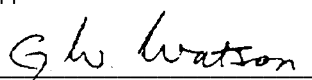
In thousands

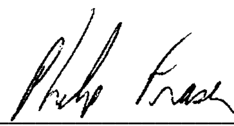
	Note	2012	2011
ASSETS			
Non-current assets			
Investment properties	[5]	**$ 1,354,665**	$ 1,258,219
Investments	[6]	**10,289**	8,420
Property and equipment	[7]	**4,574**	4,457
Other non-current assets		**45**	62
		1,369,573	1,271,158
Current assets			
Cash		**56,726**	43,348
Rent and other receivables	[8]	**3,767**	1,706
Income tax receivable		**36**	88
Inventory	[9]	**762**	960
Other current assets	[10]	**12,264**	12,271
		73,555	58,373
TOTAL ASSETS		**$ 1,443,128**	$ 1,329,531
EQUITY AND LIABILITIES			
Shareholders' equity		**$ 575,335**	$ 501,005
Non-controlling interest		**13,101**	11,538
TOTAL EQUITY		**588,436**	512,543
Non-current liabilities			
Mortgages and loans payable	[12]	**519,712**	565,683
Convertible debentures	[14]	**94,924**	93,549
Subordinated debentures	[15]	**-**	9,844
Other liabilities	[16]	**2,427**	2,682
Deferred tax	[22]	**83,871**	65,139
		700,934	736,897
Current liabilities			
Mortgages and loans payable	[12]	**105,369**	64,532
Construction loans	[13]	**14,062**	-
Subordinated debentures	[15]	**9,998**	-
Accounts payable and other liabilities	[11]	**24,329**	15,559
		153,758	80,091
TOTAL LIABILITIES		**854,692**	816,988
TOTAL EQUITY AND LIABILITIES		**$ 1,443,128**	$ 1,329,531

See accompanying notes to the consolidated financial statements.

Commitments (Note 27)

Approved on Behalf of the Board





G. Wayne Watson, Director Philip Fraser, Director

Consolidated Statements of Income and Comprehensive Income

For the Years Ended December 31

In thousands (except per share amounts),

	Note	2012	2011
Property revenue		**$ 133,641**	$ 126,089
Property operating expenses		**(53,197)**	(49,737)
Net rental income		**80,444**	76,352
Other income			
Home sales	[19]	**469**	486
Equity income	[6]	**758**	13
Corporate income	[20]	**962**	94
		2,189	593
Other expenses			
Financing costs	[21]	**(34,633)**	(34,891)
Depreciation		**(540)**	(301)
Amortization of deferred financing costs		**(1,605)**	(1,410)
Administration		**(8,832)**	(7,672)
		(43,421)	(43,681)
Income before fair value gains, loss on disposition and income taxes		**37,023**	32,671
Fair value gains		**37,726**	52,070
Loss on disposition		**(1,286)**	-
Income before income tax expense		**73,463**	84,741
Deferred tax expense	[22]	**(19,234)**	(17,920)
Net income and comprehensive income		**54,229**	66,821
Net income and comprehensive income attributable to:			
Common shareholders		**51,727**	65,965
Non-controlling interest		**2,502**	856
		$ 54,229	$ 66,821
Net income per share attributable to common shareholders			
- basic		**$ 1.03**	$ 1.45
- diluted		**$ 0.97**	$ 1.34

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Changes in Equity

In thousands

For the Years Ended December 31,

2012	**Share Capital**	**Contributed Surplus**	**Other Paid-in Capital**	**Retained Earnings**	**Non-Controlling Interest**	**Total Equity**
At January 1, 2012	**$ 339,178**	**$ 2,251**	**$ 5,681**	**$ 153,895**	**$ 11,538**	**$ 512,543**
Comprehensive income	**-**	**-**	**-**	**51,727**	**2,502**	**54,229**
Dividends	**-**	**-**	**-**	**(29,341)**	**-**	**(29,341)**
Acquisition of non-controlling interest	**-**	**-**	**-**	**12**	**(30)**	**(18)**
Distributions to non-controlling interest	**-**	**-**	**-**	**-**	**(909)**	**(909)**
Issuance of shares for cash	**32,877**	**-**	**-**	**-**	**-**	**32,877**
Dividend reinvestment plan	**4,367**	**-**	**-**	**-**	**-**	**4,367**
Stock options exercised	**4,195**	**(589)**	**-**	**-**	**-**	**3,606**
Tax benefit of share issuance costs	**503**	**-**	**-**	**-**	**-**	**503**
Warrants exercised	**10,000**	**-**	**-**	**-**	**-**	**10,000**
Share-based compensation	**-**	**579**	**-**	**-**	**-**	**579**
At December 31, 2012	**$ 391,120**	**$ 2,241**	**$ 5,681**	**$ 176,293**	**$ 13,101**	**$ 588,436**

2011	Share Capital	Contributed Surplus	Other Paid-in Capital	Retained Earnings	Non-Controlling Interest	Total Equity
At January 1, 2011	$ 293,966	$ 2,637	$ 4,271	$ 114,234	$ 11,933	$ 427,041
Comprehensive income	-	-	-	65,965	856	66,821
Dividends	-	-	-	(26,290)	-	(26,290)
Issuance of convertible debenture	-	-	1,410	-	-	1,410
Acquisition of non-controlling interest	-	-	-	(14)	(375)	(389)
Distributions to non-controlling interest	-	-	-	-	(876)	(876)
Issuance of shares for cash	38,299	-	-	-	-	38,299
Dividend reinvestment plan	2,976	-	-	-	-	2,976
Stock options exercised	3,441	(962)	-	-	-	2,479
Tax benefit of share issue costs	496	-	-	-	-	496
Share-based compensation	-	576	-	-	-	576
At December 31, 2011	$ 339,178	$ 2,251	$ 5,681	$ 153,895	$ 11,538	$ 512,543

See accompanying notes to the consolidated financial statements.

Consolidated Statement of Cash Flows

In thousands

For the Years Ended December 31,

	Note	**2012**	2011
OPERATING ACTIVITIES			
Net Income		**$ 54,229**	$ 66,821
Add (deduct) items not affecting cash:			
Fair value gains		**(37,726)**	(52,070)
Depreciation and amortization		**2,145**	1,711
Non-cash debenture interest		**950**	782
Non-cash compensation expense		**579**	576
Amortization of fair value adjustment on assumed debt		**(229)**	-
Equity income		**(758)**	(13)
Deferred income taxes		**19,234**	17,920
Loss on disposition		**1,029**	-
Financing costs	[21]	**34,633**	34,891
Interest paid	[25]	**(34,883)**	(34,282)
Net change in non-cash operating items	[25]	**6,824**	2,955
Cash provided by operating activities		**46,027**	39,291
FINANCING ACTIVITIES			
Increase in deferred financing		**(1,260)**	(5,052)
Proceeds on issuance of common shares		**46,486**	40,747
Proceeds on issuance of convertible debentures		**-**	46,000
Mortgage financings		**56,291**	95,956
Mortgages repaid on maturity		**(27,237)**	(43,630)
Mortgage principal repayments		**(18,829)**	(17,197)
Proceeds from construction loans		**14,062**	-
Distributions paid on non-controlling interest		**(909)**	(876)
Dividends		**(24,726)**	(23,135)
Cash provided by financing activities		**43,878**	92,813
INVESTING ACTIVITIES			
Decrease in restricted cash		**(65)**	(3,735)
Acquisition of non-controlling interest		**(17)**	(381)
Equity investments		**(1,112)**	(8,355)
Net proceeds on sale of investment properties		**34,326**	-
Acquisition and development of investment property, net of debt assumed		**(86,426)**	(75,156)
Capital expenditures		**(23,233)**	(18,046)
Cash used in investing activities		**(76,527)**	(105,673)
Net increase in cash		**13,378**	26,431
Cash, beginning of year		**43,348**	16,917
Cash, end of year		**$ 56,726**	$ 43,348

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements
Dollar amounts in thousands (except share and per share amounts)

1. Corporate Information

Killam Properties Inc. ("Killam") is a real estate company specializing in the acquisition, management and development of multi-residential apartment buildings and manufactured home communities in Canada. Killam is incorporated under the Canada Business Corporations Act. Killam's common shares are publicly traded and listed on the Toronto Stock Exchange under the symbol "KMP". The consolidated financial statements comprise the financial statements of Killam and its subsidiaries as at December 31, 2012. Together, Killam and its subsidiaries are referred to as "the Company." The Company's registered office and head office operations are located at 3700 Kempt Road, Halifax, Nova Scotia, B3K 4X8.

The consolidated financial statements of the Company for the period ended December 31, 2012 were authorized for issue in accordance with a resolution of the Directors on March 5, 2013.

2. Significant Accounting Policies

(A) Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

(B) Basis of Presentation

The consolidated financial statements of the Company have been prepared on an historical cost basis, except for investment properties that have been measured at fair value. Historical cost is generally based on the fair value of the consideration given in exchange for assets. The consolidated financial statements were prepared on a going concern basis and are presented in Canadian dollars, which is Killam's functional currency, and all values are rounded to the nearest thousand ($000) except when otherwise noted. Standards and guidelines not effective for the current accounting period are described in Note 4.

(C) Basis of Consolidation

(i) Subsidiaries

The consolidated financial statements include the accounts of Killam and its subsidiaries. Non-controlling interests represent the portion of profit or loss and net assets not held by Killam, and are presented separately in the Consolidated Statements of Income and Comprehensive Income and within equity in the Consolidated Statement of Financial Position, separately from shareholders' equity.

Subsidiaries are entities controlled by Killam. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by Killam. In certain circumstances, Killam has "de facto" control over entities in which it does not own more than 50% of the voting power. In its evaluation, management considers whether Killam controls the entity by virtue of the following circumstances:

a) Power over more than half of the voting rights by virtue of an agreement with other investors;
b) Power to govern the financial and operating policies of the entity under a statute or an agreement;
c) Power to appoint or remove the majority of the members of the board of directors or equivalent governing body and control of the entity is by that board or body;
d) Power to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interest even if that results in a deficit balance.

2. Significant Accounting Policies (continued)

(ii) Joint Arrangements

The Company has contractual arrangements with other parties which represent joint ventures. These take the form of agreements to share control over the entities.

Where a joint venture is established through an interest in a company (a jointly controlled entity), the Company recognises an interest in the entity's assets and liabilities using the equity method of accounting. Under the equity method, the interest in the joint venture is carried in the Consolidated Statement of Financial Position at cost plus post acquisition changes in the Company's share of the net assets, less distributions received and less any impairment in the value of individual investments.

(D) Property Asset Acquisitions and Business Combinations

Where property is acquired through the acquisition of corporate interests, management considers the substance of the assets and activities of the acquired entity in determining whether the acquisition represents the acquisition of a business. The basis of this judgemental assessment is set out in Note 3.

Where such acquisitions are not judged to be an acquisition of a business, they are not treated as business combinations. Rather, the cost to acquire the corporate entity is allocated between the identifiable assets and liabilities of the entity based on their relative fair values at the acquisition date and acquisition related transaction costs are capitalized to the property. Accordingly, no goodwill or additional deferred taxation arises.

None of Killam's acquisitions have been determined to be an acquisition of a business and therefore none are treated as a business combination.

(E) Revenue Recognition

(i) Rental income

Revenue from rental properties is recognized when a tenant commences occupancy of a rental unit or site and rent is due. Rental income from investment properties is recognized on a straight line basis over the lease term. The Company retains all of the benefits and risks of ownership of its rental properties and therefore accounts for leases with its tenants as operating leases.

Incentives for lessees to enter into lease agreements are spread evenly over the lease term, even if the payments are not made on such a basis. The lease term is the non-cancelable period of the lease.

(ii) Service charges and expenses recoverable from tenants

Income arising from expenses recharged to tenants is recognized in the period in which the expense can be contractually recovered. Revenue related to laundry and parking are included gross of the related costs.

(iii) Manufactured Home Sales

Where revenue is obtained from the sale of manufactured homes, it is recognized when the significant risks and rewards have been transferred to the buyer. This will normally take place on the closing date of the home sale. Such sales are considered sales of goods, and not sales of real estate, as the Company does not manufacture these homes itself.

(F) Investment Properties

Investment property includes multi-family residential properties and manufactured home communities held to earn rental income and properties that are under construction or development for future use as investment properties.

(i) Completed investment property

Investment properties are measured initially at cost, including transaction costs. Transaction costs include deed transfer taxes and various professional fees. Subsequent to initial recognition, investment properties are recorded at fair value. Fair value is determined based on a combination of internal and external processes and valuation techniques. Gains and losses arising from changes in fair values are included in the income statement in the year in which they arise.

2. Significant Accounting Policies (continued)

Investment property is derecognized when it has been disposed of or permanently withdrawn from use and no future economic benefit is expected. Any gains or losses on the retirement or disposal of investment property are recognized in the Statements of Income and Comprehensive Income in the year of retirement or disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by the commencement of operating leases. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of development.

(ii) Investment property under construction ("IPUC")

The cost of development properties includes direct development costs, realty taxes and borrowing costs directly attributable to the development. Under the requirements of International Accounting Standard 40 - Investment Property ("IAS 40"), investment property under construction is measured at fair value at each reporting date, with the recognition of gains or losses in the income statement. If the fair value of an investment property under construction is not reliably determinable, but the Company expects the fair value of the property to be reliably determinable when construction is complete, it measures that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed (whichever is earlier).

(iii) Borrowing costs related to property under construction

Although investment properties under construction are measured at fair value, Killam's policy is to present its Statements of Income as if borrowing costs related to the construction are capitalized. Borrowing costs directly attributable to the acquisition or construction of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are recorded as part of the cost of the respective assets. The interest is calculated using the Company's weighted average cost of borrowings after adjusting for borrowings associated with specific developments. Where borrowings are associated with specific developments, the amounts is the gross interest incurred on those borrowings less any investment income arising on their temporary investment. Interest is capitalized from the commencement of the development work until the date of substantial completion. The capitalization of borrowing costs is suspended if there are prolonged periods when development activity is interrupted. Interest is also capitalized on the purchase cost of a site or property acquired specifically for redevelopment but only where activities necessary to prepare the asset for redevelopment are in progress. The Company considers substantial completion to have occurred when the property is capable of operating in the manner intended by management.

(G) Property and Equipment

Property and equipment are stated at historical cost less accumulated depreciation and are mainly comprised of head office buildings, leasehold improvements and, corporate and IT technology systems. The estimated useful lives, residual values and depreciation method are reviewed at each year-end, with the effect of any changes in estimate accounted for on a prospective basis. These items are amortized on a straight-line basis over their estimated useful lives ranging as follows:

Building	40 years
Heavy equipment	15 years
Vehicles	10 years
Furniture, fixtures and office equipment	5-10 years
Leaseholds	Lease term

(H) Inventory

Inventory represents manufactured homes available for sale. The manufactured homes are valued at the lower of cost (purchase price plus delivery and set-up costs) and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business based on market prices at the reporting date less costs to complete and the estimated costs of sale.

(I) Cash

Cash is comprised of bank balances and interest-earning bank accounts.

2. Significant Accounting Policies (continued)

(J) Share-Based Compensation

The Company issues share-based awards to certain employees and non-employee directors whereby employees render services as consideration for equity instruments (equity-settled transactions).

The cost of equity-settled transactions is recognized, together with a corresponding increase in contributed surplus in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The Statements of Income expense or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and is recognized in employee benefits expense.

Where the terms of an equity-settled transaction award are modified, the minimum expense recognized is the expense as if the terms had not been modified, if the original terms of the award are met. An additional expense is recognized for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. This includes any award where non-vesting conditions within the control of either the entity or the employee are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph. All cancellations of equity-settled transaction awards are treated equally.

The dilutive effect of share based awards is reflected as additional share dilution in the computation of diluted earnings per share (further details are given in Note 23).

(K) Financial Assets and Liabilities

Financial instruments are accounted for, presented, and disclosed in accordance with IFRS 7 – Financial Instruments: Disclosures ("IFRS 7"), IAS 32 and IAS 39. The Company recognizes financial assets and financial liabilities when the Company becomes a party to a contract. Financial assets and financial liabilities, with the exception of financial assets classified at fair value through profit or loss, are measured at fair value plus transaction costs on initial recognition. Financial assets at fair value through profit or loss are measured at fair value on initial recognition and transaction costs are expensed when incurred.

Measurement in subsequent periods depends on the classification of the financial instrument as follows:

<u>Financial assets at fair value through profit or loss ("FVTPL")</u>

Financial assets are classified as FVTPL when acquired principally for the purpose of trading, if so designated by management (fair value option), or if they are derivative assets. Financial assets classified as FVTPL are measured at fair value, with changes recognized in the Consolidated Statements of Income and Comprehensive Income.

Loans and receivables

Loans and receivables are non-derivative financial assets that have fixed or determinable payments and are not quoted in an active market. Subsequent to initial recognition, loans and receivables are carried at amortized cost, using the effective interest method, less a provision for impairment. A provision for impairment is established when there is objective evidence that collection will not be possible under the original terms of the contract. Indicators of impairment include delinquency of payment and significant financial difficulty of the holder. The carrying amount of the financial asset is reduced through an allowance account, and the amount of the loss is recognized in the Consolidated Statements of Income and Comprehensive Income. Any subsequent reversal of an impairment loss is recognized in profit or loss.

<u>Financial liabilities at FVTPL</u>

Financial liabilities are classified as FVTPL if they are designated as such by management, or they are derivative liabilities. Financial liabilities classified as FVTPL are measured at fair value, with changes recognized in the Consolidated Statements of Income and Comprehensive Income.

2. Significant Accounting Policies (continued)

Other financial liabilities

Other financial liabilities are financial liabilities that are not classified as FVTPL. Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of an instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all transaction costs and other premiums or discounts) through the expected life of the debt instrument to the net carrying amount of the initial recognition.

Fair value measurements recognized in the Consolidated Statement of Financial Position are categorized using a fair value hierarchy that reflects the significance of inputs used in determining the fair values:

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Quoted prices in active markets for similar assets or liabilities or valuation techniques where significant inputs are based on observable market data.

Level 3: Valuation techniques for which any significant input is not based on observable market data.

Each type of fair value is categorized based on the lowest level input that is significant to the fair value measurement in its entirety. The following summarizes the Company's classification and measurement of financial assets and liabilities:

Financial Asset and Liability	Classification	Subsequent Measurement
Cash	Fair value through Profit and Loss	Fair Value
Rent and other receivables	Loans and Receivables	Amortized cost
Accounts payable and other liabilities	Other Financial Liabilities	Amortized cost
Mortgages, loans payable and construction loans	Other Financial Liabilities	Amortized cost
Convertible debentures	Other Financial Liabilities	Amortized cost
Subordinated debentures	Other Financial Liabilities	Amortized cost

(i) Mortgages and loans payable

Mortgages and loans payable are initially recognized at fair value less directly attributable transaction costs. After initial recognition, mortgages and loans payable are subsequently measured at amortized cost using the effective interest rate method.

Financing fees and other costs incurred in connection with debt financing are deducted from the cost of the debt and amortized using the effective interest rate method. Upon refinancing, any financing costs associated with previous mortgages are written off to income. Canadian Mortgage and Housing insurance premiums are amortized over the mortgage amortization period.

Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate calculation.

(ii) Financial guarantee contracts

Financial guarantee contracts issued by the Company are those contracts that require a payment to be made to reimburse the holder of the guarantee for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognized initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the balance sheet date and the initial amount recognized less cumulative amortization.

2. Significant Accounting Policies (continued)

(iii) Convertible Debentures

Convertible debentures are separated into liability and equity components based on the terms of the contract. On issuance of the convertible debenture, the fair value of the liability component is determined using a market rate for an equivalent non-convertible bond. This amount is classified as a financial liability measured at amortized cost (net of transaction costs) until it is extinguished on conversion or redemption. The remainder of the proceeds is allocated to the conversion option that is recognized and included in shareholders' equity. The carrying amount of the conversion option is not remeasured in subsequent years. Transaction costs are apportioned between the liability and equity components of the convertible debenture based on the allocation of proceeds to the liability and equity components when the instruments are initially recognized. Upon conversion, no gain or loss is recognized.

(L) Taxation

(i) Current income tax

Current income tax assets and liabilities are measured at the amount expected to be paid to tax authorities, net of recoveries, based on the tax rates and laws enacted or substantively enacted at the balance sheet date. Current income tax relating to items recognized directly in equity is recognized in equity and not profit or loss. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

(ii) Deferred income tax

Deferred income tax is provided using the liability method on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes, except where the temporary difference arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination that, at the time of the transaction, affects neither accounting nor taxable profit or loss.

Deferred income tax assets are recognized only to the extent that it is probable that taxable profit will be available against which deductible temporary differences, carried forward tax credits or tax losses can be utilized. The carrying value of deferred income tax assets are reviewed at each balance sheet date and reduced to the extent it is no longer probable that the income tax asset will be recovered.

The Company determines the deferred tax consequences associated with temporary differences relating to investment properties as if the carrying amount of the investment property is recovered entirely through sale.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax relating to items recognized directly in equity is recognized in equity and not in profit or loss.

3. Significant Accounting Judgments, Estimates and Assumptions

In the application of Killam's accounting policies, which are described in Note 2, Management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The judgments, estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements Other Than Estimates

In the process of applying the Company's accounting policies, management has made the following judgments, which have the most significant effect on the amounts recognized in the consolidated financial statements:

2. Significant Accounting Policies (continued)

Property Acquisitions

When investment properties are acquired, management considers whether the acquisition represents the acquisition of an asset or a business. The Company accounts for an acquisition as a business combination where an integrated set of activities is acquired in addition to the property. More specifically, consideration is made of the extent to which significant processes are acquired and, in particular, the extent of ancillary services provided by the subsidiary (e.g., maintenance, cleaning, security, bookkeeping, leasing operations, etc.). The significance of any process is judged with reference to the guidance in IAS 40 about ancillary services.

Management believes that the majority of the Company's acquisitions will be classified as asset acquisitions. During the acquisition of most properties, Killam buys the asset itself and any short-term leases that are in place. Generally, Killam does not purchase any business systems or processes with a property. Management considers an acquisition to be a business combination if all the following criteria are met:

- The acquisition includes a property portfolio (multiple buildings),
- A significant staff complement is included, including a maintenance team, leasing representatives and property management personnel, and
- Systems are acquired and continue to be incorporated into operations.

Investment Properties

The Company's accounting policies relating to investment properties are described in Note 2(F). In applying this policy, judgment is applied in determining whether certain costs are additions to the carrying amount of the property and, for properties under development, identifying the point at which substantial completion of the property occurs and identifying the directly attributable borrowing costs to be included in the carrying value of the development property. Judgment is also applied in determining the extent and frequency of independent appraisals.

Leases

The Company has entered into residential property leases on its investment property portfolio. The Company has determined, based on an evaluation of the terms and conditions of the arrangements, that it retains all the significant risks and rewards of ownership of these properties and so accounts for the contracts with tenants as operating leases.

Financial Instruments

The Company's accounting policies relating to financial instruments are described in Note 2(K). The critical judgments inherent in these policies relate to applying the criteria set out in International Accounting Standard 39 - Financial Instruments: Recognition and Measurement ("IAS 39") to designate financial instruments as FVTPL, assessment of the effectiveness of hedging relationships, determining whether the Company has significant influence over investees with which it has contractual relationships in addition to the financial instrument it holds and identification of embedded derivatives subject to fair value measurement in certain hybrid instruments.

Taxes

The Company is subject to income and capital gains taxes in numerous jurisdictions. Significant judgment is required to determine the total provision for current and deferred taxes. There are many transactions and calculations for which the ultimate tax determination and timing of payment is uncertain. In particular, when calculating deferred taxation, the effective tax rate applicable on the temporary differences in investment property depends on the method by which the carrying amount of investment property will be realised. The Company recognises liabilities for current taxes based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income and deferred tax provisions in the period in which the determination is made. Deferred tax assets and liabilities are recognized on a net basis to the extent they are relating to the same fiscal entity and fall due in approximately the same period.

3. Significant Accounting Judgments, Estimates and Assumptions (continued)

Estimates

Valuation of Investment Properties

The fair value of investment property is partially determined by independent real estate valuation experts (the "external valuator") using recognized valuation techniques and partially by Management. The external valuator uses the capitalization of net income method to determine the fair market value. In some cases, the fair values are corroborated by recent real estate transactions with similar characteristics and location to those of the Company's assets. Management's internal valuation model is also based on a capitalization of normalized net operating income ("NOI") by property, using property specific quarterly capitalization rates ("Cap-Rates"), provided by an independent qualified valuation professional.

IPUC is also valued at fair value, except if such values cannot be reliably determined. In the case when a fair value cannot be reliably determined, such property is recorded at cost. The fair value of IPUC is determined using the capitalization of net income.

The determination of the fair value of investment property requires the use of estimates such as future cash flows from assets and Cap-Rates applicable to those assets. In addition, development risks (such as construction and leasing risks) are also taken into consideration when determining the fair value of IPUC. These estimates are based on local market conditions existing at the reporting date. In arriving at their estimates of market values, the external valuator uses their market knowledge and professional judgement and does not rely solely on historical transaction comparables. The critical estimates and assumptions underlying the valuation of investment properties and developments are set out in Note 5.

Fair Value of Financial Instruments

Where the fair value of financial assets and financial liabilities recorded in the Consolidated Statement of Financial Position cannot be derived from active markets, they are determined using valuation techniques, including the discounted cash flow model. Inputs to these models are taken from observable markets where possible, but where this is not feasible a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Deferred Income Taxes

The amount of the temporary differences between the accounting carrying value of the assets and liabilities versus the tax bases of those assets and liabilities and the tax rates at which the differences will be realized are outline in Note 22.

Share-Based Compensation

The compensation costs relating to the share-based compensation are based on estimates of how many options or restricted units will actually vest and be exercised.

4. Future Accounting Policy Changes

IAS 1 Financial Statement Presentation — Presentation of Items of Other Comprehensive Income ("OCI")

The amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment becomes effective for annual periods beginning on or after July 1, 2012, and has no impact on the Company's financial position.

IFRS 9 Financial Instruments: Classification and Measurement ("IFRS 9")

IFRS 9 as issued reflects the first phase of the IASBs' work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard was initially effective for annual periods beginning on or after January 1, 2013, but Amendments to IFRS 9 Mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, moved the mandatory effective date to January 1, 2015. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The adoption of the first phase of IFRS 9 will have an affect on the classification and measurement of the Company's financial assets, but is not expected to have any impact on classification and measurements of financial liabilities. The Company is currently evaluating the impact of this amendment.

4. Future Accounting Policy Changes (contiuned)

IFRS 10 Consolidated Financial Statements ("IFRS 10")

IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements ("IAS 27") that addresses the accounting for consolidated financial statements. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require Management to exercise significant judgement to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27. This standard becomes effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of this amendment.

IFRS 11 Joint Arrangements ("IFRS 11")

IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities — Non-monetary Contributions by Venturers. IFRS 11 removes the option to account for jointly controlled entities using proportionate consolidation. Instead, joint arrangements that meet the definition of a Joint Venture must be accounted for using the equity method. Otherwise joint arrangements are accounted for by recognizing the group's share of the arrangements assets and liabilities. The Company assessed the impact of the standard on its current joint ventures and does not anticipate any significant change to the current accounting on adoption of the standard, which becomes effective for annual periods beginning on or after January 1, 2013.

IFRS 12 Disclosure of Interest in Other Entities ("IFRS 12")

IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required, including:

- A requirement to disclose judgements made in determining if the Company controls, has joint control or significant influence over an entity; and
- A requirement to disclose judgements made in determining the type of joint arrangement in which the Company has an interest.

The Company will disclose its judgement in respect to any entities currently excluded from the consolidated financial statements that will be included due to the existence of potential voting rights held within the Company.

This standard becomes effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of this amendment.

IFRS 13 Fair Value Measurement ("IFRS 13")

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Company does not consider that the definition of fair value that is applied in IFRS 13 differs in a material way from its current approach and consequently anticipates there will not be any impact from this standard on its financial position. However, IFRS 13 does expand the disclosure requirements in respect of fair value measurement. In particular, the financial statements will in the future, as well as other disclosures, contain:

- An analysis of the fair value hierarchy for investment property (as well as for financial instruments — see Note 26);
- Information about the sensitivity of fair value measurements to changes in unobservable estimation inputs; and
- A detailed commentary on the Company's valuations methods and procedures.

IFRS 13 becomes effective for annual periods beginning on or after January 1, 2013. The Company does not expect IFRS 13 to have a significant impact on its consolidated financial statements, but may result in more extensive disclosure in the financial statements.

5. Investment Properties

	2012	2011
(i) Investment properties	**$ 1,296,724**	$ 1,246,645
(ii) Investment properties under construction	**57,941**	11,574
	$ 1,354,665	$ 1,258,219

(i) Investment Properties

	2012			
	Apartments	MHCs	Other	Total
Balance, beginning of year	**$ 1,012,847**	**$ 231,747**	**$ 2,051**	**$ 1,246,645**
Acquisitions	**58,756**	**65**	**-**	**58,821**
Dispositions	**-**	**(72,889)**	**-**	**(72,889)**
Capital expenditures	**19,039**	**3,345**	**83**	**22,467**
Fair value gains	**35,547**	**6,133**	**-**	**41,680**
Balance, end of year	**$ 1,126,189**	**$ 168,401**	**$ 2,134**	**$ 1,296,724**

	2011			
Balance, beginning of year	$ 866,645	$ 215,133	$ -	$ 1,081,778
Acquisitions	91,347	2,591	2,032	95,970
Transfer to IPUC	(5,373)	-	-	(5,373)
Transfer from IPUC	4,691	-	-	4,691
Capital expenditures	12,569	4,921	19	17,509
Fair value gains	42,968	9,102	-	52,070
Balance, end of year	$ 1,012,847	$ 231,747	$ 2,051	$ 1,246,645

During the year ended December 31, 2012, the Company capitalized salaries of $2.0 million (2011 - $1.8 million) as part of its project improvement, suite renovation and development programs.

Investment properties with a fair value of $1,294,317 (December 31, 2011 - $1,241,773) are pledged as security against the Company's mortgages payable.

An independent valuation was completed by an accredited national appraisal firm for the entire investment property portfolio as at January 1, 2010. As at December 31, 2012, 18% of the portfolio was independently valued (2011 - 14%). The remaining properties of the portfolio were valued internally. Management's internal valuation model is based on a capitalization of normalized NOI by property using property specific quarterly Cap-Rates, provided by an external valuator. The Company determines the normalized NOI for each property based on current in-place rents and assumptions about occupancy, less cash outflows expected to operate and manage each property.

5. Investment Properties (continued)

Investment property valuations are most sensitive to changes in the Cap-Rate. The Cap-Rate assumptions for the investment properties are included in the following table:

	December 31, 2012			December 31, 2011		
	Low	**High**	**Effective Weighted Average**	Low	High	Effective Weighted Average
Apartments			**6.02%**			**6.19%**
Halifax	5.30%	7.00%	5.85%	5.70%	7.25%	6.07%
Moncton	6.00%	8.00%	6.30%	6.00%	8.00%	6.23%
Fredericton	5.75%	6.50%	6.30%	6.00%	7.25%	6.34%
Saint John	6.00%	6.75%	6.45%	6.00%	6.75%	6.51%
St. John's	6.25%	7.00%	6.36%	6.25%	7.00%	6.33%
Charlottetown	5.75%	6.50%	6.15%	6.00%	6.50%	6.43%
Ontario	4.50%	5.25%	5.25%	5.50%	5.50%	5.50%
Other	6.25%	7.00%	7.31%	6.30%	7.25%	7.44%
MHCs			**7.04%**			**7.28%**
Ontario	7.00%	8.50%	7.34%	7.25%	8.50%	7.48%
Nova Scotia	6.50%	7.50%	6.96%	6.75%	7.75%	7.16%
New Brunswick	6.50%	8.50%	6.87%	6.50%	9.40%	7.09%
Newfoundland	7.50%	7.50%	7.50%	7.50%	7.50%	7.50%

The impact of a 10 basis point change in the Cap-Rate used to value the investment properties would affect fair value as follows:

	December 31, 2012			December 31, 2011		
	Weighted Average	Increase	Decrease	Weighted Average	Increase	Decrease
Apartments	6.02%	$ 18,958	$ 18,338	6.19%	$ 16,251	$ 16,785
MHCs	7.04%	2,435	2,366	7.28%	3,126	3,213
Total		**$ 21,393**	**$ 20,704**		$ 19,377	$ 19,998

The impact of a 1% change in NOI used to value the investment properties would affect the fair value as follows:

	December 31, 2012	December 31, 2011
	Increase/ Decrease	Increase/ Decrease
Apartments	$ 11,220	$ 10,215
MHCs	1,688	2,309
Total	**$ 12,908**	$ 12,524

5. Investment Properties (continued)

(ii) Investment Properties under Construction

For the years ended December 31,	2012	2011
Balance, beginning of year	**$ 11,574**	$ 1,033
Capital expenditures	**47,284**	9,667
Interest capitalized	**1,063**	192
Transfers from investment properties	**-**	5,373
Transfers to investment properties	**-**	(4,691)
Fair value losses	**(1,980)**	-
Balance, end of year	**$ 57,941**	$ 11,574

Interest costs associated with the general corporate borrowings used to fund development have been capitalized to the respective developments throughout 2012 using the Company's weighted-average borrowing rate of 4.50%.

6. Investments

The Company has the following significant interest in joint ventures:
a) 25% share in the ownership of a 127-unit property located in London, Ontario.
b) 25% share in the ownership of a 140-unit property located in Ottawa, Ontario.
c) 25% share in the ownership of a 199-unit property located in Mississauga, Ontario.

For the years ended December 31,	2012	2011
Balance, beginning of year	**$ 8,420**	$ -
Additions	**19,563**	8,522
Share of net income	**758**	13
Distributions	**(18,452)**	(115)
Balance, end of year	**$ 10,289**	$ 8,420

The following tables illustrate the summarized financial information of the Company's three equity accounted joint ventures:

As at	2012	2011
Current assets	**$ 3,293**	$ 166
Long-term assets	**112,245**	33,850
Current liabilities	**(3,891)**	(338)
Long-term liabilities	**(70,492)**	-
Net assets	**41,155**	33,678
Company's share of net assets of associate	**$ 10,289**	$ 8,420

For the years ended December 31,	2012	2011
Property revenue	**$ 6,708**	$ 52
Property operating expenses	**(2,936)**	(1)
	3,772	51
Interest and deferred financing expense	**(857)**	-
Fair value gains	**120**	-
Net income and comprehensive income	**$ 3,035**	$ 51
Company's share of net income and comprehensive income	**$ 758**	$ 13

7. Property and Equipment

As at	December 31, 2012		December 31, 2011	
	Cost	**Accumulated Depreciation**	Cost	Accumulated Depreciation
Land	**$ 270**	**$ -**	$ 270	$ -
Building	**1,763**	**54**	1,762	-
Heavy equipment	**622**	**220**	760	214
Vehicles	**1,076**	**273**	1,067	191
Furniture, fixtures and equipment	**3,181**	**2,054**	2,701	1,698
Leaseholds	**261**	**-**	-	-
	7,173	**$ 2,601**	6,560	$ 2,103
Less: accumulated depreciation	**(2,599)**		(2,103)	
	$ 4,574		$ 4,457	

Land and building represents the Company's ownership of a 50% interest in the land and building which its head office occupies. Under IFRS, owner-occupied property is required to be accounted for as property and equipment and not investment property. Property with a fair value of $4.2 million (December 31, 2011 - $4.2 million) is pledged as security against the Company's mortgages payable.

For the years ended December 31,	**2012**	2011
Balance, beginning of year	**$ 4,457**	$ 2,189
Acquisition of properties	**-**	2,032
Disposals	**(107)**	-
Capital expenditures	**764**	537
Depreciation	**(540)**	(301)
Balance, end of year	**$ 4,574**	$ 4,457

8. Rent and Other Receivables

As at	**December 31, 2012**	December 31, 2011
Rent receivable	**$ 926**	$ 611
Insurance receivable	**254**	191
Other receivables	**2,587**	904
	$ 3,767	$ 1,706

Included in other receivables are accruals for HST refunds, laundry revenue, commission revenues and other non-rental income. The majority of these receivables are less than 60 days old.

The Company's policy is to write-off tenant receivables when the tenant vacates the unit and any subsequent receipt of funds is netted against bad debts. The Company's bad debt expense experience has historically been less than 0.4% of revenues. As a result of the low bad debt experience, no allowance for doubtful accounts is recorded in the accounts.

8. Rent and Other Receivables (continued)

Pursuant to their respective terms, tenant receivables are aged as follows:

As at	**December 31, 2012**	December 31, 2011
0-30 days	**$ 466**	$ 295
31-60 days	**158**	105
61-90 days	**5**	11
Over 90 days	**297**	200
Total	**$ 926**	$ 611

9. Inventory

Inventory relates to manufactured homes for which sales have not closed at year-end, as well as a eight stock homes and related expenses. As at December 31, 2012, no amount of the inventory is pledged as collateral related to short-term or long-term financing.

10. Other Current Assets

As at	**December 31, 2012**	December 31, 2011
Prepaid property tax	**$ 1,282**	$ 1,155
Prepaid insurance	**335**	336
Other prepaids	**668**	867
Restricted cash	**9,979**	9,913
	$ 12,264	$ 12,271

Restricted cash consists of security deposits, funds held in trust and property tax reserves.

11. Accounts Payable and Other Liabilities

As at	**December 31, 2012**	December 31, 2011
Accounts payable	**$ 7,450**	$ 4,725
Mortgage interest payable	**1,924**	2,082
Accrued payables	**7,606**	2,027
Rent received in advance	**808**	767
Dividends payable	**2,609**	2,389
Security deposits	**3,677**	3,314
Promissory note payable	**255**	255
	$ 24,329	$ 15,559

12. Mortgages and Loans Payable

As at	**December 31, 2012**		December 31, 2011	
	Weighted Average Interest	**Debt Balance**	Weighted Average Interest	Debt Balance
Mortgages and loans payable				
Fixed rate	**4.44%**	**$ 621,397**	4.63%	$ 627,016
Variable rate	**4.13%**	**2,802**	4.50%	778
Vendor financing	**6.85%**	**882**	6.69%	2,421
Total		**$ 625,081**		$ 630,215
Current		**105,369**		64,532
Non-current		**519,712**		565,683
		$ 625,081		$ 630,215

Mortgages are secured by a first charge on the properties of the Company and vendor mortgages are secured by either a second charge on the property and/or a general corporate guarantee.

As of December 31, 2012, unamortized deferred financing costs of $9.6 million (December 31, 2011 - $9.6 million) and mark-to-market premiums on mortgages assumed on acquisition of $1.7 million (December 31, 2011 – nil) are netted against mortgages and loans payable.

Estimated future principal payments required to meet mortgage obligations as at December 31, 2012 are as follows:

	Principal Repayments by Year
2013	$ 105,369
2014	144,987
2015	112,501
2016	112,041
2017	46,311
Subsequent	111,688
	632,897
Unamortized deferred financing costs	(9,561)
Unamortized mark-to-market adjustment	1,745
	$ 625,081

The Company has credit facilities set out as follows:

I. A credit facility with a major financial institution, which consists of a $2.0 million revolving demand facility that can be used for the Company's acquisition program and general business purposes. The interest rate on the debt is prime plus 125 basis points on prime rate advances or 225 basis points over Banker's Acceptances (BAs). Killam has the right to choose between prime rate advances and BAs based on available rates and timing requirements. As at December 31, 2012, the Company had assets with a fair value of $1.6 million pledged to the line and had a balance outstanding of $Nil.

II. An operating facility which consists of a $1.0 million revolving demand facility for general business purposes, bearing interest at the lender's prime rate plus 1%. As at December 31, 2012, the Company had letters of credit totaling $0.3 million outstanding against this facility (December 31, 2010 - $0.4 million). The agreement includes certain covenants and undertakings of which the Company is in compliance.

13. Construction Loans

The Company has access to four floating rate non-revolving demand construction loans totaling $37.9 million for the purpose of financing the development of its investment properties under construction, located in Halifax, Charlottetown, Fredericton, and St. John's. Payments are made monthly on an interest-only basis. The construction loans have interest rates ranging from prime to prime plus 1%. The construction loans will be repaid in full and converted into conventional mortgages once construction has been completed. As at December 31, 2012, $14.1 million was drawn at a weighted average interest rate of 3.68% (December 31, 2011 - $ Nil).

14. Convertible Debentures

Face Interest Rate %	Effective Interest Rate %	Conversion Price	Face Amount	Maturity	**December 31, 2012**	December 31, 2011
5.65%	7.3%	$13.40	$ 57,500	November 30, 2017	**$ 53,733**	$ 53,115
5.45%	6.3%	$14.60	$ 46,000	June 30, 2018	**44,309**	44,059
					98,042	97,174
Less: Deferred financing charges					**(3,118)**	(3,625)
					$ 94,924	$ 93,549

Killam's $57.5 million convertible subordinated debentures are redeemable at the option of Killam after November 30, 2013, and on or before November 30, 2015 (provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is not less than 125% of the conversion price). After November 30, 2015, the debentures are redeemable at face value. Upon maturity or redemption, Killam may elect to repay all or any portion of the debentures outstanding by issuing the number of common shares obtained by dividing the aggregate of the principal amount of the debentures that have matured or are being redeemed by 95% of the weighted average market price of the common shares for the preceding 20 days (ending 5 days preceding the fixed date for redemption or maturing). At the time of issuance, the fair value of Killam's obligation to make principal and interest payments was $52.5 million and the fair value of the holders' conversion option was $5.0 million (which is reflected in "Other paid-in capital"). The effective rate of interest on the liability component, which is paid semi-annually, is calculated at 7.3%.

Killam's $46.0 million convertible subordinated debentures are redeemable at the option of Killam after June 30, 2014, and on or before June 30, 2016 (provided that the current market price of the common shares of the Company on the date on which the notice of redemption is given is not less than 125% of the conversion price). After June 30, 2016, the debentures are redeemable at face value. Upon maturity or redemption, Killam may elect to repay all or any portion of the debentures outstanding by issuing the number of common shares obtained by dividing the aggregate of the principal amount of the debentures that have matured or are being redeemed by 95% of the weighted average market price of the common shares for the preceding 20 days (ending 5 days preceding the fixed date for redemption or maturing). At the time of issuance, the fair value of Killam's obligation to make principal and interest payments was $43.9 million and the fair value of the holders' conversion option was $2.1 million (which is reflected in "Other paid-in capital"). The effective rate of interest on the liability component, which is paid semi-annually, is calculated at 6.3%.

15. Subordinated Debentures

Killam's unsecured subordinated debentures mature January 4, 2013, and consist of the following:

Face Interest Rate %	Effective Interest Rate %	Face Amount	**December 31, 2012**	December 31, 2011
5.92%	6.46%	$ 2,500	**$ 2,500**	$ 2,482
6.06%	6.62%	2,500	**2,500**	2,482
6.33%	7.10%	5,000	**4,998**	4,953
			$ 9,998	$ 9,917
Less: Deferred financing charges			**-**	(73)
Current			**$ 9,998**	-
Long-term			**-**	$ 9,844

Killam calculated the fair value of warrants issued in conjunction with the subordinated debentures as $0.9 million. This amount is reflected in "Other paid-in capital". The weighted average effective interest rate on the remaining liability component of the debentures is calculated at 6.8%.

The following table summarizes the warrants outstanding issued in conjunction with the subordinated debentures:

As at	**December 31, 2012**		December 31, 2011	
Exercise Price	**Number of Warrants Outstanding**	**Remaining Contractual Life**	Number of Warrants Outstanding	Remaining Contractual Life
$14.40	**347,222**	**0.01 years**	347,222	1.01 years
$15.20	**328,947**	**0.01 years**	328,947	1.01 years
$12.24	**-**	**-**	816,993	1.01 years
	676,169		1,493,162	

16. Other liabilities

As at	**December 31, 2012**	December 31, 2011
Promissory notes payable	**$ 2,682**	$ 2,937
Less: current portion	**(255)**	(255)
	$ 2,427	$ 2,682

Promissory notes payable relate to amounts received in advance from governmental agencies in relation to rental subsidy agreements. Killam records the forgiveness of the notes into income on a monthly basis as the amounts are earned.

17. Capital Stock and Contributed Surplus

Capital Stock

Authorized:

Unlimited number of common shares, with no par value

Unlimited number of preferred shares, issuable in series, with no par value

Issued:

The following table summarizes the changes in issued common shares of the Company:

For the years ended December 31,	**2012**		2011	
	Number of Shares	**Value**	Number of Shares	Value
Balance, beginning of year	**49,290,751**	**$ 339,178**	44,971,566	$ 293,966
Issued for cash (i)	**2,875,000**	**32,877**	3,744,400	38,299
Dividend reinvestment plan (ii)	**347,473**	**4,367**	284,843	2,976
Stock options exercised	**471,593**	**4,195**	289,942	3,441
Warrants exercised	**816,992**	**10,000**	-	-
Tax benefit of issuance costs	**-**	**503**	-	496
Balance, end of year	**53,801,809**	**$ 391,120**	49,290,751	$ 339,178

(i) Net of issue costs of $1,616 (2011 - $1,953)

(ii) Net of issue costs of $29 (2011 - $31)

Issuance of Common Shares

On December 10, 2012, Killam completed a public offering of 2,875,000 common shares for gross proceeds of $34.5 million.

Dividends

Killam paid monthly dividends as declared by the Board of Directors on or about the 15th day of each month. An annualized dividend of $0.58 was paid in 2012.

Dividend Reinvestment Plan

Killam's Dividend Reinvestment Plan ("DRIP") allows common shareholders to elect to have all cash dividends from Killam reinvested in additional common shares. Shareholders who participate in the DRIP receive an additional dividend of common shares equal to 3% of each cash dividend that was reinvested. The price per share is calculated by reference to a ten day volume weighted-average closing price of Killam's common shares on the Toronto Stock Exchange preceding the relevant dividend date, which typically is on or about the 15th day of the month following the dividend declaration.

Contributed Surplus

For the years ended December 31,	**2012**	2011
Balance, beginning of year	**$ 2,251**	$ 2,637
Stock options expensed	**116**	285
Stock options exercised	**(589)**	(962)
Restricted share units expensed	**463**	291
Balance, end of year	**$ 2,241**	$ 2,251

18. Share-Based Compensation

Share based compensation expense for the years ended December 31, 2012 and 2011 is as follows:

For the years ended December 31,	**2012**	2011
Stock option plan	**$ 116**	$ 285
Restricted share unit plan	**463**	291
Total share based compensation expense	**$ 579**	$ 576

As of December 31, 2012, Killam is no longer issuing stock options.

Stock Option Plan

Under the terms of the stock option plan:

(i) from time to time Killam designates eligible participants to whom options will be granted, and the number of shares to be optioned to each;

(ii) eligible participants are persons who are employees, officers, directors and consultants of Killam;

(iii) shares to be optioned shall not exceed 2,125,000 (December 31, 2011 – 2,125,000) and the total number of shares to be optioned to any eligible participant shall not exceed 10% of the issued and outstanding shares of the class as at the date such option is granted;

(iv) the option price for the shares is determined at the time of granting of the option but cannot be less than the fair market value of the shares at the time the option is granted less any applicable discount permitted by the Toronto Stock Exchange;

(v) the term during which any option granted may be exercised is determined by Killam at the time the option is granted but may not exceed the maximum period permitted from time to time by the Toronto Stock Exchange; and

(vi) the options issued after January 1, 2009 vest 20% immediately upon the grant date and 20% during each subsequent anniversary. The options issued prior to this date vest 20% at each anniversary date. Another requirement for vesting is the employee or director is still providing services to Killam. Any employee/director leaving prior to vesting of a tranche forfeits the right to such options.

Options granted, exercised and forfeited during the years ended December 31 are as follows:

	2012		2011	
For the year ended December 31,	**Number of Shares**	**Weighted Average Exercise Price**	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of year	**1,180,766**	**$7.49**	1,471,625	$7.70
Exercised	**(471,593)**	**$7.65**	(289,942)	$8.55
Forfeited	**(14,417)**	**$7.00**	(917)	$9.60
Outstanding, end of year	**694,756**	**$7.40**	1,180,766	$7.49

18. Share Based Compensation (Continued)

The following table summarizes the stock options outstanding:

As at	**December 31, 2012**			December 31, 2011		
Exercise Price	**Number of Options Outstanding**	**Remaining Contractual Life**	**Options Exercisable**	Number of Options Outstanding	Remaining Contractual Life	Options Exercisable
$5.32	**186,749**	**1.35 years**	**155,502**	264,251	2.33 years	149,504
$7.94	**-**	**-**	**-**	28,175	0.54 years	22,841
$8.03	**-**	**-**	**-**	137,500	1.42 years	126,042
$8.06	**-**	**-**	**-**	137,500	0.63 years	119,167
$8.11	**1,250**	**0.10 years**	**1,208**	1,250	1.09 years	958
$8.16	**506,757**	**2.40 years**	**326,366**	611,882	3.42 years	294,091
$10.04	**-**	**-**	**-**	208	0.25 years	125
	694,756		**483,076**	1,180,766		712,728

As at December 31, 2012, the exercisable options had a weighted average exercise price of $7.25 (2011 - $7.52).

Restricted Share Unit Plan

The Restricted Share Unit Plan ("RSU") gives members of the senior executive team the right to receive a percentage of their annual bonus, and non-executive members of the board of directors, the right to receive a percentage of their annual retainer in the form of restricted shares in lieu of cash. The Compensation Committee has established the following parameters on the percentage of the annual bonus and annual retainer which may be allocated to Restricted Units:

	Minimum	Maximum
Non-executive board members	0%	100%
Chief Executive Officer and Chief Financial Officer	33%	33%
Other executives	25%	50%

Killam will match the elected amount in the form of Restricted Shares having a value equal to the volume weighted average price of all common shares traded on the TSX for the five trading days immediately preceding the date on which the compensation is payable. The Restricted Shares earn notional dividends based on the same dividends paid on the common shares, and such notional dividends are used to acquire additional Restricted Shares. The initial Restricted Shares and Restricted Shares acquired through notional dividend reinvestment are credited to each person's Restricted Share account and are not issued to the employee or board member until they redeem such Restricted Shares.

The Restricted Shares will be redeemed and paid out by December 31 of the year in which the Restricted Shares have vested. The Restricted Shares shall vest with the following schedule; (a) 50% on the second anniversary of the date such Restricted Shares were granted; and (b) 50% on the third anniversary of the date the Restricted Shares were granted.

The details of the Restricted Shares issued under the RSU are shown below:

For the years ended December 31,	**2012**		2011	
	Number of Shares	**Weighted Average Issue Price**	Number of Shares	Weighted Average Issue Price
Outstanding, beginning of year	**48,082**	**$ 10.96**	-	$ -
Granted	**49,265**	**12.84**	47,346	10.96
Additional restricted share distributions	**2,862**	**11.34**	736	10.80
Outstanding, end of year	**100,209**	**$ 11.89**	48,082	$10.96

19. Home Sales

For the years ended December 31,	**2012**	2011
Home sales revenues	**$ 2,241**	$ 4,229
Cost of home sales	**(1,789)**	(3,705)
New home placement fees	**98**	56
Operating expenses	**(81)**	(94)
Income from home sales	**$ 469**	$ 486

20. Corporate Income

For the years ended December 31,	**2012**	2011
Property management fees	**$ 363**	$ 81
Interest and other revenue	**599**	13
	$ 962	$ 94

21. Financing Costs

For the years ended December 31,	**2012**	2011
Mortgage, loans payable and construction loans	**$ 28,590**	$ 29,038
Amortization of fair value adjustments on assumed debt	**(229)**	-
Convertible debenture interest	**6,632**	5,357
Subordinated debenture interest	**703**	688
Capitalized interest	**(1,063)**	(192)
	$ 34,633	$ 34,891

22. Income Taxes

The income tax provisions differ from that computed using the statutory rates for the following reasons:

For the years ended December 31,	**2012**		2011	
Net income before income taxes	**$ 73,463**		$ 84,741	
Income tax expense at federal statutory rates	**21,069**	**28.7%**	25,677	30.3%
Non-taxable component of fair value gain	**(3,209)**	**(4.4)%**	(7,399)	(8.7)%
Non-deductible share compensation	**166**	**0.2%**	174	0.2%
Impact of change in effective tax rates	**578**	**0.8%**	(635)	(0.7)%
Other	**630**	**0.9%**	103	0.1%
Deferred tax expense	**$ 19,234**	**26.2%**	$ 17,920	21.1%

Deferred income taxes reflect the net effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred income tax assets and liabilities are as follows:

	Consolidated Statement of Financial Position		Consolidated Statements of Income	
	2012	2011	**2012**	2011
Real estate properties	**$ 86,980**	$ 64,370	**$ 22,610**	$ 14,043
Loss carryforwards	**(3,884)**	-	**(3,884)**	3,613
Convertible debentures	**1,565**	1,796	**(231)**	(163)
Other	**(790)**	(1,027)	**739**	427
Net deferred tax expense			**$ 19,234**	$ 17,920
Net deferred tax liabilities	**$ 83,871**	$ 65,139		

Reconciliation of net deferred tax liabilities	**2012**	2011
Balance, beginning of year	**65,139**	47,137
Recognized in statement of income	**19,234**	17,920
Recognized in equity:		
on issuance of shares	**(502)**	(496)
on issuance of convertible debentures	**-**	578
Balance, end of year	**$ 83,871**	$ 65,139

The temporary differences associated with investments in subsidiaries for which a deferred tax liability has not been recognized, aggregate to $65,186, (December 31, 2011 - $9,709).

23. Per Share Information

The following are the weighted average number of shares outstanding for the years ended December 31, 2012 and 2011. The fully diluted amounts shown below exclude stock options and warrants whose exercise price exceeded the average market price for the period and are considered anti-dilutive.

For the years ended December 31,	**2012**	2011
Weighted average shares outstanding - basic	**50,226,973**	45,523,031
Unexercised dilutive options	**506,233**	423,392
Restricted share units	**63,869**	14,833
Convertible debentures	**7,441,730**	6,128,943
Weighted average shares outstanding - diluted	**58,238,805**	52,090,199
Calculation of Numerator for Diluted Share Amounts		
Net income applicable to common shareholders	**$ 51,727**	$ 65,965
Adjustment for dilutive effect of convertible debentures	**4,642**	3,697
Numerator for diluted per share amounts	**$ 56,369**	$ 69,662

24. Segmented Information

The Company operates in two rental segments of the multi-family residential industry: apartments and MHCs, all located in Canada. The Company also operated in the manufactured home sales segment; information on this segment is provided in the Consolidated Statements of Income and Comprehensive Income and Note 19.

The accounting policies of these segments are the same as those described in the summary of significant accounting policies. The segments are analyzed based on income from property operations before interest and amortization. The operating results and capital assets of the segments are set out as follows:

As at and for the years ended December 31, 2012,	**Apartments**	**MHCs**	**Other**	**Total**
Property revenue	**$ 110,464**	**$ 22,653**	**$ 524**	**$ 133,641**
Property operating expenses	**(44,510)**	**(8,421)**	**(266)**	**(53,197)**
Property operating income	**$ 65,954**	**$ 14,232**	**$ 258**	**$ 80,444**
Home sales, equity income & corporate income	**-**	**-**	**2,189**	**2,189**
Financing costs	**(22,954)**	**(5,036)**	**(6,643)**	**(34,633)**
Depreciation and amortization	**(846)**	**(559)**	**(740)**	**(2,145)**
Administration	**(1,710)**	**(461)**	**(6,661)**	**(8,832)**
Income before fair value gains, loss on disposition and income taxes	**$ 40,444**	**$ 8,176**	**$ (11,597)**	**$ 37,023**
Total assets	**$ 1,244,087**	**$ 188,834**	**$ 10,207**	**$ 1,443,128**
Total liabilities	**$ 585,050**	**$ 84,148**	**$ 185,494**	**$ 854,692**
Capital expenditures	**$ 19,039**	**$ 3,345**	**$ 83**	**$ 22,467**

24. Segmented Information (Continued)

As at and for the years ended December 31, 2011	Apartments	MHCs	Other	Total
Property revenue	$ 100,301	$ 25,710	$ 78	$ 126,089
Property operating expenses	(40,694)	(9,005)	(38)	(49,737)
Property operating income	59,607	16,705	40	76,352
Home sales, equity income & corporate income	-	-	593	593
Financing costs	(22,289)	(6,520)	(6,082)	(34,891)
Depreciation and amortization	(761)	(285)	(665)	(1,711)
Administration	(1,348)	(475)	(5,849)	(7,672)
Income before fair value gains and income taxes	$ 35,209	$ 9,425	$ (11,963)	$ 32,671
Total assets	$ 1,071,445	251,069	7,017	$ 1,329,531
Total liabilities	$ 527,177	107,898	181,913	$ 816,988
Capital expenditures	$ 12,569	$ 4,921	$ 19	$ 17,509

The apartment segment is further analyzed on property revenue, property operating expenses and fair value of investment property by region:

2012	**Property Revenue**	**Property Operating Expenses**	**Property Operating Income**	**Fair Value of Investment Properties**
Halifax, NS	**$ 50,555**	**$ (18,406)**	**$ 32,149**	**$ 555,778**
Moncton, NB	**13,113**	**(6,465)**	**6,648**	**114,712**
Fredericton, NB	**12,626**	**(5,548)**	**7,078**	**101,290**
Saint John, NB	**9,719**	**(5,104)**	**4,615**	**69,481**
St. John’s, NL	**6,692**	**(2,196)**	**4,496**	**81,712**
Charlottetown, PE	**6,765**	**(2,742)**	**4,023**	**68,778**
Ontario	**6,926**	**(2,214)**	**4,712**	**109,195**
Other Atlantic	**4,068**	**(1,835)**	**2,233**	**25,243**
	$ 110,464	**$ (44,510)**	**$ 65,954**	**$ 1,126,189**

24. Segmented Information (Continued)

2011	Property Revenue	Property Operating Expenses	Property Operating Income	Fair Value of Investment Properties
Halifax, NS	$ 45,475	$ (17,206)	$ 28,269	$ 478,895
Moncton, NB	11,294	(5,504)	5,790	115,707
Fredericton, NB	11,026	(4,818)	6,208	99,009
Saint John, NB	9,839	(4,967)	4,872	70,526
St. John’s, NL	5,802	(1,955)	3,847	74,960
Charlottetown, PE	6,560	(2,583)	3,977	64,039
Ontario	6,096	(1,848)	4,248	83,581
Other Atlantic	4,209	(1,813)	2,396	26,130
	$ 100,301	$ (40,694)	$ 59,607	$ 1,012,847

There are no transactions with a single tenant that account for 10% or more of the Company’s total revenues.

25. Supplemental Cash Flow Information

Year ended December 31,	**2012**	2011
Net income items related to investing and financing activities		
Interest paid on mortgages payable and other	**$ 28,511**	$ 28,961
Interest paid on convertible debentures	**5,756**	4,705
Interest paid on subordinated debentures	**616**	616
	$ 34,883	$ 34,282
Changes in non-cash operating assets and liabilities		
Rent and other receivables	**$ (2,061)**	$ 2,908
Income tax receivable	**53**	(51)
Inventory	**197**	670
Prepaids and other	**73**	(462)
Accounts payable and other liabilities	**8,562**	(110)
	$ 6,824	$ 2,955

26. Financial Risk Management Objectives and Policies

The Company’s principal financial liabilities are comprised of mortgages, construction loans, debentures and trade payables. The main purpose of these financial liabilities is to finance the Company’s investment properties and operations. The Company has various financial assets such as trade receivables and cash which arise directly from its operations.

The Company my also enter into derivative transactions, primarily natural gas and oil swap contracts, to manage the price risk arising from fluctuations in these commodities. The Company did not enter into any derivative transactions in 2012 or 2011. It is, and has been, the Company’s policy that no speculative trading in derivatives shall be undertaken.

The main risks arising from the Company’s financial instruments are interest rate risk, credit risk, and liquidity risk. These risks are managed as follows:

26. Financial Risk Management Objectives and Policies (Continued)

(i) Interest rate risk

The Company is exposed to interest rate risk as a result of its mortgages and loan payable, however this risk is mitigated through the Company's strategy to have the majority of its mortgages payable in fixed-term arrangements. The Company also structures its financings so as to stagger the maturities of its debt, minimizing the Company's exposure to interest rate volatility in any one year.

As at December 31, 2012, no mortgages or vendor debt had floating interest rates except for two demand loans for $2.8 million. These loans have an interest rate of prime plus 1.0% - 1.5% (December 31, 2011 - 1.5%). During 2012, Killam obtained construction loans of $14.1 million with floating interest rates ranging from prime to prime plus 1% and consequently, Killam was exposed to short-term interest rate risk on these loans.

An annualized 1% change in the interest rate on Killam's entire mortgage and vendor debt at December 31, 2012 would affect financing costs by approximately $6.3 million per year. However, only $88.8 million of Killam's mortgage and vendor debt matures in the next twelve months and assuming these mortgages are refinanced at similar terms, but at a 1% higher interest rate, this would impact the Company by $0.9 million per year.

(ii) Credit risk

Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease term commitments. The Company mitigates the risk of credit loss through the diversification of its existing portfolio and limiting its exposure to any one tenant. Credit assessments are conducted with respect to all new leasing and the Company also obtains a security deposit to assist in potential recovery requirements. In addition, the receivable balances are monitored on an ongoing basis with the result that the Company's exposure to bad debt is not significant. The Company's bad debt expense experience has historically been less than 0.4% of revenues. None of Killam's tenants account for more than 1% of the tenant receivables as at each of the period-ends presented in these financial statements. The maximum exposure to credit risk is the carrying amount of each class of financial assets as disclosed in this note.

(iii) Liquidity risk

Senior Management manages the Company's cash resources based on financial forecasts and anticipated cash flows. The maturities of the Company's long-term financial liabilities are set out in Notes 12 to 16 of the consolidated financial statements. The Company structures its financings so as to stagger the maturities of its debt, thereby minimizing the Company's exposure to liquidity risk in any one year. In addition, the Company's apartments qualify for Canada Mortgage and Housing Corporation ("CMHC") insured debt, reducing the refinancing risk on mortgage maturities. The Company's MHCs do not qualify for CMHC insured debt, however, they continue to have access to mortgage debt. Management does not expect to be faced with liquidity concerns on the maturity of its mortgages as funds continue to be accessible in the multi-residential sector.

During the year ended December 31, 2012, the Company refinanced $21.6 million of maturing apartment mortgages with new mortgages totaling $28.4 million for net proceeds of $6.8 million and refinanced $10.2 million of maturing MHC mortgages for net proceeds of $4.0 million. In addition, the Company placed mortgages on unencumbered apartment and MHC properties of $5.0 million and $1.2 million, respectively.

The following table presents the contractual maturities of the Company's liabilities over the next five years:

Year	Mortgage and Loans Payable	Construction Loans	Convertible Debentures	Subordinated Debentures	December 31 Total
2013	$ 105,369	$ 14,062	$ -	$ 10,000	**$ 129,431**
2014	144,987	-	-	-	**144,987**
2015	112,501	-	-	-	**112,501**
2016	112,041	-	-	-	**112,041**
2017	46,311	-	57,500	-	**103,811**
Thereafter	111,688	-	46,000	-	**157,688**
	$ 632,897	$ 14,062	$ 103,500	$ 10,000	**$ 760,459**

26. Financial Risk Management Objectives and Policies (Continued)

Capital Management

The primary objective of the Company's capital management is to ensure that it maintains a healthy capital ratio in order to support its business and maximize shareholder value. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the dividend payment to shareholders, issue new shares, issue debt securities or adjust mortgage financing on properties.

The Company monitors capital using a total debt to total assets ratio. The Company's strategy is to maintain its total debt to total assets ratio between 55-65%. The calculation of the total debt to total assets is summarized as follows:

As at	**December 31, 2012**	December 31, 2011
Mortgages, loans payables and construction loans	**$ 639,143**	$ 630,215
Convertible debentures	**94,924**	93,549
Subordinated debentures	**9,998**	9,844
Total debt	**$ 744,065**	$ 733,608
Total assets	**$ 1,443,128**	$ 1,329,531
Total debt as a percentage of total assets	**51.6%**	55.2%

The above calculation is sensitive to changes in the fair value of investment properties, in particular, Cap-Rate changes. A 10 basis point increase in weighted average Cap-Rate as at December 31, 2012 would increase the debt as a percentage of assets by 80 basis points.

Fair Value

Financial instruments are defined as a contractual right or obligation to receive or deliver cash or another financial asset. The fair values of the Company's financial instruments, except for mortgages and loans payable, approximate their recorded values at December 31, 2012 and December 31, 2011 due to their short-term nature and or the credit terms of those instruments. The following table presents the classification, subsequent measurement, carrying values and fair values (where available) of the Company's financial assets and liabilities.

		December 31, 2012		December 31, 2011	
Classification	Subsequent Measurement	**Carrying Value**	**Fair Value**	Carrying Value	Fair Value
Other Financial Liabilities:					
Mortgages (b)	Amortized cost	**$ 625,081**	**$ 687,119**	$ 630,215	$ 743,179
Convertible debentures (a)	Amortized cost	**$ 98,042**	**$ 102,942**	$ 97,174	$ 99,201
Subordinated debentures (b)	Amortized cost	**$ 9,998**	**$ 10,104**	$ 9,917	$ 10,018

Cash and cash equivalents and derivative instrument liabilities are classified as held for trading and carried at their fair values.

The Company's short-term financial instruments, comprising amounts receivable, restricted cash, accounts payable and accrued liabilities, security deposits, and construction loans are carried at amortized cost which, due to their short-term nature, approximates their fair value.

(a) The fair value of the convertible debentures are based on quoted market price as at the balance sheet date.

(b) Long-term financial instruments include mortgages, convertible debentures, and subordinated debentures. The fair values of these financial instruments are based upon discounted future cash flows using discount rates that reflect current market conditions for instruments with similar terms and risks. Such fair value estimates are not necessarily indicative of the amounts the Company might pay or receive in actual market transactions.

26. Financial Risk Management Objectives and Policies (Continued)

The interest rates used to discount the estimated cash flows, when applicable, are based on the Government yield curve at the reporting date, plus an adequate credit spread, and were as follows:

As at	**December 31, 2012**	December 31, 2011
Mortgages - Apartments	**2.27%**	2.07%
Mortgages - MHCs	**4.02%**	3.97%
Subordinated debentures	**5.50%**	5.45%

The Company uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation techniques:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.

Level 2: other techniques for which all inputs that have a significant effect on the recorded fair value are observable, either directly or indirectly.

Level 3: techniques which use inputs that have significant effect on the recorded fair value that are not based on observable market data.

As at December 31, 2012 or 2011, the Company did not have any financial assets or liabilities measured at fair value on the Consolidated Statement of Financial Position.

27. Commitments

As at December 31, 2012, Killam has commitments related to its four development projects of $16.6 million.

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. These matters are generally covered by insurance. Management believes that the final outcome of such matters will not have a material adverse effect on the financial position, results of operations or liquidity of the Company. However, actual outcomes may differ from Management's expectations.

28. Financial Guarantees

Killam Properties Inc. is the guarantor for borrowings held through its three equity investments. As at December 31, 2012, the maximum potential obligation resulting from these guarantees is $72.3M, all related to long-term mortgage financing (December 31, 2011 – Nil). These loans are secured by a first ranking mortgage over the associated investment property. Management has reviewed the contingent liability associated with its financial guarantee contracts and, at December 31, 2012, Management has determined that a provision is not required to be recognized in the Statement of Financial Position. (December 31, 2011 - nil).

29. Related Party Transactions

Killam has contracted APM Construction Services Inc. ("APM") to act as Project Manager on the Charlotte Court and The Plaza construction projects. APM is an entity controlled by a director of Killam. APM will be paid an industry standard management fee of approximately 4% of the construction costs. For the year ended December 31, 2012, Killam has paid APM $0.8 million for construction management services (December 31, 2011 - $0.2 million).

Killam has a 50% interest in a commercial complex which houses its head office. The remaining 50% interest is owned by a company controlled by an executive of Killam. In addition, the property manager for the commercial complex is controlled by the executive and is paid an industry standard property management fee.

Key management personnel remuneration

The remuneration of directors and other key management personnel which include the Directors, President & Chief Executive Officer, Executive Vice-President & Chief Financial Officer, and Vice-Presidents of Killam during the years ended December 31, 2012 and 2011 was as follows:

	2012	2011
Salaries and incentives	**$ 2,892**	$ 2,441
Restricted share awards	**633**	519
Total	**$ 3,525**	$ 2,960

30. Subsequent Events

On January 4, 2013, the Company repaid matured subordinated debentures, consisting of a $10 million payment.

On January 15, 2013, the Company acquired a 5.2 acre development site on Saginaw Parkway in Cambridge, Ontario. The purchase price of $4.1 million was satisfied with cash. The site is zoned for a maximum height of seven storeys and density of 180 units.

On January 18, 2013, and February 18, 2013, the Company announced dividends of $0.04833 per share, payable on February 15, 2013 and March 15, 2013, respectively, to shareholders of record on January 31, 2013 and February 28, 2013 respectively.

On January 25, 2013, the Company acquired a 102-unit apartment building in Ottawa, Ontario. The purchase price of $10.4 million was satisfied with cash.

On February 18, 2013, the Company acquired a 0.8 acre development site on St. George Blvd in Moncton, New Brunswick. The purchase price of $1.1 million was satisfied with cash.

On March 4, 2013, the Company acquired a new 83-unit luxury apartment building located at 200 Royale Boulevard in Halifax, Nova Scotia. The purchase price was $19.1 million and was satisfied with a new 10-year CMHC mortgage of $12.6 million at 3.03%, and the balance in cash.

Five-Year Summary [1]

In thousands (except per share data)

Statement of Income Information	2012	2011	2010	2009	2008
Net rental income	**$80,444**	$76,352	$70,460	$62,606	$56,458
Income from home sales	**$469**	$486	$403	$234	$1,172
Equity income	**$758**	$13	$ -	$ -	$ -
Corporate income	**$962**	$94	$547	$424	$763
Financing costs	**($34,633)**	($34,891)	($31,610)	($30,699)	($29,999)
Administration	**($8,832)**	($7,672)	($7,765)	($7,045)	($6,648)
Gain on debt settlement	**$ -**	$ -	$ -	$638	$ -
Depreciation and amortization	**($2,145)**	($1,711)	($2,114)	($28,831)	($28,712)
Fair value gains	**$37,726**	$52,070	$39,098	$ -	$ -
Loss on disposition	**($1,286)**	$ -	$ -	$ -	$ -
Future tax recovery	**$ -**	$ -	$ -	$830	$1,958
Deferred tax expense	**($19,234)**	($17,920)	($14,611)	$ -	$ -
Net income (loss)	**$54,229**	$66,821	$54,408	($1,843)	($5,008)
Net income (loss) attributable to common shareholders	**$51,727**	$65,965	$53,786	($1,843)	($5,008)
Net income (loss) per share - basic	**$1.03**	$1.45	$1.24	($0.05)	($0.15)
Net income (loss) per share - diluted	**$0.97**	$1.34	$1.19	($0.05)	($0.15)
Balance Sheet Information					
Total assets	**$1,443,128**	$1,329,531	$1,116,333	$739,373	$738,668
Total liabilities	**$854,692**	$816,988	$689,292	$562,171	$565,475
Total equity	**$588,436**	$512,543	$427,041	$177,202	$173,193
Statement of Cash Flow Information					
Cash provided by operating activities	**$46,027**	$39,291	$34,280	$26,226	$22,364
Cash provided by (used in) financing activities	**$43,878**	$92,813	$68,855	($300)	$4,862
Cash used in investing activities	**($76,527)**	($105,673)	($97,887)	($19,299)	($37,527)
Funds From Operations (FFO) [2]					
FFO	**$36,096**	$31,757	$29,036	$24,283	$20,092
FFO per share	**$0.72**	$0.70	$0.67	$0.67	$0.60
Share Information					
Weighted average number of shares - basic	**50,227**	45,523	43,393	36,247	33,604
Weighted average number of shares - fully diluted	**58,239**	52,090	47,201	36,341	33,630
Shares outstanding at December 31	**53,802**	49,291	44,972	38,519	34,028
Share price at December 31	**$12.49**	$11.57	$10.45	$8.80	$4.47

(1) Financial results for 2012, 2011 and 2010 are based on IFRS. Results for 2008 and 2009 are based on previous Canadian GAAP.

(2) Killam changed its definition of FFO with the adoption of IFRS in 2011. FFO and FFO per share for 2008 to 2010 have been adjusted to reflect this definition.

Corporate Information

Board of Directors

Timothy R. Banks[3]
President & CEO,
APM Group of Companies
Charlottetown, Prince Edward Island

Philip D. Fraser
President & CEO, Killam Properties Inc.
Halifax, Nova Scotia

Robert G. Kay[1]
Chairman,
Springwall Group International
and Springwall Sleep Products Inc.
Moncton, New Brunswick

James C. Lawley[1][2]
General Manager, Scotia Fuels Ltd.
Halifax, Nova Scotia

Arthur G. Lloyd
Executive Vice President Investments,
Western North America,
Ivanhoé Cambridge
Calgary, Alberta

George J. Reti[2][3]
Corporate Director,
Chairman of the Board
Calgary, Alberta

Robert G. Richardson, FCA
Executive Vice President & CFO
Killam Properties Inc.
Halifax, Nova Scotia

Manfred J. Walt, CA[3]
President & CEO, Walt & Co. Inc.
Toronto, Ontario

G. Wayne Watson, CA[1][2]
Corporate Director,
Chairman of the Audit Committee
Halifax, Nova Scotia

(1) member of the Audit Committee
(2) member of the Corporate Governance, Nomination and Succession Committee
(3) member of the Compensation Committee

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Our report is also available on-line at:
killamproperties.com/financial-reports/

Executive Team

Philip Fraser
President & Chief Executive Officer

Robert Richardson, FCA
Executive Vice President
& Chief Financial Officer

Ruth Buckle
Vice President, Property Management

Erin Cleveland, CA
Vice President, Finance

Pamela Crowell
Vice President,
Property Management (MHCs)

Jeremy Jackson
Vice President, Marketing

Michael McLean
Vice President, Development

Dale Noseworthy, CA, CFA
Vice President, Investor Relations
and Corporate Planning

Ronald Barron
Corporate Secretary

Investor Inquiries

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Stewart McKelvey
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Registrar and Transfer Agent

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Share Listing

Toronto Stock Exchange (TSX)
Trading Symbol: KMP

Monthly Dividend

$0.04833 per share

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ANNUAL GENERAL MEETING

The Annual General Meeting of Shareholders will be held on Wednesday, May 8, 2013, at 2:00 pm Atlantic Time at the Halifax Marriott Harbourfront Hotel, 1919 Upper Water Street, Halifax, Nova Scotia.

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