



Quarterly Report to Unitholders

For the period ended March 31, 2003

H&R reported financial results in the first quarter that reflect the consistent implementation of our strategy to acquire quality assets and increase cash distributions to unitholders.

Financial Results

Several core-business acquisitions contributed to an increase in operating revenue of nearly 18% in the first three months of the year, compared to the same period in 2002. Total net earnings rose 8% and distributable income 11%, while, per unit, net earnings increased 6% and distributable income rose 9% in the first quarter.

Operating Strategy

Since inception in 1996, H&R's operating strategy has been to focus its investments and expertise on quality commercial properties, using a disciplined approach to asset management and acquisitions to generate stable distributable income and maximize return on equity for unitholders. We lease our properties to highly creditworthy tenants through long-term leases matched with primarily long-term, fixed-rate financing. As a result, the REIT maintained at the end of the first quarter a portfolio occupancy rate of 99% and an average term to maturity of 12.3 years for leases and 12.7 years for mortgages.

Acquisitions

During the first quarter 2003, H&R announced the \$70 million acquisition of five retail properties in the United States, leased on a long-term basis to Lowe's, Walgreens and Eckerd, and acquired for \$17 million a state-of-the-art distribution facility in Oakville, Ontario leased to UPS Logistics. H&R also completed the sale of an office property in downtown Toronto for \$22.5 million, generating a capital gain of \$3.6 million, which is included in distributable income.

In early May, the REIT announced the acquisition of seven retail and industrial properties comprising nearly one million square feet in the United States and Canada at a cost of \$92 million. These properties are leased long term to creditworthy tenants such as Lowe's, Georgia Pacific, Borders, Rona/Revy Home Improvements, Best Buy, Loeb's, Linen N' Things and United Auto Parts.

In keeping with our operating strategy, H&R recently acquired for \$116 million a portfolio of 17 U.S. retail properties in ten states from New York Life Insurance Company. The properties are comprised of 834,500 square feet, are leased to investment grade tenants having average lease terms of 15 years, and are financed with non-recourse, 15-year debt. The highly creditworthy tenants include Eckerd, Winn-Dixie, Lowe's, Walgreens, Sam's Club, Kohl's, Shaw's Supermarkets and Kroger. The REIT's levered return on investment is approximately 14.5% for this transaction.

H&R has produced levered returns on equity between 13% and 15% with all the acquisitions to date this year.

Financing

At the end of April, H&R closed the first of four \$25-million tranches of a previously announced \$100-million private placement equity financing with a Canadian institutional money manager. A portion of the proceeds was used to fund the recent acquisitions. Accounting for the acquisitions, but excluding the receipt of the remaining three tranches totaling \$75 million, H&R has an acquisition capacity in excess of \$100 million.

Tom Hofstedter
May 15, 2003

Unaudited Consolidated Financial Statements of

H&R REAL ESTATE INVESTMENT TRUST

For the three months ended March 31, 2003

H&R REAL ESTATE INVESTMENT TRUST

Consolidated Balance Sheets and Statements of Unitholders' Equity

(In thousands of dollars)

	March 31 2003 (unaudited)	December 31 2002 (audited)	March 31 2002 (unaudited)
Assets			
Income properties (note 2)	\$ 1,977,398	\$ 1,922,200	\$ 1,825,253
Mortgages receivable (note 3)	70,481	60,079	64,150
Deferred expenses (note 4)	29,079	28,859	25,209
Prepaid expenses and sundry assets	15,042	11,504	10,805
Accrued rent receivable	11,309	10,913	9,725
Accounts receivable	7,770	7,131	6,611
Cash and cash equivalents	7,214	10,208	23,283
	<u>\$ 2,118,293</u>	<u>\$ 2,050,894</u>	<u>\$ 1,965,036</u>

Liabilities and Unitholders' Equity

Liabilities:			
Mortgages payable (note 5)	\$ 1,263,826	\$ 1,239,224	\$ 1,001,665
Bank indebtedness (note 6)	40,954	1,280	157,842
Accounts payable	40,012	42,742	48,766
	<u>1,344,792</u>	<u>1,283,246</u>	<u>1,208,273</u>
Unitholders' equity (note 7)	775,964	767,484	756,763
Cumulative foreign translation adjustment	(2,463)	164	-
	<u>\$ 2,118,293</u>	<u>\$ 2,050,894</u>	<u>\$ 1,965,036</u>

Consolidated Statements of Unitholders' Equity

Unitholders' equity, beginning of period	\$ 767,484	\$ 754,737	\$ 754,737
Proceeds from issuance of units	6,795	13,164	579
Issue costs	-	(121)	(106)
Net earnings	23,619	84,022	21,861
Distributions to unitholders	(21,934)	(84,318)	(20,308)
Unitholders' equity, end of period	<u>\$ 775,964</u>	<u>\$ 767,484</u>	<u>\$ 756,763</u>

See accompanying notes to consolidated financial statements

H&R REAL ESTATE INVESTMENT TRUST

Unaudited Consolidated Statements of Earnings

(In thousands of dollars, except per unit amounts)

	Three Months Ended March 31	
	2003	2002
Operating revenue:		
Rentals from income properties	\$ 75,222	\$ 64,390
Mortgage interest income and other	5,195	3,978
	<hr/> 80,417	<hr/> 68,368
Operating expenses:		
Property operating costs	27,531	24,824
Mortgage and other interest	22,750	16,408
Depreciation of income properties	4,346	3,340
Amortization of deferred expenses	1,021	781
	<hr/> 55,648	<hr/> 45,353
Operating income from properties	<hr/> \$ 24,769	<hr/> \$ 23,015
Trust expenses	1,150	1,154
Net earnings	<hr/> \$ 23,619	<hr/> \$ 21,861
Basic net earnings per unit (note 9)	<hr/> \$ 0.33	<hr/> \$ 0.31
Diluted net earnings per unit (note 9)	<hr/> \$ 0.33	<hr/> \$ 0.31

See accompanying notes to consolidated financial statements

H&R REAL ESTATE INVESTMENT TRUST

Unaudited Consolidated Statements of Cash Flows

(In thousands of dollars)

	Three Months Ended	
	March 31	
	2003	2002
Cash provided by (used in):		
Operations:		
Net earnings	\$ 23,619	\$ 21,861
Items not affecting cash:		
Depreciation	4,346	3,340
Amortization of deferred leasing costs	854	712
Gain on sale of income properties	(3,633)	(1,497)
Funds from operations	25,186	24,416
Net changes in:		
Amortization of deferred financing costs	167	69
Other non-cash operating items (note 10)	(10,162)	1,548
	15,191	26,033
Financing:		
Bank indebtedness	39,674	155,589
Mortgages payable:		
Acquisitions	-	172,767
Repayments	(7,708)	(8,230)
Proceeds from issuance of units, net	6,795	473
Distributions to unitholders	(21,934)	(20,308)
	16,827	300,291
Investments:		
Income properties		
Proceeds on disposition of income properties	11,446	2,551
Acquisitions	(36,056)	(318,204)
Mortgages receivable	(10,402)	(11,719)
	(35,012)	(327,372)
Decrease in cash and cash equivalents	(2,994)	(1,048)
Cash and cash equivalents, beginning of period	10,208	24,331
Cash and cash equivalents, end of period	\$ 7,214	\$ 23,283
Supplemental cash flow information:		
Interest paid	22,411	16,360
Supplemental disclosure of non-cash investing activities:		
Acquisitions of income properties through assumption of mortgages payable	49,045	125,500
Acquisitions of income properties through repayment of mortgages receivable	-	42,710
Mortgages payable assumed by purchasers on disposition of income properties	11,054	30,983
Mortgages receivable granted to purchasers on disposition of income properties	-	14,566

See accompanying notes to consolidated financial statements

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

H&R Real Estate Investment Trust (the "Trust") is an unincorporated trust with each unitholder participating pro rata in distributions of income and, in the event of termination of the Trust, participating pro rata in the net assets remaining after satisfaction of all liabilities.

1. Basis of Presentation:

Interim Financial Statements:

The interim financial statements follow the same accounting policies and methods of their application as the December 31, 2002 annual financial statements.

In the opinion of the Trust, the accompanying unaudited consolidated financial statements contain all the adjustments necessary to present fairly the financial position as of March 31, 2003, December 31, 2002 and March 31, 2002, and the results of operations for the three months ended March 31, 2003 and 2002 and the changes in cash flow for the three months ended March 31, 2003 and 2002. While the Trust believes that disclosures presented are adequate to make the information not misleading, it is suggested that these financial statements be read in conjunction with the financial statements and notes included in the Trust's Annual Report for the year ended December 31, 2002.

The results of operations for the three months ended March 31, 2003 are not necessarily indicative of the results for the full year.

2. Income properties:

			March 31 2003	December 31 2002	March 31 2002
	Cost	Accumulated depreciation	Net book value	Net book value	Net book value
Land	\$ 399,765	-	\$ 399,765	\$ 388,070	\$ 367,664
Buildings	1,623,990	46,357	1,577,633	1,534,130	1,457,589
	\$ 2,023,755	\$ 46,357	\$ 1,977,398	\$ 1,922,200	\$ 1,825,253

3. Mortgages receivable:

The mortgages receivable are secured by real property, bear interest at a weighted average of 9.1% (December 31, 2002 - 8.8%, March 31, 2002 - 10.5%) per annum and are repayable between 2003 and 2008. The Trust has options to acquire interests in these properties subject to mortgages.

4. Deferred expenses:

			March 31 2003	December 31 2002	March 31 2002
	Cost	Accumulated amortization	Net book value	Net book value	Net book value
Leasing	\$ 28,611	\$ 7,394	\$ 21,217	\$ 21,059	\$ 19,167
Financing	8,995	1,133	7,862	7,800	6,042
	\$ 37,606	\$ 8,527	\$ 29,079	\$ 28,859	\$ 25,209

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

5. Mortgages payable:

The mortgages payable are secured by the income properties, bearing fixed interest, with a weighted average rate of 7.4% (December 31, 2002 - 7.4%, March 31, 2002 - 7.6%) per annum and maturing between 2003 and 2023. Included in the mortgages payable are US \$84,736 (Cdn \$124,562) at March 31, 2003 (December 31, 2002 - US \$51,649 (Cdn \$81,606), March 31, 2002 - US \$8,063 (Cdn \$12,819)). Future principal payments are as follows:

Year ending December 31:

2003	\$	26,632
2004		62,779
2005		56,779
2006		61,387
2007		77,034
Thereafter		979,215
	\$	1,263,826

6. Bank indebtedness:

The bank indebtedness bears interest at rates approximating the prime rate of a Canadian chartered bank, is secured by fixed charges over certain income properties and is due on demand. At March 31, 2003, the prime interest rate was 4.75% (December 31, 2002 - 4.5%, March 31, 2002 - 3.75%) per annum.

7. Unitholders' equity:

(a) The following units are issued and outstanding:

As at December 31, 2001	69,771,049
Issued under the distribution reinvestment plan and direct unit purchase plan	42,918
As at March 31, 2002	69,813,967
Issued under the distribution reinvestment plan and direct unit purchase plan	364,853
Options exercised	731,998
As at December 31, 2002	70,910,818
Issued under the distribution reinvestment plan and direct unit purchase plan	117,830
Options exercised	468,334
As at March 31, 2003	71,496,982

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

(b) Incentive unit option plan:

The Trust may grant options to its officers, employees and certain trustees for up to 5,800,000 units. The exercise price of each option approximates the market price of the Trust's units on the date of grant. The options vest at 33.3% per year from the grant date, being fully vested after three years, and expire ten years after the date of the grant.

A summary of the status of the plan as at March 31, 2003 and 2002 and the changes during the period ended on those dates are as follows:

	2003	2003	2002	2002
		Weighted average exercise price (\$)		Weighted average exercise price (\$)
Options	Units		Units	
Outstanding, beginning of period	3,848,834	11.93	3,805,832	11.42
Granted	468,168	13.36	-	-
Exercised	(468,334)	11.10	-	-
Outstanding, end of period	3,848,668	12.20	3,805,832	11.42
Options exercisable at March 31	1,679,168	11.40	2,151,705	10.92

The options outstanding at March 31, 2003 are exercisable at varying prices ranging from \$9.17 to \$13.36 with a weighted average remaining life of 7.9 years. The vested options are exercisable at varying prices ranging from \$9.17 to \$12.58 with a weighted average remaining life of 6.6 years.

8. Stock based compensation:

The Trust has adopted the new recommendations of The Canadian Institute of Chartered Accountants with respect to stock-based compensation and other stock-based payments, Section 3870. The Trust applies the settlement method of accounting for stock-based compensation awards granted. Accordingly, no compensation cost has been recognized for its unit option plan. The only stock-based compensation or payment granted by the Trust is pursuant to its unit option plan.

As a result, CICA Handbook Section 3870 requires disclosure of proforma amounts to reflect the impact if the Trust had elected to adopt the fair value method of accounting provisions of CICA Handbook Section 3870 for the unit option plan. Accordingly, the Trust's net earnings and basic net earnings per unit would have been decreased to the proforma amounts as indicated below for the three months ended March 31.

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

	Three Months Ended	
	March 31 2003	March 31 2002
Net earnings		
Reported	23,619	\$ 21,861
Proforma	23,519	21,861
Basic net earnings per unit		
Reported	\$ 0.33	\$ 0.31
Proforma	0.33	0.31

The fair value of the stock options used to compute proforma net earnings and proforma basic net earnings per unit is the estimated fair value of each option grant on the grant date using the Black-Scholes option pricing model with the following weighted average assumptions:

	Three Months Ended
Weighted Average Assumptions	March 31 2003
Expected distribution yield	9.0%
Expected Volatility	12.5%
Risk free interest rate	5.0%
Expected option life in years	10.0

No options were issued during the three months ended March 31, 2002.

9. Per unit amounts:

The following table sets forth the computation of basic net earnings per unit and diluted net earnings per unit using weighted average units outstanding and adjusted weighted average units, respectively:

	Three Months Ended	
	March 31 2003	March 31 2002
Weighted average units outstanding	71,009,978	69,786,291
Effect of dilutive securities:		
Employee unit options	464,789	669,939
Adjusted weighted average units and assumed conversions	71,474,767	70,456,230

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

10. Changes in other non-cash operating items:

	March 31 2003	March 31 2002
Deferred expenses	\$ (2,859)	\$ (4,937)
Prepaid expenses and sundry assets	(3,538)	(4,210)
Accrued rent receivable	(396)	(397)
Accounts receivable	(639)	(2,419)
Accounts payable	(2,730)	13,511
	<u>\$ (10,162)</u>	<u>\$ 1,548</u>

11. Distributable Income:

Distributable income, which is not defined within Canadian generally accepted accounting principles, has been calculated with reference to the terms of the Declaration of Trust as follows:

	March 31 2003	March 31 2002
Net earnings	\$ 23,619	\$ 21,861
Depreciation	4,346	3,340
Accrued rent	(396)	(397)
Distributable Income	<u>\$ 27,569</u>	<u>\$ 24,804</u>
Distributable income per unit (note 9)	<u>\$ 0.39</u>	<u>\$ 0.36</u>
Cash distribution per unit	<u>\$ 0.31</u>	<u>\$ 0.29</u>

12. Segment disclosures:

Geographic information:

Segmented information on rentals from income properties and identifiable assets by geographic region is as follows:

	Rentals from income properties		Income Properties	
	March 31, 2003	March 31, 2002	March 31, 2003	March 31, 2002
Canada	72,981	63,772	\$ 1,806,477	\$ 1,803,591
United States	2,951	618	170,921	21,662
	<u>\$ 75,932</u>	<u>\$ 64,390</u>	<u>\$ 1,977,398</u>	<u>\$ 1,825,253</u>

Revenues are attributed to countries based on location of the properties.

H&R REAL ESTATE INVESTMENT TRUST

Notes to Unaudited Consolidated Financial Statements

(In thousands of dollars, except per unit amounts)

March 31, 2003

13. Significant transactions:

On January 31, 2003, the Trust completed the sale of a 148,000 square foot office property for \$22.5 million. This was paid for in part by the purchaser assuming the existing mortgage payable of approximately \$11.1 million. A gain of approximately \$3.6 million was realized on this transaction.

On February 19, 2003, the Trust acquired a 255,000 square foot single tenant industrial building for approximately \$17.4 million.

During March 2003, the Trust acquired four retail properties totalling 406,000 square feet for approximately \$65.0 million. Mortgages payable of \$49.0 million were assumed on these properties.

14. Subsequent events:

The Trust entered into an agreement to sell, on a private placement basis, \$100 million of units to accounts managed by a single Canadian institutional money manager. The financing will be effected in four equal tranches. The first \$25 million of trust units was issued on April 30, 2003. The three additional tranches will be issued on or about July 31, 2003, October 31, 2003 and January 15, 2004.

The Trust acquired four industrial and 21 retail properties in Canada and the United States totalling 1,819,000 square feet at a cost of approximately \$212.7 million. The Trust assumed mortgages of \$106.2 million on these properties.

H&R REAL ESTATE INVESTMENT TRUST

Management's Discussion & Analysis

For the three months ended March 31, 2003

The following discussion should be read in conjunction with the consolidated financial statements of the REIT and the notes thereto for the first quarter of 2003, with the Management's Discussion and Analysis for December 31, 2002 including the section on "Risks and Uncertainties", and with the consolidated financial statements and notes thereto for year-end of December 31, 2002.

RESULTS OF OPERATIONS

Net earnings for the first quarter ended March 31, 2003 of \$23.6 million or \$0.33 per unit, increased by 8.0% on a dollar basis and by 6.5% on a per unit basis over the net earnings of \$21.9 million or \$0.31 per unit for March 31, 2002.

Depreciation of \$4.3 million (Q1 2002 - \$3.3 million) and amortization of \$1.0 million (Q1 2002 - \$0.8 million) are included in the determination of net earnings. The REIT does not consider depreciation expense when calculating distributions paid to unitholders.

Income from rental operations before depreciation, amortization and trust expenses (in thousands of dollars)

Three months ended March 31	<u>2003</u>	<u>2002</u>
Rentals from income properties	\$75,222	\$64,390
Mortgage interest income and other	<u>5,195</u>	<u>3,978</u>
	80,417	68,368
Property operating costs	27,531	24,824
Operating income before interest	52,886	43,544
Mortgage and other interest	<u>22,750</u>	<u>16,408</u>
Income from operations before depreciation, amortization and trust expenses	<u>\$30,136</u>	<u>\$27,136</u>

RENTALS FROM INCOME PROPERTIES

Rentals from income properties increased 16.8% from \$64.4 million in Q1 2002 to \$75.2 million in Q1 2003. The increase is primarily the result of the REIT's ongoing strategy of adding to its properties either through acquisitions or its mezzanine financing program. A total of 10 properties were added and two properties were sold between March 31, 2002 and March 31, 2003 representing a net increase in the book value of income properties (after depreciation) of \$152.1 million.

Property operating costs and mortgage and other interest have also increased from \$24.8 million and \$16.4 million to \$27.5 million and \$22.8 million respectively for the first quarter of 2003. These increases reflect the increase in activity resulting from the additional properties added to the portfolio.

H&R REAL ESTATE INVESTMENT TRUST

Management's Discussion & Analysis

For the three months ended March 31, 2003

The occupancy rate in the REIT's portfolio as at March 31, 2003 remains unchanged at 99% from December 31, 2002 and March 31, 2002. The exposure to lease rollovers as a result of lease expiries over the next 5 years (as a percentage of the REIT owned portion of the properties) is as follows:

2003	0.76%	for the balance of the year
2004	2.91%	
2005	2.21%	
2006	2.15%	
2007	<u>4.36%</u>	
	12.39%	

MORTGAGE INTEREST INCOME AND OTHER INCOME

The REIT earned \$5.2 million in mortgage interest income and other income in the first quarter of 2003 compared to \$4.0 million in 2002. Included in this amount is a gain on sale of income properties (see "sale of income properties" below) of \$3.6 million (Q1 2002 - \$1.5 million). The balance of this type of income (when excluding gains on sale) has therefore declined by 35.7% quarter over quarter from \$2.5 million in the first quarter of 2002 to \$1.6 million in the same period of 2003.

This reduction is mainly due to the decline in the average mortgage receivable assets balance between the two quarters ended March 31, 2002 and 2003 (see "changes in financial position – mortgages receivable" below) and a reduction in the interest rate earned on a \$30 million mortgage effective April 2002. As more development opportunities arise in the future this trend could then reverse itself. The weighted average interest earned on these investments in the first quarter of 2003 was 9.1% compared to the 10.5% earned in the first quarter of 2002 and 8.8% earned in the year ended December 31, 2002.

SALE OF INCOME PROPERTIES

The REIT's philosophy is to dispose of assets that no longer fit its investment strategy and re-deploy the proceeds in more attractive investment opportunities. During this quarter, the REIT disposed of one non-core 148,000 square foot office property as compared to a 294,000 square foot retail property for the quarter ended March 31, 2002. The sale of this property yielded a profit of approximately \$3.6 million for the quarter ended March 31, 2003 compared to \$1.5 million earned during the first quarter ended March 31, 2002.

TRUST EXPENSES

Trust expenses were flat quarter over quarter, and amounted to 1.5% of rentals from income properties in Q1 2003, down from 1.8% for the first quarter of 2002.

DISTRIBUTION TO UNITHOLDERS

The REIT is currently required to distribute not less than 80% of its normalized distributable income to Unitholders on a monthly basis.

Depreciation, accrued rent and other non-cash items (including gains on sale) are added to, or deducted from, net earnings to determine the amount of income available for distribution. Accrued rent represents the adjustment made to normalize rents for certain tenants whose rental rate increases substantially over the term of their respective leases. This adjustment is required by Canadian generally accepted accounting principles and represents a non-cash item to be deducted in determining distributable income.

H&R REAL ESTATE INVESTMENT TRUST

Management's Discussion & Analysis

For the three months ended March 31, 2003

Distributable income increased by \$2.8 million from \$24.8 million for the quarter ended March 31, 2002 to \$27.6 million for the quarter ended March 31, 2003. This represents an increase on a per unit basis from \$0.36 for the quarter ended March 31, 2002 to \$0.39 per unit for the quarter ended March 31, 2003.

The primary reason for this increase is the higher capital gain realized in Q1 2003 of \$3.6 million compared to \$1.5 million in Q1 2002 (see "Sale of Income Properties" above). The balance of the increase is attributable to the acquisition of properties between April 2002 and March 2003 plus rental escalations in existing leases, offset by the lower rate of interest earned on mortgage receivables (see "Mortgage Interest Income and Other Income" above) and the general softening in the multi-tenant office market in the GTA which has given rise to lower rents on renewal and new leasing, as well as slightly higher vacancies in the office portfolio.

Adjusting for these gains previously mentioned will result in normalized distributable income of \$24.0 million or \$0.34 per unit for the quarter ended March 31, 2003 versus \$23.3 million or \$0.34 per unit for the same period in 2002.

Total distributions in the current quarter, at 10.2c per unit per month, amounted to \$21.9 million or 79.6% of distributable income. This compares to \$20.3 million at 9.7c per unit per month representing an 81.9% payout in the same quarter of the prior year. The primary reason for the quarter over quarter decline is the \$3.6 million gain on sales (Q1 2002 - \$1.5 million) which was not distributed to unitholders. The percentage distributions to normalized distributable income described previously is 91.5% for the quarter ended March 31, 2003 (Q1 2002 - 87.1%). Management expects this ratio to decline to approximately 86% for the 2003 fiscal year assuming distributions remain constant throughout the year.

Readers are cautioned that distributable income is a non-GAAP measure and should not be construed as an alternative to net earnings determined in accordance with GAAP as an indicator of the REIT's performance. The REIT's method of calculating distributable income may differ from other issuers' methods and accordingly distributable income may not be comparable to measures used by other issuers.

Calculation of Distributable Income (in thousands of dollars)	2003	2002
Three months ended March 31		
Net earnings	\$23,619	\$21,861
Add (deduct)		
Depreciation	4,346	3,340
Accrued rent	(396)	(397)
Distributable Income	<u>\$27,569</u>	<u>\$24,804</u>

CHANGES IN FINANCIAL POSITION

ASSETS

Income Properties

During the first quarter ended March 31, 2003, the REIT acquired five properties and disposed of one property.

In January 2003, a non-core multi-tenant office building located in Toronto, Ontario totalling 148,000 square feet was sold for gross proceeds of \$22.5 million, realizing a gain of \$3.6 million.

H&R REAL ESTATE INVESTMENT TRUST

Management's Discussion & Analysis

For the three months ended March 31, 2003

In February 2003, the REIT acquired a new 255,000 square foot logistics warehouse in Oakville, Ontario for approximately \$17.4 million. The property is leased to UPS Logistics Group.

During March 2003, three free standing retail home improvement stores leased to Lowes Companies Inc. were purchased for approximately \$60.4 million. The stores, comprising a total of 395,000 square feet, are all located in the Atlanta, Georgia area. An additional 11,000 square foot retail store leased to Eckerd Corporation in the same region was purchased for \$4.6 million.

Consequently, as a result of these transactions, income properties increased by 2.9% to \$1.977 billion at March 31, 2003 from \$1.922 billion at December 31, 2002.

Mortgages Receivable

The REIT provides mezzanine financing for development projects that are consistent with the REIT's objectives and philosophy.

At March 31, 2003 there were five projects for which the REIT had provided mezzanine development financing as compared to four at December 31, 2002.

Mortgages receivable increased 17.3% from \$60.1 million at December 31, 2002 to \$70.5 million at March 31, 2003. This increase is primarily due to new financing of \$6.4 million provided in this quarter for an industrial project in Kitchener, Ontario as well as an additional \$3.8 million advanced on Phase II of the Bell Canada Complex in Mississauga, Ontario.

Deferred Expenses

Deferred expenses increased slightly by \$0.2 million from \$28.9 million at December 31, 2002 to \$29.1 million at March 31, 2003, an increase of 0.8%. This increase reflects the normal increase in activity resulting from additional properties added to the portfolio offset by the ongoing amortization of this asset.

Other Assets

Accounts receivable and accrued rents receivable were not significantly different between December 31, 2002 and March 31, 2003.

Prepaid expenses and sundry assets increased from \$11.5 million at December 31, 2002 to \$15.0 million at March 31, 2003, an increase of 30.8%. The increase is primarily as a result of a number of deposits made in the quarter for US property purchases as well as commitment fees advanced for certain mortgages.

Cash and cash equivalents decreased by \$3.0 million between December 31, 2002 and March 31, 2003. Of the balance of \$7.2 million, \$4.5 million related to funds being held in escrow until the expiry of certain non-recourse public mortgage bonds and other non-recourse US mortgages.

LIABILITIES

The REIT's Declaration of Trust limits the indebtedness to a maximum of 65% of the gross book value of the REIT. At March 31, 2003 the REIT's indebtedness was 60.3% compared to 59.3% at December 31, 2002. This increase is due to the increase in mortgages payable and bank indebtedness as outlined below.

Mortgages Payable

Mortgages payable increased by 2.0% from the December 2002 year-end figure of \$1.239 billion to \$1.264 billion at March 31, 2003. This \$24.6 million net increase is primarily a result of three mortgages totaling \$49.0 million assumed on the closing of the three Lowes stores purchased in Georgia (see "Assets – Income Properties" above).

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The mortgages payable balance was however reduced by \$11.1 million with the sale of the office property at 250 University Avenue, Toronto when the mortgage was assumed by the purchaser as well as by the regular monthly self amortizing principal payments made in the normal course of business operations.

Bank Indebtedness

Liabilities at March 31, 2003 included bank indebtedness of \$41.0 million compared to \$1.3 million at December 31, 2002, an increase of \$39.7 million. The debt bears interest at rates approximating the prime rate of a Canadian Chartered bank and is secured by fixed charges over certain income properties and is due on demand. These funds were primarily used to provide the equity required for the asset purchases previously described.

Accounts Payable

Accounts payable decreased by \$2.0 million from \$42.7 million at December 31, 2002 to \$40.7 million at March 31, 2003. This decrease reflects regular fluctuations occurring in the normal course of business operations.

UNITHOLDERS' EQUITY

Unitholders' equity increased by \$8.5 million between December 31, 2002 and March 31, 2003 as a result of an excess of net earnings over distributions to unitholders coupled with the proceeds from the REIT's distribution reinvestment program, as well as the exercise of options by officers and trustees of the REIT during the quarter.

CUMULATIVE FOREIGN EXCHANGE ADJUSTMENTS

As a result of the strengthening of the Canadian dollar against the US dollar during the quarter, an unrealized loss of \$2.5 million was recorded on the financial statements at March 31, 2003 as compared to a gain of \$0.2 million at December 31, 2002. This amount reflects the net adjustment to the equity invested in US properties, with the REIT's debt being held in US dollars currently acting as a natural hedge against its total investment in US dollars.

However, as part of the REIT's strategy of providing stable distributable income to its unitholders, the REIT has implemented a hedging strategy on its US income to minimize exposure to currency fluctuations.

LIQUIDITY AND CAPITAL RESOURCES

Funds from operations during the first quarter amounted to \$25.2 million, an increase from \$24.4 million in the same quarter of 2002. This cash provided from operating activities, together with proceeds from issue of units, conventional mortgage financing and short term bank financing, have been used mainly to fund net property acquisitions of \$36.1 million and distributions to unitholders of \$21.9 million for the three months ended March 31, 2003.

Management expects to be able to meet all of the REIT's ongoing obligations and to finance future growth through the issue of new equity as well as by using conventional real estate debt, short term financing from the bank and through a related party and the REIT's stable cash flow. A significant source of future liquidity will be the proceeds from the \$100 million private placement that was agreed to subsequent to the end of the quarter whereby the funds are to be received in four \$25 million tranches every three months beginning April 30, 2003.

ACCOUNTING CHANGES

The REIT has adopted the new CICA recommendations on stock-based compensation and other stock-based transactions. The standard sets out a fair value based method of accounting, which is required for certain, but not all, stock-based transactions. The section must be applied to all stock-based payments to non-employees, and to employee awards that are direct awards of stock, that call for settlement in cash or other

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assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments. The new standard permits the REIT to continue its existing policy that no compensation cost is recorded on the grant of unit options to employees. However, the standard does require that the REIT disclose for each period, the proforma net earnings and the proforma earnings per unit, as if the fair value based method had been used to account for the employee unit option awards.

In accordance with the section, the accounting standard was applied to all awards granted subsequent to January 1, 2002, the effective date of the section. Based on the total number of options granted in the first quarter of 2003, if the Trust had used the fair value method of accounting for its unit option plan, the proforma net earnings would have been \$23.5 million and proforma basic net earnings per unit would have been \$0.33 for the three months ended March 31, 2003.

The fair value of each option grant is estimated on the date of grant using the Black Scholes option pricing model with the following assumptions: distribution yield of 9.0%, expected volatility of 12.5%, risk free interest rates of 5.0% and expected option life of ten years.

SUBSEQUENT EVENTS

Subsequent to the quarter end, the REIT entered into an agreement to sell, on a private placement basis, \$100 million of units to accounts managed by a single Canadian institutional money manager with proceeds to be received in four equal tranches. The first \$25 million of trust units was issued on April 30, 2003 with the three additional tranches to be issued on or about July 31, 2003, October 31, 2003 and January 15, 2004.

The REIT also continued to purchase income properties in accordance with its normal operating policies and procedures, closing 25 transactions for approximately \$213 million in April and May 2003.

RISKS AND UNCERTAINTIES

The REIT is exposed to interest rate risk on its borrowings. It minimizes this risk by restricting total debt to 65% of aggregate assets and by obtaining long-term fixed rate debt to replace short-term floating rate borrowings. In addition, the weighted average term to maturity of long-term debt is closely matched to the remaining average lease terms.

The REIT is exposed to credit risk as an owner of real estate in that tenants may become unable to pay the contracted rents. Management mitigates this risk by carrying out appropriate credit checks and related due diligence on the significant tenants. Management has diversified the REIT's holdings so that it owns several categories of properties (office, industrial and retail) and acquires properties throughout Canada and the United States. In addition, management ensures that no tenant or related group of tenants, other than investment grade tenants, account for a significant portion of the cash flow. The only tenants which account for more than 5% of the rentals from income properties of the REIT are TCPL, Bell Canada and Bell Mobility, but each individually represent less than 15% of the rentals from income properties of the REIT and currently are at least A rated by a recognized rating agency.

The REIT is also exposed to credit risk as a lender on the security of real estate in the event that a borrower is unable to make the contracted payments. Such risk is mitigated through credit checks and related due diligence of the borrowers and through careful evaluation of the worth of the underlying assets.

The REIT is exposed to foreign exchange fluctuations as a result of ownership of assets in the United States. In order to mitigate the risk of significant fluctuations, a hedging program has been implemented to protect income earned in US dollars.

The REIT has been structured to ensure that mandated investment guidelines and operating criteria are strictly adhered to. These policies govern such matters as the type and location of properties that the REIT can acquire, the maximum leverage allowed, the requirement for appropriate insurance coverage as well as environmental policies.

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The REIT has maintained its ability to properly manage both operational and financial risks. The REIT's properties are leased under long-term arrangements to a diversified base of creditworthy tenants with strong covenants and are financed with long-term fixed rate mortgages.

Other than as described above, no single tenant is critical to the REIT's ability to meet its financial obligations. The REIT's broad tenant base assists in attempting to fulfill its primary goal of maintaining a predictable cash flow. Risk is further minimized through a low vacancy rate and relatively few short to medium-term lease renewals.

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Supplemental financial information, page 1.

For the three months ended March 31, 2003

The following are details of selected supplemental financial information for the three months ended March 31, 2003.

OVERVIEW OF PORTFOLIO

(Net ownership position)

	March 31, 2003			
	Office	Industrial	Retail	Total
Number of Properties	26	73	18	117
Total Leasable Area (square feet)	5,747,273	10,495,183	2,022,712	18,265,168
Occupancy *	96%	100%	99%	99%
Average Rent per sq.ft.	\$17.64	\$5.30	\$16.01	\$10.37
Average Age of Buildings (years)	12.33	12.77	4.95	11.76
Average Interest Rate on Outstanding Mortgages *	7.6%	7.2%	6.9%	7.4%

* Weighted average

	December 31, 2002			
	Office	Industrial	Retail	Total
Number of Properties	27	72	14	113
Total Leasable Area (square feet)	5,895,448	10,240,292	1,617,066	17,752,806
Occupancy *	97%	100%	99%	99%
Average Rent per sq.ft.	\$17.68	\$5.23	\$16.31	\$10.38
Average Age of Buildings (years)	12.06	12.81	4.53	11.80
Average Interest Rate on Outstanding Mortgages *	7.6%	7.2%	6.9%	7.4%

* Weighted Average

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Supplemental financial information, page 2.

For the three months ended March 31, 2003

NET OPERATING INCOME

Diversification by Asset Class

	3 Months ended March 31, 2003	Year ended December 31, 2002
Office	60%	60%
Industrial	27%	27%
Retail	13%	13%

Diversification by Region

	3 Months ended March 31, 2003	Year ended December 31, 2002
Ontario	61%	62%
Alberta	22%	24%
Quebec	10%	10%
United States	4%	1%
Other	3%	3%

ASSETS

Book Value by Asset Class (\$millions)

	As at March 31, 2003	As at December 31, 2002
Office	\$1,093	\$1,113
Industrial	\$552	\$539
Retail	\$332	\$270

Book Value by Region (\$millions)

	As at March 31, 2003	As at December 31, 2002
Ontario	\$1,084	\$1,084
Alberta	\$470	\$471
Quebec	\$187	\$187
United States	\$171	\$115
Other	\$65	\$65

TENANTS

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Supplemental financial information, page 3.

For the three months ended March 31, 2003

(Analysis of largest 10 tenants
as a percentage of rental from income properties)

	Tenant	% of rentals from income properties	Lease term to maturity (years)
1.	Bell Canada	14.94%	18.50
2.	TransCanada PipeLines Limited	11.36%	18.00
3.	Bell Mobility	6.72%	19.00
4.	Purolator Courier Limited	3.18%	18.25
5.	Finning International	3.04%	19.00
6.	Lowe's Companies, Inc.	2.99%	15.50
7.	Royal Bank of Canada	2.76%	8.00
8.	Public Works of Canada	2.09%	13.25
9.	Rona Inc.	1.96%	17.00
10.	Nestle Canada Inc.	1.58%	16.50
	Total	50.62%	

LEASE EXPIRIES

Percent of total expiring and average net rent on expiry

	Office		Industrial		Retail		Total	
	%	Rent \$	%	Rent \$	%	Rent \$	%	Rent \$
*2003	0.73	12.56	-	-	0.03	16.13	0.76	12.70
2004	1.23	19.45	1.59	5.54	0.09	21.26	2.91	11.91
2005	1.73	17.59	0.22	6.21	0.26	16.10	2.21	16.28
2006	1.49	14.31	0.43	5.23	0.23	19.69	2.15	13.07
2007	0.78	16.52	3.49	5.08	0.09	29.90	4.36	7.64
Total	<u>5.96</u>	<u>16.40</u>	<u>5.73</u>	<u>5.26</u>	<u>0.70</u>	<u>19.72</u>	<u>12.39</u>	<u>11.44</u>

* For the balance of the year

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Supplemental financial information, page 4.

For the three months ended March 31, 2003

DEBT RATIOS

Debt to Gross Book Value (Guideline maximum 65%)						
	1998	1999	2000	2001	2002	2003
Quarter 1	44%	48%	48%	42%	58%	60%
Quarter 2	38%	49%	48%	55%	58%	
Quarter 3	47%	38%	50%	55%	59%	
Quarter 4	45%	48%	50%	48%	59%	
Percentage of Fixed Rate Debt to Total Debt						
	83%	79%	83%	99%	99%	97%

DEBT MATURITY

Balances due on Maturity					
	March 31, 2003		December 31, 2002		March 31, 2003
	(\$000's) *	Average Interest Rate (%)	(\$000's) *	Average Interest Rate (%)	Future Principal Repayments (\$000's)
**2003	638	9.25	1,811	9.57	26,632
2004	26,936	5.18	27,748	5.81	62,779
2005	19,256	7.05	19,256	7.05	56,779
2006	21,575	6.98	21,575	6.98	61,387
2007	<u>35,636</u>	8.18	<u>35,636</u>	8.18	<u>77,034</u>
Total	<u>104,041</u>		<u>106,026</u>		<u>284,611</u>

* Balances due on maturity exclusive of normal periodic self-amortizing principal repayments

** For the balance of the year

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Supplemental financial information, page 5.

For the three months ended March 31, 2003

Allocation of Debt (including bank indebtedness)

	March 31, 2003	December 31, 2002
Recourse – Debt to Gross Book Value of Subject Assets	52.0%	51.0%
Non Recourse – Debt to Gross Book Value of Subject Assets	76.9%	76.3%
Total Debt to Gross Book Value	60.3%	59.3%
Non Recourse Debt as a Percentage of Total Debt	43.6%	42.1%

Other Statistics

	March 31, 2003	December 31, 2002
Mortgage term to maturity	12.7 years	12.8 years
Lease term to maturity	12.3 years	12.2 years
Tax deferred percentage of distributions	*50%	53%
Payout ratio (including gain on sale of income properties)	79.6%	86.2%

* Estimate

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