Annual Report 2012

GRANITE REIT

Table of Contents

77 King St. W., Suite 4010
P.O. Box 159, TD Centre
Toronto, ON, M5K 1H1 Canada

LETTER TO UNITHOLDERS

Dear Unitholders:

2012 was a transformational year for the company: at the outset, MI Developments Inc. and at the conclusion, Granite REIT. With the name change, new office location, investment in new people and conversion to a real estate investment trust, Granite is positioned for growth and diversification.

Granite's 2012 results reflect the execution of Granite's strategic plan. Importantly Granite has taken the necessary actions to stabilize and grow Granite.

The components of Granite's strategic plan are interdependent. However, it is crucial to note that the success with Granite's existing portfolio of assets and the continuing strengthening of Granite's relationship with its key tenant, Magna International Inc. are key factors in providing Granite with the foundation as well as the flexibility for future diversification and enhancement of its asset and tenant base.

Granite's 2012 initiatives allow Granite to grow and diversify based upon:

- A strong balance sheet, stable rental revenues, an enhanced credit facility and financing flexibility which enable Granite to focus on acquisitions and potential strategic sales.
- A major tenant and client in Magna, a world leader in its field, that is the backbone of Granite's stable revenue profile. Granite will continue to respect this relationship and deliver on commitments to its largest tenant.
- A management team and worldwide group of employees who are experienced in both the real estate and tenant relationship aspects of Granite REIT.
- An independent board of trustees that is focused on the best interests of all unitholders.

In implementing Granite's strategy, Granite completed its first significant acquisition in February 2013, an important step towards value creating growth, new tenant and new property diversification. Each of these themes will be the major thrusts as the year unfolds while Granite concentrates on investment in its key markets of Canada, the U.S. and selected parts of Europe. Granite enters 2013 positioned for growth and diversification of its asset base, rental revenues and net cash flow.

TOM HESLIP
March 5, 2013

Management's Discussion and Analysis of Results of Operations and Financial Position

For the three month period and year ended December 31, 2012

Management's Discussion and Analysis of Results of Operations and Financial Position (''MD&A'') of Granite Real Estate Inc. (''Granite'' or the ''Company'') summarizes the significant factors affecting the consolidated operating results, financial condition, liquidity and cash flows of Granite for the three month period and year ended December 31, 2012. Unless otherwise noted, all amounts are in Canadian dollars (''Cdn. dollars'') and all tabular amounts are in millions of Cdn. dollars. This MD&A should be read in conjunction with the accompanying audited consolidated financial statements for the year ended December 31, 2012, which are prepared in accordance with United States generally accepted accounting principles (''U.S. GAAP''). This MD&A is prepared as at March 5, 2013. Additional information relating to Granite, including the Annual Information Form (''AIF'') for fiscal 2012 can be obtained from the Company's website at www.granitereit.com, on SEDAR at www.sedar.com and on EDGAR at www.sec.gov.

In this MD&A, unless otherwise specified or the context otherwise indicates, ''Granite'', the ''Company'', ''we'', ''us'' and ''our'' refer to Granite Real Estate Inc. and its subsidiaries and, for periods subsequent to January 3, 2013, its successor entities Granite Real Estate Investment Trust (''Granite REIT'') and Granite REIT Inc., combined and its subsidiaries.

OVERVIEW

Granite is a Canadian-based real estate company engaged in the ownership and management of predominantly industrial properties in North America and Europe (the ''Real Estate Business'' or the ''Business''). As at December 31, 2012, the Company owned and managed approximately 28 million square feet in 104 rental income properties. Our tenant base currently includes Magna International Inc. and its operating subsidiaries (together ''Magna'') as our largest tenants, together with tenants from other industries.

Segmented Information and Discontinued Operations

The Company's reportable segments reflect the manner in which the Company is organized and managed by its senior management. The Company's operations have historically been segmented between the Business (continuing operations) and the Racing & Gaming Business (discontinued operations). Following the close of business on June 30, 2011, and as a result of a court-approved plan of arrangement (the ''Arrangement''), the financial position and results of operations of the assets transferred to entities owned by Mr. Frank Stronach and his family (the ''Stronach Shareholder'') including the Racing & Gaming Business, as well as those related to lands held for development, a property located in the United States and an income-producing property located in Canada (the assets and business transferred to the Stronach Shareholder pursuant to the Arrangement are collectively referred to as the ''Arrangement Transferred Assets & Business''), have been presented as discontinued operations and, as such, have been excluded from continuing operations. Accordingly, in the accompanying consolidated financial statements, the Company's single reportable segment pertains to the Company's income-producing properties.

REAL ESTATE BUSINESS — CONTINUING OPERATIONS

OVERVIEW

The real estate assets of our Business are comprised of income-producing properties and properties under development (see *''REAL ESTATE BUSINESS — RENTAL PORTFOLIO — Real Estate Properties'')*. Our income-producing properties consist of light industrial properties, heavy industrial manufacturing facilities, corporate offices, product development and engineering centres and test facilities. The Company holds a global portfolio of 104 income-producing industrial and commercial properties located in nine countries: Canada, the United States, Mexico, Austria, Germany, the Czech Republic, the United Kingdom, Spain and

Poland. This portfolio represents approximately 28 million square feet of leaseable area with a gross book value of approximately $1.7 billion (net book value of $1.1 billion) at December 31, 2012. The lease payments are primarily denominated in three currencies: the euro, the Cdn. dollar and the U.S. dollar.

SIGNIFICANT MATTERS

Completion of REIT Conversion

Effective January 3, 2013, the Company completed its conversion from a corporate structure to a stapled unit Real Estate Investment Trust (''REIT'') structure.

The Company's conversion to a REIT was implemented pursuant to a court approved plan of arrangement under the *Business Corporations Act* (Quebec). Under the plan of arrangement, all of the common shares of Granite Real Estate Inc. were exchanged, on a one-for-one basis, for stapled units, each of which consists of one unit of Granite REIT and one common share of Granite REIT Inc. Effective January 4, 2013, the stapled units started trading on the Toronto Stock Exchange under the symbol ''GRT.UN'' and on the New York Stock Exchange under the symbol ''GRP.U''. Granite REIT and Granite REIT Inc. are reporting issuers under Canadian provincial securities laws and file reports with the United States Securities & Exchange Commission (the ''SEC'') under U.S. securities laws and, through Granite REIT Holdings Limited Partnership and its subsidiaries, are carrying on the business previously conducted by Granite Real Estate Inc. The assets, liabilities and operations of the new combined stapled unit structure are comprised of all the assets, liabilities and operations of Granite Real Estate Inc.

Transition to International Financial Reporting Standards (''IFRS'')

In connection with the REIT conversion, the Company will adopt IFRS in place of the current U.S. GAAP reporting standards effective for interim and annual periods commencing after December 31, 2012. Comparative IFRS information for the 2012 fiscal periods will also be reported. Granite is in the process of finalizing its evaluation of the impact of the conversion to IFRS on the consolidated financial statements (see *''FUTURE CHANGES IN SIGNIFICANT ACCOUNTING POLICIES''*).

Currency Change for Financial Reporting and Dividends

The consolidated financial statements for periods prior to January 1, 2012 were reported using the U.S. dollar. As a result of the Company's shareholder base becoming increasingly Canadian and the Company's stated intention of converting to a Canadian REIT and to mitigate the impact of foreign exchange fluctuations on our reported results, effective January 1, 2012, the Company's reporting currency was changed to the Cdn. dollar. All comparative financial information contained in this MD&A and the accompanying consolidated financial statements for the three month period and year ended December 31, 2012 has been recast to reflect the Company's results as if they had been historically reported in Cdn. dollars. The consolidated U.S. dollar balance sheet at December 31, 2011 was translated into the Cdn. dollar reporting currency by translating assets and liabilities at the end-of-period exchange rate and translating equity balances at historical exchange rates. The consolidated statements of income (loss) were translated into Cdn. dollars using the weighted average exchange rate for the applicable period. The resulting foreign currency translation adjustment is reported as a component of other comprehensive income (loss) and accumulated other comprehensive loss (see *''NEW ACCOUNTING PRONOUNCEMENTS AND DEVELOPMENTS — Change in Reporting Currency''*). With the change in reporting currency, beginning May 9, 2012, dividends have been declared in Cdn. dollars and dividend payments have been made only in Cdn. dollars.

Acquisition of Two Properties in the United States

On February 13, 2013, a subsidiary of Granite REIT acquired a 90% interest in two income-producing multi purpose industrial properties located in the United States for approximately U.S. $35.8 million, excluding acquisition costs. The acquisition was funded through a combination of U.S. $14.3 million which was substantially sourced from Granite's credit facility and first mortgage debt of U.S. $21.5 million representing Granite REIT's proportionate share of the total first mortgage debt on the two properties.

FOREIGN CURRENCIES

Fluctuations in the Cdn. dollar's value relative to other currencies will result in fluctuations in the reported Cdn. dollar value of revenues, expenses, income, cash flows, assets and liabilities. At December 31, 2012, approximately 67% of the Business' rental revenues are denominated in currencies other than the Cdn. dollar (see *''REAL ESTATE BUSINESS — RENTAL PORTFOLIO — Annualized Lease Payments''*). As such, material changes in the value of the Cdn. dollar relative to these foreign currencies (primarily the euro and U.S. dollar) may have a significant impact on the Business' results.

The following table reflects the changes in the average exchange rates during the three month periods and years ended December 31, 2012 and 2011, as well as the exchange rates as at December 31, 2012, September 30, 2012 and December 31, 2011, between the most common currencies in which the Company conducts business and the Cdn. dollar.

	Average Exchange Rates Three Months Ended December 31,			**Average Exchange Rates Year Ended December 31,**		
	2012	2011	Change	**2012**	2011	Change
1 U.S. dollar equals Cdn. dollars	**0.991**	1.023	(3%)	**0.999**	0.989	1%
1 euro equals Cdn. dollars	**1.286**	1.379	(7%)	**1.285**	1.376	(7%)

	Exchange Rates as at				
	December 31, 2012	September 30, 2012	December 31, 2011	Change from September 30, 2012	Change from December 31, 2011
1 U.S. dollar equals Cdn. dollars	**0.995**	0.984	1.017	1%	(2%)
1 euro equals Cdn. dollars	**1.312**	1.265	1.319	4%	(1%)

The results of operations and financial position of all United States and most European operations are translated into Cdn. dollars using the exchange rates shown in the preceding table. The changes in these foreign exchange rates impacted the reported Cdn. dollar amounts of the Company's revenues, expenses, income, assets and liabilities. From time to time, the Company may enter into derivative financial arrangements for currency hedging purposes, but the Company's policy is not to utilize such arrangements for speculative purposes. Throughout this MD&A, reference is made, where relevant, to the impact of foreign exchange fluctuations on reported Cdn. dollar amounts.

RENTAL PORTFOLIO

Annualized Lease Payments

Annualized lease payments represent the total annual rent of the Business assuming the contractual lease payments as at the last day of the reporting period were in place for an entire year, with rents denominated in foreign currencies being converted to Cdn. dollars based on exchange rates in effect at the last day of the reporting period (see *''REAL ESTATE BUSINESS — FOREIGN CURRENCIES''*). The Company's annualized lease payments as at December 31, 2012, including the change from September 30, 2012 or December 31, 2011, are as follows:

	Three Months Ended December 31, 2012	**Year Ended December, 2012**
Annualized lease payments, beginning of period	$181.1	$182.8
Contractual rent adjustments	0.4	2.3
Completed projects on-stream	1.6	3.0
Disposals and vacancies	(0.6)	(0.9)
Renewals and re-leasing of income-producing properties	(0.6)	(0.7)
Effect of changes in foreign currency exchange rates	3.3	(1.3)
Annualized lease payments, as at December 31, 2012	**$185.2**	**$185.2**

During the fourth quarter of 2012, annualized lease payments increased by $4.1 million from $181.1 million at September 30, 2012 to $185.2 million at December 31, 2012. The strengthening of the euro and the U.S. dollar against the Cdn. dollar increased annualized lease payments by $3.3 million. The completion of an expansion project and roof and pavement improvement projects in the United States and Canada increased annualized lease payments by $1.6 million. Contractual rent adjustments increased annualized lease payments by $0.4 million, including $0.3 million related to Consumer Price Index (''CPI'') based increases on properties representing 1.4 million square feet of leaseable area in Austria and $0.1 million from fixed contractual adjustments on properties representing 0.3 million square feet of leaseable area in the United States and Canada. The vacancy of a 0.3 million square foot income-producing property in the United Kingdom reduced annualized lease payments by $0.6 million. Lease renewals of three properties in Canada, representing 0.5 million square feet of leaseable area, resulted in a net decrease in annualized lease payments by $0.6 million as two of these properties were re-leased at lower negotiated rental rates than the expiring lease rates.

On a year to date basis, annualized lease payments increased by $2.4 million from $182.8 million at December 31, 2011 to $185.2 million at December 31, 2012. Completed projects, related to expansion and roof and pavement improvement projects primarily in the United States, Germany and the Czech Republic, increased annual lease payments by $3.0 million. Contractual rent adjustments increased annualized lease payments by $2.3 million; including $1.6 million from CPI based contractual adjustments on properties representing 9.5 million square feet of leaseable area primarily in Canada, Austria and the United States and $0.7 million from fixed contractual adjustments on properties representing 0.9 million square feet of leaseable area. The weakening of the U.S. dollar and the euro against the Cdn. dollar reduced annualized lease payments by $1.3 million. Annualized lease payments were also negatively impacted by $0.6 million related to the vacancy of a property in the United Kingdom and by $0.3 million due to the disposal of an income-producing property in the United States. Renewals and re-leasing reduced annualized lease payments by a net $0.7 million due to lease renewals to five Magna tenants representing 0.7 million square feet of leaseable area.

The annualized lease payments by currency at December 31, 2012 and December 31, 2011 were as follows:

	December 31, 2012		December 31, 2011	
Euro	**$ 76.1**	**41%**	$ 74.6	41%
Canadian dollar	**61.9**	**33**	61.6	34
U.S. dollar	**46.0**	**25**	44.9	24
Other	**1.2**	**1**	1.7	1
	$185.2	**100%**	$182.8	100%

Lease Expiration

The following table sets out lease expiries, by square footage, for our portfolio at December 31, 2012.

(in thousands)	Vacant	2013	2014	2015	2016	2017	2018	2019 & Beyond	Total
Canada	392	1,174	—	586	368	3,583	913	951	7,967
U.S.	—	1,251	—	63	—	599	576	3,074	5,563
Mexico	143	714	—	68	—	1,097	75	307	2,404
Austria	—	447	—	81	299	5,702	1,129	379	8,037
Germany	—	1,835	—	—	29	—	389	1,084	3,337
Other	283	90	75	—	—	33	—	254	735
Total	**818**	**5,511**	**75**	**798**	**696**	**11,014**	**3,082**	**6,049**	**28,043**

Real Estate Properties

The Company's real estate assets are comprised of income-producing properties and properties under development. The net book values of the real estate assets are as follows:

	December 31, 2012	December 31, 2011
Income-producing real estate properties, net	**$1,131.8**	$1,152.2
Properties under development	**4.4**	2.6
Real estate properties, net	**$1,136.2**	$1,154.8

Income-Producing Properties:

At December 31, 2012, the Company had 104 income-producing properties, representing approximately 28 million square feet of rentable space. The income-producing properties are comprised predominantly of industrial buildings strategically located and leased primarily by Magna to provide automotive parts and modules to the world's manufacturers of cars and light trucks for their assembly plants throughout North America and Europe. The portfolio also includes several office buildings that comprise 3% of the total square footage of the Company's income-producing properties, including the head offices of Magna in Canada and Austria. The book value of the income-producing portfolio by country as at December 31, 2012 was as follows:

	Book Value	**Percent of Total**
Canada	$ 402.0	36%
Austria	293.9	26
U.S.	218.1	19
Germany	120.3	11
Mexico	62.6	5
Other countries	34.9	3
	$1,131.8	**100%**

During the third quarter of 2012, the Company disposed of a 0.1 million square foot income-producing property for net proceeds of $1.2 million and recorded a nominal loss on disposal.

Properties Under Development:

At December 31, 2012, the Company had five expansion and improvement projects in progress with the Magna group (two in Canada, two in the United States and one in the Czech Republic) and an improvement project to a 0.3 million square foot facility with a non-Magna tenant in Canada. The total projected cost of these expansion or improvement projects is approximately $11.8 million, of which $4.4 million was spent at December 31, 2012, with the remainder expected to be funded during 2013 from cash from operations.

BUSINESS AND OPERATIONS OF MAGNA, OUR LARGEST TENANT

Magna is the tenant at 89 of the Company's income-producing properties. Magna is a diversified global automotive supplier. Magna designs, develops and manufactures technologically advanced automotive systems, assemblies, modules and components, and engineers and assembles complete vehicles, primarily for sale to original equipment manufacturers of cars and light trucks. Magna's product capabilities span a number of major automotive areas, including interior systems, seating systems, closure systems, body and chassis systems, vision systems, electronic systems, exterior systems, powertrain systems, roof systems, hybrid electric vehicles/systems and complete vehicle engineering and assembly.

Granite's relationship with Magna is an arm's length landlord and tenant relationship governed by the terms of Granite's leases with Magna. The terms of the Company's lease arrangements with Magna generally provide for the following:

- obligation of Magna to pay for costs of occupancy, including operating costs, property taxes and maintenance and repair costs;
- rent escalations based on either fixed-rate steps or inflation;
- renewal options tied to market rental rates or inflation;
- environmental indemnities from the tenant; and
- right of first refusal in favour of Magna on sale of property.

Renewal terms, rates and conditions are typically set out in our leases with Magna and form the basis for tenancies that continue beyond the expiries of the initial lease terms.

Magna And The Automotive Industry

According to its public disclosure, Magna's success is primarily dependent upon the levels of North American and European car and light truck production by Magna's customers and the relative amount of content Magna has in the various programs. The challenges of the automotive industry, and other factors, have resulted in Magna seeking to take advantage of lower operating cost countries and consolidating, moving, closing and/or selling operating facilities to align its capacity utilization and manufacturing footprint with vehicle production and consumer demand. Granite management expects Magna to continuously seek to optimize its global manufacturing footprint and consequently, Magna may not renew leases for facilities currently under lease at the end of their expiries.

For the 2012 fiscal year, there were seven leases expiring representing 0.7 million of square feet and annual lease payments of $3.5 million or 1.9% of Granite's annualized lease payments at December 31, 2011. The 2012 lease expiries were all renewed with a weighted average lease term of 4.3 years and annual lease payments of $3.0 million at December 31, 2012. Five leases relating to 2013 expiries were also renewed during 2012, representing 0.8 million square feet and annual lease payments of $2.8 million. In addition, during the fiscal 2012 year, the lease expiries on three properties occupied by Magna were extended in conjunction with expansion projects undertaken at these properties. The weighted average lease term of these lease extensions is 7.4 years at December 31, 2012.

For the 2013 fiscal year, there are 26 leases expiring, representing 5.0 million of square feet and annual lease payments of $25.0 million, or 13.5% of Granite's annualized lease payments at December 31, 2012. A majority of these leases expire towards the end of the 2013 year. Negotiations on many of these leases are in progress and will continue throughout the year.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2012

Highlights

(in millions, except per share information)	Three Months Ended December 31, 2012	2011	Change
Statement of Income			
Rental revenue	**$ 45.3**	$ 46.4	(2%)
Property operating costs	**2.4**	0.6	300%
General and administrative	**10.3**	9.9	4%
Depreciation and amortization	**10.8**	11.0	(2%)
Interest expense and other financing costs, net	**4.1**	4.1	—
Foreign exchange losses (gains), net	**0.6**	(0.3)	300%
Write-down of long-lived assets	**—**	16.7	(100%)
Income before income taxes	**17.1**	4.4	289%
Income tax expense	**2.0**	0.8	150%
Income from continuing operations and net income	**$ 15.1**	$ 3.6	319%
Funds from Operations (''FFO'')	**25.9**	14.6	78%
Diluted FFO per share	**$ 0.55**	$ 0.31	77%
Cash Flows			
Income from continuing operations	**$ 15.1**	$ 3.6	319%
Items not involving current cash flows	**7.0**	26.8	(74%)
Change in non-cash working capital	**2.8**	(8.6)	133%
Cash provided by operating activities	**$ 24.9**	$ 21.8	14%
Real estate properties and fixed asset additions	**(7.4)**	(11.1)	33%
Cash used in other investing activities	**2.0**	—	100%
Cash used in investing activities	**$ (5.4)**	$(11.1)	51%
Dividends paid	**(23.4)**	(23.9)	(2%)
Cash used in other financing activities	**—**	0.3	(100%)
Cash used in financing activities	**$(23.4)**	$(23.6)	1%

Rental Revenue

Rental revenue for the three month period ended December 31, 2012 decreased $1.1 million to $45.3 million from $46.4 million in the prior year period. The change in rental revenues is discussed below:

Rental revenue, three months ended December 31, 2011	$46.4
Contractual rent adjustments	0.5
Completed projects on-stream	0.7
Renewals and re-leasing of income-producing properties	(0.4)
Vacancies of income-producing properties	(0.2)
Effect of changes in foreign currency exchange rates	(1.7)
Rental revenue, three months ended December 31, 2012	**$45.3**

The $0.5 million increase in revenue from contractual rent adjustments includes (i) $0.3 million from annual CPI based increases implemented in 2012 on properties representing 6.4 million square feet of leaseable area, (ii) $0.1 million from cumulative CPI based increases (being increases that occur every five years or once a specified cumulative increase in CPI has occurred) implemented in 2011 and 2012 on properties representing 4.2 million square feet of leaseable area and (iii) $0.1 million from fixed contract adjustments on properties representing 0.9 million square feet of leaseable area.

Completed projects on-stream contributed $0.7 million to rental revenue for the three month period ended December 31, 2012: (i) $0.2 million from the completion of seven Magna expansion projects in Austria, Germany, Mexico and the United States in 2011, which added a combined 0.4 million square feet of leaseable area, and (ii) $0.5 million from the completion of seven Magna expansion or improvement projects, such as roof and pavement replacements, in Austria, the Czech Republic, Germany, the United States and Canada in 2012, which added 0.3 million square feet of leaseable area.

Renewals and re-leasing had a $0.4 million negative impact on revenues compared to the prior year period. This decrease was primarily due to the renewal of a lease on a 0.3 million square foot facility to a Magna tenant in Canada, which was negotiated at a lower rental rate than the expiring lease rate.

Rental revenue for the three month period ended December 31, 2012 was also negatively impacted by $0.2 million due to a non-Magna tenant vacating a 0.3 million square foot facility in the United Kingdom.

Foreign exchange had a net $1.7 million negative impact on reported rental revenues. The strengthening of the Cdn. dollar against the average foreign exchange rates applied to our euro and U.S. dollar dominated rents resulted in a decrease in rental revenue of $1.3 million and $0.4 million, respectively.

Property Operating Costs

Property operating costs, which include real estate taxes, utilities, insurance, repairs and maintenance, legal and other property-related expenses, were $2.4 million for the three month period ended December 31, 2012 in comparison to $0.6 million in the prior year period. The $1.8 million increase was primarily due to a $1.6 million increase in land transfer taxes and related costs incurred with respect to internal reorganizations related to the REIT conversion and $0.3 million in appraisal, environmental and valuation costs associated with our income-producing properties. As part of the process of preparing for the REIT conversion and transition to IFRS, the Company undertook to appraise and fair value all properties during 2012. These increases were partially offset by a $0.3 million decrease in repairs and maintenance expenses not recoverable from tenants.

General and Administrative Expenses

General and administrative expenses increased by $0.4 million to $10.3 million in the fourth quarter of 2012 from $9.9 million in the prior year period. General and administrative expenses for the three month period ended December 31, 2012 include $3.8 million of advisory costs relating to the REIT conversion. General and administrative expenses for the three month period ended December 31, 2011 include $2.2 million of employee termination expense and recruiting costs, $1.9 million of legal, advisory and other costs pertaining to the strategic review process and $0.1 million of costs related to the REIT conversion. Excluding the employee termination expense, advisory and other costs mentioned above, general and administrative expenses increased by $0.8 million primarily due to higher compensation expense.

Depreciation and Amortization Expense

Depreciation and amortization expense was $10.8 million in the three month period ended December 31, 2012 compared to $11.0 million in the prior year period. The decrease of $0.2 million in depreciation expense was due to a $0.4 million reduction in foreign exchange fluctuations partially offset by $0.2 million of additional depreciation charges related to expansion and improvement projects that were completed in 2012.

Interest Expense and Other Financing Costs, Net

Net interest expense and other financing costs was $4.1 million in the three month periods ended December 31, 2012 and 2011. The impact of a $0.2 million decrease in interest expense in the fourth quarter of 2012 was offset by the impact of lower capitalized interest and interest income compared to the prior year period.

Foreign Exchange Losses (Gains), Net

The Company recognized net foreign exchange losses of $0.6 million in the three month period ended December 31, 2012 compared to net foreign exchange gains of $0.3 million in the prior year period. The drivers of foreign exchange gains and losses are primarily the re-measurement of certain assets and liabilities of Granite and its subsidiaries that are denominated in a functional currency that is different from the entity's reporting currency for accounting purposes. The foreign exchange net loss in the fourth quarter of 2012 includes a $0.4 million net loss on derivative financial instruments such as foreign exchange forward contracts.

Write-down of Long-Lived Assets

In the fourth quarter of 2011, it was determined that an industrial income producing property in each of Germany and Austria had indications of impairment and the inability for the Company to recover their carrying values. Both properties were tenanted by Magna's European interiors division which, as disclosed in Magna's public disclosures, had operating challenges. Accordingly, the Business recorded an impairment charge of $8.8 million for the Germany property and $7.9 million for the Austrian property which represented the excess of the carrying values of the assets over the estimated fair values determined based on the present value of the future estimated cash flows from the leased properties.

Income Tax Expense

Income tax expense for the fourth quarter of 2012 was $2.0 million, representing an effective tax rate of 11.7% compared to $0.8 million in the prior year period, representing a tax rate of 18.2%. The effective tax rate is lower in the fourth quarter of 2012 largely due to the changes in the Company's position with respect to differences related to prior period provisions and tax filings, and changes in unrecognized tax benefits.

Income From Continuing Operations and Net Income

Income from continuing operations and net income was $15.1 million in the three month period ended December 31, 2012 in comparison to $3.6 million in the prior year period. The increase of $11.5 million was primarily due to a decrease in the 2011 write-down of long-lived assets of $16.7 million, partially offset by higher property operating costs of $1.8 million, lower rental revenue of $1.1 million, a decrease in net foreign exchange gains of $0.9 million and higher income tax expense of $1.2 million.

Funds From Operations

	Three Months Ended December 31,		
(in thousands, except per share information)	**2012**	2011	Change
Income from continuing operations and net income	**$15,148**	$ 3,614	319%
Add back depreciation and amortization	**10,757**	10,962	(2%)
Funds from Operations (''FFO'')	**$25,905**	$14,576	78%
Basic and diluted FFO per share	**$ 0.55**	$ 0.31	77%
Basic number of shares outstanding	**46,833**	46,871	
Diluted number of shares outstanding	**46,866**	46,883	

The Company determines FFO using the definition prescribed in the U.S. by the National Association of Real Estate Investment Trusts (''NAREIT''). Under the definition of FFO prescribed by NAREIT, the impact of future income taxes and any asset impairments are included in the calculation of FFO and discontinued operations are excluded from the calculation of FFO. FFO and basic and diluted FFO per share are measures widely used by analysts and investors in evaluating the operating performance of real estate companies. However, FFO does not have a standardized meaning under U.S. GAAP and therefore may not be comparable to similar measures presented by other companies.

The $11.3 million increase in FFO compared to the prior year period is primarily due to higher income from continuing operations of $11.5 million, partially offset by decreased depreciation expense of $0.2 million (see *''RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2012''*).

RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2012 — CONTINUING OPERATIONS

The results of operations of the Business for the years ended December 31, 2012 and 2011, as discussed in this MD&A, from continuing operations include those from the income-producing property portfolio.

Highlights

(in millions, except per share information)	Years ended December 31, 2012	2011	Change
Rental revenue	**$181.1**	$180.9	—
Income before income taxes	**85.8**	53.6	60%
Income from continuing operations	**71.3**	57.9	23%
Funds from Operations ("FFO")	**114.1**	100.6	14%
Diluted FFO per share	**$ 2.43**	$ 2.14	14%

(in millions, except number of properties)	**December 31, 2012**	December 31, 2011	Change
Number of income-producing properties	**104**	105	(1%)
Leaseable area (sq. ft.)	**28.0**	27.9	—
Annualized lease payments ("ALP")	**$ 185.2**	$ 182.8	1%
Income-producing properties, at cost ("IPP")	**$1,659.3**	$1,643.8	1%
ALP as percentage of IPP	**11.2%**	11.1%	1%

Rental Revenue

Rental revenue for the year ended December 31, 2012 increased $0.2 million to $181.1 million from $180.9 million in the prior year period. The change in rental revenue is discussed below:

Rental revenue, year ended December 31, 2011	$180.9
Contractual rent adjustments	2.0
Completed projects on-stream	3.6
Renewals and re-leasing of income-producing properties	0.4
Vacancies of income-producing properties	(0.2)
Effect of changes in foreign currency exchange rates	(4.6)
Other, including straight-line adjustments of rental revenue	(1.0)
Rental revenue, year ended December 31, 2012	**$181.1**

The $2.0 million increase in revenue from contractual rent adjustments includes (i) $1.2 million from annual CPI based increases implemented in 2012 on properties representing 6.4 million square feet of leaseable area, (ii) $0.4 million from cumulative CPI based increases (being increases that occur every five years or once a specified cumulative increase in CPI has occurred) implemented in 2011 and 2012 on properties representing 4.6 million square feet of leaseable area and (iii) $0.4 million from fixed contract adjustments on properties representing 0.9 million square feet of leaseable area.

Completed projects on-stream contributed $3.6 million to rental revenue for the year ended December 31, 2012: (i) $2.4 million primarily from the completion of 12 Magna expansion projects in Austria, Germany, Mexico and the United States in 2011, which added a combined 0.4 million square feet of leaseable area, and (ii) $1.2 million from the completion of seven Magna expansion or improvement projects, such as roof and pavement replacements, in Austria, Germany, the Czech Republic, the United States and Canada in 2012, which added 0.3 million square feet of leaseable area.

Renewals and re-leasing had a net $0.4 million positive impact on revenues compared to the prior year period. Increased revenue of $0.8 million due to the commencement of a lease on a 0.3 million square foot facility, previously vacant, to a non-Magna tenant in June 2011, was partially offset by a $0.4 million decrease related to the renewal of a lease on a 0.3 million square foot facility to a Magna tenant in Canada, which was negotiated at a lower rental rate than the expiring lease rate.

Foreign exchange had a net $4.6 million negative impact on reported rental revenue. Revenue declined by $5.0 million as the average foreign exchange rate applied to our euro denominated rents weakened against the Cdn. dollar as compared to the prior year period. This decrease was partially offset by a $0.4 million increase in U.S. dollar rents as the average foreign exchange rate applied to these rents strengthened against the Cdn. dollar compared to the prior year period.

Other revenue had a $1.0 million negative impact on reported revenues and includes $0.4 million of straight-line rental revenue adjustments and $0.2 million of decreased revenue associated with the disposition of a property in the third quarter of 2012.

Property Operating Costs

Property operating costs, which include real estate taxes, utilities, insurance, repairs and maintenance, legal and other property-related expenses were $5.7 million for the year ended December 31, 2012 in comparison to $3.1 million in the prior year period. The $2.6 million increase in property operating costs was primarily due to a $1.8 million increase in appraisal, environmental and valuation costs associated with our income-producing properties. As part of the process of preparing for the REIT conversion and transition to IFRS, the Company undertook to appraise and fair value all properties during 2012. As previously noted, property costs for the year ended December 31, 2012 also included $1.6 million in land transfer taxes and other related costs associated with internal reorganizations related to the REIT conversion. These increased costs were partially offset by a $0.9 million reduction in repair and maintenance expenses primarily related to costs incurred on a vacant property in the second quarter of 2011 in conjunction with the re-leasing of the property to a non-Magna tenant in June 2011 and a decrease in repair and maintenance costs not recoverable from tenants.

General and Administrative Expenses

General and administrative expenses decreased by $15.8 million to $30.9 million in the year ended December 31, 2012 from $46.7 million in the prior year period. General and administrative expenses for the year ended December 31, 2012 include $7.9 million of advisory costs relating to the REIT conversion and $0.3 million of employee termination costs. General and administrative expenses for the year ended December 31, 2011 include $9.1 million of advisory and other related costs primarily incurred in connection with the Arrangement (see ''*ARRANGEMENT TRANSFERRED ASSETS & BUSINESS — SIGNIFICANT MATTERS — Plan of Arrangement*'') and the settlement of an outstanding legal proceeding, $7.6 million in employee termination costs and recruiting costs and $2.9 million of legal, advisory and other costs related to the strategic plan. Excluding the advisory and other costs mentioned above, general and administrative expenses decreased by $4.4 million primarily due to (i) reduced insurance expense of $2.6 million primarily related to reduced premiums associated with the Company's Directors' and Officers' liability insurance and (ii) decreased compensation of $1.7 million primarily due to payments made to a former executive of the Company and higher director fees in the prior year period related to the Arrangement (see ''*ARRANGEMENT TRANSFERRED ASSETS & BUSINESS — SIGNIFICANT MATTERS — Plan of Arrangement*'').

Depreciation and Amortization Expense

Depreciation and amortization expense increased by $0.1 million to $42.8 million in the year ended December 31, 2012 compared to $42.7 million in the prior year period primarily due to additional depreciation charges related to various expansion and improvement projects that were completed in 2011 and 2012, partially offset by the impact of foreign exchange.

Interest Expense and Other Financing Costs, Net

Net interest expense and other financing costs was $15.9 million in the year ended December 31, 2012 compared to $15.7 million in the prior year period. The increase in net interest expense is due to the lower capitalized interest of $0.7 million and lower interest income of $0.2 million during 2012 partially offset by a net $0.7 million reduction in interest expense related to short-term borrowings under the unsecured senior revolving credit facility.

Foreign Exchange Losses (Gains), Net

The Company recognized net foreign exchange losses of less than $0.1 million in the year ended December 31, 2012 compared to $0.2 million in net foreign exchange gains in the prior year period. The drivers of foreign exchange gains or losses are primarily the re-measurement of certain assets and liabilities of Granite and its subsidiaries that are denominated in a functional currency that is different from the entity's reporting currency for accounting purposes. The net foreign exchange loss for the year ended December 31, 2012 includes a net gain of $0.6 million on derivative financial instruments such as foreign exchange forward contracts (see note 18(e) in the consolidated financial statements for the year ended December 31, 2012).

Write-down of Long-lived Assets

During the year ended December 31, 2011, the Company recorded write-downs totalling $19.5 million with respect to income-producing properties in Austria, Germany and the United States. In the second quarter of 2011, the Business recorded a $2.7 million write-down of an income-producing commercial office building in the United States. In the fourth quarter of 2011, the Business recorded an $8.8 million and a $7.9 million impairment charge with respect to income-producing properties in Germany and Austria respectively (see *''RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2012''*). These write-downs represent the excess of the carrying value of the respective asset over the estimated fair value. Fair value was determined based on the present value of the estimated future cash flows from the leased property.

Income Tax Expense (Recovery)

Income tax expense for the year ended December 31, 2012 was $14.4 million compared to an income tax recovery of $4.4 million in the prior year period. The primary reason for the change is a result of the reversal in 2011 of the $12.9 million tax liability recorded in 2010 on an amalgamation that was set aside and cancelled by the Ontario Superior Court of Justice. Excluding the reversal of the liability relating to the internal amalgamation expense, the income tax expense for the year ended December 31, 2011 was $8.5 million representing an effective tax rate of 15.9% as compared to 16.8% in the current year period. Other factors influencing the current year's effective tax rate include changes in the mix of income earned in various countries in which the Company operates, an increase in the amount of unrecognized tax benefits, the revaluation of Canadian future tax liabilities related to the increase in the statutory Canadian income tax rate of 0.25% due to an enacted change to freeze the previously legislated Ontario tax rate reduction and decreases related to differences between prior period provisions and tax filings and lower non-deductible expenses.

Income From Continuing Operations

Income from continuing operations was $71.3 million in the year ended December 31, 2012 in comparison to $57.9 million in the prior year period. Excluding the recovery of income tax of $12.9 million noted above, income from continuing operations increased by $26.3 million primarily due to a decrease in the 2011 write-down of long-lived assets of $19.5 million and lower general and administrative expenses of $15.8 million. These decreases were partially offset by higher income tax expense of $5.9 million excluding the income tax recovery noted above, increased property operating costs of $2.6 million, higher net interest expense of $0.2 million and higher net foreign exchange losses of $0.3 million.

Funds From Operations

(in thousands, except per share information)	Year Ended December 31, 2012	2011	Change
Income from continuing operations	**$ 71,337**	$ 57,942	23%
Add back depreciation and amortization	**42,773**	42,701	—
Add back (deduct) loss (gain) on disposal of real estate	**21**	(91)	123%
Funds from Operations (''FFO'')	**$114,131**	$100,552	14%
Basic FFO per share	**$ 2.44**	$ 2.14	14%
Diluted FFO per share	**$ 2.43**	$ 2.14	14%
Basic number of shares outstanding	**46,855**	46,888	
Diluted number of shares outstanding	**46,876**	46,970	

As noted above, the Company determines FFO using the definition prescribed in the U.S. by NAREIT.

The $13.5 million increase in FFO compared to the prior year period is primarily due to increased income from continuing operations of $13.4 million (see *''RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2012 — Income From Continuing Operations''*).

LIQUIDITY AND CAPITAL RESOURCES — CONTINUING OPERATIONS

The Company generated cash flows from operations of $24.9 million and $116.6 million in the three month period and year ended December 31, 2012, respectively. At December 31, 2012, the Company had cash and cash equivalents of $51.1 million and shareholders' equity of $877.0 million.

Cash Flows

Three Months Ended December 31, 2012

Operating Activities

The Company generated cash from operations before changes in non-cash working capital balances of $22.1 million in the fourth quarter of 2012 compared to $30.4 million in the prior year period. The $8.3 million decrease is due to a decrease in items not involving cash flows of $19.8 million, partially offset by an $11.5 million increase in income from continuing operations (see *''RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2012''*).

The change in non-cash working capital balances provided cash of $2.8 million in the fourth quarter of 2012. The main drivers of the change in non-cash working capital for the three month period ended December 31, 2012 were:

— an increase in deferred revenue of $3.8 million primarily due to the timing of the receipt of rental payments and an ongoing capital project on behalf of non-Magna tenant. Under the terms of the lease agreement, the tenant is responsible for these costs. This reimbursement of costs will be recognized into revenue on a straight-line basis on the remaining lease term; and

— a $1.0 million increase in income taxes payable.

The increases in non-cash working capital balances are partially offset by:

— a $1.2 million increase in accounts receivable primarily due to the previously noted reimbursement of capital project costs from a non-Magna tenant; and

— a $1.2 million reduction in accounts payable and accruals.

In the fourth quarter of 2011, the change in non-cash working capital balances used cash of $8.6 million primarily due to a $5.7 million decrease in accounts payable and accrued liabilities and a $3.1 million decrease in deferred revenue due to the timing of the receipt of rental payments.

Investing Activities

Cash used in investing activities for the three month period ended December 31, 2012 was $5.4 million, which was a result of cash payments for real estate additions of $7.2 million, fixed asset additions of $0.2 million and a $0.5 million increase in other assets relating to a tenant inducement payment to a Magna tenant on renewal of their lease, partially offset by proceeds from the note receivable from the sale of Lone Star LP of $2.5 million. Cash used in investing activities for the fourth quarter of 2011 of $11.1 million was primarily due to capital expenditures on real estate properties.

Financing Activities

Cash used in financing activities for the three month period ended December 31, 2012 was related to dividend payments of $23.4 million. In the fourth quarter of 2012, the Company borrowed $42.0 million under its credit facility to facilitate corporate reorganizations in Europe. This amount was fully repaid during the quarter. In the fourth quarter of 2011, cash used in financing activities was $23.6 million, which included dividend payments of $23.9 million, partially offset by $0.3 million received from the exercise of stock options.

Year Ended December 31, 2012

Operating Activities

For the year ended December 31, 2012, the Company generated cash from operations before changes in non-cash working capital balances of $113.7 million compared to $120.0 million in the prior year period. The $6.3 million decrease is primarily due to a $19.7 million decrease in items not involving cash flows partially offset by a $13.4 million increase in income from continuing operations (see *''RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2012 — Income From Continuing Operations''*).

For the year ended December 31, 2012, the change in non-cash working capital balances was a source of cash of $3.0 million. The main drivers of the change in non-cash working capital for the year ended December 31, 2012 were:

— a $6.5 million increase in accounts payable primarily to due accruals related to advisory costs associated with the REIT conversion, higher compensation related accruals and an increase in the liability related to the deferred share units;

— a $3.1 million increase in deferred revenue primarily due to the timing of rental receipts and the previously noted deferral of the reimbursement of construction costs from a non-Magna tenant; and

— a $2.9 million decrease in accounts receivable primarily due to lower rent, process related costs and VAT receivables, partially offset by the capital project cost receivable as noted above.

These increases in non-cash working capital balances were partially offset by:

— a $8.9 million decrease in income taxes payable primarily due to the payment of taxes related to the 2011 reorganization; and

— a $0.5 million increase in restricted cash related to a segregated cash account associated with a construction holdback.

For the year ended December 31, 2011, the change in non-cash working capital balances used cash of $8.3 million which is comprised of:

— a $9.5 million decrease in accounts payable and accrued liabilities which includes a $3.0 million net reduction related to the redemption of deferred stock units by the Company's former directors following completion of the Arrangement;

— a $5.3 million decrease in income taxes payable; and

— a $3.9 million increase in accounts receivable due to process related costs receivable from tenants with respect to construction projects in Austria.

These uses of cash were partially offset by:

— a $5.7 million decrease in prepaid expenses and other due to the reduction in an amount related to the Company's Directors' and Officers' liability insurance; and

— a $4.8 million increase in deferred revenue primarily due to the receipt of a tenant payment with respect to a capital project. This amount is being amortized into revenue on a straight-line basis over the life of the lease.

Investing Activities

For the year ended December 31, 2012, investing activities used cash of $25.8 million which was comprised of $29.8 million of capital expenditures on real estate properties, $1.8 million of capital expenditures for fixed assets relating to our office moves and $0.3 million with respect to an increase in other assets. These uses of cash were partially offset by $5.0 million received as repayment of the note receivable from the sale of Lone Star LP and $1.2 million received with respect to the disposal of an income-producing property. For the year ended December 31, 2011, cash used in investing was $48.2 million which amount was primarily comprised of capital expenditures of $48.5 million for real estate additions. The decrease in capital expenditures on real estate properties in 2012 was a result of the reduction in expansion projects with Magna.

Financing Activities

Cash used in financing activities for the year ended December 31, 2012 was $96.0 million which included $93.8 million of dividend payments, $2.7 million related to the repurchase of common shares and $0.4 million in financing costs paid in respect to the credit facility that was entered into in February 2012, partially offset by $1.0 million in proceeds received on the issuance of shares from the exercise of stock options. Cash used in financing activities for the year ended December 31, 2011 of $45.9 million included $37.7 million of dividend payments, $13.0 million of net repayments of bank indebtedness under the unsecured senior revolving credit facility and a $2.2 million payment related to a mortgage on an income-producing property which matured in January 2011, partially offset by $7.0 million received from the exercise of stock options.

Bank and Debenture Financing

On February 7, 2012, the Company entered into an unsecured senior revolving credit facility in the amount of $50.0 million that was available by way of Cdn. dollar, U.S. dollar or euro denominated loans or letters of credit and was scheduled to mature on February 7, 2014. No amounts were drawn under the Company's credit facility as at December 31, 2012. The Company did not have a credit facility as at December 31, 2011.

On February 1, 2013, the Company replaced the above mentioned credit facility with an unsecured senior revolving credit facility in the amount of $175.0 million that is available by way of Cdn. dollar, U.S. dollar or euro denominated loans or letters of credit (the ''Granite Credit Facility'') and matures on February 1, 2015. However, the Company has the option to extend the maturity date by one year to February 1, 2016, subject to the agreement of lenders in respect of a minimum of 66⅔% of the aggregate amount committed under the Granite Credit Facility. The Granite Credit Facility provides the Company with the ability to increase the amount of the commitment by an additional aggregate principal amount of up to $75.0 million with the consent of the participating lenders.

Interest on drawn amounts will be calculated based on an applicable margin determined by the Company's external credit rating. Based on Granite's current credit rating, the Company would be subject to interest rate margins of up to 1.63% depending on the currency and form of advance.

In December 2004, Granite issued $265.0 million of 6.05% senior unsecured debentures (the ''Debentures''), which are due December 22, 2016, at a price of $995.70 per $1,000.00 of principal amount. The Debentures rank equally with all of Granite's existing and future unsecured indebtedness. At December 31, 2012, all of the Debentures remained outstanding. The total outstanding at December 31, 2012 was $263.6 million.

At December 31, 2012, the Company's debt to total capitalization ratio was 23%. Management believes that the Company's cash resources, cash flow from operations and available third-party borrowings will be sufficient to finance its operations and capital expenditures program over the next year. Additional acquisition and development activity will depend on the availability of suitable investment opportunities and related financing.

At December 31, 2012, the Company was in compliance with its debt agreements and related covenants.

Credit Ratings

On October 11, 2011, DBRS confirmed the BBB rating on the Company's senior unsecured debentures with a stable trend. On November 21, 2011, Moody's Investors Service announced that it had upgraded Granite's senior unsecured debenture ratings to Baa3, from Ba1 with a stable outlook.

ARRANGEMENT TRANSFERRED ASSETS & BUSINESS (INCLUDED IN DISCONTINUED OPERATIONS)

On June 30, 2011, the Company completed the Arrangement whereby the Arrangement Transferred Assets & Business were transferred to the Stronach Shareholder in consideration for the cancellation of the Company's dual class share structure through which the Stronach Shareholder controlled the Company. As a result of the Arrangement, the financial position and results of operations of the Racing & Gaming Business, as well as those related to lands held for development, a property located in the United States and an income-producing property located in Canada, have been presented as discontinued operations. For the three month period and year ended December 31, 2012, and for the six month period ended December 31, 2011, the Company's results of operations were not impacted by the Arrangement Transferred Assets & Business as they were transferred to the Stronach Shareholder effective June 30, 2011.

SIGNIFICANT MATTERS

Plan of Arrangement

On June 30, 2011, the Company completed the Arrangement under the *Business Corporations Act* (Ontario) which eliminated the Company's dual class share capital structure through which the Stronach Shareholder controlled the Company. Definitive agreements with respect to the Arrangement were entered into by the Company on January 31, 2011. The Arrangement was approved on March 29, 2011 by 98.08% of the votes cast by shareholders at the annual general and special meeting and on March 31, 2011, the Ontario Superior Court of Justice issued a final order approving the Arrangement. The Arrangement eliminated the Company's dual class capital structure through:

i) the purchase for cancellation of 363,414 Class B Shares held by the Stronach Shareholder upon the transfer to the Stronach Shareholder of the Company's Racing & Gaming Business including U.S. $20 million of working capital at January 1, 2011, substantially all of the Company's lands held for development and associated assets and liabilities (the Company was granted an option to purchase at fair value certain of these development lands if needed to expand the Company's income-producing properties), a property located in the United States, an income-producing property located in Canada and cash in the amount of U.S. $8.5 million. In addition, the Stronach Shareholder received a 50% interest in the note receivable and cash proceeds from the sale of Lone Star LP, a 50% interest in future payments, if any, under a holdback agreement relating to Magna Entertainment Corp.'s (''MEC's'') prior sale of The Meadows racetrack and a second right of refusal (behind Magna's first right of refusal) in respect of certain properties owned by the Company and leased to Magna in Oberwaltersdorf, Austria and Aurora, Canada; and

ii) the purchase for cancellation by the Company of each of the other 183,999 Class B Shares in consideration for 1.2 Class A Subordinate Voting Shares per Class B Share, which following cancellation of the Class B Shares and together with the then outstanding Class A Subordinate Voting Shares were renamed Common Shares.

The Maryland Jockey Club Complaint

On February 15, 2011, Power Plant Entertainment Casino Resorts Indiana, LLC, PPE Casino Resorts Maryland, LLC and The Cordish Company (the ''Plaintiffs'') sued, among other defendants, the Company, certain subsidiary entities and joint ventures, including The Maryland Jockey Club and certain of its subsidiaries (collectively, the ''MJC Entities''), as well as the Company's former Chairman and Chief Executive Officer, Mr. Frank Stronach, in the Circuit Court for Baltimore City in Baltimore, Maryland. The claims asserted in the Plaintiffs' complaint against the Company, the MJC Entities and Mr. Stronach (the ''Complaint'') are alleged to have arisen from events that occurred in Maryland in connection with the referendum conducted in November 2010 concerning the award of a gaming license to one of the Plaintiffs to conduct alternative gaming at the Arundel Mills Mall. The Complaint asserts a number of claims against all the defendants including, among other allegations, that the Company and Mr. Stronach, along with a number of other defendants, engaged in actions to defame the Plaintiffs by distributing allegedly false information concerning the Plaintiffs and their operations of a gaming facility in Indiana, Indianapolis Downs, LLC operating as Indiana Live. The specific claims asserted against the Company, the MJC Entities and Mr. Stronach are for alleged civil conspiracy, false light, invasion of privacy and defamation. The Complaint seeks an award of damages against all defendants in the amount of U.S. $300 million in compensatory damages and U.S. $300 million in punitive damages. Granite believes this claim is without merit. On March 25, 2011, a number of defendants, including the MJC Entities and the Company, filed a motion in the Circuit Court for Baltimore City, seeking to have the action transferred to the Circuit Court for Anne Arundel County. On April 29, 2011, the Indiana-based defendants named in the Complaint filed a notice to remove the Plaintiffs' claims relating to the Indiana defendants to the U.S. District Court for the District of Maryland. The Plaintiffs have sought to remand these claims to the Circuit Court for Baltimore City. The entire matter, in both the state and federal courts, was stayed by the United States Bankruptcy Court for the District of Delaware until it determined whether the claims were impacted by the bankruptcy of Indianapolis Downs, LLC. On September 6, 2011, the United States Bankruptcy Court for the District of Delaware entered an order denying the injunction motion and lifting the stay effective September 26, 2011. On December 21, 2011, the Circuit Court for Baltimore City issued an order staying the state court defendants' motions to transfer venue to the Circuit Court for Anne Arundel County pending resolution of whether the Maryland federal court action was remanded out of federal court. On September 26, 2012, the Maryland federal court issued an order remanding the Maryland federal court action to the Circuit Court for Baltimore City. On October 2, 2012, the parties filed a stipulation with the Circuit Court for Baltimore City proposing a further stay to allow certain of the defendants to engage plaintiffs in discussions that may potentially streamline the litigation. The stay was granted by the Circuit Court for Baltimore City on October 12, 2012. Under the terms of the Arrangement, the Company received an indemnity from the Stronach Shareholder and certain related parties against all losses suffered by the Company in relation to the Racing & Gaming Business for the period prior to, on and after the effective date of the transfer of June 30, 2011. Accordingly the Company has not recorded a liability related to this claim. Granite provided the Stronach Shareholder with the required disclosure notice listing the existing litigation with the Plaintiffs. The Company has retained independent counsel to monitor the litigation on its behalf.

MEC's Chapter 11 Filing and Plan of Reorganization

On March 5, 2009, MEC and certain of its subsidiaries filed voluntary petitions for reorganization under Chapter 11 of Title 11 of the United States Code (the ''Bankruptcy Code'') in the United States Bankruptcy Court for the District of Delaware and were granted recognition of the Chapter 11 proceedings from the Ontario Superior Court of Justice under section 18.6 of the Companies' Creditors Arrangement Act in Canada. On February 18, 2010, the Company announced that MEC had filed the Joint Plan of Affiliated Debtors, an agreement amongst the Official Committee of Unsecured Creditors, the Company and MI Developments US Financing Inc. pursuant to the Bankruptcy Code (as amended, the ''Plan'') and related Disclosure Statement in connection with the MEC Chapter 11 proceedings. The Plan provided, among other things, that the assets of MEC remaining after certain asset sales were to be transferred to the Company, including, among other assets, Santa Anita Park, Golden Gate Fields, Gulfstream Park (including MEC's interest in The Village at Gulfstream Park™, a joint venture between MEC and Forest City Enterprises, Inc.), Portland Meadows, AmTote International, Inc. and XpressBet, Inc. On March 23, 2010, the Plan was amended to include the transfer of MJC to the Company (together with the assets referred to in the preceding sentence, the ''MEC Transferred

Assets''). On April 30, 2010, the closing conditions of the Plan were satisfied or waived, and the Plan became effective following the close of business on April 30, 2010.

INCOME FROM DISCONTINUED OPERATIONS — YEAR ENDED DECEMBER 31, 2012

	Year Ended December 31,	
	2012	2011
Revenues	$ —	$262.3
Purses, awards and other	—	148.6
Operating costs	—	80.2
Property operating costs	—	0.9
General and administrative	—	21.8
Depreciation and amortization	—	3.4
Interest income	—	(0.3)
Foreign exchange gains	—	(0.1)
Equity loss	—	2.0
Income before income taxes	—	5.8
Income tax recovery	—	(1.2)
Income from operations	—	7.0
Net gain on disposition of discontinued operations, net of income taxes of $10.5 million	—	87.4
Income from discontinued operations	$ —	$ 94.4

Income from operations for the year ended December 31, 2011 amounts to $7.0 million and is comprised of net income from the Racing & Gaming Business of $9.8 million partially offset by net losses of $2.8 million from lands held for development, a property located in the United States and an income-producing property located in Canada. The Racing & Gaming Business net income included $2.0 million of its proportionate share of losses from joint venture investments. The remainder of the Racing & Gaming Business net income was generally reflective of the seasonality of when the racetracks hold live racing. The net loss of $2.8 million from the lands held for development primarily relates to carrying costs associated with these properties.

NET INCOME

Three months ended December 31, 2012

Net income for the fourth quarter of 2012 increased by $11.5 million to $15.1 million from $3.6 million in the prior year period. The increase was due to the reasons noted above (see *''RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED DECEMBER 31, 2012''*).

Year ended December 31, 2012

Net income for the year ended December 31, 2012 decreased by $81.1 million to $71.3 million from $152.4 million in the prior year period. The decrease was due to the decrease in income from discontinued operations of $94.4 million partially offset by an increase in income from continuing operations of $13.4 million (see *''RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2012 — Income From Continuing Operations''*).

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Chief Executive Officer and the Chief Financial Officer of Granite have evaluated the effectiveness of Granite's disclosure controls and procedures, as defined in National Instrument 52-109 — *Certification of Disclosure in Issuers' Annual and Interim Filings* (''NI 52-109''), as of the end of the period covered by the annual filings (as defined in NI 52-109) (the ''Evaluation Date''). They have concluded that, as of the Evaluation Date, Granite's disclosure controls and procedures were effective to ensure that material information relating to Granite and its consolidated subsidiaries would be made known to them by others within those entities and would be disclosed on a timely basis. However, as recommended by Canadian and United States securities regulators, the Company will continue to periodically evaluate its disclosure controls and procedures and will make modifications from time to time as deemed necessary to ensure that information is recorded, processed, summarized and reported within the time periods specified in the applicable rules.

Report on Internal Control Over Financial Reporting

Granite's management is responsible for establishing and maintaining internal control over financial reporting (as such term is defined in NI 52-109 and Rules 13a-15(f) and 15d-15(f) under the United States Securities Exchange Act of 1934) for the Company. Under the supervision and with the participation of Granite's Chief Executive Officer and Chief Financial Officer, management conducted an evaluation of the effectiveness of Granite's internal control over financial reporting, as of the Evaluation Date, based on the framework set forth in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its evaluation under this framework, management concluded that Granite's internal control over financial reporting was effective as of the Evaluation Date.

Ernst & Young LLP, an independent licensed public accounting firm, who audited Granite's consolidated financial statements for the year ended December 31, 2012 and whose report is included in Granite's annual report for fiscal 2012, has also issued an attestation report under standards of the Public Company Accounting Oversight Board (United States) on Granite's internal control over financial reporting as of the Evaluation Date. The attestation report precedes the financial statements included in Granite's annual report for fiscal 2012.

Changes in Internal Control Over Financial Reporting

As of the Evaluation Date, there have been no changes in Granite's internal control over financial reporting that occurred during the period beginning on the date immediately following the end of the period in respect of which Granite made its most recent previous interim filing and ended on December 31, 2012 that have materially affected, or are reasonably likely to materially affect, Granite's internal control over financial reporting.

Limitation on the Effectiveness of Controls and Procedures

Granite's management, including the Chief Executive Officer and the Chief Financial Officer, does not expect that Granite's controls and procedures will prevent all potential error and fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

COMMITMENTS, CONTRACTUAL OBLIGATIONS, CONTINGENCIES AND OFF-BALANCE SHEET ARRANGEMENTS

In the ordinary course of business activities, the Company may become subject to litigation and other claims brought by, among others, customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required. Although it is not possible to accurately estimate the extent of potential costs and losses, if any, management believes, but can provide no assurance, that the ultimate resolution of such claims would not have a material adverse effect on the financial position of the Company.

The Company has made commitments for future payments of interest and principal on long-term debt and construction and development project costs. At December 31, 2012, future payments, including interest payments, under these contractual obligations were as follows:

(in thousands)	2013	2014	2015	2016	2017	Thereafter	Total
Debentures	$16,033	$16,033	$16,033	$281,033	$ —	$ —	$329,132
Operating leases	421	421	421	421	208	453	2,345
Construction and development project commitments	8,557	—	—	—	—	—	8,557
Other	500	—	—	—	—	—	500
Total	$25,511	$16,454	$16,454	$281,454	$208	$453	$340,534

At December 31, 2012, the Company had $1.1 million of letters of credit issued with various financial institutions to guarantee its performance under various construction projects. These letters of credit are secured by cash deposits of the Company.

Off-balance sheet arrangements consist of letters of credit, construction and development project commitments, foreign currency forward contacts and certain operating agreements.

For further discussion of commitments, contractual obligations, contingencies and off-balance sheet arrangements, refer to notes 7, 9, 18 and 22 to the consolidated financial statements and ''*LIQUIDITY AND CAPITAL RESOURCES*''.

RELATED PARTY TRANSACTIONS

For a discussion of the Company's transactions with related parties, please refer to notes 1, 15, 19 and 21 to the consolidated financial statements and the section in this MD&A entitled *''ARRANGEMENT TRANSFERRED ASSETS & BUSINESS — SIGNIFICANT MATTERS*''.

NEW ACCOUNTING PRONOUNCEMENTS AND DEVELOPMENTS

Information on new accounting standards and developments is detailed in note 1 of the Company's consolidated financial statements. The accounting standards adopted that impacted the Company's financial statements are as follows:

Fair Value Measurement

In May 2011, the Financial Accounting Standards Board (''FASB'') issued Accounting Standards Update (''ASU'') 2011-04, ''Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS''. The new guidance results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and IFRS. The amendments are applied prospectively and are effective for interim and annual periods beginning after December 15, 2011. The adoption of ASU 2011-04, effective January 1, 2012, did not have any impact on the Company's consolidated financial statements except for additional disclosure requirements when applicable particularly in relation to Level 3 fair value measurements.

Comprehensive Income

In June 2011, the FASB issued ASU 2011-05, ''Comprehensive Income (Topic 220): Presentation of Comprehensive Income''. ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity, and requires the presentation of components of net income and other comprehensive income either in a single continuous statement or in two separate but consecutive statements. ASU 2011-05 is effective, on a retrospective basis, for interim and annual periods beginning after December 15, 2011. The adoption of ASU 2011-05, effective January 1, 2012, did not have any impact on the Company's consolidated financial statements.

Change in Reporting Currency

The consolidated financial statements for periods prior to January 1, 2012 were reported using the U.S. dollar. With the change in the reporting currency, all comparative financial information has been recast from U.S. dollars to Cdn. dollars to reflect our consolidated financial statements as if they had been historically reported in Cdn. dollars. The consolidated U.S. dollar balance sheet at December 31, 2011 was translated into the Cdn. dollar reporting currency by translating assets and liabilities at the end-of-period exchange rate and translating equity balances at historical exchange rates. The consolidated statements of income (loss) were translated into Cdn. dollars using the weighted average exchange rate for the applicable period. The resulting foreign currency translation adjustment is reported as a component of other comprehensive income (loss) and accumulated other comprehensive loss. The impact of the change in reporting currency on the consolidated statement of income (loss) for the three month period and year ended December 31, 2011, and the net assets/shareholders' equity as at December 31, 2011 on the Company's balance sheet, is summarized in the tables below:

Three month period ended December 31, 2011 (in millions, except per share information)	**As Previously Reported**	**Foreign Exchange**	**As Recast**
Consolidated statement of income	USD		CDN
Revenues	$ 45.3	$ 1.1	$ 46.4
Income from continuing operations and net income	3.5	0.1	3.6
Diluted earnings from continuing operations per Common or Class B Share	0.08	—	0.08

Year ended December 31, 2011 (in millions, except per share information)	**As Previously Reported**	**Foreign Exchange**	**As Recast**
Consolidated statement of income	USD		CDN
Revenues	$ 182.9	$ (2.0)	$ 180.9
Income from continuing operations	59.2	(1.3)	57.9
Net income	155.8	(3.4)	152.4
Diluted earnings from continuing operations per Common or Class B Share	1.26	(0.03)	1.23

As at December 31, 2011	**As Previously Reported**	**Foreign Exchange**	**As Recast**
Consolidated balance sheet	USD		CDN
Common Shares	$1,521.1	$ 598.4	$ 2,119.5
Contributed surplus	57.6	4.6	62.2
Deficit	(845.8)	(30.6)	(876.4)
Accumulated other comprehensive income (loss)	161.1	(557.2)	(396.1)
Total shareholders' equity	**$ 894.0**	**$ 15.2**	**$ 909.2**

The $598.4 million impact of the change in reporting currency on Common Shares is due to the effect of translating the consolidated balance at the historical exchange rate. The Cdn. dollar has appreciated since the formation of the Company. The resulting impact of translating Common Shares, contributed surplus and deficit at historical rates is recorded in accumulated other comprehensive loss.

FUTURE CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

IFRS Transition

Granite will adopt IFRS in place of U.S. GAAP reporting standards for interim and annual periods commencing after December 31, 2012. Comparative IFRS information for the previous fiscal year will also be provided, including the Company's IFRS transition balance sheet as at January 1, 2012.

The following discussion has been prepared using the standards and interpretations currently issued and expected to be effective at the end of the Company's first annual IFRS reporting period, which will be December 31, 2013. Certain accounting policies expected to be adopted under IFRS may not be adopted and the application of such policies to certain transactions or circumstances may be modified and, as a result, the impact of Granite's conversion to IFRS may be different than its current expectation.

Management does not expect that the adoption of IFRS will have any material impact on the Company's business activities or cash flows. However, it will impact certain aspects of Granite's reported financial results, the more significant of which relate to the accounting for investment properties, classification of leases, accounting for income taxes, classification of trust units, certain financial statement presentation and disclosure matters and the effects of transitional provisions of IFRS for first time adopters. The nature of the adjustments that are anticipated in our first quarter 2013 interim results are described below:

a) Real estate properties — The Company considers its real estate properties to be investment properties under International Accounting Standard 40, Investment Property (''IAS 40''). Similar to U.S. GAAP, investment property is initially recorded at cost, however, subsequent to initial recognition, IFRS requires that an entity choose either the cost or fair value model to account for its investment properties. Granite expects to use the fair value model when preparing its financial statements under IFRS. Using internal resources as well as independent appraisers, fair value will primarily be determined by discounting the expected future cash flow, generally over 10 years, and using a weighted average discount and terminal capitalization rate which takes into account several factors including the nature, jurisdiction and location of the property. Based on the preliminary work completed to date, the fair value of Granite's investment properties is estimated to be at least equal to gross book value. In connection with recording investment properties at fair value, deferred leasing commissions, tenant inducements and certain deferred rent receivable and deferred revenue balances will not be recognized. Recording investment properties at fair value will also result in adjustments to Granite's deferred tax balances. Depreciation and impairments are not recorded under the fair value model, however, the gains or losses arising from a change in the fair value of investment properties in a period will be recognized in income. The adjustments as a result of implementing the fair value model as at January 1, 2012 will be recorded to opening deficit.

b) Cumulative foreign currency translation differences — IAS 21, The Effects of Changes in Foreign Exchange Rates, requires an entity to determine the translation differences in accordance with IFRS from the date a subsidiary was formed. IFRS allows cumulative translation differences for all foreign operations to be deemed zero at the date of transition to IFRS. Granite expects to deem all cumulative translation differences to be zero on transition to IFRS by adjusting amounts through opening deficit.

c) Trust Units — In conjunction with the REIT conversion, Granite's Common Shares were exchanged for stapled units. Under IAS 32, Financial Instruments, equity instruments can be considered a liability if the holder has the right to put the instrument back to the issuer for cash or another financial asset unless certain conditions are met. Granite expects to meet the conditions that will result in the stapled units being presented as equity in its financial statements. Notwithstanding the presentation of these units as equity, the aforementioned exception provided for the presentation of the stapled units as equity does not extend to the accounting for share-based payments. Accordingly, Granite's stock option and share unit plans, as amended under the REIT conversion, will be recorded as liabilities upon conversion to a REIT and revalued at each interim period.

d) Income Taxes — Under both U.S. GAAP and IFRS, deferred income taxes are recorded for the temporary differences arising in respect of its assets and liabilities at the tax rates that are expected to apply to the period when the asset is realized or the liability settled, based on tax rates and laws that have been enacted or substantively enacted by the reporting date. Primarily, as a result of the increase to the carrying value of investment properties from the fair value adjustment on transition, a deferred tax liability will be recorded at January 1, 2012. However, as a result of the REIT conversion effective January 3, 2013, it is anticipated that certain deferred tax amounts will be reversed as an adjustment to deferred tax expense. Additionally, Granite is continuing to evaluate the application of IAS 12, Income Taxes, to certain of its subsidiaries, particularly those qualifying as a REIT for tax purposes.

Management continues to evaluate the potential impact that IFRS will have on the Company's consolidated financial statements particularly as it relates to the REIT conversion. Granite also expects the transition to IFRS to impact internal controls, information technology systems and other procedures primarily as it relates to the real estate valuation process as well as new disclosures in the financial statements required under IFRS. Management has monitored new contractual agreements for IFRS impact and does not expect the adoption of IFRS to have an impact on compensation arrangements.

OUTSTANDING SHARES AND STAPLED UNITS

As part of the REIT conversion, effective January 3, 2013, Granite Real Estate Inc. acquired and cancelled 46,832,908 of its Common Shares, being 100% of its issued and outstanding Common Shares. Under the plan of arrangement all Common Shares of the Company were exchanged for stapled units, each of which consists of one unit of Granite REIT and one common share of Granite REIT Inc. (see *''SIGNFICANT MATTERS — Completion of REIT Conversion'')*. As at the date of this MD&A, Granite REIT had 46,882,891 stapled units issued and outstanding. The increase of 49,983 stapled units results from 50,000 stock options exercised subsequent to the REIT conversion net of the repurchase for cash of 17 Common Shares from dissenting shareholders.

DIVIDENDS AND DISTRIBUTIONS

In March 2012, the Board of Directors (the ''Board'') declared a dividend of U.S. $0.50 in respect of the three month period ended December 31, 2011, which was paid on or about April 12, 2012 to shareholders of record at the close of business on March 23, 2012. In May, August and November 2012, the Board declared a quarterly dividend with respect to the three month periods ended March 31, June 30, and September 30, 2012, respectively. The dividends of Cdn. $0.50 per Common Share were paid on or about June 14, 2012, September 13, 2012 and December 13, 2012, to shareholders of record at the close of business on May 25, 2012, August 24, 2012 and November 23, 2012, respectively.

In conjunction with the REIT conversion, in January and February 2013, the Board of Trustees of Granite REIT declared monthly distributions with respect to the one month periods ended January 31, 2013 and February 28, 2013, respectively. The distribution of $0.175 per stapled unit declared in January 2013 was paid on February 15, 2013 to unitholders of record at the close of business on January 31, 2013 and the distribution declared in February 2013 will be paid on March 15, 2013 to unitholders of record at the close of business on February 28, 2013.

CRITICAL ACCOUNTING ESTIMATES

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates that affect the amounts reported and disclosed in the consolidated financial statements. Management bases estimates on historical experience and various other assumptions that are believed to be reasonable in the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. On an ongoing basis, management evaluates its estimates. However, actual results could differ from those estimates under different assumptions or conditions.

The Company's significant accounting policies are included in note 1 to the consolidated financial statements. Management believes the following critical accounting policies involve the most significant judgments and estimates used in the preparation of the Company's consolidated financial statements.

Principles Of Consolidation

We consolidate entities when we have the ability to control the operating and financial decisions and policies of that entity, including if the entity is determined to be a variable interest entity and we are the primary beneficiary. We apply the equity method of accounting where we can exert significant influence, but not control, over the operating and financial decisions and policies of the entity. We use the cost method of accounting where we are unable to exert significant influence over the entity.

Long-lived Assets

The Company's most significant asset is its net investment in real estate properties. Properties are stated at cost less accumulated depreciation, reduced for impairment losses where appropriate. The carrying values of the Company's long-lived assets (including real estate properties and fixed assets) not held for sale are evaluated at least annually or whenever events or changes in circumstances present indicators of impairment. If such indicators are present, the Company completes a net recoverable amount analysis for the long-lived assets by determining whether the carrying value of such assets can be recovered through projected undiscounted cash flows. If the sum of expected future cash flows, undiscounted and without interest charges, is less than net book value, the excess of the net book value over the estimated fair value, based on discounted future cash flows and, if appropriate, appraisals, is charged to operations in the period in which such impairment is determined by management.

When properties are classified by the Company as available for sale or discontinued operations, the carrying value is reduced, if necessary, to the estimated net realizable value. ''Net realizable'' value is determined based on discounted net cash flows of the assets and, if appropriate, appraisals and/or estimated net sales proceeds from pending offers.

For real estate properties, depreciation is provided on a straight-line basis over the estimated useful lives of buildings, which typically range from 20 to 40 years.

Accounting estimates related to long-lived assets and the impairment assessments thereof, are subject to significant measurement uncertainty and are susceptible to change as such estimates require management to make forward-looking assumptions regarding cash flows and business operations. Any resulting impairment charge could have a material impact on the Company's results of operations and financial position.

Cost Capitalization

The Company capitalizes acquisition, development and expansion costs, including direct construction costs, interest and indirect costs wholly attributable to development. Interest is capitalized to projects under development or construction based on the average accumulated expenditures outstanding during the period multiplied by the Company's average borrowing rate on existing debt. The Company capitalizes direct and indirect costs, including real estate taxes and certain operating expenses of the development property if activities necessary to ready the development property for its intended use is in progress. Costs of internal personnel and other indirect costs that are not wholly attributable to a project are expensed as incurred. Project related costs are capitalized until the project is substantially completed and the property is available for occupancy.

Stock-Based Compensation

Compensation expense for stock options is based on the fair value of the options at the grant date and is recognized over the period from the grant date to the date the award is vested and its exercisability does not depend on continued service by the option holder. Compensation expense is recognized as general and administrative expenses, with a corresponding amount included in equity as contributed surplus. The contributed surplus balance is reduced as options are exercised and the amount initially recorded for the options in contributed surplus is credited to Common Shares, along with the proceeds received on exercise. In the event that options are forfeited or cancelled prior to having vested, any previously recognized expense is reversed in the period of forfeiture or cancellation.

The fair value of stock options is estimated at the date of grant using the Black-Scholes option valuation model. The Black-Scholes option valuation model was developed for use in estimating the fair value of freely traded options, which are fully transferable and have no vesting restrictions. In addition, this model requires the input of subjective assumptions, including expected dividend yields, future stock price volatility and expected time until exercise. Although the assumptions used reflect management's best estimates, they involve inherent uncertainties based on market conditions outside of the Company's control. Because the Company's outstanding stock options have characteristics that are significantly different from those of traded options, and because changes in any of the assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide the only measure of the fair value of the Company's stock options.

The Company's restricted share unit plan is measured at fair value at the date of grant and amortized to compensation expense from the effective date of the grant to the final vesting date. Compensation expense is recognized in general and administrative expenses with a corresponding amount included in equity as contributed surplus. The contributed surplus balance is reduced and credited to Common Shares as shares are issued in satisfaction of the share units. Restricted share units granted under this plan may be subject to cliff or graded vesting. Compensation expense for awards with cliff or graded vesting is recognized on a straight-line basis over the period from grant date to the final vesting date.

For further details, refer to note 13 to the consolidated financial statements.

Revenue Recognition

Where the Company has retained substantially all the benefits and risks of ownership of its rental properties, leases with its tenants are accounted for as operating leases. Where substantially all the benefits and risks of ownership of the Company's rental properties have been transferred to its tenants, the Company's leases are accounted for as direct financing leases. For leases involving land and buildings, if the fair value of the land exceeds 25% of the consolidated fair value of the land and building at the inception of the lease, the Company evaluates the land and building separately in determining the appropriate lease treatment. In such circumstances, the land lease is typically accounted for as an operating lease and the building is accounted for as either an operating lease or a direct financing lease, as appropriate.

Granite's leases (the ''Leases'') are net leases under which the lessee is responsible for the direct payment of all operating costs related to the properties, including property taxes, insurance, utilities and routine repairs and maintenance. Revenues and operating expenses do not include any amounts related to operating costs paid directly by the lessees.

The Leases may provide for either scheduled fixed rent increases or periodic rent increases based on increases in a local price index. Where periodic rent increases depend on increases in a local price index, such rent increases are accounted for as contingent rentals and recognized in income in applicable future years. Where scheduled fixed rent increases exist in operating leases, the total scheduled fixed lease payments of the lease are recognized in income evenly on a straight-line basis over the term of the lease. The amount by which the straight-line rental revenue differs from the rents collected in accordance with the lease agreements is recognized in deferred rent receivable.

Granite's classification of its leases as either operating leases or direct financing leases, and the resulting revenue recognition treatment, depends on estimates made by management. If these estimates are inaccurate, there is risk that revenues and income for a period may otherwise differ from reported amounts.

Income Taxes

The Company uses the liability method of tax allocation for accounting for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is provided to the extent that it is more likely than not that future tax assets will not be realized.

The Company accounts for uncertain tax positions by evaluating if the available evidence indicates it is more likely than not, based on technical merits, that the position will be sustained on audit, including resolutions of related appeals or litigation processes, if any. The Company measures the appropriate amount of the benefit to recognize which is the maximum amount that is more likely than not to be realized. The tax position is reversed when it is no longer more likely than not capable of being sustained. The maximum amount which is more likely than not to be recognized at each reporting date will represent the Company's best estimate, given the information available at the reporting date, although the outcome of the tax position is not absolute or final.

Granite conducts operations in a number of countries with varying statutory rates of taxation. Judgement is required in the estimation of income taxes, and future income tax assets and liabilities, in each of the Company's operating jurisdictions. This process involves estimating actual current tax exposure, assessing temporary differences that result from the different treatments of items for tax and accounting purposes, assessing whether it is more likely than not that future income tax assets will be realized and, based on all the available evidence, determining if a valuation allowance is required on all or a portion of such future income tax assets. Granite's effective tax rate can vary significantly quarter to quarter due to changes in (i) the proportion of income earned in each tax jurisdiction, (ii) current and future statutory rates of taxation, (iii) estimates of tax exposures, (iv) the assessment of whether it is more likely than not that future income tax assets will be realized and (v) the valuation allowances recorded on future tax assets. Management's estimates used in establishing the Company's tax provision are subject to uncertainty. Actual results may be materially different from such estimates.

RISKS AND UNCERTAINTIES

Investing in our stapled units involves a high degree of risk. There are a number of risk factors that could have a material adverse effect on our business, financial condition, operating results and prospects. These risks and uncertainties are discussed in our AIF filed with securities regulators in Canada and available online at www.sedar.com and Annual Report on Form 40-F filed with the SEC and available online at www.sec.gov, each in respect of the year ended December 31, 2012.

SELECTED ANNUAL AND QUARTERLY DATA

Refer to note 1 of the consolidated financial statements for a description of the accounting policies used in the determination of the financial data.

(in thousands, except per share information)

Years ended December 31,	2012	2011[1]	2010[1]
Revenue:			
Rental Revenue	**$ 181,115**	$ 180,937	$ 177,229
Interest and other revenue from MEC	**—**	—	1,893
	$ 181,115	$ 180,937	$ 179,122
Income from continuing operations[2]	**$ 71,337**	$ 57,942	$ 68,403
Net income (loss):			
Continuing operations[2]	**$ 71,337**	$ 57,942	$ 68,403
Discontinued operations[2]	**—**	94,449	(121,269)
	$ 71,337	$ 152,391	$ (52,866)
Cash dividends declared per share	**$ 1.99**	$ 0.80	$ 0.55
Basic earnings per share from continuing operations[2]	**$ 1.52**	$ 1.24	$ 1.47
Diluted earnings per share from continuing operations[2]	**$ 1.52**	$ 1.23	$ 1.47
Basic earnings (loss) per share	**$ 1.52**	$ 3.25	$ (1.13)
Diluted earnings (loss) per share	**$ 1.52**	$ 3.24	$ (1.13)
Total Assets	**$1,218,205**	$1,245,414	$1,933,258
Total Debt	**$ 263,589**	$ 263,236	$ 262,884

Year ended December 31, 2012	**Mar 31**	**Jun 30**	**Sep 30**	**Dec 31**	**Total**
Revenue:					
Real Estate Business					
Rental revenue	$45,660	$45,455	$44,685	$45,315	$181,115
Income from continuing operations and net income(2):					
Real Estate Business(3)	$18,563	$18,707	$18,919	$15,148	$ 71,337
Basic and diluted earnings per share:	$ 0.40	$ 0.40	$ 0.40	$ 0.32	$ 1.52
FFO:					
Real Estate Business(3)	$29,406	$29,374	$29,446	$25,905	$114,131
Diluted FFO per share:					
Real Estate Business(3)	$ 0.63	$ 0.63	$ 0.63	$ 0.55	$ 2.43
Diluted shares outstanding:					
Real Estate Business(3)	46,906	46,896	46,846	46,866	46,876

Year Ended December 31, 2011	Mar 31(1)	Jun 30(1)	Sep 30(1)	Dec 31(1)	Total(1)
Revenue:					
Real Estate Business					
Rental revenue	$44,231	$ 44,861	$45,485	$46,360	$180,937
Income from continuing operations(2):					
Real Estate Business(3)	$12,689	$ 26,362	$15,277	$ 3,614	$ 57,942
Net income:					
Real Estate Business(3)	$12,689	$ 26,362	$15,277	$ 3,614	$ 57,942
Discontinued operations(2)	10,765	83,684	—	—	94,449
	$23,454	$110,046	$15,277	$ 3,614	$152,391
Basic and diluted earnings per share from continuing operations(2):					
Real Estate Business(3)	$ 0.27	$ 0.56	$ 0.33	$ 0.08	$ 1.24
Basic earnings per share:	$ 0.50	$ 2.34	$ 0.33	$ 0.08	$ 3.25
Diluted earnings per share:	$ 0.50	$ 2.33	$ 0.33	$ 0.08	$ 3.24
FFO:					
Real Estate Business(3)	$23,136	$ 36,938	$25,902	$14,576	$100,552
Diluted FFO per share:					
Real Estate Business(3)	$ 0.49	$ 0.78	$ 0.55	$ 0.31	$ 2.14
Diluted shares outstanding:					
Real Estate Business	46,947	47,165	46,862	46,883	46,970

(1) Information was previously presented in U.S. dollars (see *''SIGNIFICANT MATTERS — Currency Change for Financing Reporting and Dividends''*).

(2) As a result of the Arrangement, the results of operations of the Arrangement Transferred Assets & Business have been presented as discontinued operations for all periods presented. The Racing & Gaming Business results of operations are included in the Company's consolidated results of operations subsequent to the effective date of the Plan of April 30, 2010 (see *''ARRANGEMENT TRANSFERRED ASSETS & BUSINESS — SIGNIFICANT MATTERS — MEC's Chapter 11 Filing and Plan of Reorganization''*). Subsequent to the second quarter of 2011, the Company's results of operations were not impacted by the Arrangement Transferred Assets & Business as they were transferred to the Stronach Shareholder effective June 30, 2011.

(3) The Real Estate Business' results for 2012 include (i) $0.3 million, $0.8 million, $0.3 million and $0.3 million ($0.2 million, $0.7 million, $0.2 million and $0.2 million net of income taxes) in the first, second, third and fourth quarters respectively, of appraisal, environmental and valuation costs related to income-producing properties, (ii) $1.6 million ($1.2 million net of income taxes) in the fourth quarter of land transfer taxes and associated costs related to the REIT conversion, (iii) $0.8 million, $0.7 million, $2.6 million and $3.8 million ($0.8 million, $0.7 million, $2.5 million and $2.8 million net of income taxes) in the first, second, third and fourth quarters respectively, of advisory costs related to the planned REIT Conversion and (iv) $0.3 million ($0.2 million net of income taxes) in the first quarter relating to employee terminations costs.

The Real Estate Business' results for 2011 include (i) $5.9 million, $2.3 million and $0.9 million ($5.9 million, $1.8 million and $0.7 million net of income taxes) in the first, second and third quarters respectively, of advisory and other costs primarily incurred in connection with the Arrangement (see *''ARRANGEMENT TRANSFERRED ASSETS & BUSINESS — SIGNIFICANT MATTERS — Plan of Arrangement''*) and the settlement of an outstanding legal proceeding, (ii) $2.7 million ($1.7 million net of income taxes) in the second quarter relating to a write-down of an income-producing commercial office building, (iii) $12.9 million in income tax recovery relating to an internal amalgamation completed in 2010 that was set aside and cancelled during the second quarter, (iv) $5.4 million ($3.8 million net of income taxes) and $1.6 million ($1.1 million net of income taxes) in the third and fourth quarters respectively relating to employee termination costs and (v) a write-down of $16.7 million ($13.5 million net of income taxes) relating to two income-producing properties in Austria and Germany in the fourth quarter.

FORWARD-LOOKING STATEMENTS

This MD&A may contain statements that, to the extent they are not recitations of historical fact, constitute ''forward-looking statements'' within the meaning of applicable securities legislation, including the United States Securities Act of 1933, as amended and the United States Securities Exchange Act of 1934, as amended. Forward-looking statements may include, among others, statements regarding the Company's future plans, goals, strategies, intentions, beliefs, estimates, costs, objectives, capital structure, cost of capital, tenant base, tax consequences, economic performance or expectations, or the assumptions underlying any of the foregoing. In particular, this MD&A contains forward-looking statements regarding the Company's expectations with respect to the REIT conversion as well as certain accounting policies expected to be adopted under IFRS. Words such as ''may'', ''would'', ''could'', ''will'', ''likely'', ''expect'', ''anticipate'', ''believe'', ''intend'', ''plan'', ''forecast'', ''project'', ''estimate'', ''seek'' and similar expressions are used to identify forward-looking statements. Forward-looking statements should not be read as guarantees of future events, performance or results and will not necessarily be accurate indications of whether or the times at or by which such future performance will be achieved. Undue reliance should not be placed on such statements. In particular, Granite cautions that there can be no assurance that the anticipated reduction in cash income taxes payable following the REIT conversion will be realized or that the application of IFRS accounting policies expected to be adopted may not be adopted and the application of such policies to certain transactions or circumstances can be different than expected, or at all. Forward-looking statements are based on information available at the time and/or management's good faith assumptions and analyses made in light of our perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances, and are subject to known and unknown risks, uncertainties and other unpredictable factors, many of which are beyond the Company's control, that could cause actual events or results to differ materially from such forward-looking statements. Important factors that could cause such differences include, but are not limited to, the risk of changes to tax or other laws that may adversely affect the REIT; the ability to realize the anticipated reduction in cash income taxes payable following the REIT conversion and the risks set forth in the ''Risk Factors'' section in the Company's Annual Information Form for 2012, filed on SEDAR at sedar.com and attached as Exhibit 1 to the Company's Annual Report on Form 40-F for the year ended December 31, 2012 filed with the SEC and available online at www.sec.gov, all of which investors are strongly advised to review. The ''Risk Factors'' section also contains information about the material factors or assumptions underlying such forward-looking statements. Forward-looking statements speak only as of the date the statements were made and unless otherwise required by applicable securities laws, the Company expressly disclaims any intention and undertakes no obligation to update or revise any forward-looking statements contained in this MD&A to reflect subsequent information, events or circumstances or otherwise.

GRANITE
REAL ESTATE

Audited Consolidated Financial Statements and Notes

For the year ended December 31, 2012

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

Management of Granite Real Estate Inc. (the ''Company'') is responsible for the preparation and presentation of the consolidated financial statements and all the information in the 2012 Annual Report. The consolidated financial statements were prepared by management in accordance with United States generally accepted accounting principles (''U.S. GAAP'').

Where alternative accounting methods exist, management has selected those it considered to be most appropriate in the circumstances. Financial statements include certain amounts based on estimates and judgments. Management has determined such amounts on a reasonable basis to ensure that the consolidated financial statements are presented fairly in all material respects. Financial information presented elsewhere in this Annual Report has been prepared by management to ensure consistency with information contained in the consolidated financial statements. The consolidated financial statements have been audited by the independent auditors, reviewed by the Audit Committee and approved by the Board of Directors of the Company.

Management is responsible for the development and maintenance of systems of internal accounting and administrative cost controls of high quality, consistent with reasonable cost. Such systems are designed to provide reasonable assurance that the financial information is accurate, relevant and reliable and that the Company's assets are appropriately accounted for and adequately safeguarded. Management has determined that, as at December 31, 2012 and based on the framework set forth in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, internal control over financial reporting is effective. The Company's Chief Executive Officer and Chief Financial Officer, in compliance with Section 302 of the U.S. Sarbanes-Oxley Act of 2002 (''SOX''), provide a SOX-related certification in connection with the Company's annual disclosure document in the U.S. (Form 40-F) to the U.S. Securities and Exchange Commission. According to National Instrument 52-109, a similar certification is provided to the Canadian Securities Administrators.

The Company's Audit Committee is appointed by its Board of Directors annually and is comprised solely of outside independent directors. The Audit Committee meets periodically with management, as well as with the independent auditors, to satisfy itself that each is properly discharging its responsibilities, to review the consolidated financial statements and the independent auditors' report and to discuss significant financial reporting issues and auditing matters. The Audit Committee reports its findings to the Board of Directors for consideration when approving the consolidated financial statements for issuance to the shareholders.

The consolidated financial statements have been audited by Ernst & Young LLP, the independent auditors, in accordance with United States generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States) on behalf of the shareholders. The Auditors' Report outlines the nature of their examination and their opinion on the consolidated financial statements of the Company. The independent auditors have full and unrestricted access to the Audit Committee.

THOMAS HESLIP
Chief Executive Officer

MICHAEL FORSAYETH
Chief Financial Officer

Toronto, Canada,
March 5, 2013.

INDEPENDENT AUDITORS' REPORT OF REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of **Granite Real Estate Inc.**

We have audited the accompanying consolidated financial statements of **Granite Real Estate Inc.** (the ''Company''), which comprise the consolidated balance sheets as at December 31, 2012 and 2011, and the consolidated statements of income (loss), comprehensive income (loss), changes in deficit and cash flows for each of the years in the three-year period ended December 31, 2012, 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 United States generally accepted accounting principles, 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 and the standards of the Public Company Accounting Oversight Board (United States). 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' judgment, 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. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, 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 the Company as at December 31, 2012 and 2011, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2012 in accordance with United States generally accepted accounting principles.

Other matter

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2012, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 5, 2013 expressed an unqualified opinion on the Company's internal control over financial reporting.

Ernst & Young LLP

Toronto, Canada
March 5, 2013

Chartered Accountants
Licensed Public Accountants

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROLS UNDER THE STANDARDS OF THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD (UNITED STATES)

The Board of Directors and Shareholders of
Granite Real Estate Inc.

We have audited Granite Real Estate Inc.'s internal control over financial reporting as of December 31, 2012, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the ''COSO criteria''). Granite Real Estate Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Discussion and Analysis of Results of Operations and Financial Position, under the heading of ''CONTROLS AND PROCEDURES — Report on Internal Control Over Financial Reporting''. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Granite Real Estate Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) and Canadian generally accepted auditing standards, the consolidated balance sheets as at December 31, 2012 and 2011, and the consolidated statements of income (loss), comprehensive income (loss), changes in deficit and cash flows for each of the years in the three-year period ended December 31, 2012, and a summary of significant accounting policies and other explanatory information of the Company and our report dated March 5, 2013 expressed an unqualified opinion thereon.

Ernst & Young LLP

Chartered Accountants
Licensed Public Accountants

Toronto, Canada
March 5, 2013

Consolidated Balance Sheets

(Refer to note 1 — Basis of Presentation)
(Canadian dollars in thousands)

As at December 31	Note	2012	2011 *(previously in US dollars — note 1(c))*
ASSETS			
Non-current assets:			
Real estate properties, net	2	**$1,136,158**	$1,154,780
Deferred rent receivable		**11,518**	12,704
Future tax assets	6	**3,924**	1,292
Note receivable	3	**—**	2,543
Fixed assets, net	4	**1,837**	36
Other assets	5	**3,532**	3,598
		1,156,969	1,174,953
Current assets:			
Current portion of note receivable	3	**2,612**	5,339
Accounts receivable		**3,662**	6,557
Income taxes receivable		**2,622**	1,012
Prepaid expenses and other		**745**	645
Cash and cash equivalents		**51,073**	56,908
Restricted cash		**522**	—
Total assets		**$1,218,205**	$1,245,414
LIABILITIES AND SHAREHOLDERS' EQUITY			
Non-current liabilities:			
Senior unsecured debentures, net	7	**$ 263,589**	$ 263,236
Future tax liabilities	6	**27,626**	30,224
Deferred revenue		**4,782**	3,989
		295,997	297,449
Current liabilities:			
Deferred revenue		**5,839**	3,599
Accounts payable and accrued liabilities	8	**26,464**	14,441
Income taxes payable		**12,904**	20,685
Total liabilities		**341,204**	336,174
Shareholders' equity:			
Common Shares			
(Shares issued — 46,833; December 31, 2011 — 46,871)	10	**2,117,256**	2,119,515
Contributed surplus	11	**63,055**	62,215
Deficit		**(898,526)**	(876,375)
Accumulated other comprehensive loss	12	**(404,784)**	(396,115)
Total shareholders' equity		**877,001**	909,240
Total liabilities and shareholders' equity		**$1,218,205**	$1,245,414
Commitments and contingencies	22		

See accompanying notes

On behalf of the Board:

/s/ G. WESLEY VOORHEIS
Director

/s/ GERALD J. MILLER
Director

Consolidated Statements of Income (Loss)

(Canadian dollars in thousands, except per share figures)

Years ended December 31,	Note	2012	2011	2010
			(previously in US dollars — note 1(c))	
Revenues				
Rental		**$181,115**	$180,937	$ 177,229
Interest and other income from MEC	19(a)	**—**	—	1,893
		181,115	180,937	179,122
Operating costs and expenses (income)				
Property operating costs		**5,694**	3,061	2,864
General and administrative		**30,930**	46,708	44,710
Depreciation and amortization		**42,773**	42,701	42,413
Interest expense and other financing costs, net	7(b)	**15,871**	15,749	18,753
Foreign exchange losses (gains), net		**44**	(218)	70
Write-down of long-lived assets	14	**—**	19,473	—
Impairment recovery related to loans receivable from MEC	19(a)	**—**	—	(10,037)
Operating income		**85,803**	53,463	80,349
Gain (loss) on disposal of real estate	2	**(21)**	91	—
Other gains, net	19(b)	**—**	—	2,049
Purchase price consideration adjustment	15	**—**	—	20,439
Income before income taxes		**85,782**	53,554	102,837
Income tax expense (recovery)	6	**14,445**	(4,388)	34,434
Income from continuing operations		**71,337**	57,942	68,403
Income (loss) from discontinued operations, net of income tax	21	**—**	94,449	(121,269)
Net income (loss)		**$ 71,337**	$152,391	$ (52,866)
Basic earnings (loss) per Common or Class B Share	16			
— continuing operations		**$ 1.52**	$ 1.24	$ 1.47
— discontinued operations		**—**	2.01	(2.60)
Total		**$ 1.52**	$ 3.25	$ (1.13)
Diluted earnings (loss) per Common or Class B Share	16			
— continuing operations		**$ 1.52**	$ 1.23	$ 1.47
— discontinued operations		**—**	2.01	(2.60)
Total		**$ 1.52**	$ 3.24	$ (1.13)
Weighted average number of Common and Class B Shares outstanding during the year (in thousands)				
— Basic		**46,855**	46,888	46,708
— Diluted		**46,876**	46,970	46,708

See accompanying notes

Consolidated Statements of Comprehensive Income (Loss)

(Canadian dollars in thousands)

Years ended December 31,	Note	2012	2011	2010
			(previously in US dollars — note 1(c))	
Net income (loss)		**$71,337**	$152,391	$ (52,866)
Other comprehensive income (loss):				
Foreign currency translation adjustment	12	**(8,669)**	1,076	(103,381)
Recognition of foreign currency translation gain in net income (loss)	12	**—**	—	(43)
Change in net unrecognized actuarial pension loss	12	**—**	—	(119)
Reclassification to net income (loss) of foreign currency translation gain of discontinued operations upon deconsolidation	12	**—**	(639)	—
Reclassification to net income (loss) of net unrecognized actuarial pension loss of discontinued operations upon deconsolidation	12	**—**	119	—
Comprehensive income (loss)		**$62,668**	$152,947	$(156,409)

See accompanying notes

Consolidated Statements of Changes in Deficit

(Canadian dollars in thousands)

Years ended December 31,	Note	2012	2011	2010
			(previously in US dollars — note 1(c))	
Deficit, beginning of year		**$(876,375)**	$(310,593)	$(233,689)
Net income (loss)		**71,337**	152,391	(52,866)
Dividends		**(93,488)**	(37,543)	(24,038)
Distribution under Plan of Arrangement	1, 21	**—**	(680,630)	—
Deficit, end of year		**$(898,526)**	$(876,375)	$(310,593)

See accompanying notes

Consolidated Statements of Cash Flows
(Canadian dollars in thousands)

Years ended December 31,	Note	2012	2011	2010
			(previously in US dollars — note 1(c))	
OPERATING ACTIVITIES				
Income from continuing operations		**$ 71,337**	$ 57,942	$ 68,403
Items not involving current cash flows	17(a)	**42,342**	62,032	27,323
Changes in non-cash working capital balances	17(b)	**2,967**	(8,297)	(1,483)
Cash provided by operating activities		**116,646**	111,677	94,243
INVESTING ACTIVITIES				
Real estate property additions		**(29,808)**	(48,511)	(10,124)
Proceeds from note receivable		**4,973**	—	—
Fixed asset additions		**(1,841)**	(16)	(69)
Proceeds on disposal of real estate, net		**1,221**	133	—
Decrease (increase) in other assets		**(346)**	155	(2,717)
Loan repayments from MEC		**—**	—	62,099
Loan advances to MEC, net		**—**	—	(14,269)
Acquisition of MEC Transferred Assets, net of cash	15	**—**	—	(50,518)
Cash used in investing activities		**(25,801)**	(48,239)	(15,598)
FINANCING ACTIVITIES				
Dividends paid		**(93,822)**	(37,723)	(24,000)
Repurchase of Common Shares		**(2,694)**	—	—
Issuance of shares		**956**	7,023	—
Financing costs paid		**(410)**	—	—
Proceeds from bank indebtedness		**42,000**	36,500	79,000
Repayment of bank indebtedness		**(42,000)**	(49,500)	(66,000)
Repayment of long-term debt		**—**	(2,242)	(231)
Cash used in financing activities		**(95,970)**	(45,942)	(11,231)
Effect of exchange rate changes on cash and cash equivalents		**(710)**	2,118	(7,891)
Net cash flows provided by (used in) continuing operations		**(5,835)**	19,614	59,523
DISCONTINUED OPERATIONS				
Cash provided by (used in) operating activities		**—**	293	(2,166)
Cash provided by (used in) investing activities		**—**	(47,944)	5,963
Cash used in financing activities		**—**	—	(119,837)
Net cash flows used in discontinued operations		**—**	(47,651)	(116,040)
Net decrease in cash and cash equivalents during the year		**(5,835)**	(28,037)	(56,517)
Cash and cash equivalents, beginning of year		**56,908**	84,945	141,462
Cash and cash equivalents, end of year		**51,073**	56,908	84,945
Less: cash and cash equivalents of discontinued operations, end of year		**—**	—	(18,573)
Cash and cash equivalents of continuing operations, end of year		**$ 51,073**	$ 56,908	$ 66,372

See accompanying notes

Notes to Consolidated Financial Statements

(All amounts, except per share amounts, in thousands of Canadian dollars unless otherwise noted)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Organization, Segmented Information and Basis of Presentation

Organization

On June 13, 2012, Granite Real Estate Inc. (''Granite'' or the ''Company'') changed its name from MI Developments Inc. following shareholder approval of the name change at its annual general and special meeting. The Company is the successor to Magna International Inc.'s (''Magna'') real estate division, which prior to its spin-off from Magna on August 29, 2003 was organized as an autonomous business unit within Magna. The Company was formed as a result of four companies that amalgamated on August 29, 2003 under the *Business Corporations Act* (Ontario): 1305291 Ontario Inc., 1305272 Ontario Inc., 1276073 Ontario Inc. and the Company. These companies were wholly-owned subsidiaries of Magna and held Magna's real estate division and the controlling interest in Magna Entertainment Corp. (''MEC''). Class A Subordinate Voting Shares and Class B Shares were distributed to the shareholders of Magna of record on August 29, 2003 on the basis of one Class A Subordinate Voting Share for every two Class A Subordinate Voting Shares of Magna held, and one Class B Share for every two Class B Shares of Magna held. The Company also acquired Magna's controlling interest in MEC as a result of this spin-off transaction.

On March 5, 2009, MEC and certain of its subsidiaries filed voluntary petitions for reorganization under Chapter 11 of Title 11 of the United States Code (the ''Bankruptcy Code'') in the United States Bankruptcy Court for the District of Delaware and were granted recognition of the Chapter 11 proceedings from the Ontario Superior Court of Justice under section 18.6 of the Companies' Creditors Arrangement Act in Canada. On February 18, 2010, the Company announced that MEC had filed the Joint Plan of Affiliated Debtors, an agreement amongst the Official Committee of Unsecured Creditors, the Company and MI Developments US Financing Inc. pursuant to the Bankruptcy Code (as amended, the ''Plan'') and related Disclosure Statement in connection with the MEC Chapter 11 proceedings. The Plan provided, among other things, that the assets of MEC remaining after certain asset sales were to be transferred to the Company, including, among other assets, Santa Anita Park, Golden Gate Fields, Gulfstream Park (including MEC's interest in The Village at Gulfstream Park™, a joint venture between MEC and Forest City Enterprises, Inc.), Portland Meadows, AmTote International, Inc. (''AmTote'') and XpressBet, Inc. (''XpressBet®''). On March 23, 2010, the Plan was amended to include the transfer of The Maryland Jockey Club (''MJC'') to the Company (together with the assets referred to in the preceding sentence, the ''MEC Transferred Assets''). On April 30, 2010, the closing conditions of the Plan were satisfied or waived, and the Plan became effective following the close of business on April 30, 2010.

On June 30, 2011, the Company completed a court-approved plan of arrangement (the ''Arrangement'') under the *Business Corporations Act* (Ontario) which eliminated the Company's dual class share capital structure through which Mr. Frank Stronach and his family controlled the Company (the ''Stronach Shareholder''). Definitive agreements with respect to the Arrangement were entered into by the Company on January 31, 2011. The Arrangement was approved on March 29, 2011 by 98.08% of the votes cast by shareholders at the annual general and special meeting and, on March 31, 2011, the Ontario Superior Court of Justice issued a final order approving the Arrangement. The Arrangement eliminated the Company's dual class share capital structure through:

i) the purchase for cancellation of 363,414 Class B Shares held by the Stronach Shareholder upon the transfer to the Stronach Shareholder of the Company's Racing & Gaming Business including U.S. $20 million of working capital at January 1, 2011, substantially all of the Company's lands held for development and associated assets and liabilities (the Company was granted an option to purchase at fair value certain of these development lands if needed to expand the Company's income-producing properties), a property located in the United States, an income-producing property located in Canada and cash in the amount of U.S. $8.5 million. In addition, the Stronach Shareholder received a 50% interest in the note receivable and cash proceeds from the sale of Lone Star LP (note 3), a 50% interest in any future payments under a holdback agreement relating to MEC's prior sale of The Meadows racetrack (note 22(e)) and a second right of refusal (behind Magna's first right of refusal) in respect of certain properties owned by the Company and leased to Magna in Oberwaltersdorf, Austria and Aurora, Canada (the assets and liabilities transferred to the Stronach Shareholder pursuant to the Arrangement are collectively referred to as the ''Arrangement Transferred Assets & Business''); and

ii) the purchase for cancellation by the Company of each of the other 183,999 Class B Shares in consideration for 1.2 Class A Subordinate Voting Shares per Class B Share, which following cancellation of the Class B Shares and together with the then outstanding Class A Subordinate Voting Shares were renamed Common Shares.

On January 3, 2013, Granite completed its conversion from a corporate structure to a stapled unit Real Estate Investment Trust (''REIT'') structure (note 23(a)).

Segmented Information and Discontinued Operations

The Company's reportable segments reflect the manner in which the Company is organized and managed by its senior management. Subsequent to the effective date of the Plan on April 30, 2010 until the completion of the Arrangement on June 30, 2011, the Company's operations were segmented between the ''Real Estate Business'' and the ''Racing & Gaming Business''. The Company's reportable segments were determined based upon the distinct nature of their operations and that each segment offered different services and was managed separately. However, as a result of the Arrangement noted above, the financial position and results of operations of the Arrangement Transferred Assets & Business have been presented as discontinued operations (note 21) and, as such, have been excluded from continuing operations for all periods presented. Accordingly, the Company's single reportable segment pertains to the Real Estate Business' income-producing properties.

The Company's lands held for development and associated assets and liabilities, a property located in the United States and an income producing property located in Canada were previously presented in the Real Estate Business segment and have been presented as discontinued operations for the years ended December 31, 2011 and 2010.

Real Estate Business

Granite is a Canadian-based real estate company engaged in the ownership and management of predominantly industrial properties in North America and Europe. The Company owns and manages approximately 28 million square feet in 104 rental income properties. The Company's tenant base currently includes operating subsidiaries of Magna International Inc. (together ''Magna'') as its largest tenants, together with tenants from other industries.

Racing & Gaming Business

As a result of the Plan, following the close of business on April 30, 2010, the Company became the owner and operator of horse racetracks and a supplier, via simulcasting, of live horse racing content to the inter-track, off-track and account wagering markets.

As a result of the Arrangement, the Racing & Gaming Business is included in discontinued operations (note 21). The Racing & Gaming Business owned and operated four thoroughbred racetracks located in the United States, as well as the simulcast wagering venues at these tracks, including: Santa Anita Park, Golden Gate Fields, Gulfstream Park (which includes a casino with alternative gaming machines) and Portland Meadows; XpressBet®, a United States based national account wagering business; AmTote, a provider of totalisator services to the pari-mutuel industry; and a thoroughbred training centre in Palm Meadows, Florida. The Racing & Gaming Business also included: a 50% joint venture interest in The Village at Gulfstream Park™, an outdoor shopping and entertainment centre located adjacent to

Gulfstream Park; a 50% joint venture interest in HRTV, LLC, which owns Horse Racing TV®, a television network focused on horse racing; a 51% interest in Maryland RE & R LLC, a joint venture with real estate and racing operations in Maryland, including Pimlico Race Course, Laurel Park and a thoroughbred training centre and a 49% joint venture interest in Laurel Gaming LLC, a joint venture established to pursue gaming opportunities at the Maryland properties.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in Canadian dollars following United States generally accepted accounting principles (''U.S. GAAP'').

(b) Consolidated Financial Statements

The accompanying consolidated financial statements include the accounts of Granite and its subsidiaries (references to ''Granite'' or the ''Company'' include Granite's subsidiaries). All significant intercompany balances and transactions have been eliminated on consolidation.

(c) Change in Reporting Currency

The consolidated financial statements for periods prior to January 1, 2012 were reported using the U.S. dollar. As a result of the Company's shareholder base becoming increasingly Canadian and the Company's stated intention of becoming a Canadian Real Estate Investment Trust, and to mitigate the impact of foreign exchange fluctuations on the Company's reported results, effective January 1, 2012, the Company's reporting currency was changed to the Canadian dollar. With the change in the reporting currency, all comparative financial information has been recast from U.S. dollars to Canadian dollars to reflect the Company's consolidated financial statements as if they had been historically reported in Canadian dollars. The consolidated U.S. dollar balance sheet at December 31, 2011 was translated into the Canadian dollar reporting currency by translating assets and liabilities at the end-of-period exchange rate and translating equity balances at historical exchange rates. The consolidated statements of income (loss) were translated into Canadian dollars using the weighted average exchange rate for the applicable period. The resulting foreign currency translation adjustment is reported as a component of other comprehensive income (loss) and accumulated other comprehensive loss. The impact of the change in reporting currency on the consolidated statements of income (loss) for the years ended December 31, 2011 and 2010 and the net assets/shareholders' equity as at December 31, 2011 on the Company's consolidated balance sheet is summarized in the tables below:

Year ended December 31, 2011	As Previously Reported	Foreign Exchange	As Recast
Consolidated statement of income	**USD**		**CDN**
Revenues	$182,949	$(2,012)	$180,937
Income from continuing operations	59,196	(1,254)	57,942
Net income	155,797	(3,406)	152,391
Diluted earnings from continuing operations per Common or Class B Share	1.26	(0.03)	1.23

Year ended December 31, 2010	As Previously Reported	Foreign Exchange	As Recast
Consolidated statement of loss	**USD**		**CDN**
Revenues	$173,894	$5,228	$179,122
Income from continuing operations	66,541	1,862	68,403
Net loss	(52,704)	(162)	(52,866)
Diluted earnings from continuing operations per Common or Class B Share	1.42	0.05	1.47

As at December 31, 2011	As Previously Reported	Foreign Exchange	As Recast
Consolidated balance sheet	**USD**		**CDN**
Common Shares	$1,521,093	$ 598,422	$2,119,515
Contributed surplus	57,636	4,579	62,215
Deficit	(845,770)	(30,605)	(876,375)
Accumulated other comprehensive income (loss)	161,085	(557,200)	(396,115)
Total shareholders' equity	$ 894,044	$ 15,196	$ 909,240

The $598.4 million impact of the change in reporting currency on Common Shares is due to the effect of translating the consolidated balance at the historical exchange rate. The Canadian dollar has appreciated since the formation of the Company. The resulting impact of translating Common Shares, contributed surplus and deficit at historical exchange rates is recorded in accumulated other comprehensive loss.

(d) Foreign Currency Translation

The assets and liabilities of the Company's self-sustaining operations having a functional currency other than the Canadian dollar are translated into the Company's Canadian dollar reporting currency using the exchange rate in effect at the year-end and revenues and expenses are translated at the average rate during the year. Unrealized foreign exchange gains or losses on translation of the Company's net investment in these operations are recognized as a component of ''other comprehensive income (loss)'' and are included in the ''accumulated other comprehensive loss'' component of shareholders' equity.

The appropriate amounts of foreign currency translation adjustments in the ''accumulated other comprehensive loss'' component of shareholders' equity are released from ''other comprehensive income (loss)'' and included in the consolidated statements of income (loss) when there is a sale or partial sale of the Company's investment in a self-sustaining operation having a functional currency other than the Canadian dollar, or upon a complete or substantially complete liquidation of the investment.

Foreign exchange gains and losses on transactions occurring in a currency different from an operation's functional currency are reflected in income, except for gains and losses on foreign exchange forward contracts subject to hedge accounting in accordance with the Company's accounting policy for ''Financial Instruments'' as described below.

(e) Financial Instruments

All financial instruments, including derivative financial instruments, are included on the Company's consolidated balance sheets and measured either at their fair values or, under certain circumstances, at cost or amortized cost. Unrealized gains and losses resulting from changes in fair values are recognized in the consolidated statements of income (loss).

All of the Company's consolidated financial assets are classified as ''held for trading'', ''held to maturity'', ''loans and receivables'' or ''available for sale'' and all of the Company's consolidated financial liabilities are classified as ''held for trading'' or ''other financial liabilities''. All of the Company's consolidated financial instruments are initially measured at fair value, with subsequent measurements dependent on the classification of each financial instrument.

''Held for trading'' financial assets, which include ''cash and cash equivalents'', are measured at fair value and all gains and losses are included in income in the period in which they arise. ''Loans and receivables'', which include certain ''other assets'', ''note receivable'' and ''accounts receivable'', are recorded at amortized cost. The Company does not currently have any consolidated financial assets classified as ''held to maturity'' or ''available for sale''.

''Other financial liabilities'', which include ''senior unsecured debentures, net'' and ''accounts payable and accrued liabilities'' are recorded at amortized cost. The Company does not have any consolidated financial liabilities classified as ''held for trading''.

The Company's policy for the treatment of financing costs related to the issuance of debt is to present debt instruments on the consolidated balance sheets net of the related financing costs, with the net balance accreting to the face value of the debt over its term.

The Company may utilize derivative financial instruments from time to time in the management of its foreign currency and interest rate exposures. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company from time to time uses hedge accounting, as described below, to ensure that counterbalancing gains, losses, revenues and expenses, including the effects of counterbalancing changes in cash flows, are recognized in income in the same period or periods. When hedge accounting is not employed, the Company measures and recognizes the fair value of the hedging instrument on the consolidated balance sheets with changes in such fair value being recognized in the consolidated statements of income (loss) in the period in which they occur.

Hedge Accounting

When hedge accounting is employed, the Company first formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking such hedge transactions. This process includes linking derivative financial hedging instruments to forecasted transactions. The Company also formally assesses both at the hedge's inception and on an ongoing basis, whether the derivative financial instruments used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items and whether the hedging relationship may be expected to remain highly effective in future periods. Any portion of the change in fair value of the hedging instrument that does not offset changes in the fair value of the hedged item (the ineffectiveness of the hedge) is recorded directly in the consolidated statements of income (loss). When it is determined that a hedging relationship is not, or has ceased to be, highly effective, the use of hedge accounting is discontinued on a prospective basis.

Unrecognized gains or losses associated with derivative financial instruments that have been terminated or cease to be effective as a hedging instrument prior to maturity are amortized in the consolidated statements of income (loss) over the remaining term of the original hedge. If the hedged item is sold or settled prior to the termination of the related derivative financial instrument, the entire unrecognized gain or loss, and any subsequent gain or loss on such derivative instrument, is recognized in the consolidated statements of income (loss).

Net cash flows arising from derivative financial instruments used to hedge anticipated foreign currency transactions and interest rate fluctuations are classified in the same manner as the cash flows from the hedged transactions on the consolidated statements of cash flows.

Foreign Exchange Forward Contracts

The Company, on occasion, purchases foreign exchange forward contracts to hedge specific anticipated foreign currency transactions. When hedge accounting is employed, the fair value of the hedging instrument is recognized on the consolidated balance sheets. Foreign exchange translation gains and losses, together with any premium or discount, on derivative financial instruments are recognized in ''other comprehensive income (loss)'' and included in the ''accumulated other comprehensive loss'' component of shareholders' equity until the hedged transaction is included in the consolidated statements of income (loss). At that time, the amount previously included in ''accumulated other comprehensive loss'' is released from ''other comprehensive income (loss)'' and included in the consolidated statements of income (loss).

(f) Cash and Cash Equivalents

Cash and cash equivalents include cash on account, demand deposits and short-term investments with maturities of less than three months at the date of acquisition.

(g) Restricted Cash

Restricted cash represents a segregated cash account associated with a construction holdback. These funds will be paid to the contractors upon satisfactory completion of the construction project.

(h) Real Estate Properties

In all cases below, ''cost'' represents acquisition and development costs, including direct construction costs, capitalized interest and indirect costs wholly attributable to development.

Revenue-Producing Properties

Revenue-producing properties are stated at cost less accumulated depreciation, reduced for impairment losses where appropriate.

Government grants and tax credits received for capital expenditures are reflected as a reduction of the cost of the related asset.

Depreciation is provided on a straight-line basis over the estimated useful lives of buildings (including buildings under capital leases), which typically range from 20 to 40 years.

Development Properties

The Company's development properties are stated at cost, reduced for impairment losses when appropriate. Properties under development are classified as such until the property is substantially completed and available for occupancy. Depreciation is not recorded for development properties.

The Company capitalizes acquisition, development and expansion costs, including direct construction costs, interest and indirect costs wholly attributable to development. Interest is capitalized to projects under development or construction based on the average accumulated expenditures outstanding during the period multiplied by the Company's average borrowing rate on existing debt. The Company capitalizes direct and indirect costs, including real estate taxes and certain operating expenses of the development property if activities necessary to ready the development property for its intended use are in progress. Costs of internal personnel and other indirect costs that are not wholly attributable to a project are expensed as incurred.

Properties Held for Sale

Properties held for sale are carried at the lower of (i) cost less accumulated depreciation and (ii) net realizable value. Depreciation ceases once a property is classified as held for sale.

(i) Fixed Assets

Fixed assets are recorded at cost less accumulated depreciation. Depreciation is provided on a straight-line basis over the estimated useful lives of the fixed assets, which typically range from 3 to 5 years for computer hardware and software and 5 to 7 years for other furniture and fixtures. Leasehold improvements are amortized over the term of the applicable lease.

Government grants and tax credits received for capital expenditures are reflected as a reduction of the cost of the related asset.

(j) Impairment of Long-lived Assets

For long-lived assets (including real estate properties and fixed assets) not held for sale, the Company assesses at least annually whether there are indicators of impairment. If such indicators are present, the Company completes a net recoverable amount analysis for the long-lived assets by determining whether the carrying value of such assets can be recovered through projected undiscounted cash flows. If the sum of expected future cash flows, undiscounted and without interest charges, is less than net book value, the excess of the net book value over the estimated fair value, based on discounted projected future cash flows and, if appropriate, appraisals, is charged to operations in the period in which such impairment is determined by management.

When long-lived assets are classified by the Company as held for sale or discontinued operations, the carrying value is reduced, if necessary, to the estimated net realizable value. ''Net realizable value'' is determined based on discounted projected net cash flows of the assets and, if appropriate, appraisals and/or estimated net sales proceeds from pending offers.

Accounting estimates related to long-lived assets are subject to significant measurement uncertainty and are susceptible to changes as such estimates require management to make forward-looking assumptions regarding cash flows and business operations.

(k) Deferred Financing Costs

The costs of obtaining a revolving credit facility are capitalized and amortized over the term of the facility.

(l) Revenue Recognition

Where the Company has retained substantially all the benefits and risks of ownership of its rental properties, leases with its tenants are accounted for as operating leases. Where substantially all the benefits and risks of ownership of the Company's rental properties have been transferred to its tenants, the Company's leases are accounted for as direct financing leases. For leases involving land and buildings, if the fair value of the land exceeds 25% of the consolidated fair value of the land and building at the inception of the lease, the Company evaluates the land and building separately in determining the appropriate lease treatment. In such circumstances, the land lease is typically accounted for as an operating lease, and the building is accounted for as either an operating lease or a direct financing lease, as appropriate.

The Company's leases (the ''Leases'') are net leases under which the lessee is responsible for the direct payment of all operating costs related to the properties, including property taxes, insurance, utilities and routine repairs and maintenance. Revenues and operating expenses do not include any amounts related to operating costs paid directly by the lessees.

The Leases may provide for either scheduled fixed rent increases or periodic rent increases based on increases in a local price index. Where periodic rent increases depend on increases in a local price index, such rent increases are accounted for as contingent rentals and recognized in income in applicable future years. Where scheduled fixed rent increases exist in operating leases, the total scheduled fixed lease payments of the lease are recognized in income evenly on a straight-line basis over the term of the lease. The amount by which the straight-line rental revenue differs from the rents collected in accordance with the lease agreements is recognized in ''deferred rent receivable''.

(m) Stock-Based Compensation Plans

Compensation expense for stock option grants is based on the fair value of the options at the grant date and is recognized over the period from the grant date to the date the award is vested and its exercisability does not depend on continued service by the option holder. Compensation expense is recognized as general and administrative expenses, with a corresponding amount included in equity as contributed surplus. The contributed surplus balance is reduced as options are exercised and the amount initially recorded for the options in contributed surplus is credited to Common Shares, along with the proceeds received on exercise. In the event that options are forfeited or cancelled prior to having vested, any previously recognized expense is reversed in the period of forfeiture or cancellation.

The Company's restricted share unit plan is measured at fair value at the date of grant and amortized to compensation expense from the effective date of the grant to the final vesting date. Compensation expense is recognized in general and administrative expenses with a corresponding amount included in equity as contributed surplus. The contributed surplus balance is reduced and credited to Common Shares as shares are issued in satisfaction of the share units. Restricted share units granted under this plan may be subject to either cliff or graded vesting. Compensation expense for awards with cliff or graded vesting is recognized on a straight-line basis over the period from the grant date to the final vesting date.

Compensation expense and a corresponding liability are recognized for deferred share units (''DSUs'') based on the market value of the underlying shares. During the period in which the DSUs are outstanding, the liability is adjusted for changes in the market value of the underlying stock, with such adjustments being recognized as compensation expense in general and administrative expenses in the period in which they occur.

The stock-based compensation plans are described in note 13.

(n) Income Taxes

The Company uses the liability method of tax allocation for accounting for income taxes. Under the liability method of tax allocation, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is provided to the extent that it is more likely than not that future tax assets will not be realized. Management's estimates used in establishing the Company's tax provision are subject to uncertainty. Actual results may be materially different from such estimates.

The Company accounts for uncertain tax positions by evaluating if the available evidence indicates it is more likely than not, based on technical merits, that the position will be sustained on audit, including resolutions of related appeals or litigation processes, if any. The Company measures the appropriate amount of the benefit to recognize which is the maximum amount that is more likely than not to be realized. The tax position is reversed when it is no longer more likely than not capable of being sustained. The maximum amount which is more likely than not to be recognized at each reporting date will represent management's best estimate, given the information available at the reporting date, although the outcome of the tax position is not absolute or final.

(o) Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the reporting periods. Management believes that the estimates utilized in preparing the consolidated financial statements are reasonable and prudent; however, actual results could differ from those estimates.

(p) Comparative Amounts

The Company has added separate line items for real estate and fixed asset additions on the consolidated statements of cash flows for the years ended December 31, 2011 and 2010 to conform to the current year's presentation.

(q) Revenue Recognition — Racing & Gaming Business

Racing revenues included pari-mutuel wagering revenues, gaming revenues and non-wagering revenues. Pari-mutuel wagering revenues associated with horseracing were recorded on a daily basis. Pari-mutuel wagering revenues were recognized gross of purses, stakes and awards and pari-mutuel wagering taxes. The costs relating to these amounts are included in ''purses, awards and other'' in discontinued operations (note 21).

Gaming revenues represented the net win earned on slot wagers. Net win is the difference between wagers placed and winning payouts to patrons, and was recorded at the time wagers were made. The costs associated with gaming revenues represented statutory required amounts distributed to the state as tax and to the horsemen to supplement purses and are included in ''purses, awards and other'' in discontinued operations (note 21).

Non-wagering revenues included totalisator equipment sales and service revenues from AmTote earned in the provision of totalisator services to racetracks, food and beverage sales, program sales, admissions, parking, sponsorship, rental fees and other revenues. Revenues derived principally from totalisator equipment sales were recognized upon shipment or acceptance of the equipment by the customer depending on the terms of the underlying contracts. Revenues generated from service contracts in the provision of totalisator services were recognized when earned based on the terms of the service contract. Revenues from food and beverage sales and program sales were recorded at the time of sale. Revenues from admissions and parking were recorded on a daily basis, except for seasonal amounts which were recorded rateably over the racing season. Revenues from sponsorship and rental fees were recorded rateably over the terms of the respective agreements or when the related event occurred.

(r) Advertising — Racing & Gaming Business

Costs incurred for producing advertising associated with horseracing and slot operations were generally expensed when the advertising program commenced. Costs incurred with respect to promotions for specific live race days were expensed on the applicable race day.

(s) Accounting Changes

Fair Value Measurement

In May 2011, the Financial Accounting Standards Board (''FASB'') issued Accounting Standards Update (''ASU'') 2011-04, ''Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (''IFRS'')''. The new guidance results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and IFRS. The amendments are applied prospectively and are effective for interim and annual periods beginning after December 15, 2011. The adoption of ASU 2011-04, effective January 1, 2012, did not have any impact on the Company's consolidated financial statements except for additional disclosure requirements when applicable particularly in relation to Level 3 fair value measurements.

Comprehensive Income

In June 2011, the FASB issued ASU 2011-05, ''Comprehensive Income (Topic 220): Presentation of Comprehensive Income''. ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity, and requires the presentation of components of net income and other comprehensive income either in a single continuous statement or in two separate but consecutive statements. ASU 2011-05 is effective, on a retrospective basis, for interim and annual periods beginning after December 15, 2011. The adoption of ASU 2011-05, effective January 1, 2012, did not have any impact on the Company's consolidated financial statements.

2. REAL ESTATE PROPERTIES, NET

(a) Real estate properties consist of:

As at December 31,	2012	2011 (previously in US dollars — note 1(c))
Income-producing properties		
Land and improvements	**$ 202,196**	$ 202,753
Buildings, parking lots and roadways — cost	**1,457,122**	1,441,086
Buildings, parking lots and roadways — accumulated depreciation	**(527,577)**	(491,615)
	1,131,741	1,152,224
Development properties		
Properties under development	**4,417**	2,556
	$1,136,158	$1,154,780

During the year, the Company disposed of a 138 thousand square foot income-producing property for net proceeds of $1.2 million and recorded a nominal loss on disposal.

(b) Future minimum rental payments to be received under operating leases in effect at December 31, 2012, substantially all of which are with Magna, are shown in the following table. These amounts are determined using foreign exchange rates as at December 31, 2012, and include contracted fixed rent increases but exclude any future Consumer Price Index increases and rents from any renewals on lease expiry.

2013	$ 180,320
2014	159,729
2015	155,982
2016	152,218
2017	144,822
Thereafter	179,540
	$ 972,611

3. NOTE RECEIVABLE

On May 16, 2011, the sale of Lone Star LP was completed and the unsecured creditors of MEC received the first U.S. $20.0 million of the net proceeds from the sale and the Company received U.S. $25.8 million, net of a working capital adjustment and closing costs. The net proceeds received by the Company of U.S. $25.8 million consisted of U.S. $10.8 million in cash, U.S. $0.5 million of which was being held in escrow to cover any potential claims by the purchaser and a note receivable of U.S. $15.0 million. The note receivable bears interest at 5.0% per annum and was payable in three U.S. $5.0 million instalments plus accrued interest every nine months on February 15, 2012, November 15, 2012 and August 15, 2013. The note receivable is unsecured and has been guaranteed by the parent company of the purchaser. In connection with the Arrangement, the proceeds from the sale of Lone Star LP are shared equally between the Company and the Stronach Shareholder. Payments are made to the Stronach Shareholder who remits 50% of those payments to the Company pursuant to the terms of the Arrangement.

The Company received its portion of the first and second instalments of the note receivable of $2.5 million each plus accrued interest of $0.3 million and $0.2 million on February 21 and November 16, 2012 respectively. During the third quarter of 2012, the Company and the Stronach Shareholder agreed to forgive U.S. $250 thousand collectively of the amount being held in escrow as settlement of a claim by the purchaser.

4. FIXED ASSETS, NET

Fixed assets consist of:

As at December 31,	2012	2011
		(previously in US dollars — note 1(c))
Office equipment	**$1,246**	$ —
Leasehold improvements	**920**	—
Computer hardware and software	**648**	507
	2,814	507
Accumulated depreciation	**(977)**	(471)
	$1,837	$ 36

5. OTHER ASSETS

Other assets consist of:

As at December 31,	2012	2011
		(previously in US dollars — note 1(c))
Tenant inducements	**$2,171**	$1,976
Deferred leasing costs	**1,041**	1,195
Deferred financing costs	**222**	—
Long-term receivables	**98**	427
	$3,532	$3,598

6. INCOME TAXES

(a) The details of income (loss) before income taxes from continuing operations, by jurisdiction, are as follows:

Years ended December 31,	2012	2011	2010
		(previously in US dollars — note 1(c))	
Domestic	**$10,294**	$(10,327)	$ (3,787)
Foreign	**75,488**	63,881	106,624
Income before income taxes	**$85,782**	$ 53,554	$102,837

(b) The provision for (recovery of) income taxes from continuing operations differs from the expense that would be obtained by applying Canadian statutory tax rates as a result of the following:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Expected income taxes at the Canadian statutory tax rate of 26.5% (2011 — 28.25%, 2010 — 31%)	**$22,732**	$15,129	$31,879
Foreign rate differentials	**(9,072)**	(9,261)	(11,491)
Change in provisions for uncertain tax positions and tax filings	**(996)**	(247)	—
Non-deductible expenses	**(374)**	1,606	1,496
Effect of change in tax rates	**546**	—	—
Impairment recovery relating to loans receivable from MEC	**—**	—	5,605
Purchase price consideration adjustment	**—**	—	(8,175)
Tax resulting from internal amalgamation (note 6(h))	**—**	(12,892)	12,892
Withholding taxes and other items	**1,609**	1,277	2,228
Income tax expense (recovery)	**$14,445**	$ (4,388)	$34,434

(c) The details of the income tax expense (recovery) from continuing operations are as follows:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Current income tax expense (recovery):			
Domestic	**$ 2,481**	$(11,852)	$13,401
Foreign	**17,091**	10,991	10,379
	19,572	(861)	23,780
Future income tax expense (recovery):			
Domestic	**(700)**	805	(117)
Foreign	**(4,427)**	(4,332)	10,771
	(5,127)	(3,527)	10,654
Income tax expense (recovery)	**$14,445**	$(4,388)	$34,434

(d) A future income tax provision (recovery) from continuing operations has been recognized on temporary differences, which consist of the following:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Changes in tax value of assets from book value	**$(4,205)**	$(4,707)	$ 3,566
Impairment provision relating to loans receivable from MEC	**—**	—	5,605
Other	**(922)**	1,180	1,483
Total future tax expense (recovery)	**$(5,127)**	$(3,527)	$10,654

(e) Future tax assets consist of the following temporary differences:

As at December 31,	2012	2011 (previously in US dollars — note 1(c))
Tax value of assets in excess of book value	**$3,924**	$1,292

(f) Future tax liabilities consist of the following temporary differences:

As at December 31,	2012	2011 (previously in US dollars — note 1(c))
Book value of assets in excess of tax value	**$24,083**	$25,802
Other	**3,543**	4,422
Total future tax liabilities	**$27,626**	$30,224

(g) Net cash payments of income taxes amounted to $29.3 million for the year ended December 31, 2012 (2011 — $15.1 million; 2010 — $10.4 million).

(h) The Company conducts operations in a number of countries with varying statutory rates of taxation. Judgement is required in the estimation of income taxes and future income tax assets and liabilities, in each of the Company's operating jurisdictions. This process involves estimating actual current tax exposure, assessing temporary differences that result from the different treatments of items for tax and accounting purposes, assessing whether it is more likely than not that future income tax assets will be realized and, based on all the available evidence, determining if a valuation allowance is required on all or a portion of such future income tax assets. The Company reports a liability for unrecognized tax benefits resulting from uncertain tax positions taken or expected to be taken in a tax return. The Company recognizes interest and penalties, if any, related to unrecognized tax benefits in income tax expense.

During 2010, an internal amalgamation was undertaken with the unintended result of causing the Company to incur a $12.9 million tax liability which was recorded as a current tax expense during 2010. During the year ended December 31, 2011, the Ontario Superior Court of Justice accepted the Company's application to have the amalgamation set aside and cancelled with the result that a current income tax recovery of $12.9 million was recorded during the year ended December 31, 2011.

As at December 31, 2012, the Company had $13.2 million (2011 — $10.9 million) of unrecognized income tax benefits (including $0.9 million (2011 — $0.7 million) of related accrued interest and penalties), all of which could ultimately reduce the Company's effective tax rate. The Company is currently under audit in Canada, the United States, Germany and Mexico. The Company believes that it has adequately provided for reasonably foreseeable outcomes related to the tax examinations and that any settlement will not have a material adverse effect on our consolidated financial position or results from operations. However, the Company cannot predict with any level of certainty the exact nature of any future possible settlements.

A reconciliation of the beginning and ending amounts of unrecognized tax benefits is as follows:

Years ended December 31,	2012	2011	2010
		(previously in US dollars — note 1(c))	
Unrecognized tax benefits balance, beginning of year	**$10,885**	$10,388	$ 8,704
Increases (decreases) for tax positions of prior years	**598**	(247)	—
Increases for tax positions of current year	**1,782**	826	2,081
Foreign currency impact	**(82)**	(82)	(397)
Unrecognized tax benefits balance, end of year	**$13,183**	$10,885	$10,388

It is reasonably possible that the gross unrecognized tax benefits, as of December 31, 2012, could decrease in the next 12 months by an estimated $3.6 million to $4.9 million (2011 — $0.3 million; 2010 — nil) relating primarily to tax years becoming statute barred for purposes of future tax examinations by local taxing authorities and the settlement of current tax examinations.

For the year ended December 31, 2012, $0.1 million of interest and penalties was recorded (2011 — nil; 2010 — nil) as part of the provision for income taxes in the consolidated statements of income (loss).

As at December 31, 2012, the following tax years remained subject to examination by the major tax jurisdictions:

Major Jurisdictions	
Canada	2007 through 2012
United States	2007 through 2012
Mexico	2007 through 2012
Austria	2009 through 2012

At December 31, 2012, the Company had capital loss carryforwards totalling approximately $594 million that do not expire. In addition, Granite has Foreign Investment in Real Property Tax Act losses of approximately $513.5 million that are available to offset any future U.S. capital gains and expire in 2015 and 2017. A full valuation allowance is required related to both of these losses as sufficient uncertainty exists regarding the realization of the future tax asset.

7. SENIOR UNSECURED DEBENTURES, NET

(a) Senior Unsecured Debentures

On December 22, 2004, Granite issued $265.0 million of 6.05% senior unsecured debentures (the ‘‘Debentures’’) due December 22, 2016, at a price of $995.70 per $1,000.00 of principal amount. The Debentures rank equally with all Granite's existing and future senior unsecured indebtedness.

The Debentures are redeemable, in whole or in part, at Granite's option at any time and from time to time, at a price equal to accrued and unpaid interest plus the greater of (a) 100% of the principal amount of the Debentures to be redeemed; and (b) the Canada Yield Price. The Canada Yield Price means, in respect of a Debenture, a price equal to which, if the Debenture were to be issued at such price on the redemption date, would provide a yield thereon from the redemption date to its maturity date equal to 42.5 basis points above the yield that a non-callable Government of Canada bond, trading at par, would carry if issued on the redemption date with a maturity date of December 22, 2016. At December 31, 2012, all of the Debentures remained outstanding.

Interest on the Debentures is payable on a semi-annual basis. The unamortized portion of the $3.1 million of expenses incurred in connection with the issuance of the Debentures is presented as a reduction of the carrying amount on the Company's consolidated balance sheets. These costs, together with the discount in the issue price of the Debentures of $1.1 million, are being accreted into the carrying value of the Debentures over the term to maturity with a corresponding charge to interest expense.

(b) The Company's net interest expense, including interest expense and other financing costs on bank indebtedness (note 9) and the senior unsecured debentures, is comprised as follows:

Years ended December 31,	2012	2011	2010
		(previously in US dollars — note 1(c))	
Gross interest cost	**$16,882**	$17,647	$19,243
Less: interest capitalized	**(491)**	(1,193)	(183)
Interest expense	**16,391**	16,454	19,060
Interest income	**(520)**	(705)	(307)
Interest expense, net	**$15,871**	$15,749	$18,753

Interest capitalized relates to real estate properties under development.

Gross interest cost consists of the following:

Years ended December 31,	2012	2011	2010
		(previously in US dollars — note 1(c))	
Interest on indebtedness initially incurred for a term of more than one year	**$16,385**	$16,400	$16,572
Other interest	**497**	1,247	2,671
	$16,882	$17,647	$19,243

Consolidated interest paid in cash for the year ended December 31, 2012 was $16.7 million (2011 — $17.6 million; 2010 — $18.0 million).

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of:

As at December 31,	2012	2011
		(previously in US dollars — note 1(c))
Accounts payable	**$ 5,558**	$ 4,538
Accrued salaries and wages	**3,913**	1,549
Accrued interest payable	**387**	387
Accrued construction payable	**8,167**	4,233
Accrued director share-based compensation	**2,283**	986
Other accrued liabilities	**6,156**	2,748
	$26,464	$14,441

9. BANK INDEBTEDNESS

At December 31, 2012 the Company had an unsecured senior revolving credit facility in the amount of $50 million that was available by way of Canadian, U.S. dollar or euro denominated loans or letters of credit (the ''2012 Granite Credit Facility'') and was scheduled to mature on February 7, 2014. The 2012 Granite Credit Facility provided the Company with the ability to increase the amount of the commitment by an additional aggregate principal amount of up to $25 million with the consent of the participating lenders. Interest on drawn amounts was calculated based on an applicable margin determined by the Company's external credit rating. During 2012, the Company was subject to interest at a rate per annum equal to the base rate (i.e. LIBOR, Canadian prime business rate or Canadian dollar bankers' acceptance rate) depending on the currency the Company borrowed in plus an applicable margin of up to 1.75%. No amounts were drawn under the Company's credit facility as at December 31, 2012. The Company did not have a credit facility as at December 31, 2011.

At December 31, 2012, the Company did not have any issued letters of credit outstanding (2011 — $0.1 million).

On February 1, 2013, the Company replaced the $50 million credit facility noted above and entered into an unsecured senior revolving credit facility in the amount of $175 million that is available by way of Canadian dollar, U.S. dollar or euro denominated loans or letters of credit (the ''Granite Credit Facility'') and matures on February 1, 2015. However, the Company has the option to extend the maturity date by one year to February 1, 2016, subject to the agreement of lenders in respect of a minimum of 66⅔% of the aggregate amount committed under the Granite Credit Facility. The Granite Credit Facility provides the Company with the ability to increase the amount of the commitment by an additional aggregate principal amount of up to $75 million with the consent of the participating lenders.

Interest on drawn amounts will be calculated based on an applicable margin determined by the Company's external credit rating. Based on Granite's current credit rating, the Company would be subject to interest at a rate per annum equal to the base rate (i.e. LIBOR, Canadian prime business rate or Eurocurrency rate) depending on the currency the Company borrows in plus an applicable margin of up to 1.63%.

10. SHARE CAPITAL

Prior to June 30, 2011, the Company had two classes of outstanding share capital: Class A Subordinate Voting Shares and Class B Shares. In accordance with the Arrangement (note 1), on June 30, 2011 the Company's Articles were amended to delete the Class B Shares from the authorized capital of Granite and to make non-substantive consequential changes to its Articles including renaming the Class A Subordinate Voting Shares as Common Shares and eliminating provisions which no longer apply due to the elimination of the Class B Shares. On June 30, 2011, 363,414 Class B Shares held by the Stronach Shareholder were purchased for cancellation upon the transfer to the Stronach Shareholder of the Arrangement Transferred Assets & Business. The remaining 183,999 Class B Shares were purchased for cancellation in consideration for 1.2 Class A Subordinate Voting Shares per Class B Share which were renamed Common Shares.

Changes in the Company's share capital for the years ended December 31, 2012, 2011 and 2010 are shown in the following table:

	Common Shares		Class B Shares		Total	
	Number (000s)	Stated Value	Number (000s)	Stated Value	Number (000s)	Stated Value
	(previously in US dollars — note 1(c))					
Shares issued and outstanding, January 1 and December 31, 2010	46,161	$ 2,102,392	547	$ 24,957	46,708	$ 2,127,349
Issued on exercise of stock options	490	8,735	—	—	490	8,735
Purchase for cancellation:						
Stronach Shareholder	—	—	(363)	(16,569)	(363)	(16,569)
Non-Stronach Shareholders	220	8,388	(184)	(8,388)	36	—
Shares issued and outstanding, December 31, 2011	46,871	2,119,515	—	—	46,871	2,119,515
Issued on exercise of stock options	30	1,143	—	—	30	1,143
Issued on settlement of share units	15	350	—	—	15	350
Repurchase for cancellation	(83)	(3,752)	—	—	(83)	(3,752)
Shares issued and outstanding, December 31, 2012	**46,833**	**$ 2,117,256**	—	$ —	**46,833**	**$ 2,117,256**

On November 25, 2011, the Toronto Stock Exchange (''TSX'') accepted the Company's Notice of Intention to Make a Normal Course Issuer Bid (''NCIB'') to purchase up to 3,998,589 Common Shares, representing approximately 10% of the public float and 8.5% of the issued and outstanding Common Shares. The NCIB terminated on November 28, 2012. Purchases of Common Shares were made at the market price at the time of purchase and all Common Shares purchased were cancelled. As at December 31, 2012, the Company has repurchased 82,980 Common Shares for cash consideration of $2.7 million. The $1.1 million excess of the weighted average consideration originally received for the Common Shares repurchased over the cash paid was charged to contributed surplus (note 11).

11. CONTRIBUTED SURPLUS

Changes in the Company's contributed surplus are shown in the following table:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Contributed surplus, beginning of year	**$62,215**	$63,542	$63,083
Repurchase of Common Shares (note 10)	**1,058**	—	—
Transfer to share capital	**(537)**	(1,712)	—
Stock-based compensation	**319**	385	459
Contributed surplus, end of year	**$63,055**	$62,215	$63,542

12. ACCUMULATED OTHER COMPREHENSIVE LOSS

Changes in the Company's accumulated other comprehensive loss are shown in the following table:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Accumulated other comprehensive loss, beginning of year	**$(396,115)**	$(396,671)	$(293,128)
Foreign currency translation adjustment[(i)]	**(8,669)**	1,076	(103,381)
Recognition of foreign currency translation gain in net income (loss)[(ii)]	**—**	—	(43)
Change in net unrecognized actuarial pension loss	**—**	—	(119)
Reclassification to net income (loss) of foreign currency translation gain of discontinued operations upon deconsolidation[(iii)]	**—**	(639)	—
Reclassification to net income (loss) of net unrecognized actuarial pension loss of discontinued operations upon deconsolidation[(iii)]	**—**	119	—
Accumulated other comprehensive loss, end of year[(iv)]	**$(404,784)**	$(396,115)	$(396,671)

(i) The Company incurs unrealized foreign currency translation gains and losses related to its self-sustaining operations having functional currencies other than the Canadian dollar. The foreign currency translation losses for the years ended December 31, 2012 and 2010 are primarily due to the weakening of the euro and the U.S. dollar against the Canadian dollar. The foreign currency translation gain for the year ended December 31, 2011 is primarily due to the strengthening of the U.S. dollar against the Canadian dollar, partially offset by the weakening of the euro against the Canadian dollar.

(ii) For the year ended December 31, 2010, $0.1 million included in ''other gains, net'' represents the remaining foreign currency translation gain realized from the final liquidation of a foreign operation.

(iii) Included in ''income (loss) from discontinued operations, net of income tax'' on the consolidated statements of income (loss) for the year ended December 31, 2011 is the reclassification to net income (loss) of a $0.6 million foreign currency translation gain and a $0.1 million unrecognized actuarial pension loss associated with the Racing & Gaming Business upon deconsolidation.

(iv) Accumulated other comprehensive loss consists of:

As at December 31,	**2012**	2011
		(previously in US dollars — note 1(c))
Foreign currency translation adjustment	**$(404,784)**	$(396,115)

13. STOCK-BASED COMPENSATION

Stock Options

On August 29, 2003, the Board of Directors approved the Incentive Stock Option Plan (the ''Granite Plan''), which allows for the grant of stock options or stock appreciation rights to directors, officers, employees and consultants. Amendments to the Granite Plan were approved by the Company's shareholders at the May 11, 2007 annual and special meeting, and became effective on June 6, 2007. At December 31, 2012, a maximum of 2.09 million Common Shares are available to be issued under the Granite Plan.

The Company historically granted stock options to certain directors and officers to purchase Common Shares. Options expire on the 10th anniversary of the date of grant, subject to earlier cancellation in the events specified in the stock option agreement entered into by the Company with each recipient of options. No stock options have been granted since August 2010.

A reconciliation of the changes in stock options outstanding is presented below:

	2012		2011		2010	
	Number (000s)	**Weighted Average Exercise Price**	Number (000s)	Weighted Average Exercise Price	Number (000s)	Weighted Average Exercise Price
Outstanding, beginning of year	**235**	**$31.99**	835	$22.66	882	$24.50
Granted	**—**	**—**	—	—	95	12.90
Exercised	**(30)**	**31.85**	(490)	14.22	—	—
Cancelled or forfeited	**—**	**—**	(110)	31.85	(142)	27.55
Outstanding, end of year	**205**	**$32.01**	235	$31.99	835	$22.66

The total intrinsic values of options exercised in 2012 and 2011 were $0.6 million and $6.4 million, respectively. On January 4, 2013, 50,000 stock options were exercised by a former officer of the Company.

The following table provides further detail with respect to options outstanding and exercisable at December 31, 2012:

Options Outstanding and Exercisable

Number (000s)	Exercise Price	Weighted Average Remaining Life in Years
95	$ 31.85	0.7
50	35.62	2.0
50	32.21	4.7
10	14.54	6.9
205	**$ 32.01**	**2.3**

The Company estimates the fair value of stock options at the date of grant using the Black-Scholes option valuation model. The Black-Scholes option valuation model was developed for use in estimating the fair value of freely traded options, which are fully transferable and have no vesting restrictions. In addition, this model requires the input of subjective assumptions, including expected dividend yields, future stock price volatility and expected time until exercise. Although the assumptions used reflect management's best estimates, they involve inherent uncertainties based on market conditions outside of the Company's control. Because the Company's outstanding stock options have characteristics that are significantly different from those of traded options, and because changes in any of the assumptions can materially affect the fair value estimate, in management's opinion, the existing model does not necessarily provide the only measure of the fair value of the Company's stock options.

The weighted average assumptions used in determining the fair value of the stock options granted are shown in the table below:

Years ended December 31,	**2012**	2011	2010
Risk-free interest rate	**—**	—	1.3%
Expected dividend yield	**—**	—	3.3%
Expected volatility of Common Shares	**—**	—	58.7%
Weighted average expected life (years)	**—**	—	2.0
Weighted average fair value per option granted	**—**	—	$ 3.50

Deferred Share Units

Effective November 3, 2003, Granite established a Non-Employee Director Share-Based Compensation Plan (the ''DSP''), which provides for a deferral of up to 100% of each outside director's total annual remuneration from the Company, at specified levels elected by each director, until such director ceases to be a director of the Company. The amounts deferred are reflected by notional deferred share units (''DSUs'') whose value reflects the market price of the Company's Common Shares at the time that the particular payment(s) to the director is determined. The value of a DSU will appreciate or depreciate with changes in the market price of the Common Shares. The DSP also takes into account any dividends paid on the Common Shares. Effective January 1, 2008, the DSP was amended such that directors were required to receive at least 50% of their Board retainer fees in DSUs. Under the DSP, when a director leaves the Board, the director receives a cash payment at an elected date equal to the value of the accrued DSUs at such date. There is no option under the DSP for directors to receive Common Shares in exchange for DSUs.

A reconciliation of the changes in DSUs outstanding is presented below:

Years ended December 31,	**2012**	2011	2010
Outstanding, beginning of year	**31**	156	116
Granted	**30**	35	52
Redeemed	**—**	(160)	(12)
Outstanding, end of year	**61**	31	156

During the year ended December 31, 2011, 160,137 DSUs were redeemed by the former directors of the Company following completion of the Arrangement for cash proceeds of $4.7 million. During the year ended December 31, 2010, 11,640 DSUs were redeemed by a director, who left the Board in 2009, for cash proceeds of $0.1 million.

Restricted Share Units

Effective August 7, 2011, Granite established an Executive Share Unit Plan (the ''Share Plan''). The Share Plan is designed to provide equity-based compensation in the form of share units to executives and other key employees (the ''Participants''). The maximum number of Common Shares which may be issued pursuant to the Share Plan is 1.0 million. The Share Plan entitles a Participant to receive one Common Share for each share unit or a cash payment equal to the market value of the share unit, which on any date is the volume weighted average trading price of a Common Share on the TSX or New York Stock Exchange over the preceding five trading days. Vesting conditions in respect of a grant are determined by the Compensation Committee at the time the grant is made and may result in the vesting of more or less than 100% of the number of share units. The Share Plan also provides for the accrual of dividend equivalent amounts based on dividends paid on the Common Shares. Share units are, unless otherwise agreed, settled within 60 days following vesting. During the second quarter of 2012, the Company received shareholder approval of the Share Plan and the settlement of share units by the issuance of Common Shares.

A reconciliation of the changes in share units is presented below:

	2012		2011	
Years ended December 31,	**Number (000s)**	**Weighted Average Grant Date Fair Value**	Number (000s)	Weighted Average Grant Date Fair Value
Outstanding, beginning of year	**26**	**$25.42**	—	$ —
Granted	**40**	**35.61**	38	25.38
Settled	**(24)**	**25.69**	(12)	25.28
Forfeited	**(4)**	**25.42**	—	—
Outstanding, end of year	**38**	**$35.63**	26	$25.42

During the year ended December 31, 2012, 15 thousand share units, with a weighted average grant date fair value of $25.75, vested and were settled with the issuance of Common Shares. Also during the year ended December 31, 2012, prior to receiving shareholder approval of the settlement of share units by the issuance of Common Shares, nine thousand share units, with a weighted average grant date fair value of $25.59, were settled for cash in the amount of $0.3 million. During the year ended December 31, 2011, 12 thousand share units, with a weighted average grant date fair value of $25.28, were settled for cash in the amount of $0.4 million. At December 31, 2012, unrecognized compensation cost related to the Share Plan was $0.9 million, which will be amortized over the weighted average remaining requisite service period of approximately 2.0 years.

Stock-based compensation expense for the year ended December 31, 2012 was $1.8 million, which includes $1.3 million pertaining to DSUs and $0.5 million pertaining to share units. During the year ended December 31, 2011, the Company recognized stock-based compensation expense of $2.4 million which includes a $1.6 million pertaining to DSUs and $0.8 million pertaining to share units. During the year ended December 31, 2010, the Company recognized stock-based compensation expense of $3.5 million, which includes $3.0 million pertaining to DSUs and $0.5 million pertaining to stock options.

14. WRITE-DOWN OF LONG-LIVED ASSETS

Write-downs relating to long-lived assets have been recognized as follows:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Continuing operations			
Industrial properties — Europe(i)	$ —	$16,738	$ —
Commercial office — U.S.(ii)	—	2,735	—
	—	19,473	—
Discontinued operations — Arrangement Transferred Assets & Business			
Development properties — Land and improvements(iii)	—	—	40,959
XpressBet®(iv)	—	—	3,540
	—	—	44,499
	$ —	$19,473	$44,499

(i) During the fourth quarter of 2011, the Company recorded a $16.7 million write-down of two income producing properties in Austria and Germany. The Company obtained information related to the leasing of these properties that indicated the existence of potential impairments and the inability to recover their carrying values. The write-downs represent the excess of the carrying values of the assets over the estimated fair values determined by the present value of the expected future cash flows from the leased properties. The write-downs reduced the cost of each property's land and building values.

(ii) In the second quarter of 2011, the Company recorded a $2.7 million write-down of a revenue-producing commercial office building. The write-down represents the excess of the carrying value of the asset over the estimated fair value. Fair value was determined based on the present value of the estimated future cash flows from the leased property. The write-downs reduced the cost of the building.

(iii) During the year ended December 31, 2010, the Company recorded impairment charges of $41.0 million relating to parcels of land held for development located in California, Florida, Michigan and Ilz, Austria. In connection with the Arrangement, in the fourth quarter of 2010 (note 1), the Company obtained information related to the above noted properties that indicated the existence of potential impairments and inability to recover the carrying value. The write-down represents the excess of the carrying value of the assets over the estimated fair values based on external real estate appraisals. The write-down reduced the cost of the land and was included in discontinued operations for the year ended December 31, 2010 (note 21).

(iv) During the year ended December 31, 2010, XpressBet®'s operations were adversely impacted by certain credit card companies choosing to block otherwise exempt internet gambling related transactions. As a result, the 2011 business plan reflected reductions in estimated future cash flows based on lower expectations for growth and profitability as it was anticipated that it would require additional time and investment to re-acquire customers that either reduced or ceased their account wagering activity. Accordingly, during the year ended December 31, 2010, XpressBet® recorded an impairment charge of $3.2 million relating to goodwill and $0.3 million relating to its trademark which is included in discontinued operations for the year ended December 31, 2010 (note 21).

During the year ended December 31, 2010, an unconsolidated joint venture of the Racing & Gaming Business recorded a write-down of goodwill in the amount of $29.4 million for which the Company's share of the write-down was $15.0 million which is included in discontinued operations on the consolidated statements of income (loss) (note 21).

15. ACQUISITION OF MEC TRANSFERRED ASSETS

The Company accounted for the transfer of the MEC Transferred Assets, in consideration for satisfying the Company's claims relating to the 2007 MEC Bridge Loan, the 2008 MEC Loan and the MEC Project Financing Facilities (all as defined in note 19(a)), with an estimated fair value of U.S. $346.4 million less U.S. $40.0 million of cash acquired at April 30, 2010 and the cash payment of U.S. $89.0 million to the unsecured creditors of MEC plus U.S. $1.5 million as a reimbursement for certain expenses incurred in connection with the action commenced by the Creditors' Committee, under the acquisition method of accounting. Accordingly, the fair value of the consideration was allocated to the net assets acquired and liabilities assumed based on the determination of fair values at April 30, 2010. Determination of fair value required the use of significant assumptions and estimates including future expectant cash flows and applicable discount rates and the use of third party valuations.

During the measurement period, the total purchase price consideration of U.S. $396.9 million was retrospectively adjusted by $20.4 million to the date of acquisition on April 30, 2010, due to additional information obtained relating to certain preliminary amounts previously recorded for the assets acquired and liabilities assumed. The total purchase price consideration adjustment of $20.4 million is comprised of the following items:

	2010
	(previously in US dollars — note 1(c))
Directors' and officers' insurance proceeds(i)	$ 8,443
Bankruptcy claims(ii)	11,169
Proceeds from the sale of Lone Star LP(iii)	(578)
Changes in fair value of net assets retained under the Plan(iv)	1,405
Purchase price consideration adjustment	$20,439

(i) Directors' and officers' insurance proceeds

Under the Plan, rights of the Company and MEC against MEC's directors' and officers' insurers were preserved with regard to the settlement in order to seek appropriate compensation for the release of all current and former officers and directors of the Company and MEC and their respective affiliates. At April 30, 2010, the Company was in continued discussions with the insurers regarding its claim. Given the complex nature of the claim and related discussions, the expected proceeds could not be reasonably estimated. During the measurement period, settlement agreements were subsequently entered into in September 2010 and October 2010 with the insurers, resulting in the Company receiving compensation of $5.9 million and $2.5 million, respectively. Given that these events confirmed facts and circumstances that existed at April 30, 2010, the Company recognized a retrospective adjustment of $8.4 million to the purchase price consideration and related allocations to the MEC Transferred Assets on April 30, 2010.

(ii) Bankruptcy claims

At April 30, 2010, the settlement of allowed administrative, priority and other claims which the Company assumed under the Plan were ongoing and subject to court approval. Consequently, at each reporting date during the measurement period, the Company made estimates of such settlements based on claims that were resolved, continued to be objected to and/or negotiated and claims which were pending court approval. As a result, the Company revised the estimates related to expected allowed administrative, priority and other claims assumed by the Company under the Plan by approximately $11.2 million as a result of information received and/or the cash settlement of certain allowed administrative, priority and other claims previously outstanding. Accordingly, the Company recognized a retrospective adjustment of $11.2 million to the purchase price consideration and related allocations to the MEC Transferred Assets on April 30, 2010.

(iii) Proceeds from the sale of Lone Star LP

At April 30, 2010, the Company estimated the expected proceeds from the sale of Lone Star LP. During the measurement period, the Company revised its estimates relating to the expected proceeds as a result of information obtained relating to the estimated closing costs and Lone Star LP's anticipated working capital position. Accordingly, the Company recognized a retrospective adjustment of $0.6 million to the purchase price consideration and related allocations to the MEC Transferred Assets on April 30, 2010.

(iv) Changes in fair value of net assets retained under the Plan

At April 30, 2010, the Company estimated the working capital, including pre-petition accounts receivable on account of track wagering and litigation and other accruals, of the MEC Transferred Assets under the Plan. During the measurement period, the Company revised its estimates relating to pre-petition accounts receivable relating to track wagering and litigation accruals and other liabilities as a result of information obtained relating to the estimated and/or actual settlement of such amounts. As a result of changes in fair value of the MEC Transferred Assets, there was a corresponding change in the determination of future tax balances associated with differences between estimated fair value and the tax basis of assets acquired and liabilities assumed. Accordingly, the Company recognized a retrospective adjustment of $1.4 million to the purchase price consideration and related allocations to the MEC Transferred Assets on April 30, 2010.

16. EARNINGS (LOSS) PER SHARE

Basic and diluted earnings (loss) per share are computed as follows:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Income from continuing operations	**$ 71,337**	$ 57,942	$ 68,403
Income (loss) from discontinued operations	**—**	94,449	(121,269)
Net income (loss)	**$ 71,337**	$152,391	$ (52,866)
Weighted average number of Common and Class B Shares outstanding (in thousands)	**46,855**	46,888	46,708
Adjustment:			
Stock options and share units	**21**	82	—
	46,876	46,970	46,708
Basic earnings (loss) per Common or Class B Share			
— from continuing operations	**$ 1.52**	$ 1.24	$ 1.47
— from discontinued operations	**—**	2.01	(2.60)
	$ 1.52	$ 3.25	$ (1.13)
Diluted earnings (loss) per Common or Class B Share			
— from continuing operations	**$ 1.52**	$ 1.23	$ 1.47
— from discontinued operations	**—**	2.01	(2.60)
	$ 1.52	$ 3.24	$ (1.13)

The computation of diluted earnings (loss) per share for the year ended December 31, 2012 excludes the effect of the potential exercise of 50,000 (2011 — 225,000; 2010 — 881,544) options to acquire Common Shares of the Company because these options were not ''in the money''.

17. DETAILS OF CASH FROM OPERATING ACTIVITIES

(a) Items not involving current cash flows are shown in the following table:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Straight-line rent adjustment	**$ 1,526**	$ 1,353	$ 1,093
Stock-based compensation expense	**1,616**	1,994	3,459
Depreciation and amortization	**42,773**	42,701	42,413
Future income taxes	**(5,127)**	(3,527)	10,654
Foreign exchange forward contracts	**359**	—	(10)
Amortization of issuance costs and accretion of discount of Debentures	**353**	353	353
Amortization of deferred financing costs	**188**	—	—
Foreign exchange on note receivable	**174**	(409)	—
Write-down of long-lived assets	**—**	19,473	—
Purchase price consideration adjustment	**—**	—	(20,439)
Impairment recovery related to loans receivable from MEC	**—**	—	(10,037)
Other	**480**	94	(163)
	$ 42,342	$ 62,032	$ 27,323

(b) Changes in non-cash working capital balances are shown in the following table:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Accounts receivable	**$ 2,945**	$(3,912)	$ (1,067)
Prepaid expenses and other	**(100)**	5,673	(5,601)
Accounts payable and accrued liabilities	**6,515**	(9,530)	(5,601)
Income taxes	**(8,926)**	(5,347)	13,984
Deferred revenue	**3,055**	4,819	(2,583)
Restricted cash	**(522)**	—	—
Loans receivable from MEC, net	**—**	—	(615)
	$ 2,967	$(8,297)	$ (1,483)

(c) Non-cash investing and financing activities

On April 30, 2010, the Company acquired the MEC Transferred Assets with the purchase price being settled by the outstanding MEC loans of U.S. $347.1 million and cash payments aggregating U.S. $90.5 million.

On June 30, 2011, the Company cancelled 363,414 Class B Shares upon the disposition of the Arrangement Transferred Assets & Business (note 1). In addition, the remaining 183,999 Class B Shares were purchased for cancellation for Class A Subordinate Voting Shares which were renamed Common Shares.

During 2012, 15 thousand Common Shares were issued under the Company's Share Plan (note 13).

18. DERIVATIVE FINANCIAL INSTRUMENTS AND FAIR VALUE INFORMATION

(a) Fair Value

The Company has determined the estimated fair values of its consolidated financial instruments using available market information and appropriate valuation methodologies. However, considerable judgment is required to develop these estimates. Accordingly, these estimated fair values are not necessarily indicative of the amounts the Company would realize in a current market exchange. The methods and assumptions used to estimate the fair value of financial instruments are described below:

Note receivable

The fair value of the note receivable approximates its carrying value as it bears interest at current market rates.

Accounts receivable, cash and cash equivalents, restricted cash, accounts payable and accrued liabilities

Due to the short period to maturity of these instruments, the carrying values as presented in the consolidated balance sheets are reasonable estimates of their fair value.

Senior unsecured debentures

The fair value of the senior unsecured debentures is determined using the quoted market price of the senior unsecured debentures. At December 31, 2012, the fair value of the senior unsecured debentures was approximately $294.2 million (2011 — $291.8 million).

(b) Credit Risk

The Company's consolidated financial assets that are exposed to credit risk consist primarily of cash and cash equivalents, accounts receivable and note receivable.

Cash and cash equivalents include short-term investments, such as commercial paper, which are only invested in governments and corporations with a minimum credit rating of A− (based on Standard & Poor's rating scale) or A3 (based on Moody's Investor Services' rating scale). Concentration of credit risk is further reduced by limiting the amount that is invested in any one government or corporation. The Company does not have investments in asset-backed commercial paper.

Magna contributed approximately 97% of the Company's rental revenue. As at December 31, 2012 and 2011, the Company's allowance for doubtful accounts in ''accounts receivable'' on the consolidated balance sheets was a nominal amount.

The credit risk associated with the note receivable is mitigated by the guarantee provided by the parent company of the note holder (note 3). Exposure to losses on the note receivable is dependent on the note holder's financial condition. The Company monitors its exposure throughout the year.

(c) Interest Rate Risk

The Company's consolidated results of operations are primarily exposed to interest rate risk on its credit facility. As there was no outstanding balance on this financial liability as at December 31, 2012, a 50 basis point change in annual interest rates, with all other variables held constant, would have no impact on the consolidated ''interest expense and other financing costs, net'' for the year ended December 31, 2012.

The Company is also exposed to interest rate risk on short-term investments with maturities of up to three months from the date of acquisition that are included in ''cash and cash equivalents'' on the Company's consolidated balance sheets. The balance of the Company's short-term investments fluctuates depending on the timing of the Company's operating cash flows, capital expenditures and other liquidity requirements. Assuming the balance of short-term investments at December 31, 2012 were outstanding throughout the entire year then ended, a 50 basis point change in annual interest rates, with all other variables held constant, would have impacted consolidated ''interest expense and other financing costs, net'' for the year ended December 31, 2012 by approximately $0.2 million.

(d) Currency Risk

The Company is structured such that its foreign operations are self-sustaining. As a result, the Company's currency risk associated with financial instruments is limited as its financial assets and liabilities are generally denominated in the functional currency of the subsidiary that holds the financial instrument.

The Company periodically purchases foreign exchange forward contracts to hedge specific anticipated foreign currency transactions. At December 31, 2012, the Company held two foreign exchange forward contracts to purchase $12.8 million and sell euro 10.0 million. One contract matures on January 15, 2013 and the other on March 14, 2013. These contracts were entered into by the Company to mitigate its foreign exchange exposure on its net cash flows. Based on the foreign exchange rates at December 31, 2012, the fair value of these foreign exchange forward contracts at December 31, 2012 was a liability of $0.4 million, which is included in ''accounts payable and accrued liabilities'' on the Company's consolidated balance sheets. At December 31, 2011, the Company did not have any foreign exchange forward contracts outstanding.

(e) Derivative Financial Instruments

The following tables summarize the impact of these derivative financial instruments on the Company's consolidated financial statements as at December 31, 2012 and 2011 and for the years ended December 31, 2012, 2011 and 2010:

At at December 31,	2012	2011
Derivatives not designated as hedging instruments		
Foreign exchange forward contracts		
— included in accounts payable and accrued liabilities	$359	$ —

Years ended December 31,	Location of Gains Recognized in Income on Derivatives	Amount of Gains Recognized in Income on Derivatives		
		2012	2011	2010
			(previously in US dollars — note 1(c))	
Derivatives not designated as hedging instruments				
Foreign exchange forward contracts	Foreign Exchange Gains	$566	$ —	$ 10

(f) Fair Value Measurements

Fair value measurements are based on inputs of observable and unobservable market data that a market participant would use in pricing an asset or liability. ASC 820, ''Fair Value Measurements and Disclosures'', establishes a fair value hierarchy which is summarized below:

Level 1: Fair value determined based on quoted prices in active markets for identical assets or liabilities.

Level 2: Fair value determined using significant observable inputs, generally either quoted prices in active markets for similar assets or liabilities or quoted prices in markets that are not active.

Level 3: Fair value determined using significant unobservable inputs, such as pricing models, discounted cash flows or similar techniques.

The following tables represent information related to the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis and the level within the fair value hierarchy in which the fair value measurements fall:

As at December 31, 2012	Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
ASSETS AND LIABILITIES CARRIED AT FAIR VALUE ON A RECURRING BASIS			
Assets carried at fair value			
Cash and cash equivalents	$51,073	$ —	$ —
Restricted cash	522	—	—
Assets carried at fair value	$51,595	$ —	$ —
Liabilities carried at fair value			
Foreign exchange forward contracts(i)	$ —	$359	$ —

As at December 31, 2011	Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(previously in US dollars — note 1(c))		
ASSETS CARRIED AT FAIR VALUE ON A RECURRING BASIS			
Cash and cash equivalents	$56,908	$ —	$ —
ASSETS CARRIED AT FAIR VALUE ON A NON-RECURRING BASIS			
Income-producing properties(ii)	$ —	$ —	$12,774

(i) Foreign exchange forward contracts are a Level 2 fair value measurement as the fair value of the contracts is determined based on foreign exchange rates in effect at December 31, 2012.

(ii) During the year ended December 31, 2011, two income-producing properties with an aggregate cost of $29.2 million were written down to an aggregate fair value of $12.8 million (note 14). This is a Level 3 fair value measurement as the fair value of the income-producing properties was determined based on the present value of estimated future cash flows from the leased property.

19. TRANSACTIONS WITH RELATED PARTIES

In 2011, the Company agreed to pay reasonable legal and advisory fees of certain Class A Shareholders incurred in connection with the Arrangement. In accordance with such agreement, a $2.1 million payment was made to a company owned by an individual who became Chairman of the Board of Directors following the completion of the Arrangement, for legal and advisory services relating to the Arrangement.

On July 1, 2011, following completion of the Arrangement, Mr. Frank Stronach no longer serves as the Chairman and Chief Executive Officer of the Company and the Stronach Shareholder no longer has a controlling interest in the Company. Consequently, Mr. Stronach and the Company ceased to be related parties for accounting purposes. Furthermore, effective July 1, 2011, the Company and Magna are no longer considered to be related parties for accounting purposes due to the factors noted above.

The transactions with Mr. Stronach, Magna and MEC that occurred while related with the Company prior to the completion of the Arrangement on June 30, 2011 are noted below.

(a) Loans to MEC

The outstanding balances of the loans receivable from MEC were settled on April 30, 2010 as part of the Plan and the acquisition of the MEC Transferred Assets (note 15). These loans were comprised of: a bridge loan of up to U.S.$80.0 million (subsequently increased to U.S.$125.0 million) through a non-revolving facility (the ''2007 MEC Bridge Loan''); project financing facilities made available to Gulfstream Park Racing Association, Inc. and Remington Park, Inc., the wholly-owned subsidiaries of MEC that owned and/or operated Gulfstream Park and Remington Park, respectively, in the amounts of U.S.$162.3 million and U.S.$34.2 million, respectively, plus costs and capitalized interest (together, the ''MEC Project Financing Facilities''); a loan of up to a maximum commitment, subject to certain conditions being met, of U.S.$125.0 million (plus costs and fees) (the ''2008 MEC Loan''); and a debtor-in-possession loan extended to MEC in connection with MEC's Chapter 11 proceedings (the ''DIP Loan''). For the years ended December 31, 2012 and 2011, the Company did not receive interest and other income from MEC as the loans were settled on April 30, 2010 (2010 — $1.9 million).

In connection with the development and completion of the Plan (note 1(a)), the Company estimated the values and resulting recoveries of loans receivable from MEC, net of any related obligations, pursuant to the terms of the Plan. As a result of such analysis, the Company estimated that it would be unable to realize on all amounts due in accordance with the contractual terms of the MEC loans. Accordingly, for the year ended December 31, 2009, the Company recorded a $95.7 million impairment provision related to the loans receivable from MEC, which represented the excess of the carrying amounts of the loans receivable and the estimated recoverable value.

As a result of the transfer of the MEC Transferred Assets under the Plan effective April 30, 2010 (note 15), the Company reduced the impairment provision by $10.0 million in the three-month period ended June 30, 2010 as a result of assessing the fair value of the MEC Transferred Assets on April 30, 2010. Estimated recoverable value was determined based on the future cash flows from expected proceeds to be received from court-approved sales of MEC's assets, discounted at the loans' effective interest rate, and the fair value of the collateral based on third-party appraisals or other valuation techniques, such as discounted cash flows, for those MEC assets that were transferred to the Company under the Plan or for which the court had yet to approve for sale under the Plan, net of expected allowed administrative, priority and other claims to be paid by the Company under the Plan.

A reconciliation of the changes in the impairment recovery related to the loans receivable from MEC at the date the MEC Transferred Assets were acquired is presented below:

	2010 (previously in US dollars — note 1(c))
Directors' and officers' insurance proceeds[i]	$ 13,065
Sale proceeds from liquidated assets under the Plan[ii]	7,577
Bankruptcy claims[iii]	(15,988)
Changes in fair value of net assets retained under the Plan[iv]	5,383
Impairment recovery	$ 10,037

The significant changes in facts or circumstances that resulted in the recognition of the $10.0 million reduction in the impairment provision in the year ended December 31, 2010 are primarily as a result of the following:

(i) Directors' and officers' insurance proceeds

Under the Plan, rights of the Company and MEC against MEC's directors' and officers' insurers were preserved with regard to the settlement in order to seek appropriate compensation for the release of all current and former officers and directors of the Company and MEC and their respective affiliates. At April 30, 2010, the Company was in discussions with the insurers regarding its claim. Given the complex nature of the claim and related discussions, the expected proceeds could not be reasonably estimated. A settlement agreement was subsequently entered into in July 2010 with one of the insurers, resulting in the Company receiving compensation of $13.1 million. Given that these events confirmed facts and circumstances that existed at April 30, 2010, the Company recognized an asset and reduced the impairment provision by $13.1 million related to the MEC Transferred Assets on April 30, 2010.

(ii) Sale proceeds from liquidated assets under the Plan

The estimates of sale proceeds from liquidated assets under the Plan increased by approximately $7.6 million primarily as a result of the sale of Thistledown. Thistledown was initially approved for sale in an auction on September 30, 2009; however, the purchaser had the right to terminate the agreement, which it exercised. The sale of Thistledown went back to auction on May 25, 2010 and the court approved the sale of Thistledown to a third party which subsequently closed on July 27, 2010. Given that the completion of the sale of Thistledown confirmed facts and circumstances that existed at April 30, 2010, the Company used such information to establish the fair value of Thistledown when assessing the fair value of the underlying collateral of the loans. Accordingly, the Company reduced the impairment provision by $7.6 million related to the MEC Transferred Assets on April 30, 2010.

(iii) Bankruptcy claims

The settlement of allowed administrative, priority and other claims which the Company assumed under the Plan were ongoing and subject to court approval. Consequently, the Company made estimates of such settlements based on claims that were resolved, continued to be objected to and/or negotiated and claims which were pending court approval. As a result, the Company revised the estimates related to expected allowed administrative, priority and other claims assumed by the Company under the Plan by approximately $16.0 million as a result of additional information received and/or the cash settlement of certain allowed administrative, priority and other claims previously outstanding. Accordingly, the Company increased the impairment provision by $16.0 million related to the MEC Transferred Assets on April 30, 2010.

(iv) Changes in fair value of net assets retained under the Plan

The Company estimated the working capital of the MEC Transferred Assets under the Plan based on available unaudited internally prepared results and operating projections. On the effective date of the Plan, the fair value of the working capital differed from the original estimates as a result of actual operating results and events related to the bankruptcy process. The Company also estimated the fair value of the real estate of the MEC Transferred Assets taking into consideration: (i) certain economic and industry information relevant to the MEC Transferred Assets' operating business; (ii) various indications of interest received by MEC in connection with the sales marketing efforts conducted by financial advisors of MEC during the Chapter 11 proceedings; and (iii) third party real estate appraisals. Throughout the bankruptcy process and to the effective date of the Plan, the Company continually updated such information related to market conditions and assumptions related to the real estate values based on the premise of highest and best use. The appraisals included additional information related to assumptions regarding potential uses, costs related to obtaining appropriate entitlements and demolition costs, and comparable sales data for real estate transactions in each jurisdiction. As a result of changes in fair value of the MEC Transferred Assets, there was a corresponding change in the determination of future tax balances associated with differences between estimated fair value and the tax basis of assets acquired and liabilities assumed. Accordingly, the Company reduced the impairment provision by $5.4 million related to the MEC Transferred Assets on April 30, 2010.

(b) Magna Lease Termination

During the year ended December 31, 2010, the Company and Magna agreed to terminate the lease on a property in the United States. In conjunction with the lease termination, Magna agreed to pay the Company a fee of $2.0 million, which amount will be collected based on a repayment schedule over the remaining term of the original lease which was scheduled to expire in September 2013. The amount has been recognized in ''other gains, net'' in the Company's consolidated statements of income (loss) for the year ended December 31, 2010.

(c) Expansion Costs Reimbursed to Magna

During the first half of 2011, the Company paid $3 (2010 — $0.5 million) to Magna as reimbursement for expenditures incurred by Magna in relation to expansions of income-producing properties.

(d) Revenue and Charges from Magna

Substantially all rental revenue relate to leases with Magna. Magna charged the Company for certain administrative and professional services and use of shared facilities. For the first half of 2011, these charges totaled $0.1 million (2010 — $2.4 million) and are included in ''general and administrative'' expenses in the Company's consolidated statements of income (loss).

(e) Legal, Consulting and Other Services

In conjunction with the Arrangement (note 1), during the first half of 2011, a U.S. $1.0 million payment was approved to an affiliate of Mr. Frank Stronach for services rendered as Chairman of the Company. In

December 2010, the Compensation Committee recommended to the Board and the Board subsequently approved a U.S. $2.0 million payment to an affiliate of Mr. Stronach, Chairman of the Company, for services rendered on behalf of the Company.

During the first half of 2011, the Company incurred $0.1 million (2010 — $0.1 million) for consulting services from a company affiliated with a former director of the Company.

These legal, consulting and other costs are included in ''general and administrative'' expenses in the Company's consolidated statements of income (loss).

20. SEGMENTED INFORMATION

The following tables present certain information with respect to geographic segmentation:

Revenues — years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Europe	**$ 75,867**	$ 77,894	$ 75,631
Canada	**61,319**	60,146	58,983
United States	**31,632**	30,762	32,158
Mexico	**12,297**	12,135	12,350
	$181,115	$180,937	$179,122

Real estate properties, net — as at December 31,	**2012**	2011
		(previously in US dollars — note 1(c))
Europe	**$ 449,599**	$ 461,529
Canada	**404,336**	410,150
United States	**219,653**	215,167
Mexico	**62,570**	67,934
	$1,136,158	$1,154,780

Fixed assets, net — as at December 31,	**2012**	2011
		(previously in US dollars — note 1(c))
Europe	**$ 266**	$ 5
Canada	**1,571**	31
	$1,837	$36

21. DISCONTINUED OPERATIONS

As a result of the approval by the Company's shareholders and the Ontario Superior Court of Justice of the Arrangement (note 1), the Company has presented the Arrangement Transferred Assets & Business as discontinued operations in the accompanying consolidated financial statements.

The Company's results of operations related to discontinued operations are shown in the following table:

Years ended December 31,	**2012**	2011	2010
		(previously in US dollars — note 1(c))	
Revenues	$ —	$262,345	$ 189,876
Purses, awards and other	—	148,584	103,878
Operating costs	—	80,208	93,233
Property operating costs	—	933	1,770
General and administrative	—	21,759	27,853
Depreciation and amortization	—	3,445	9,526
Interest income	—	(310)	(422)
Foreign exchange gains	—	(51)	(101)
Equity loss	—	1,952	29,951
Write-down of long-lived and intangible assets	—	—	44,499
Operating income (loss)	—	5,825	(120,311)
Loss on disposal of real estate	—	—	(1,305)
Income (loss) before income taxes	—	5,825	(121,616)
Income tax recovery	—	(1,196)	(347)
Income (loss) from operations	—	7,021	(121,269)
Net gain on disposition of discontinued operations, net of income tax of $10.5 million	—	87,428	—
Income (loss) from discontinued operations, net of income tax	$ —	$ 94,449	$(121,269)

The distribution of the assets and liabilities under the Arrangement is considered a non-pro-rata distribution and therefore has been recorded at fair value. Accordingly, the gain on disposition of discontinued operations was determined as the difference in the fair values and carrying values of the net assets disposed of, net of costs of disposal. The difference between the fair value of the net assets disposed of and the carrying value of the 363,414 Class B Shares cancelled in the amount of $680.6 million has been recorded in the consolidated statements of changes in deficit as ''Distribution under Plan of Arrangement'' for the year ended December 31, 2011. A summary of the fair values and carrying values of the Arrangement Transferred Assets & Business is as follows:

	Fair Value	Carrying Value	Gain	Fair Value Measurement[(i)]
	(previously in US dollars — note 1(c))			
Development Properties				
Current assets	**$ 2,320**	**$ 2,320**	**$ —**	Levels 1 and 2
Land held for development	**218,039**	**132,257**	**85,782**	Level 3
Current liabilities	**(4,250)**	**(4,250)**	**—**	Level 2
Future taxes	**(1,395)**	**(1,395)**	**—**	Level 3
Income-Producing Property and Property in United States				
Land and building	**15,997**	**9,354**	**6,643**	Level 3
Racing & Gaming Business				
Current assets	**82,650**	**82,650**	**—**	Levels 1 and 2
Fixed assets	**6,935**	**6,935**	**—**	Level 2
Racing lands and other long-term assets	**392,471**	**384,754**	**7,717**	Level 3
Technology companies	**45,872**	**40,562**	**5,310**	Level 3
Current liabilities	**(37,698)**	**(37,698)**	**—**	Level 2
Future taxes	**(24,414)**	**(24,414)**	**—**	Level 3
Other liabilities	**(4,311)**	**(4,311)**	**—**	Level 2
Gain on disposition before transaction costs and income taxes	**692,216**	**586,764**	**105,452**	
Transaction costs			**(8,042)**	
Net gain on disposition before undernoted			**97,410**	
Reclassification to net income of foreign currency translation gain and net unrecognized actuarial pension loss			**520**	
Income taxes			**(10,502)**	
Net gain on disposition of discontinued operations, net of income tax			**$ 87,428**	

(i) Refer to note 18(f) for the fair value hierarchy

The fair values of the racetrack assets of the Racing & Gaming Business were determined based on the underlying real estate as this was considered to be the highest and best use. The fair values of the real estate were primarily determined by external real estate appraisals reflecting estimated prices at which comparable assets could be purchased and adjusted for the estimated costs to convert the land for its appraised purpose.

The fair values of fixed assets, which include machinery and equipment and furniture and fixtures, were determined using a market approach based upon management's review of current prices at which comparable assets could be purchased under similar circumstances.

The fair values of the technology companies, which primarily included XpressBet® and AmTote, were determined in consultation with an external valuator using a discounted cash flow analysis under the income valuation methodology. The income approach required estimating a number of factors including projected revenue growth, customer attrition rates, profit margin and the discount rate. Projected revenue growth, customer attrition rates and profit margin were based upon past experience and management's best estimate of future operating results. The discount rate represents the respective entity's weighted average cost of capital including a risk premium where warranted.

The fair value of the 50% joint venture interest in The Village at Gulfstream Park™ was determined based on an external real estate appraisal using discounted cash flow analysis under the income valuation method. The fair value of the 51% joint venture interest in MJC was determined based on the underlying real estate determined by external real estate appraisals as this was considered to be the highest and best use.

The fair values of the lands held for development, a property located in the United States and an income-producing property located in Canada were determined by external real estate appraisals or broker opinions that reflected a market approach using estimated prices at which comparable assets could be purchased.

The remaining assets and liabilities of the Racing & Gaming Business, as well as the other assets and liabilities associated with the lands held for development, were primarily cash and cash equivalents, restricted cash, accounts receivable, income taxes receivable, other current assets, accounts payable and accrued liabilities, and deferred revenue, for which the carrying value approximated fair value. The current and long-term portions of the proceeds from the sale of Lone Star LP, representing 50% of the outstanding total proceeds from the sale, approximate fair value as the note receivable bears interest at current market rates negotiated between arm's-length parties.

22. COMMITMENTS AND CONTINGENCIES

(a) In the ordinary course of business activities, the Company may become subject to litigation and other claims brought by, among others, customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required. Although it is not possible to accurately estimate the extent of potential costs and losses, if any, management believes, but can provide no assurance, that the ultimate resolution of such claims would not have a material adverse effect on the financial position of the Company.

(b) On February 15, 2011, Power Plant Entertainment Casino Resorts Indiana, LLC, PPE Casino Resorts Maryland, LLC and The Cordish Company (the ''Plaintiffs'') sued, among other defendants, the Company, certain subsidiary entities and joint ventures, including The Maryland Jockey Club and certain of its subsidiaries (collectively, the ''MJC Entities''), as well as the Company's former Chairman and Chief Executive Officer, Mr. Frank Stronach, in the Circuit Court for Baltimore City in Baltimore, Maryland. The claims asserted in the Plaintiffs' complaint against the Company, the MJC Entities and Mr. Stronach (the ''Complaint'') are alleged to have arisen from events that occurred in Maryland in connection with the referendum conducted in November 2010 concerning the award of a gaming license to one of the Plaintiffs to conduct alternative gaming at the Arundel Mills Mall. The Complaint asserts a number of claims against all the defendants including, among other allegations, that the Company and Mr. Stronach, along with a number of other defendants, engaged in actions to defame the Plaintiffs by distributing allegedly false information concerning the Plaintiffs and their operations of a gaming facility in Indiana, Indianapolis Downs, LLC operating as Indiana Live. The specific claims asserted against the Company, the MJC Entities and Mr. Stronach are for alleged civil conspiracy, false light, invasion of privacy and defamation. The Complaint seeks an award of damages against all defendants in the amount of U.S.$300 million in compensatory damages and U.S.$300 million in punitive damages. Granite believes this claim is without merit. On March 25, 2011, a number of defendants, including the MJC Entities and the Company, filed a motion in the Circuit Court for Baltimore City, seeking to have the action transferred to the Circuit Court for Anne Arundel County. On April 29, 2011, the Indiana-based defendants named in the Complaint filed a notice to remove the Plaintiffs' claims relating to the Indiana defendants to the U.S. District Court for the District of Maryland. The Plaintiffs have sought to remand these claims to the Circuit Court for Baltimore City. The entire matter, in both the state and federal courts, was stayed by the United States Bankruptcy Court for the District of Delaware until it determined whether the claims were impacted by the bankruptcy of Indianapolis Downs, LLC. On September 6, 2011, the United States Bankruptcy Court for the District of Delaware entered an order denying the injunction motion and lifting the stay effective September 26, 2011. On December 21, 2011, the Circuit Court for Baltimore City issued an order staying the state court defendants' motions to transfer venue to the Circuit Court for Anne Arundel County pending resolution of whether the Maryland federal court action was remanded out of federal court. On September 26, 2012, the Maryland federal court issued an order remanding the Maryland federal court action to the Circuit Court for Baltimore City. On October 2, 2012, the parties filed a stipulation with the Circuit Court for Baltimore City proposing a further stay to allow certain of the defendants to engage plaintiffs in discussions that may potentially streamline the litigation. The stay was granted by the Circuit Court for Baltimore City on October 12, 2012. Under the terms of the Arrangement, the Company received an indemnity from the Stronach Shareholder and certain related parties against all losses suffered by the Company in relation to the Racing & Gaming Business for the period prior to, on and after the effective date of the transfer of June 30, 2011. Accordingly, the Company has not recorded a liability related to this claim. Granite provided the Stronach Shareholder with the required disclosure notice listing the existing litigation with the Plaintiffs. The Company has retained independent counsel to monitor the litigation on its behalf.

(c) The Company had total letters of credit outstanding of $1.1 million issued with various financial institutions at December 31, 2012 to guarantee its performance under various construction projects. These letters of credit are secured by cash deposits of the Company.

(d) At December 31, 2012, the Company's contractual commitments related to construction and development projects as well as environmental reports amounted to approximately $9.1 million.

(e) On November 14, 2006, MEC completed the sale to PA Meadows, LLC of all the outstanding shares of Washington Trotting Association, Inc., Mountain Laurel Racing, Inc. and MEC Pennsylvania Racing, Inc. (collectively ''The Meadows'') through which MEC owned and operated The Meadows, a standardbred racetrack in Pennsylvania. On closing, MEC received cash consideration and a holdback agreement (''The Meadows Holdback Agreement''), under which U.S. $25.0 million was payable to MEC over a five-year period, subject to the offset for certain indemnification obligations as well as the purchaser having available excess cash flow. As part of the acquisition of the MEC Transferred Assets, the Company received the right to receive any payments under The Meadows Holdback Agreement. Payments from The Meadows Holdback Agreement may commence once the purchaser has available excess cash flow, if any. In connection with the Arrangement (note 1), any proceeds received from PA Meadows, LLC will be shared equally between the Company and the Stronach Shareholder.

(f) At December 31, 2012, the Company had commitments under operating leases requiring future minimum annual rental payments as follows:

2013	**$ 421**
2014	**421**
2015	**421**
2016	**421**
2017	**208**
Thereafter	**453**
	$2,345

23. SUBSEQUENT EVENTS

(a) Effective January 3, 2013, the Company completed its conversion to a REIT. The conversion was implemented pursuant to a court approved plan of arrangement whereby all of the Common Shares of Granite were exchanged, on a one-for-one basis, for stapled units, each of which consisted of one unit of Granite Real Estate Investment Trust and one common share of Granite REIT Inc. (together ''Granite REIT''). A wholly owned subsidiary of Granite REIT will continue to carry on, directly and indirectly, the business previously conducted by the Company. Subsequent to the REIT conversion, distributions of $0.175 per stapled unit were declared on January 15 and February 14, 2013. The distribution declared in January 2013 in the amount of $8.2 million was paid on February 15, 2013 and the distribution declared in February 2013 of $8.2 million will be paid on March 15, 2013. In addition, the Company amended the equity-based compensation plans disclosed in note 13 to reflect the REIT structure. The option holders of the Granite Plan exchanged their existing options to acquire Common Shares for options to acquire stapled units on a one-for-one basis. The Share Plan was amended so that a right to acquire stapled units or receive a payment based on the fair value of the stapled units will be substituted for the holder's right to acquire Common Shares or a payment based on the value of such shares. The DSP was amended to provide that each DSU outstanding will entitle the holder thereof to receive a payment based on the fair value of a new class of preferred shares of Granite that are designed to be equal in value to a stapled unit and a new deferred share unit plan was created by Granite REIT Inc. whereby non-executive board members will be entitled to receive a portion of their annual retainer as deferred share units which will entitle them to receive a payment based on the fair value of a preferred share of the Company that will be equal in value to a stapled unit.

(b) On February 13, 2013, Granite REIT acquired a 90% interest in two income-producing multi purpose industrial properties located in the United States for approximately U.S. $35.8 million, excluding acquisition costs. The acquisition was funded through a combination of U.S. $14.3 million which was substantially sourced from the Granite Credit Facility and first mortgage debt of U.S. $21.5 million, representing Granite REIT's proportionate share of the total first mortgage debt on the two properties.

(c) On February 28, 2013, the Company and the Stronach Shareholder entered into a settlement agreement with PA Meadows, LLC relating to The Meadows Holdback Agreement (note 22(e)). The Stronach Shareholder will receive proceeds of U.S.$10 million consisting of U.S.$3 million in cash and a promissory note of U.S.$7 million which will be shared equally with the Company. The promissory note is non-interest bearing and is to be paid in equal U.S.$1 million installments commencing March 31, 2013 to September 30, 2013.

REIT Information

Board of Trustees

G. Wesley Voorheis
Chairman

Peter Dey
Vice-Chairman

Michael Brody
Trustee

Barry Gilbertson
Trustee

Thomas Heslip
Trustee

Gerald J. Miller
Trustee

Scott I. Oran
Trustee

Officers

Thomas Heslip
Chief Executive Officer

Michael Forsayeth
Chief Financial Officer

Jennifer Tindale
Executive Vice President,
General Counsel and Secretary

John De Aragon
Executive Vice President,
Real Estate Investment

Lorne Kumer
Executive Vice President, Real Estate
Portfolio and Asset Management

Stefan Wierzbinski
Executive Vice President Europe

Office Location

77 King Street West
Suite 4010, P.O. Box 159
Toronto-Dominion Centre
Toronto, ON M5K 1H1
Phone: (647) 925-7500
Fax: (416) 861-1240

Investor Relations Queries

Thomas Heslip
Chief Executive Officer
(647) 925-7539

Michael Forsayeth
Chief Financial Officer
(647) 925-7600

Transfer Agents and Registrars

Canada
Computershare Trust Company
of Canada
100 University Avenue
Toronto, Ontario, Canada M5J 2Y1
Phone: 1 (800) 564-6253
www.computershare.com

United States
Computershare Trust Company N.A.
250 Royall Street
Canton, Massachusetts, USA 02021
Phone: 1 (800) 962-4284

Exchange Listings

Stapled Units	–	Toronto Stock Exchange (GRT.UN) and New York Stock Exchange (GRP.U)

Please refer to our website (www.granitereit.com) for information on Granite's compliance with the corporate governance standards of the New York Stock Exchange and applicable Canadian standards and guidelines.

Publicly Available Documents

Copies of the financial statements for the year ended December 31, 2012 are available through the Internet on the Electronic Data Gathering Analysis and Retrieval System (EDGAR), which can be accessed at www.sec.gov, and on the System for Electronic Document Analysis and Retrieval (SEDAR), which can be accessed at www.sedar.com. Other required securities filings can also be found on EDGAR and SEDAR.

GRANITE REIT

Granite REIT

77 King Street West
Suite 4010, P.O. Box 159
Toronto-Dominion Centre
Toronto, ON M5K 1H1
Phone: (647) 925-7500
Fax: (416) 861-1240
www.granitereit.com