Fundamental Research Corp.
Investment Analysis for Intelligent Investors

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Capital Direct I Income Trust – Strong 2016 / Continuing to Grow Portfolio Size

Sector/Industry: Real Estate Mortgages **www.incometrustone.com**

Offering Summary	
Issuer	Capital Direct I Income Trust
Securities Offered	Classes A, C, and F Trust Units
Unit Price	$10
Minimum Subscription	$5,000
Hurdle Rate	N/A
Distribution to Investors	80% of net income on a quarterly basis
Redemption	Class A - penalty of 5% of NAV in year 1, decreasing by 1% every year; no penalty after year 5 / Class C & Class F - penalty of 2% within 6 months and no penalty after that
Management Fee	2.0% p.a. of NAV on Classes A and C units / 1.0% p.a. of NAV on Class F units
Auditor	Johnsen Archer LLP

Investment Highlights

- Mortgage investments (net of provisions) held by Capital Direct I Income Trust ("trust", "fund") increased by 66% YoY from $89 million to $147 million by the end of 2016. The portfolio was at $155 million at the end of Q1-2017.
- The trust's primary focus is on single-family owner occupied residential mortgages.
- At the end of March 2017, 50.6% of the mortgages were in British Columbia (BC), 38.9% in Ontario (ON), 9.6% in Alberta (AB), and 0.9% in Atlantic Canada.
- The average mortgage size at the end of March 2017 was $106k. The loan-to-value ("LTV") was 52.5%.
- In 2016, the trust reported a realized loss of 0.56% of the total portfolio, down from 0.72% in 2015. The average loan loss has been 0.40% p.a. since 2010.
- The trust uses leverage to enhance returns. At the end of Q1-2017, debt to capital was 27%. Comparables typically use debt levels of up to 45%.
- Investors' dividend yield (weighted average of all unit types) was 7.6% p.a. in 2016.
- We are maintaining our overall rating of 2 and risk rating of 2.

Risks

- Loans are short term and need to be sourced and replaced quickly.
- Timely deployment of capital is crucial.
- A drop in housing prices will result in higher LTVs, and higher default risk, as the value of collateral decreases.
- No hurdle rate.
- The fund has the ability to use leverage, which increases the exposure of the fund to negative events.
- In addition to first mortgages, the fund invests in second and third mortgages, which carry higher risks.

FRC Rating	
Expected Yield (next 12M)	7.5% - 9% p.a. depending on unit class
Rating	2
Risk	2

*see back of report for rating definitions

Overview

Approximately 85% - 90% of the residential mortgages in Canada are originated by federally or provincially regulated entities such as chartered banks, credit unions and caisses populaires. The remaining mortgages are originated by lenders that are either partially regulated or totally unregulated. Mortgage Investment Entities ("MIEs") account for a major share of the unregulated mortgage lending sector in the country. They are considered unregulated as they are not subject to federal government mortgage lending rules, such as reserve requirements and loan to value limits. This is primarily because, unlike banks and other major financial institutions, MIEs do not take deposits. Note that MIEs are audited / regulated by their respective provincial securities commissions, so the term 'unregulated' only applies to the federal mortgage lending rules. **In a recent study conducted by us for the Canada Mortgage Housing Corportaion ("CMHC"), we estimated that MIEs account for $8 to $10 billion, or just 0.5% of the $1.43 trillion Canadian residential market.**

Capital Direct I Income Trust is structured as an income trust and qualifies as a registered investment, and eligible for deferred plans, such as RRSP, RRIF, TFSA, RESP, etc. The business model and structure are very similar to a Mortgage Investment Corporation ("MIC"). Both structures allow investors to invest in a pool of diversified mortgages and receive income from them.

The trust was created on June 23, 2006, in Vancouver, BC. The manager of the trust is Capital Direct Management Ltd., a subsidiary of a private corporation, Capital Direct Lending Corp. ("Capital Direct", "company"), which was incorporated in 1997. The mortgage investments for the trust are sourced through Capital Direct.

Capital Direct is owned by three partners, Richard Nichols, Derek Tripp, and Tim Wittig, and has 28 employees. In addition to the three partners, the company's senior management team includes a Chief Compliance Officer ("CCO"), Martha Kane. She joined the company in September 2015. A brief biography of the CCO, as provided by the company, follows:

- *Martha Kane joined Capital Direct in 2015 bringing with her 25 years of experience in the financial services industry. She started her career in front of the investor as a financial planner then moved on to hold various roles in a dealer environment including as CCO of a national firm. To compliment her industry experience, Martha served as a Senior Advisor and Acting Manager of Examination at the BCSC. Martha has a Bachelor of Commerce (Hons) from the Asper School of Business and subsequently obtained a Certified Planner Designation (CFP).*

The board of governors consists of five individuals, namely, Richard Nichols, Derek Tripp, David B. Rally, Paul Wylie and Tim Wittig. Paul Wylie is an independent director. The non-independent directors owned 0.5% of the outstanding units as of March 31, 2017. The trust units purchased by the directors were at a price of $10 per unit (the same price as investors).

	Dec-15	% of Total	Dec-16	% of Total	Mar-17	% of Total
Richard F.M. Nichols	9,132	0.17%	9,655	0.09%	10,006	0.08%
Derek R. Tripp	14,042	0.26%	14,847	0.14%	15,386	0.13%
Tim Wittig	8,503	0.16%	17,373	0.16%	18,002	0.15%
David Rally	5,192	0.10%	10,645	0.10%	11,032	0.09%
Total	**36,869**	**0.69%**	**52,520**	**0.49%**	**54,426**	**0.46%**

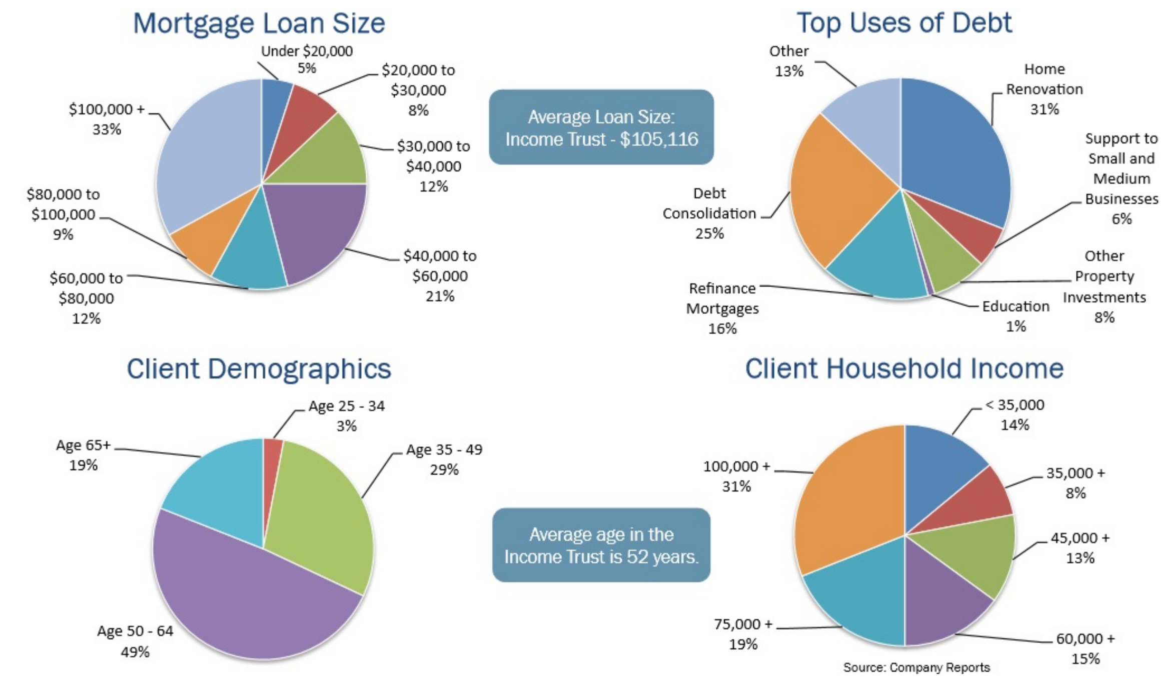
Capital Direct has offices in Vancouver, Calgary, Edmonton, Toronto, and the Maritimes (Nova Scotia and New Brunswick, and PEI). We consider the nationwide reach a major advantage for the trust as it spreads out risks across geographic locations.

Capital Direct is in the business of sourcing, underwriting, selling and administrating residential mortgages on behalf of retail investors, registered funds and private mortgage lenders. It has originated approximately **$1.10 billion in mortgages** since inception in 1997, and currently originates between $150 and $175 million per year. These mortgages are sold to the trust, and to third-party retail and institutional investors. **As of December 31, 2016, Capital Direct administered approximately $195 million in mortgages – which included $148 million for the trust, and the remaining $47 million for other investors.**

The company acquires 75% of its clients directly through advertisements, and 25% from referrals by other brokers and banks. Capital Direct maintains a significant advertising budget, and is a well-known brand, especially in Vancouver and Toronto. Their long track record and aggressive marketing campaigns, we believe, give them a strong edge over the competition, and creates barriers to entry for new entrants.

Investment Mandate

The trust's primary focus is on single-family owner occupied residential mortgages. The homeowner may use the loan at his or her discretion. The following charts show the breakdown of how the borrowers use funds, client demographics, household income, etc.

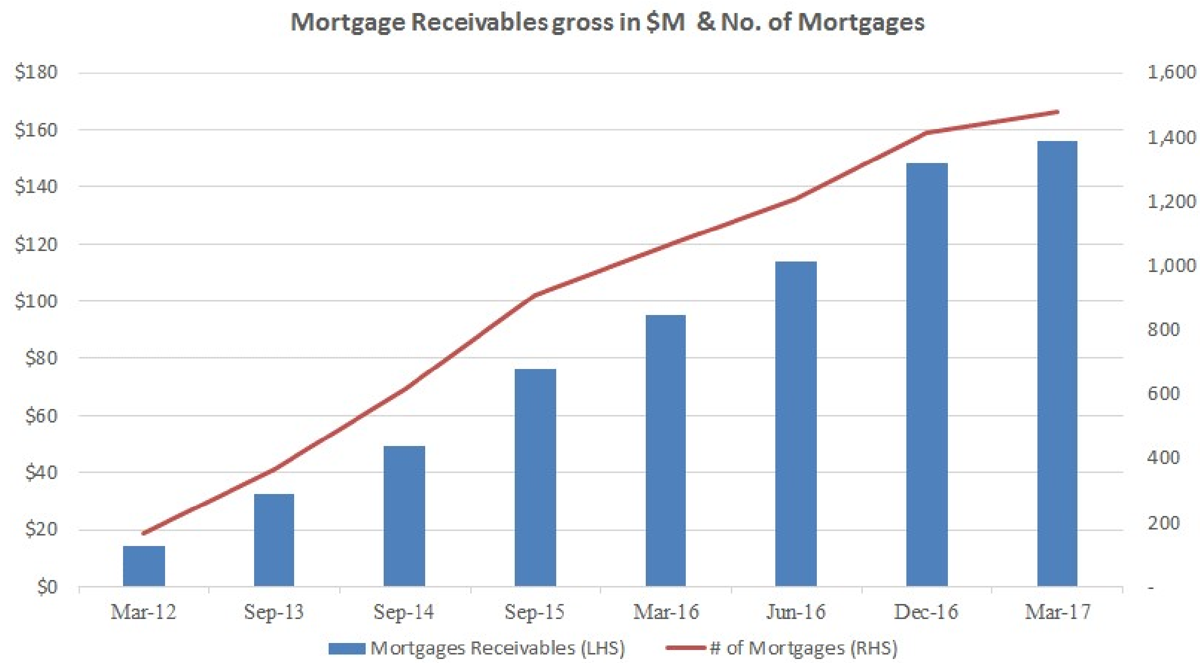


Management's investment criteria (listed below) remains unchanged from our previous report.

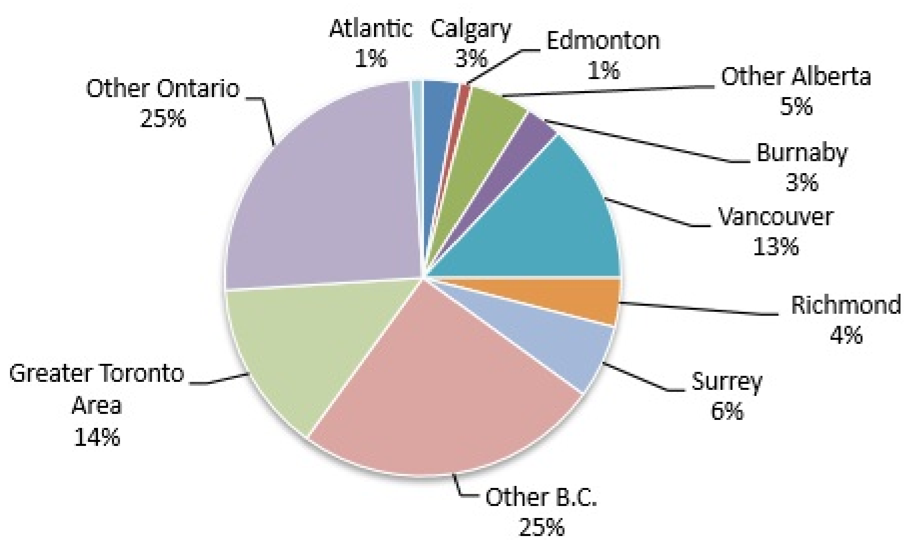
- The mortgages will primarily be on residential property situated within Canada. No more than 5% of the trust's assets will be invested in mortgages on the same property.
- The trust will not directly invest in real property; however, it may hold property acquired as a result of foreclosure.
- The trust will not make loans to, nor invest in securities issued by the manager or its affiliates. The trust will not make loans to any of the directors or officers of the manager, or their associates, or members of the board of governors.
- The trust may only invest in "qualified investments", as defined in the tax act for a trust governed by a deferred plan.
- The trust may invest in mortgages with any term; however, the focus will always be on 1-2 year terms.
- The trust may only borrow funds in order to acquire or invest in specific mortgage investments or mortgage portfolios. The maximum amount the trust is able to borrow is 50% of the book value of the mortgage portfolio.

Portfolio Update and Analysis

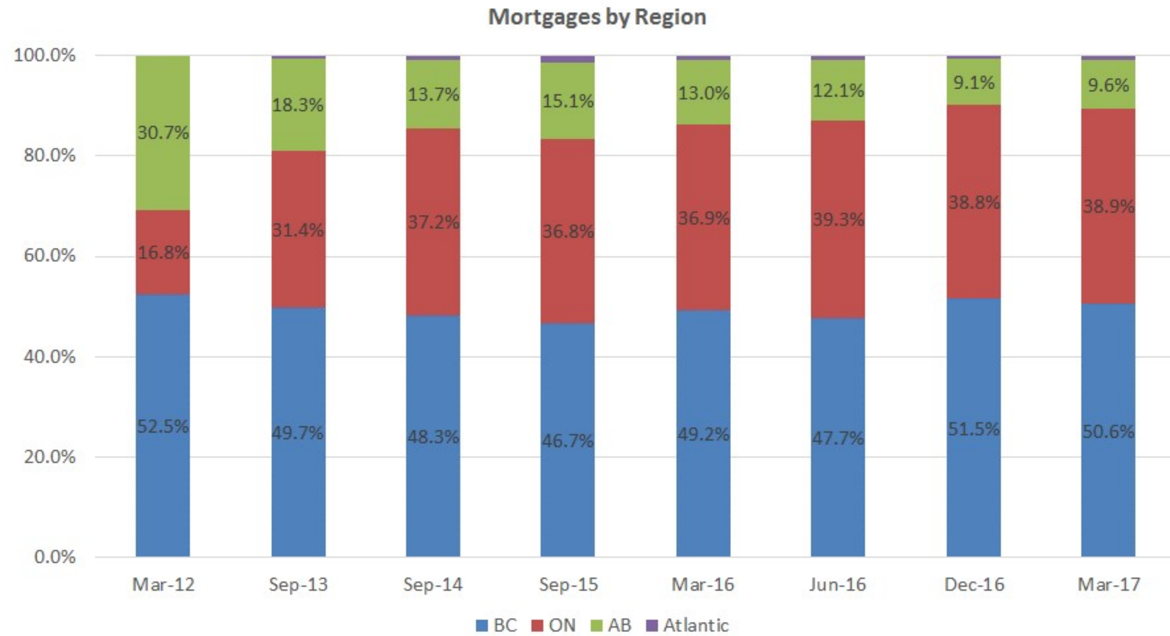
As of March 31, 2017, the trust had $154.79 million in mortgage receivables (net of provisions) across 1,478 properties, up from $88.67 million across 1,208 properties at the end of 2015. The following chart shows the growth in the portfolio since 2012.



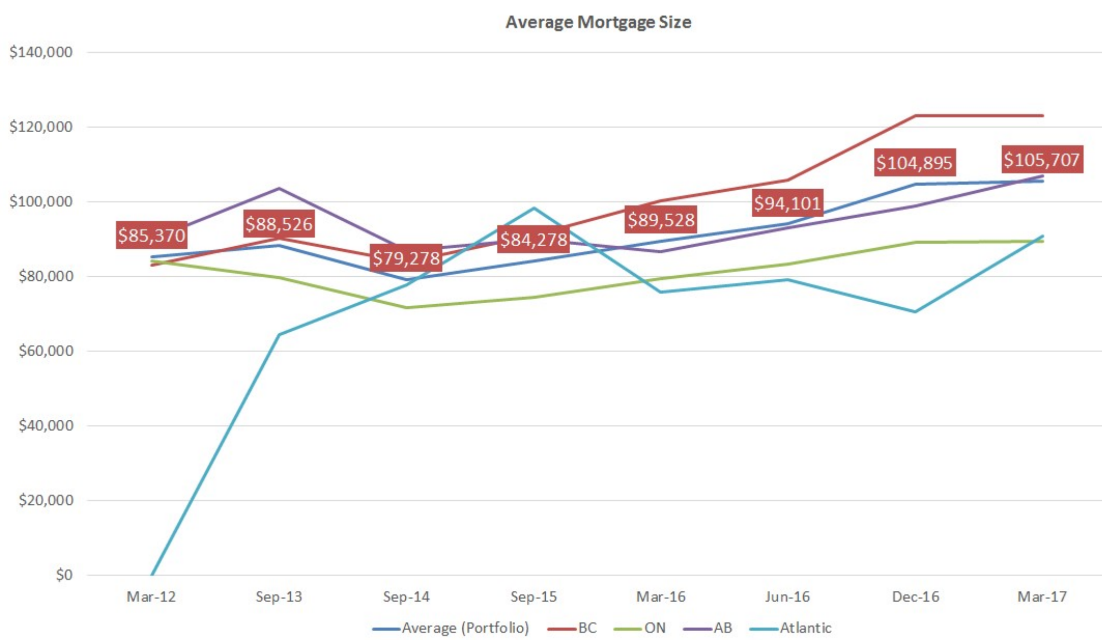
Mortgages by Region: A majority of the properties are within a 90-km radius of metropolitan areas. Properties close to metropolitan areas are less vulnerable to economic downturns. The table below shows the distribution of mortgages by region. At the end of March 2017, 50.6% of the mortgages were in BC, 38.9% in ON, 9.6% in AB, and 0.9% in Atlantic Canada.



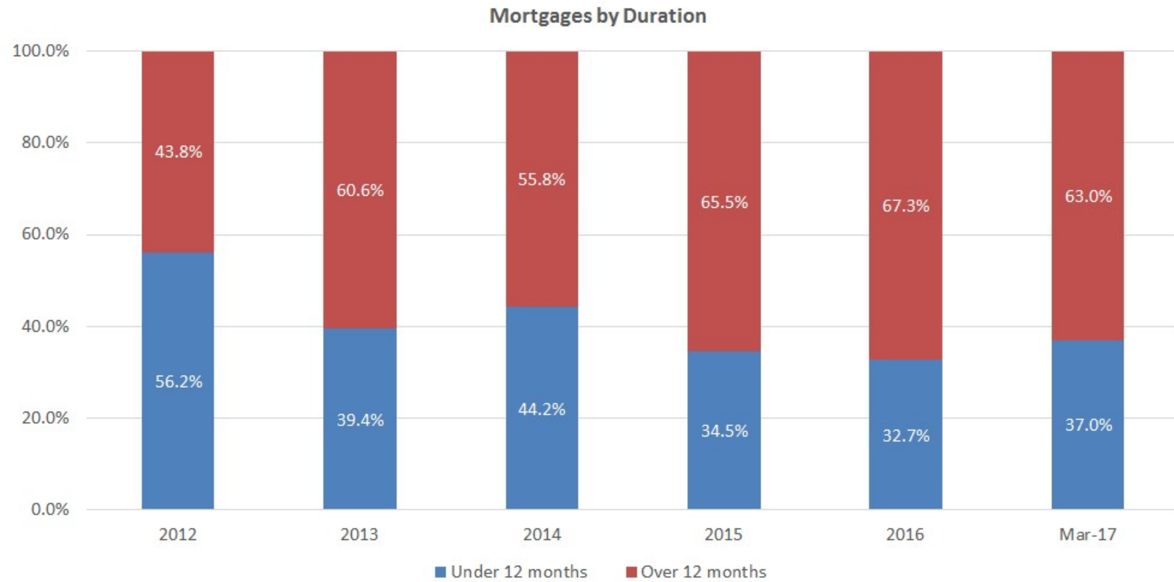
The following chart shows the distribution since 2012. Since 2012, the trust had been increasing its exposure to ON, while reducing its exposure to AB, which we believe was a very prudent move considering the steep decline in oil prices and the following uncertainties in the Alberta real estate market.



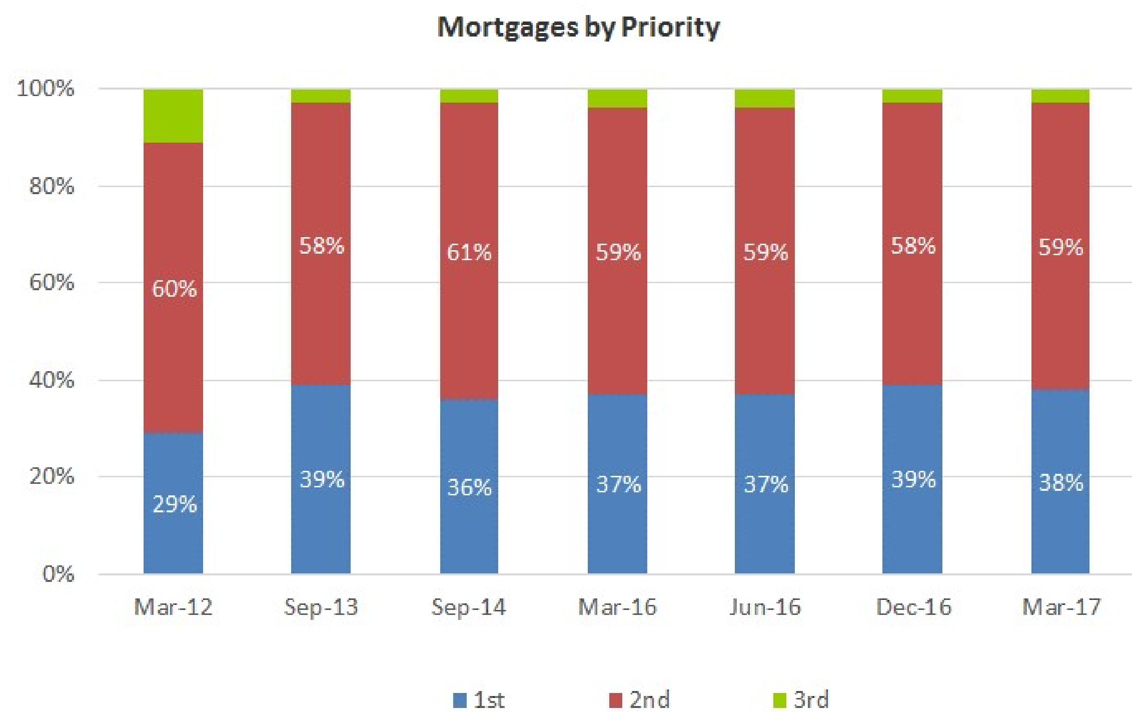
Mortgages by Size: One of the primary features of the trust's portfolio, we believe, is the low mortgage size. The average mortgage size at the end of Q1-2017was $106k versus $94k at the end of 2015. BC had the highest average ($123k) and ON had the lowest average ($89k). The averge has been increasing primarily because of the rising real estate prices in BC and ON.



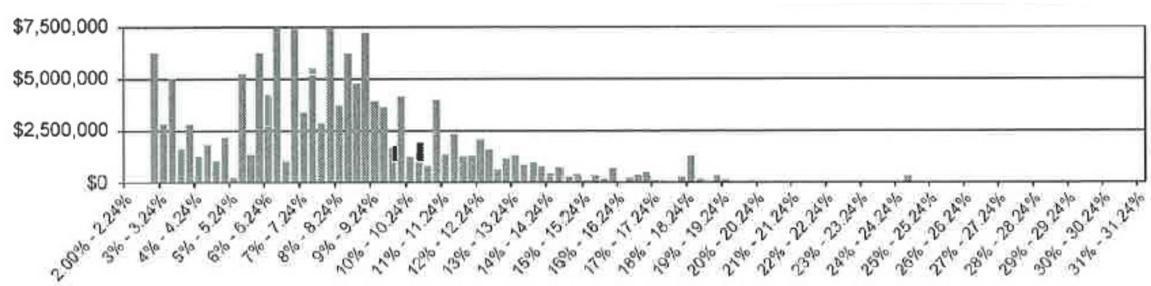
Mortgages by Duration: At the end of Q1-2017, approximately 37% of the portfolio had terms of 12 months or less.



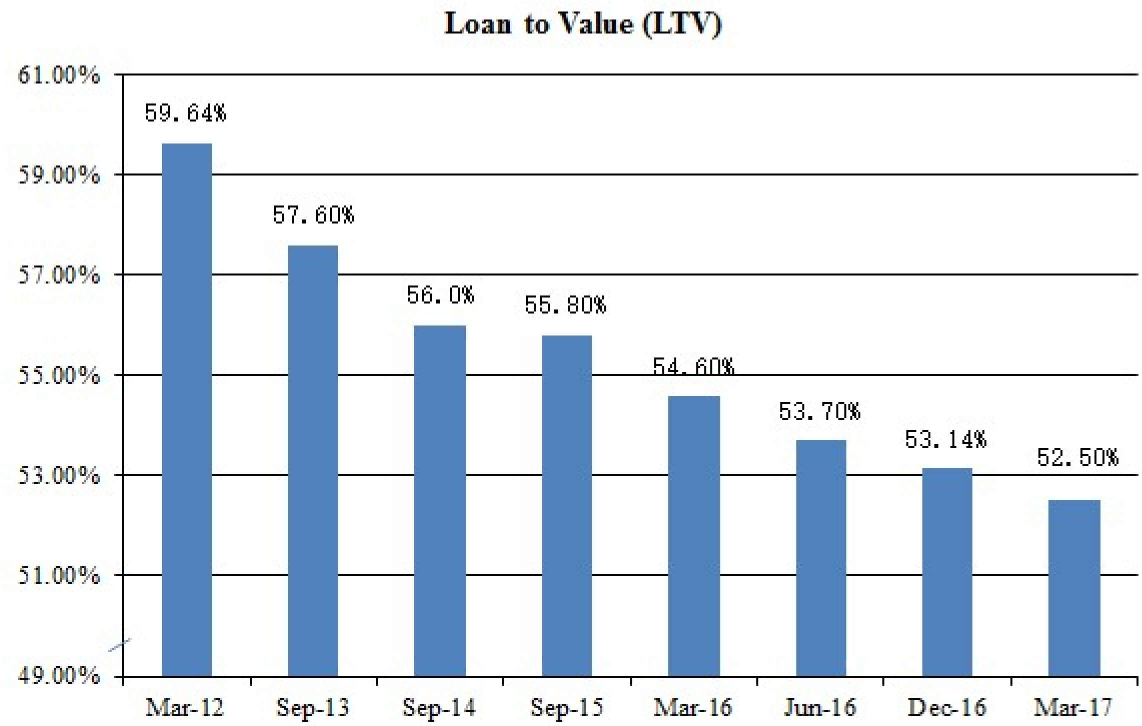
Mortgages by Priority: First mortgages accounted for 38% as of March 2017 (versus 37% as of December 2015). Second mortgages were at 59% and third mortgages were at 3%.



The following chart shows the interest rates charged to the borrowers. The average rate in 2016 was 7.99% p.a. versus 8.66% p.a. in 2015. The following chart shows the distribution of rates by mortgages. Management expects the lending rate in 2017 to remain relatively stable; moving in line with the Bank of Canada's overnight rate.



Loan to Value (LTV): The portfolio's LTV has been on a decreasing trend since 2012, as shown below.



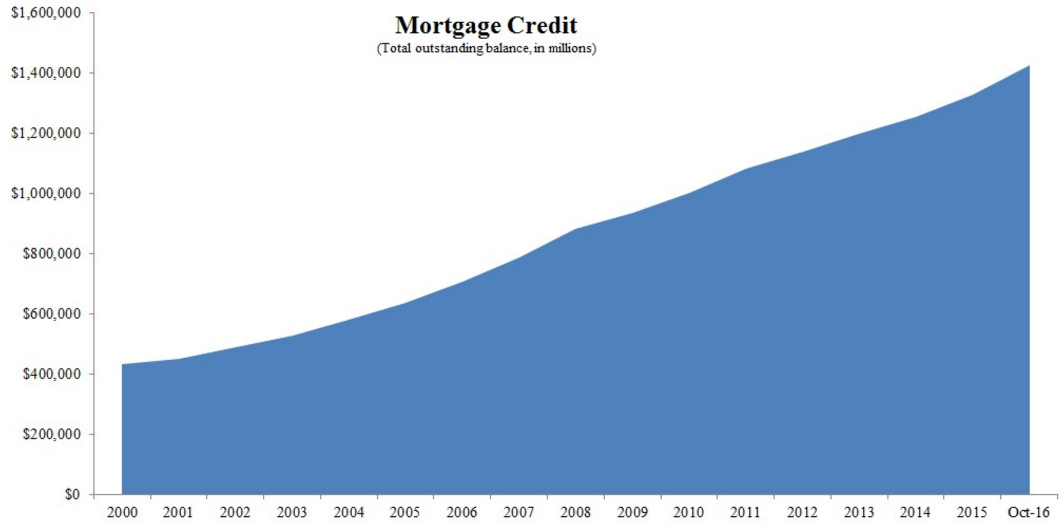
Source: Capital Direct

In summary, we believe the trust has maintained its portfolio's risk profile. Although the average mortgage size increased, we believe the reduction in LTV and an increase in first mortgages offsets the increase in risk.

The following section provides an overview of the mortgage lending market.

Private Mortgage Lending Update

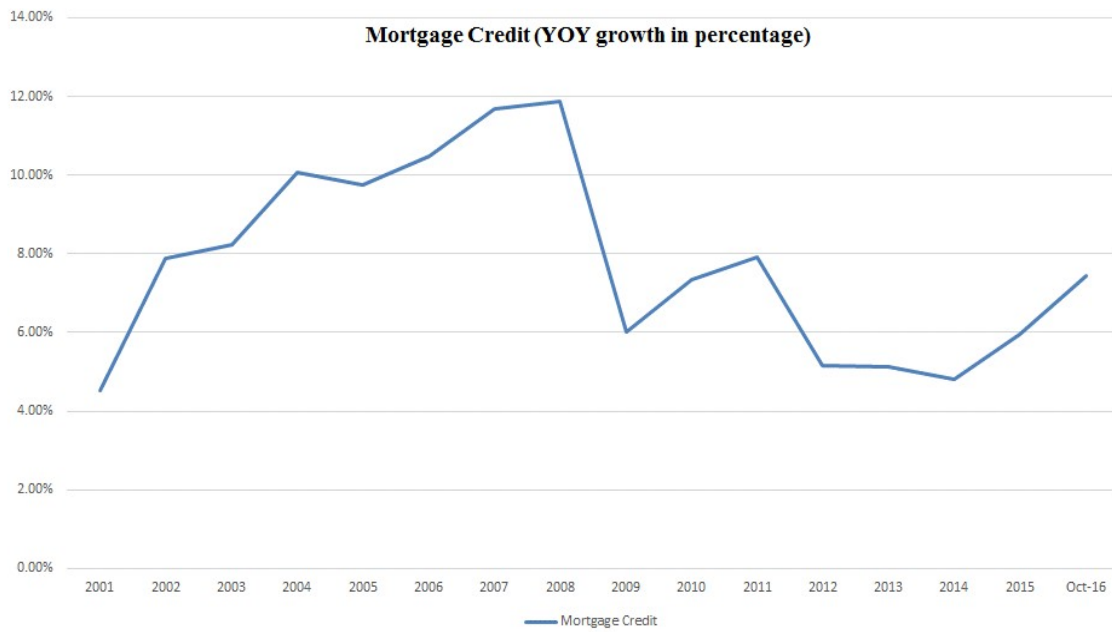
Total residential mortgage credit in Canada (outstanding balance of the major private institutional lenders) increased from $0.43 trillion in 2000, to $1.43 trillion by October 2016, reflecting a compounded annual growth rate ("CAGR") of 7.8%, and a 7.4% YOY increase.



Source: Statistics Canada

As of October 2016, mortgage credit accounted for 72%, and consumer credit accounted for the remaining 28%, of total household debt.

The following chart shows the annual growth rate of mortgage credit. As shown below, the growth rates increased significantly in 2016, primarily because of the low interest rate environment and the strong increase in housing prices.



Source: Statistics Canada

With regard to the financing required for the purchase, buyers have historically financed 67% of their purchase through a mortgage and/or a home equity line of credit, ranging from 81% for first-time buyers, to 67% for second-time buyers, and 50% for those purchasing their third or subsequent home.

The tighter lending policies set by banks and conventional lenders have been encouraging more and more unregulated private lenders to enter the market over the last decade. On October 17, 2016, the federal government announced four key changes to the existing mortgage rules:

- All new insured mortgages will need to undergo a stress test; implying that a home buyer would not only need to qualify at the loan rate, but also at the Bank of Canada's five-year fixed posted mortgage rate, which is currently (4.64%) much higher than the rates offered by mortgage lenders.

- Insurance for low-ratio mortgages (down payment of over 20%) will only be provided by government backed lenders for the following: purchase price of under $1 million, a maximum amortization period of 25 years, a minimum credit score of 600, and the property must be owner-occupied.

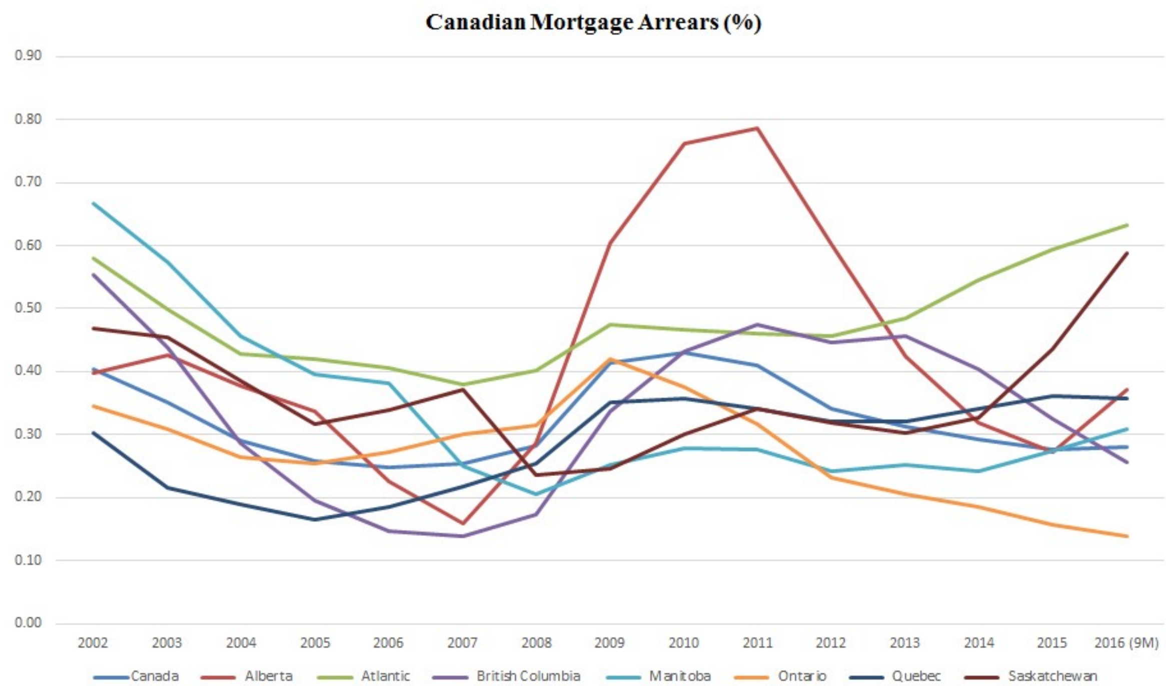
- New reporting rules for the primary residence capital gains exemption.

- The government is considering options to shift some of the risk of defaults against insured mortgages to lenders.

We believe the above changes clearly indicate the government's intent to stabilize the real estate market in the country and potentially avoid a major downturn, similar to the U.S. The finance department estimates home sales could fall by up to 8% in 2017, before rebounding. We see these changes are likely to drive more borrowers to MIEs and other private lenders.

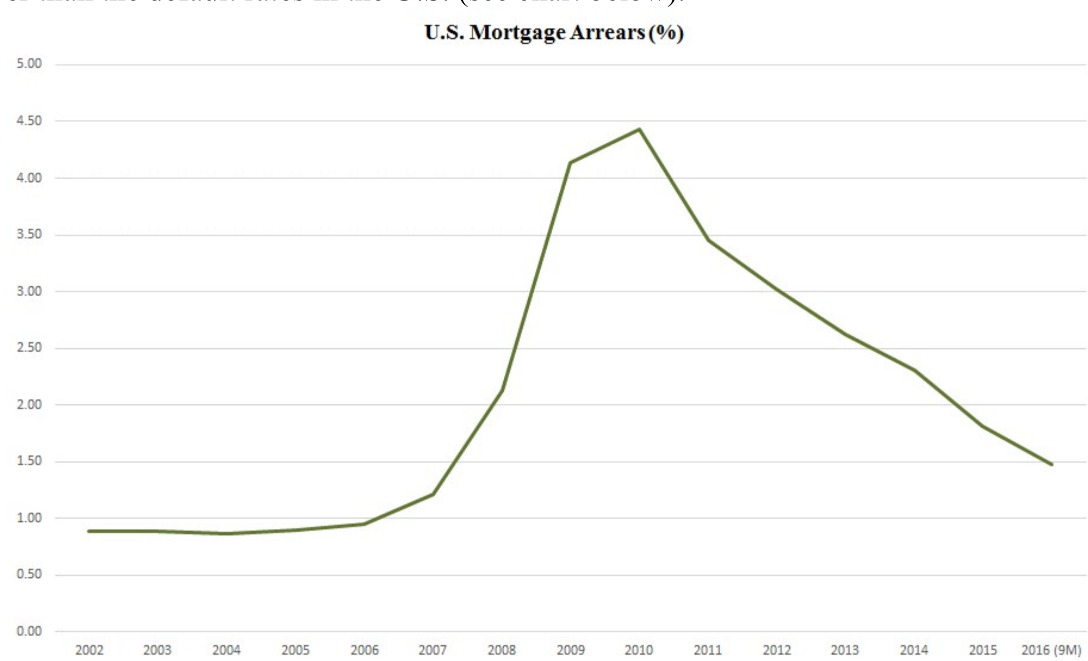
The other factors that have been contributing to increased lending are the strong growth in housing prices, decreasing unemployment rates (see chart below), a low interest rate environment, and the relatively low default rates.

Although there was a rise in mortgage arrears during the recession (mid-1990s and 2008-2009), the rates have dropped considerably since 2010, as shown in the chart below.



Source: CMHC

The national average was 0.28% in Q3-2016, versus 0.43% in 2010. This is significantly lower than the default rates in the U.S. (see chart below).



Source: CMHC

The following table shows the average, minimum and maximum rates in Canada since 2002. BC's rate of 0.24% in Q3-2016, is well below the historical average of 0.34%. The U.S. national average was 1.41% in Q3-2016.

%	2002 - 2016 (Average)	Low	High	Q3-2016
Canada	**0.32**	**0.25**	**0.43**	**0.28**
Alberta	0.42	0.16	0.79	0.41
Atlantic	0.48	0.38	0.63	0.63
British Columbia	0.34	0.14	0.55	0.24
Manitoba	0.34	0.21	0.67	0.31
Ontario	0.27	0.14	0.42	0.13
Quebec	0.29	0.17	0.36	0.34
Saskatchewan	0.36	0.24	0.59	0.61
U.S.	**2.07**	**0.87**	**4.43**	**1.41**

Data Source: CMHC

As mentioned earlier, the low interest rate environment is another factor that is driving lending. The following chart shows the overnight lending rate since 2007.

Overnight Lending Rate

We believe that all of the above factors indicate strong deal flow for MIEs and private lenders in 2017.

We believe the health of Vancouver and Toronto's residential real estate markets directly / indirectly impact the trust.

Toronto and Vancouver Market Update

In an effort to cool down the housing market in the Greater Toronto Area, the Ontario government announced a few changes to existing rules. Among the changes, the key ones are a 15% tax on non-resident buyers of properties in the Greater Golden Horseshoe area, a tax on vacant homes, and expanded rent control measures. The first two changes are in line with the changes seen in Vancouver last year. We believe the correction in Vancouver prices after these initiatives came into play in 2016 may have prompted the Ontario government to move in a similar direction. The tighter rent control measures, we believe, are likely to soften investment into apartment projects, which will impact lenders.

The Toronto market continues to remain robust. Total MLS sales were up by 17% YoY in March 2017 to 12,077 units. The average price was up 33% YoY to $917k. The table below summarizes the key parameters.

Toronto	Jan-16	Jan-17	YoY	Feb-16	Feb-17	YoY	Mar-16	Mar-17	YoY
Residential Sales	4,672	5,188	11%	7,621	8,014	5%	10,326	12,077	17%
New Listings	8,906	7,338	-18%	11,234	9,834	-12%	14,795	17,051	15%
Active Listings	9,966	5,034	-49%	10,902	5,400	-50%	12,132	7,865	-35%
Sales to Active Listings	46.88%	103.06%		69.90%	148.41%		85.11%	153.55%	
MLS ® Home Price Index composite benchmark price	$630,193	$770,745	22%	$685,738	$875,983	28%	$688,011	$916,567	33%

Source: Toronto Real Estate Board

A factor that is indicating that the market is healthy is the extremely high sales to active listings ratio – which was at 154% in March 2017, up from 85% in March 2016.

The following table shows that sales were high across all major property types:

Toronto sales by type	Jan-16	Jan-17	YOY	Feb-16	Feb-17	YoY	Mar-16	Mar-17	YoY
Detached	2,109	2,261	7%	3,627	3,721	3%	4,954	5,887	19%
Semi detached	452	423	-6%	725	651	-10%	986	1,002	2%
Att/Row/Townhouse	375	421	12%	591	619	5%	830	937	13%
Condo Townhouse	356	356	0%	511	546	7%	721	789	9%
Condo Apartment	1,302	1,636	26%	2,046	2,360	15%	2,641	3,261	23%
Link	67	81	21%	103	99	-4%	177	170	-4%
Co-op Apt	7	3	-57%	7	7	0%	7	11	57%
Det Condo	1	2	100%	3	7	133%	5	13	160%
Co ownership Apt	3	5	67%	8	4	-50%	5	7	40%
Total	**4,672**	**5,188**	**11%**	**7,621**	**8,014**	**5%**	**10,326**	**12,077**	**17%**

Source: Toronto Real Estate Board

Although the recently announced changes will have a cooling effect, we estimate the low inventory will keep the Toronto market strong this year. As mentioned in our previous reports, we believe a slight correction in the Toronto market (as seen in the Vancouver market) will be healthy for the long-term.

Vancouver's real estate sales continued to drop, but at a lower rate in March, compared to the first two months of the year. The sales to active ratio increased from 32% in February to 47% in March. An increase in this ratio, we believe, is typically a good indicator for prices.

Metro Vancouver	Jan-16	Jan-17	YoY	Feb-16	Feb-17	YoY	Mar-16	Mar-17	YoY
Residential Sales	2,519	1,523	-40%	4,172	2,425	-42%	5,173	3,579	-31%
New Listings	4,442	4,140	-7%	5,812	3,666	-37%	6,278	4,762	-24%
Active Listings	6,635	7,238	9%	7,299	7,594	4%	7,358	7,586	3%
Sales to Active Listings	37.97%	21.04%		57.16%	31.93%		47.05%	47.20%	
MLS ® Home Price Index composite benchmark price	$775,300	$896,000	16%	$795,500	$906,700	14%	$815,000	$919,300	13%

Source: Real Estate Board of Greater Vancouver

Sales of detached properties dropped the most.

Vancouver sales by type	Mar-16	Mar-17	YoY
Detached	2,135	1,150	-46%
Apartments	2,252	1,841	-18%
Attached property	786	588	-25%
Total	**5,173**	**3,579**	**-31%**

Source: Real Estate Board of Greater Vancouver

Although we continue to adopt a cautious outlook, we believe Vancouver's housing market is reasonably healthy in the near-term (due to low supply), and do not expect a major correction. Immigration and foreign investment is expected to continue due to the city's global appeal, Canada's economic stability, and the weakness in the C$.

Structure

The following section presents a summary of the trust's structure.

At the end of March 2017, there were 11.89 million units outstanding held across 1,400+ investors.

Units Outstanding	31-Mar-17	% of Total
Class A	5,751,490	48.4%
Class C	1,503,560	12.6%
Class F	4,637,294	39.0%
Total	**11,892,344**	**100.0%**

- Class A (since inception) - offered to investors directly
- Class F (introduced in 2014) – offered to funds managed by portfolio managers and other fee-based investment advisors.
- Class C (introduced in 2016) – offered to investors who purchase units through Dealers (IIROC and Exempt Market Dealers).

There is no market or exchange that the trust units trade on. The units are non-transferable. They are eligible for redemption twice a year (June 30 and December 31).

For Class A units, if redemption requests are within the first 5 years, the following redemption schedule applies. If notice of a Class A redemption is given prior to the first anniversary of acquisition of such units, redemption will be 95% of the net asset value per unit on the redemption date. The redemption amount will increase by 1% each year until on, or after the fifth anniversary, at which time redemptions will be equal to 100% of the net asset value of the units on the redemption date.

As for Classes C and F, a 2% penalty applies in the first 180 days. There is no penalty for requests after 180 days.

The trust is managed by the manager, Capital Direct Management Ltd. The manager is entitled to a share of the profits as well as a management fee as per below:

- **2.0% of NAV in annual management fees for Class A and C units, and 1.0% of NAV for Class F units (paid monthly).** This fee is in line with comparables; the range on similar offerings is 1% - 3%. The NAV is calculated by management every quarter.

- As per the OM, 80% of the aggregate of net income will be paid to the unitholders on a quarterly basis, and the remaining 20% will be paid to the manager. In order to provide a higher share of returns to investors, management distributed 90% of the net income to investors from Q4-2008 to Q3-2015. The share was reverted back to the original 80% from Q4-2015 to Q3-2016, and then increased to 90% in Q4-2016. **The overall impact was that investors received a 82.8% share of the profits in 2016.**

There are **no sales commissions** charged to the trust - any sales commissions paid (maximum of 1.5% of the Class A gross proceeds + a 1% trailer fee) will be the responsibility of the manager.

Financials

The following table shows a summary of the income statement since 2011. Our previous reports included an analysis of the financial statements since inception.

Income Statement	2011	2012	2013	2014	2015	2016	Q1-2017
Revenues							
Interest Income	$1,154,458	$1,584,171	$2,561,432	$3,948,088	$6,155,599	$9,857,086	$3,051,233
Other Income	$72,792	$106,324	$173,377	$303,728	$661,990	$1,185,920	$476,055
	$1,227,250	**$1,690,495**	**$2,734,809**	**$4,251,816**	**$6,817,589**	**$11,043,006**	**$3,527,288**
Expenses							
Audit Fees	$67,275	$60,300	$55,000	$75,250	$94,134	$98,204	$49,033
Bank Charges	$27,923	$30,510	$59,395	$94,370	$131,609	$188,392	$8,917
Interest on Loan Payable	$84,727	$131,177	$350,013	$689,472	$1,051,910	$1,163,928	$366,977
Legal Fees	$64,287	$72,464	$109,644	$174,877	$216,601	$390,689	$26,846
Management Fees	$145,619	$227,121	$321,564	$461,707	$647,100	$1,282,154	$432,585
Loan Loss Provision	$29,976	$91,085	$242,195	$488,142	$916,110	$477,919	$250,546
Trustee Fees	$12,294	$16,517	$60,781	$70,494	$68,618	$102,291	$10,500
	$432,101	**$629,174**	**$1,198,592**	**$2,054,312**	**$3,126,082**	**$3,703,577**	**$1,145,404**
Net Income	**$795,149**	**$1,061,321**	**$1,536,217**	**$2,197,504**	**$3,691,507**	**$7,339,429**	**$2,381,884**
Net Asset Value	$10.00	$10.00	$10.00	$10.00	$10.00	$10.00	$13.08
Units Outstanding	1,070,923	1,442,321	2,041,233	2,778,432	5,338,206	10,670,521	6,030,683
Distributions							
Investors	715,634	955,189	1,382,595	1,977,754	3,215,496	6,075,876	2,143,696
Management	79,515	106,132	153,622	219,750	476,011	1,263,553	238,188
Investors' Share	90.0%	90.0%	90.0%	90.0%	87.1%	82.8%	90.0%

YE – December 31st

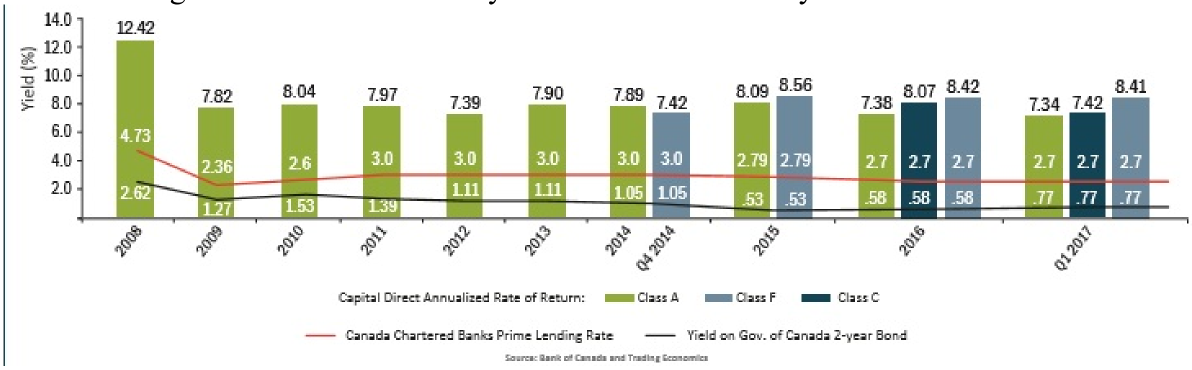
Revenues grew by 62% YoY in 2016 to $9.86 million. Net Income grew by 99% YoY to $7.34 million in 2016.

Interest + Other income as a percentage of mortgage receivables was 9.4% p.a. in 2016, versus 9.6% p.a. in 2015. The dividend yield (dividends as a percentage of invested capital) was 7.6% p.a. in 2016 versus 7.9% in 2015.

% of Mortgage Receivable	2011	2012	2013	2014	2015	2016	2017 (3M)*
Interest Income	10.83%	9.71%	9.16%	8.80%	8.65%	8.36%	8.09%
Other Income	0.68%	0.65%	0.62%	0.68%	0.93%	1.01%	1.26%
Interest Income + Others	**11.51%**	**10.36%**	**9.78%**	**9.47%**	**9.58%**	**9.37%**	**9.35%**
Less:							
Management Fee	-1.37%	-1.39%	-1.15%	-1.03%	-0.91%	-1.09%	-1.15%
G&A Expenses	-1.61%	-1.10%	-1.02%	-0.92%	-0.72%	-0.66%	-0.25%
Loan Loss Provision	-0.28%	-0.56%	-0.87%	-1.09%	-1.29%	-0.41%	-0.66%
Interest	-0.79%	-0.80%	-1.25%	-1.54%	-1.48%	-0.99%	-1.10%
Net	7.46%	6.51%	5.49%	4.90%	5.19%	6.23%	6.19%
Investors' Returns (% of Invested Capital)	**7.97%**	**7.60%**	**7.94%**	**8.21%**	**7.92%**	**7.59%**	**7.60%**
2-year GOC	1.32%	1.06%	1.06%	0.98%	0.54%	0.62%	0.78%

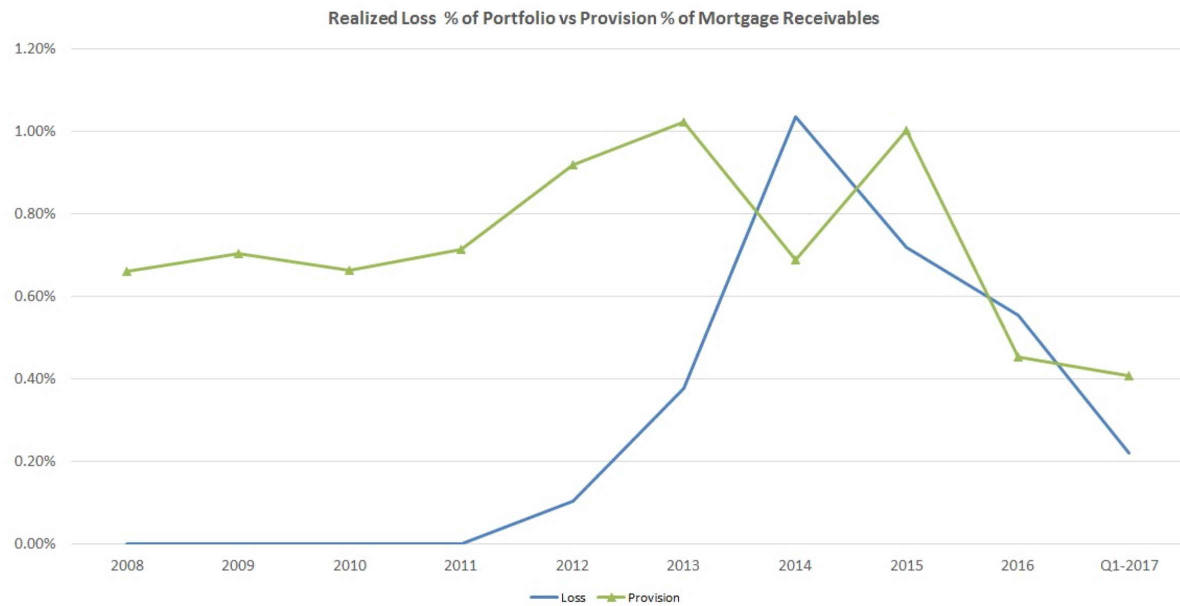
Note that the above figures may be slightly different from the figures reported by Capital Direct due to the difference in the method of calculation. We used the average of the opening balance, and year-end balance of the mortgages outstanding, and invested capital, to arrive at the above figures.

The following charts show investors' yield relative to GOC 2-year bonds:



* Class C's higher return is due to minimal expenses charged to Class C in Q1-2016 when it was introduced.

The following chart shows the realized losses and the loan loss provision as a percentage of mortgage receivables since 2010.



In 2016, the trust reported approximately $0.65 million in realized losses, or 0.5% of the total portfolio. This compared to a loss of $0.51 million in 2015, or 0.7% of the portfolio. The average loan loss was 0.40% p.a. since 2010. In Q1-2017, the realized loss was 0.2%.

At the end of March 2017, the trust had a loan loss provision of $0.62 million, or 0.41% of the portfolio. The trust had assigned a provision of 1.00% at the end of 2015. We estimate that comparable MIEs typically assign 0.8% - 1.0% of their portfolios as loan loss provisions. The lower loan loss provision, we believe, reflects the overall health of the trust's portfolio.

	2010	2011	2012	2013	2014	2015	2016	Q1-2017
Actual Losses	-	-	17,030	106,052	465,260	511,711	654,748	171,571
Actual Losses (% of mortgage receivable)	0.00%	0.00%	0.10%	0.38%	1.04%	0.72%	0.56%	0.22%
Distributions	$497,354	$715,634	$955,189	$1,382,595	$1,977,754	$3,215,496	$6,075,876	$2,143,696
Reinvested	$232,843	$330,497	$495,024	$690,083	$1,118,084	$1,900,488	$3,739,538	$1,321,880
Reinvested (as a % of Distributions)	47%	46%	52%	50%	57%	59%	62%	62%
Redemptions	$132,798	$10,000	$588,593	$636,516	$1,661,741	$1,419,586	$3,210,287	$10,316
Redemption (% of invested capital)	2%	0%	5%	4%	7%	3%	4%	0.0%
Loan loss provision (year end)	$46,136	$76,112	$150,167	$286,310	$309,192	$713,591	$536,762	$615,737
Provision % of Receivable	0.66%	0.71%	0.92%	1.02%	0.69%	1.00%	0.46%	0.41%

As shown above, investors continue to reinvest a significant portion of the distributions

(62% in 2016) – which, we believe, is a very positive sign and shows their confidence in the investment.

Redemptions totaled $3.21 million in 2016, or 4% of the average invested capital. Note that the trust has redeemed approximately 4% of invested capital every year since 2010 – this indicates management's ability and willingness to meet redemption requests. According to management, they have never declined any redemption request to date. Redemptions can be requested with 30 days' notice of June 30th and December 31st.

The following table shows a summary of the company's balance sheet.

Balance Sheet	2011	2012	2013	2014	2015	2016	Q1-2017
Assets							
Cash	$288,331	$187,552	$569,309	$556,175	$194,106	$1,982,407	$6,007,628
Accounts Receivable	$119,180			$120,045	$1,736,095	$5,226,932	$2,756,025
Prepaid Expense							
Assets held for sale		$15,949					
Mortgage Investments (net)	$12,837,727	$19,781,725	$36,139,391	$53,633,836	$88,672,929	$147,121,047	$154,791,463
	$13,245,238	**$19,985,226**	**$36,708,700**	**$54,310,056**	**$90,603,130**	**$154,330,386**	**$163,555,116**
Liabilities							
Loan Payable	$2,183,086	$5,083,066	$15,631,451	$24,911,835	$35,619,549	$44,018,502	$42,949,755
Accounts Payable & Accured Liabilities	$352,925	$478,948	$664,922	$1,613,901	$1,601,517	$3,606,666	$1,681,934
	$2,536,011	$5,562,014	$16,296,373	$26,525,736	$37,221,066	$47,625,168	$44,631,689
Net Asset	$10,709,227	$14,423,212	$20,412,327	$27,784,320	$53,382,064	$106,705,218	$118,923,427
SE + Liabilities	**$13,245,238**	**$19,985,226**	**$36,708,700**	**$54,310,056**	**$90,603,130**	**$154,330,386**	**$163,555,116**
Debt to Capital	17%	26%	43%	47%	40%	29%	27%
Debt as a % of Mortgage Outstanding	17%	26%	43%	46%	40%	30%	28%
Interest Coverage Ratio	10.4	9.1	5.4	4.2	4.5	7.3	7.5

The fund's cash position can vary from time to time as loans are paid out and new loans are funded. The cash position at the end of May 2017 was $6 million. The high cash position, we believe, was a result of approximately $11 million new subscriptions received in Q1-2017. The trust was yet to fully deploy the new capital at the end of the quarter.

Line of credit – Since our previous report, the trust's line of credit (prime + 0.75%) with Canadian Western Bank was increased from $40 million to $50 million. As of March 31, 2017, $43 million was withdrawn, reflecting debt to capital of 27%. **The interest coverage ratio in 2016 was 7.3x, which is fairly strong, and indicates that operating profits generated by the trust can easily cover annual debt obligations.** As the interest rate on the line of credit is significantly lower than the trust's lending rate, we believe taking on debt (at acceptable levels), to acquire mortgages, will improve investors' returns. We estimate that comparable MIEs typically use debt levels ranging between 20% and 40%.

Risk

Investors are exposed to the following risks:

- Loans are short term and need to be sourced and replaced quickly.
- Timely deployment of capital is crucial.

- A drop in housing prices will result in higher LTVs, and higher default risk, as the value of collateral decreases.
- Unit holders' principal is not guaranteed, as the NAV per unit could decrease from current levels (as a result of loan losses). Unit holders are also not guaranteed minimum distributions.
- No hurdle rate.
- The net income distribution between investors and the manager has been 90%:10% in the past few years; however, there is no guarantee that this trend will continue going forward.
- The fund has the ability to use leverage, which would increase the exposure of the fund to negative events.
- The fund invests in second and third mortgages (historically 60% to 65% of the portfolio) which carry higher risk.
- Annual redemptions may be limited to 10% of the total invested capital, and may not be paid in cash.

Rating

We are maintaining our overall rating and our risk rating at 2.

FRC Rating	
Expected Yield (next 12M)	7.5% - 9% p.a. depending on unit class
Rating	2
Risk	2

Fundamental Research Corp. Rating Scale:

Rating – 1: Excellent Return to Risk Ratio
Rating – 2: Very Good Return to Risk Ratio
Rating – 3: Good Return to Risk Ratio
Rating – 4: Average Return to Risk Ratio
Rating – 5: Weak Return to Risk Ratio
Rating – 6: Very Weak Return to Risk Ratio
Rating – 7: Poor Return to Risk Ratio
A "+" indicates the rating is in the top third of the category, A "-" indicates the lower third and no "+" or "-" indicates the middle third of the category.

Fundamental Research Corp. Risk Rating Scale:
1 (Low Risk)
2 (Below Average Risk)
3 (Average Risk)
4 (Speculative)
5 (Highly Speculative)

FRC Distribution of Ratings			
Rating - 1	0%	Risk - 1	0%
Rating - 2	27%	Risk - 2	4%
Rating - 3	47%	Risk - 3	37%
Rating - 4	10%	Risk - 4	37%
Rating - 5	4%	Risk - 5	9%
Rating - 6	1%	Suspended	12%
Rating - 7	0%		
Suspended	11%		

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