Siddharth Rajeev, B.Tech, MBA, CFA
Analyst

January 10, 2014

Capital Direct I Income Trust – Residential Mortgages in BC, ON and AB

Sector/Industry: Real Estate Mortgages

www.incometrustone.com

Offering Summary	
Issuer	Capital Direct I Income Trust
Date of OM	15-Sep-13
Offering	No minimum / Maximum of $125M
Securities Offered	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	Allowed; with a penalty of 5% of NAV in year 1, decreasing by 1% every year; no penalty after year 5
Management Fee	2.0% p.a. of NAV (paid monthly in arrears)
Auditor	Johnsen Archer LLP

FRC Rating	
Yield (5-year average)	8.98% p.a.
Rating	2
Risk	2

*see back of report for rating definitions

Investment Highlights

- Capital Direct I Income Trust ("trust") invests in first, second, or third mortgages secured on residential properties primarily in BC, Ontario, and Alberta. Approximately 97% of the current portfolio of the trust are first and second mortgages.
- The trust is managed by Capital Direct Management Ltd., which is a subsidiary of a private corporation, Capital Direct Lending Corp. ("Capital Direct", "company"), incorporated in 1997.
- As per management, Capital Direct has originated approximately $699 million in mortgages since inception, and is currently originating between $5 and $8 million per month.
- The trust currently has $32 million in assets under management ($18 million in equity from 173 investors, and $14 million in debt) across 365 properties.
- The trust units are entitled to quarterly cash distributions of 80% of the profits of the fund, and are eligible for redemption semi-annually.
- Mortgage terms are typically 6-24 months, minimizing real estate price fluctuation risk, interest rate risk, and duration.
- The last five year average yield for investors was approximately 8.98% p.a.

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 loan-to-value ("LTV"), and higher default risk, as the value of collateral decreases.
- 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.
- There are penalties for early redemption in the first five years.
- Loans are primarily interest only loans.
- The fund has the ability to use leverage (the current debt to capital is 43%), which would increase the exposure of the fund to negative events.
- The fund can invest in second and third mortgages which carry higher risk.

Overview

Capital Direct I Income Trust is an open-ended investment trust that extends loans / mortgages to individuals secured by properties. The loans in the current portfolio are secured by residential properties primarily located within 90km of urban cities in BC, Alberta and Ontario. We initiated coverage on the trust on June 12, 2012. This is our first update report. **We have raised our overall rating to 2 (from 2-), and lowered our risk rating to 2 (from 3).**

The proceeds from the offering will be invested in a portfolio of loans including both first, second or third mortgages on residential properties. **Approximately 97% of the current portfolio of the trust are first and second mortgages.** The trust units are entitled to quarterly cash distributions of 80% of the profits of the fund, and are eligible for redemption semi-annually. Management receives the remaining 20% of the profits, and an annual management fee of 2% of the net asset value ("NAV").

Mortgages are short-term in nature (12 – 24 months) to borrowers that are unable to secure traditional sources of financing. The average loan to value ("LTV") of the fund is currently at 57.6%. The following are examples of typical borrowers:

- asset rich, but no steady income.
- self-employed entrepreneurs unable to show confirmed income
- non-residents or new immigrant with no credit history
- a person with significant equity in a property, but needs cash to bring the property to rentable condition
- borrower needs quick cash while home is up for sale
- debt consolidation - homeowners who have a weak credit rating, and seeking to consolidate debt to lower interest payments, re-store credit rating, etc.

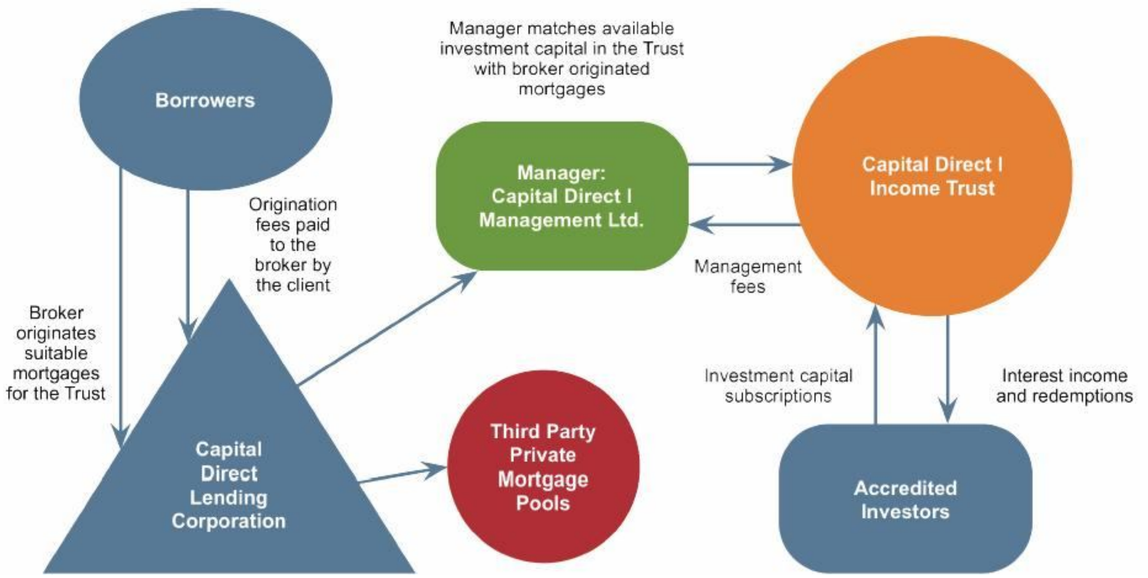
Private lenders generally have more flexibility, compared to banks, in structuring mortgages to a borrower's needs, and therefore, they can typically charge higher rates of interest than banks. The mortgages in the current portfolio of the trust currently have a weighted average interest rate of 8% - 9% p.a. If payments become delinquent, the trust may begin the foreclosure process on the property. To date, management says there have been two foreclosures since inception. Total loan losses since inception have been just $24k.

Management looks for a viable exit strategy when assessing a loan application. There is a wide variety of exit strategies, but the most common exits would be refinancing by a more traditional lender, sale of the property, etc. Generally, for a refinancing, the borrower will borrow short term from Capital Direct, and use the money to increase the value of the property (through renovations, complete construction of a building, property improvements, etc.). Once completed, the borrower tries to refinance from a traditional lender.

The trust currently has $32 million in assets under management ($18 million in equity from 173 investors, and $14 million in debt) across 365 properties. **The trust's objective is to raise approximately $4 million in the next 12 months through the current offering memorandum.**

Manager

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., which was incorporated in 1997. The mortgage investments for the trust will be sourced through Capital Direct.



Sources: Capital Direct

Capital Direct, which is owned by Richard Nichols, Derek Tripp, and Tim Wittig, is in the business of sourcing, underwriting, selling and administrating residential mortgages on behalf of retail investors, registered funds and private mortgage lenders. **Capital Direct has offices in Vancouver, Calgary, Edmonton, Toronto, and the Maritimes (Nova Scotia and New Brunswick, and PEI).** Their nationwide reach, we believe, is a major advantage for the trust, as it spreads out risks across geographic locations. The company has approximately 50 employees.

As per management, Capital Direct has originated approximately $699 million in mortgages since inception in 1997, and is currently originating between $5 and $8 million per month. Capital Direct receives a 1% - 3% fee per origination. These mortgages are sold to the trust, and to third-party retail and institutional investors. The origination fees are not passed on to the trust. Currently, they administer approximately $102 million in mortgages – which includes $32 million for the trust, and the remaining $70 million for other investors.

Capital Direct acquires 75% of its clients directly through advertisements, and 25% from referrals by other brokers and banks. The company, we believe, maintains a significant advertising budget, and is a well-known brand, especially in Vancouver.

As Capital Direct sells the mortgages it originates to third-parties, we asked management how they ensure the quality of mortgages that goes into the trust. Their response was that their ownership in the trust (which is approximately 3% of the total units outstanding) aligns their interest with investors. Also, Capital Direct posts information on all the mortgages originated, since inception, on their website (a snapshot is shown below). This allows investors to actually verify if the mortgages in the trust are sub-par.

Face Amount	Area	Prov	Interest Rate	Int. Start Date	Payment	1st Pymt	LTV	Appraisal Value	Mtg.s Prior	Date of Acquisition	Paid Out
$58,900	Abbotsford	BC	6.10%	10/18/12	$357	11/15/12	19%	$310,000	$0	Oct-18-12	-
$9,907							65%	$406,000	$255,092	Oct-17-12	-
$107,830							72%	$468,000	$228,921	Oct-15-12	-
$166,700							75%	$1,140,000	$688,525	Oct-11-12	-
$30,000	Okotoks	AB	7.00%	10/1/12	$213	10/15/12	45%	$860,000	$355,000	Oct-11-12	-
$50,685	Cumberland	BC	10.55%	9/25/12	$481	10/15/12	72%	$280,000	$149,755	Oct-5-12	-
$35,110	Vancouver	BC	7.85%	10/1/12	$268	11/1/12	36%	$442,500	$123,846	Oct-2-12	-
$87,800	Toronto	ON	Yr 1: 10.99%; Yr 2: P+10.99%	9/25/12	$860	10/15/12	61%	$1,150,000	$609,000	Sep-25-12	-
$36,875	Delta	BC	11.75%	9/24/12	$382	10/15/12	57%	$470,000	$232,677	Sep-24-12	-

Source: Company Reports

Management Team

Brief biographies of the management team, as provided by the company, follow:

Richard F.M. Nichols - President and Director

Founding Partner and President of the Mortgage Broker from 1997 to the present. During his tenure, the Mortgage Broker has evolved from a Vancouver-based company into an inter-provincial organization. Mr. Nichols oversaw the Mortgage Broker's expansion into new markets including Calgary, Edmonton, and other Central Canadian cities, and later developed a subsidiary in three Atlantic Provinces. He attended the University of Prince Edward Island where he studied finance and capital budgeting and received his Bachelors of Business Administration (BBA). In 1993, Mr. Nichols graduated with honors from the Masters of Business Administration (MBA) program at the University of British Columbia. While completing his Masters degree, Mr. Nichols studied international marketing at the Haute Etude Commerciale in Paris, France. Mr. Nichols is an Accredited Mortgage Professional certified by the Canadian Institute of Mortgage Brokers and Lenders (CIMBL) and the Canadian Association of Accredited Mortgage Professionals (CAAMP). He is an active member of Mortgage Brokers Association of British Columbia (MBABC), Independent Mortgage Brokers Association of Ontario (IMBA) and other provincial and national mortgage-brokering professional and trade organizations. He is also a longstanding member of the Vancouver Board of Trade. In the Spring of 2010, Mr. Nichols was elected to the Corus CKNW Orphan's Fund board of directors. His tenure should result in an entire rebranding of the 65 year old foundation, by fostering a connection between the donors and their stories and the grant recipients themselves.

Derek R. Tripp - Vice President and Director
Founding Partner and Vice President of the Mortgage Broker from 1997 to the present. Mr. Tripp brings 25 years of financial experience to the Mortgage Broker. He has underwritten over $300 million in mortgages and specializes in builder's mortgages. During his tenure at the Mortgage Broker, Mr. Tripp has been instrumental in expanding the company into new provinces throughout Canada. Mr. Tripp studied Urban Land Economics in Real Estate at the University of British Columbia. He is an Accredited Mortgage Professional certified by the Canadian Institute of Mortgage Brokers and Lenders (CIMBL) and the Canadian Association of Accredited Mortgage Professionals (CAAMP) and is a licensed mortgage broker in BC and Alberta and a licensed mortgage agent in Ontario. He is a member of the Alberta Mortgage Brokers Association (AMBA), Independent Mortgage Brokers Association of Ontario (IMBA) and other provincial and national mortgage-brokering professional and trade organizations.

Tim Wittig - Vice President and Director
Partner, Vice President and Director of the Mortgage Broker from 2010 to the present. Mr. Wittig brings 25 years of business experience to the Mortgage Broker. He studied history and political science (Joint Honours) at both the University of Waterloo and the University of British Columbia before answering his entrepreneurial call. In 1987, Mr. Wittig and a partner founded Shaftebury Brewing Company ("Shaftebury") in Vancouver. Mr. Wittig was instrumental in establishing Shaftebury as one of the most successful craft breweries in the Pacific Northwest. Mr. Wittig's entrepreneurial spirit was recognized when he was twice nominated for Ernst & Young's Entrepreneur of The Year Award and when he was a recipient of Business In Vancouver's prestigious Forty Under 40 Award. He has been an investor in private mortgages since 1998 and is a licensed mortgage broker. He is an active member of various professional organizations including the Canadian Association of Accredited Mortgage Professionals (CAAMP), the Mortgage Brokers Association of British Columbia (MBABC) and the Independent Mortgage Brokers Association of Ontario (IMBA).

David Rally - Vice President, Legal Affairs
Vice President, Legal Affairs, of the Mortgage Broker from 1997 to the present. Mr. Rally is a lawyer and has been associate counsel at Beck, Robinson & Company since 1989. In his work as a lawyer, Mr. Rally deals extensively in real estate law, including bank mortgages, private financing and commercial leasing as well as in realizations and insurance law. He has acted as counsel before all levels of court in British Columbia and is a member of good standing of the Bars of British Columbia and Upper Canada (Ontario). Mr. Rally served as an advisor in establishing in-house paralegal services for a well-known real estate service provider and is also licensed as a mortgage broker in Ontario. Mr. Rally studied in the Economics (Honours) program at the University of British Columbia and obtained an LL.B. from the University of British Columbia in 1988.

Paul Wylie - Independent member of the Board of Governors

Mr. Wylie's experience includes over 17 years with two leading financial institutions within North America. Most recently Mr. Wylie worked as a Senior Vice-President and Branch Manager with the financial institutions. Throughout his banking career, he has held numerous management roles in various divisions including: private banking, credit, sales and service and wealth management. Mr. Wylie was educated at the University of Toronto, Wharton Business School and the Canadian Securities Institute. He has gained a number of designations including a Bachelors of Arts, Certified Investment Management Analyst, Financial Management Advisor and has completed the Partners, Directors and Senior Officer's Course. Mr. Wylie has also served on the executive board of his local Big Brothers & Sisters chapter and the community board of Energy International Thermonuclear Research Canada.

The board of governors consists of five individuals, namely, Richard Nichols, Derek Tripp, David B. Rally, Paul Wylie and Tim Wittig. The board's mandate is to identify and establish procedures for resolving situations where there exists a conflict or potential conflict between the interests of the manager and mortgage broker, and the interests of the trust unitholders. Some of the roles of the board include, approving every material contract, review portfolio performance, appoint auditors, etc.

We believe that the board of a company should include independent or unrelated directors who are free of any relationships or business that could materially interfere with the director's ability to act in the best interest of the company. Although there is only one independent director on the company's board, the non-independent directors combined, own 3.3% of the outstanding units (as of September 2013). The trust units purchased by the directors were at a price of $10 per unit (the same price as investors).

Mortgage Lending Market

The private mortgage lending market is a highly competitive market. The currently low interest rate environment has been attracting a lot of investors to higher yield opportunities, such as Mortgage Investment Corporations. Although the structure of the trust is slightly different from MICs, they have very similar business models.

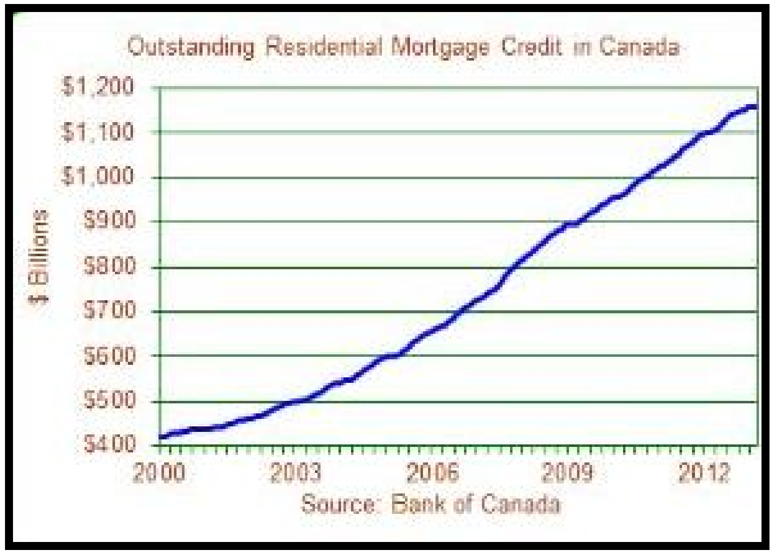
Canada Mortgage Housing Corporation's recent removal of insurance for home equity loans, and tighter lending policies by the banks, have resulted in an increasing number of homeowners seeking loans from private lenders.

The Canadian Association of Accredited Mortgage Professionals *(CAAMP)* estimated that private mortgage companies, and other private lenders, accounted for less than 3% of mortgage funding in 2012. **CAAMP estimated that, in 2012, 8% of homeowners used their home equity to borrow money, with a total borrowed amount of $39 billion.** The top five uses of funds were (Source: CAAMP):

- Renovations: $17.5 billion
- Purchases (including education**):** $8.6 billion
- Investments: $5.6 billion
- Debt consolidation and repayment: $4.7 billion

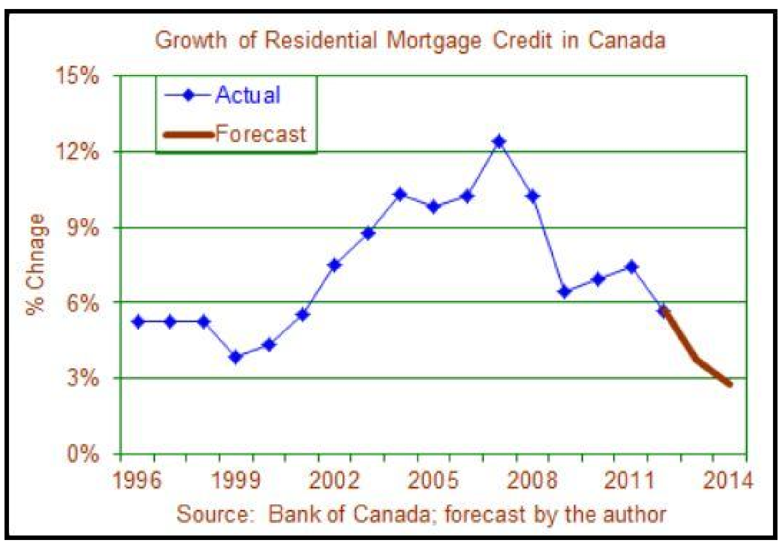
- Others**:** $2.5 billion

The following chart shows the Canadian residential mortgage market size from 2000 to 2012.



Source: CAAMP

The chart below displays the annual YOY growth in the mortgage market.



Source: CAAMP

In 2012, the mortgage market expanded by just under 6.0%. The forecast is that the market will continue to expand, but at a decreasing rate. The anticipated growth in 2013 was 4.5-5%, followed by 3% in 2014 (Source: CAAMP).

Current Portfolio

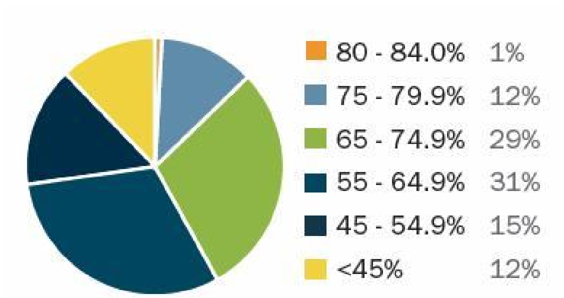
The short-term structure of the trust's mortgages make it so their income is minimally affected by home prices and interest rates in the short term. These factors would normally be a significant concern with traditional mortgage lenders. The term of a loan for the trust is 12 - 24 months, allowing them to re-price interest rates almost annually. The trust also has a low LTV of 58%. There would have to be a significant one year shift in home prices to cause the LTV to rise to levels where the underlying property was valued at less than the mortgage. **However, in the long term, real estate prices will impact deal flow to Capital Direct.** Real estate prices will affect the amount of mortgage volume, sales activity. and impact real estate starts and development. If home prices decline, people will have less collateral to borrow with.

As of September 2013, the trust's portfolio size was about $33 million, with 365 properties across British Columbia, Alberta, and Ontario, with a duration of up to 24 months (44% have less than 12 months maturity) – the average term is 12.1 months.

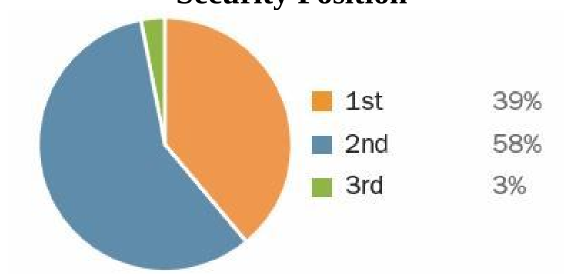
The charts below outline the trust portfolio's current distribution of mortgages by province, and loan-to-value (LTV). Approximately 50% of the portfolio is secured by properties in BC. According to management, a majority of the 365 properties are within a 90 km radius of metropolitan areas – **properties close to metropolitan areas, we believe, are less vulnerable to economic downturns.**

Prov	#Loans	Fair Value	%Portfolio
Atlantic	3	$194,561	0.60%
AB	57	$5,908,247	18.28%
BC	178	$16,060,019	49.70%
ON	127	$10,149,689	31.41%
TOTAL	365	$32,312,516	100.00%

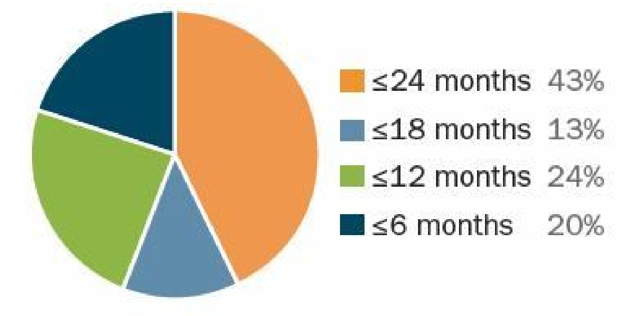
LTV



Security Position



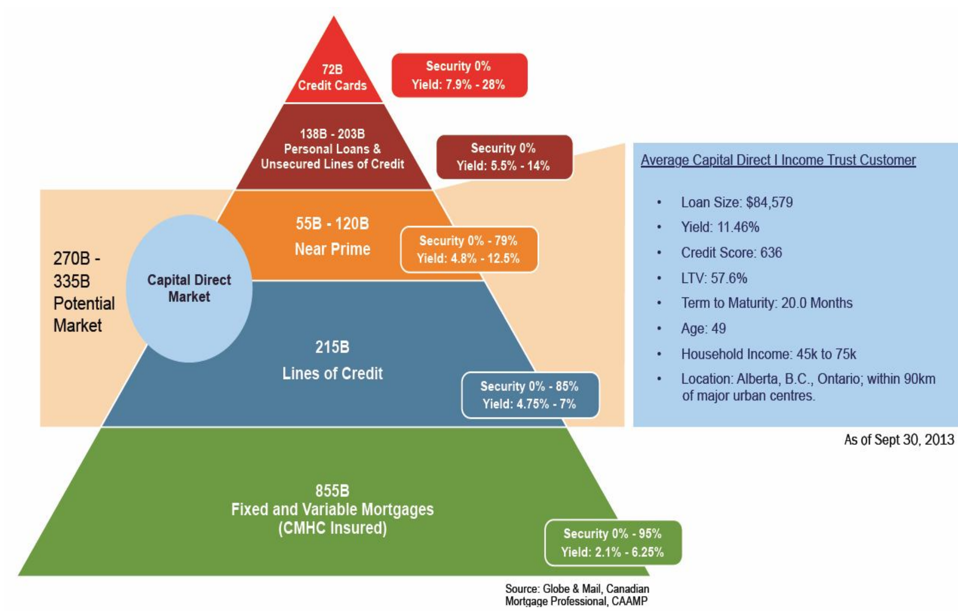
Term to Maturity



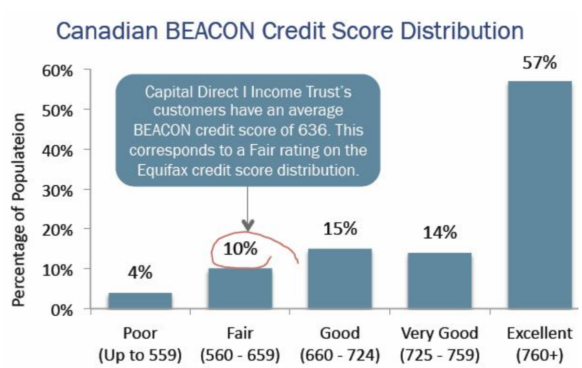
Source: Capital Direct

The average LTV is currently at 57.6%. First mortgages accounted for 39% (up from 29% since our previous report). Second mortgages have remained flat at 59%. Third mortgages dropped from 11% to 3%. **We were pleased to see that the trust has maintained its weighted LTV in the 55% to 60% range.**

The following chart gives a snapshot of a typical Capital Direct borrower's profile.

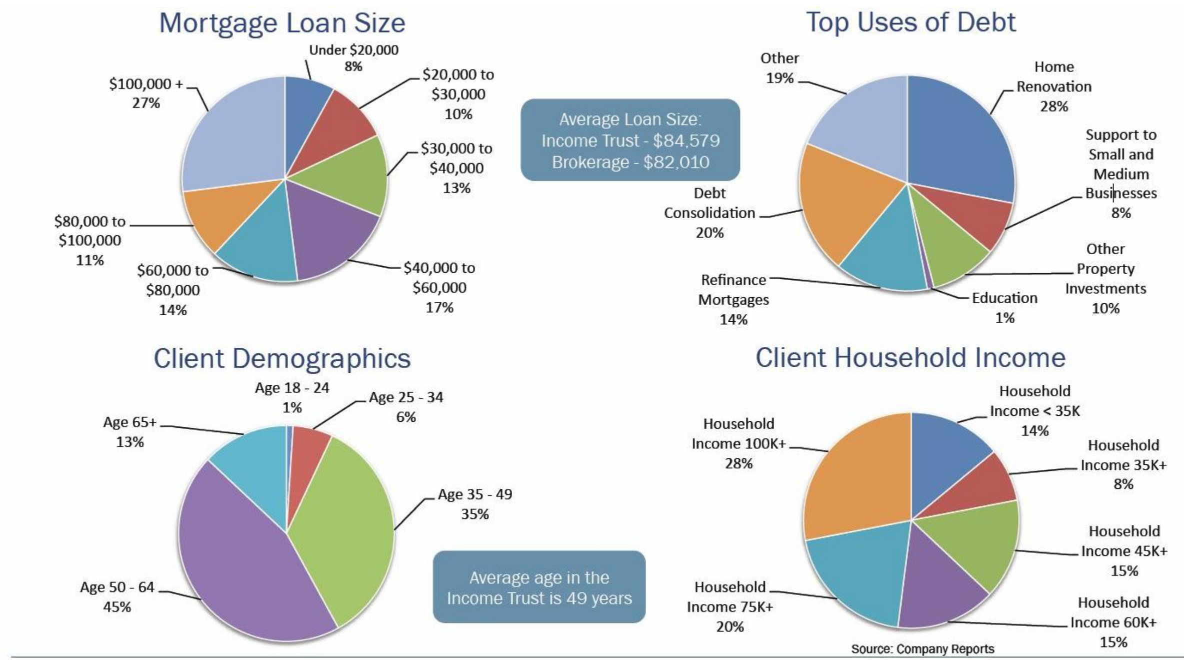


Source: Capital Direct



Source: Capital Direct

As mentioned earlier, 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.



Source: Capital Direct

Investment Criteria

As per management, typically, 33% of customers renew at end of their terms. Approximately 12% refinance prior to maturity.

The investment criteria for the selection of mortgage investments in the trust is summarized below:

- The mortgages will primarily be on residential property situated within Canada. Once the trust's assets reach $10 million (already achieved), 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 co-invest with a third party(ies) in a mortgage, but has never done so in the past.
- The trust may invest in mortgages with any length of 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 the greater of $1.0 million and 40% of the book value of the trust mortgage portfolio, and at an interest less than the interest rate charged, or yield earned, by the trust's overall mortgage portfolio.
- The trust may participate in mortgages on a syndication basis, subject to approval by the credit committee of the investment amount, and the proposed syndication partners.
- Management uses independent property appraisals when evaluating loan applications.

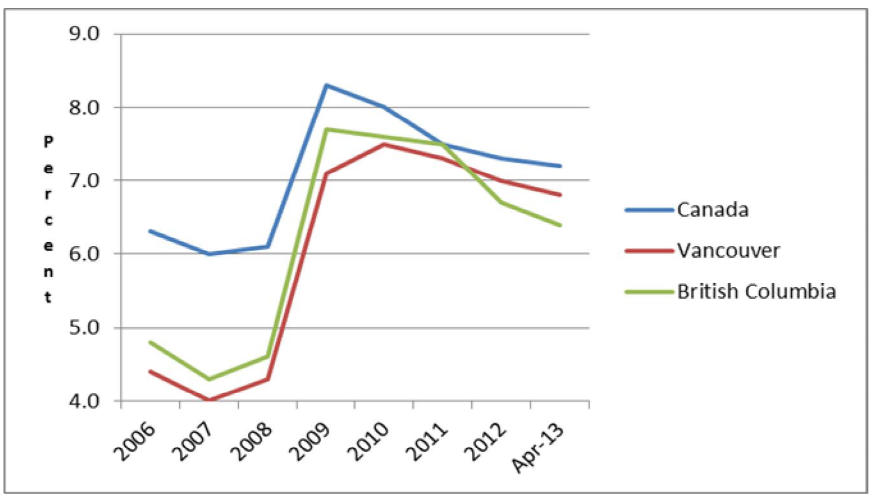
GDP

As BC and AB account for 68% of the portfolio at this time, the following section outlines our outlook on the residential market in these two provinces.

Unemployment

The GDP of Greater Vancouver is forecasted to grow at 3% annually over the next 4 years (Source: Conference Board of Canada). BC's growth is expected to be 2.6% in 2014 (BCREA).

The unemployment rate for the month ended April 2013, was 6.8% for the Vancouver metropolitan area, and 6.4% for BC, compared to the national rate of 7.2%. We are expecting the unemployment rate to decrease in 2014 as the economy strengthens.



Source: Statistics Canada

Population

One of the main drivers of housing demand is population growth; the higher the population growth, the more the demand for housing units and mortgages. **Over the period 2006-2011, the population of Greater Vancouver increased by 9.3%, outpacing the national growth rate of 5.9%.** Interprovincial migration and immigration are fueling the higher population growth, as compared to the Canadian average. The following shows YOY growth in population from 2010. Alberta's growth was well above the national average, while BC experienced relatively slower growth.

FRC Fundamental Research Corp.

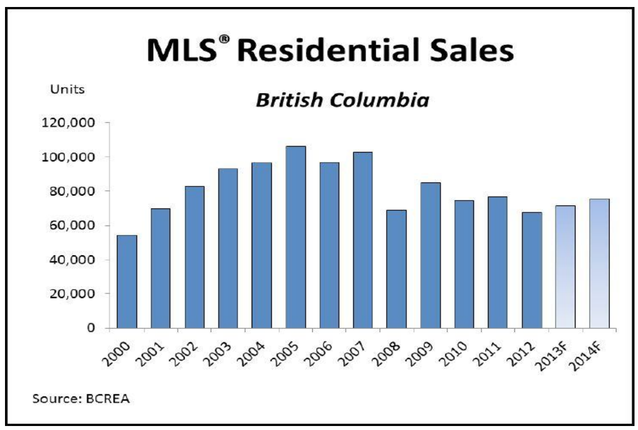
	2010	2011	2012	2013	Average (2010 - 2013)
Alberta	1.45%	1.54%	2.60%	3.51%	2.28%
Manitoba	1.02%	1.05%	1.32%	1.20%	1.15%
Ontario	1.06%	0.98%	1.12%	0.94%	1.02%
Quebec	1.10%	0.99%	0.95%	0.88%	0.98%
British Columbia	1.25%	0.74%	0.98%	0.85%	0.96%
Canada	1.12%	0.99%	1.20%	1.16%	1.12%

Source: Statistics Canada

Net international migration to both Alberta and British Columbia is set to be on the rise over the next few years. BC is third, and Alberta is fourth, in Canada, for international migration behind Quebec and Ontario.

Housing

Sales activity slowed in BC in 2012, but is forecasted to recover in the short term (see chart below). BCREA estimates 3.9% growth in sales for 2013, and 6.1% in 2014. The average home price is expected to increase by 2.2% 2014.



Vancouver experienced a substantial sales activity decline of 22.7% in 2012, but is expected to have increased by 6.9% in 2013, and 8.5% in 2014 (Source: BCREA). Home prices are expected to increase by 1.6% in 2014.

The table below summarizes the key housing market indicators for Alberta:

	2011	2012	2013(E)	2014(E)
GDP (Percentage Change)	5.1	3	2.2	2.8
Employment (Percentage Change)	3.8	2.7	1.8	1.8
Unemployment (%)	5.5	4.6	4.6	4.6
Net Immigration	42,673	85,978	59,600	58,400
Housing Starts (Percentage Change)	25,704 (-5.1)	33,396 (29.9)	32700 (-2.1)	33,100 (1.2)
Residential Resales (Percentage Change)	53,756 (8.1)	60,369 (12.3)	61,600 (2.0)	63,300 (2.8)
Average Residential Resale Price (Percentage Change)	$353,394 (0.3)	$363,208 (2.8)	$347,000 (3.0)	$381,900 (2.1)

* Residential - Single and Multi-Family Units

Source: CMHC (Q2-2013)

Key highlights of the above table are presented below:

- Alberta's **economic growth** will remain above the national average, as **real GDP** is forecasted to rise by 2.8% in 2014, compared to the national average of 2.4%.
- Residential vacancy rates dropped in 2012, primarily because of a record rate of **net immigration** of 85,978 people. Going forward, due to increasing international migration, a net inflow of 59,600, and 58,400 people, during 2013, and 2014, respectively, is expected.
- In Q1-2013, average weekly earnings in Alberta surged 6% YOY. Also, the **employment situation** is expected to remain strong, at least for the next 2 years. Employment growth is projected at 1.8% p.a., which is higher than national average of 1.3%, for both 2013, and 2014.
- **Housing starts** experienced strong growth of about 30%YOY in 2012.
- The average residential resale price is expected to increase by 2.1% in 2014.

Overall, we believe the economic indicators are strong enough to keep the residential market healthy in BC and AB.

Structure of the Offering

The fund is structured as an income trust. The fund currently qualifies, and intends to remain qualified, as a registered investment, and eligible for deferred plans, such as LIF, RRSP, TFSA, RESP, etc. The trust's structure is 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 major differences between the two structures are - a MIC is required to hold at least 50% of its holdings in residential mortgages and cash, whereas a mutual fund trust does not have such a restriction.

The trust will be managed by the manager, Capital Direct Management Ltd. **The manager will be entitled to a share of the profits as well as a management fee.** Details of the profit sharing are below:

- 80% of the aggregate of net income and net realized capital gains will be paid to the unitholders on a quarterly basis. **Since Q4-2008, management has handed out 90% of the net income to investors.** Note that there is no guarantee that management will maintain the percentage at 90%.
- The remaining 20% of the aggregate of net income, and net realized capital gains, will be paid to the manager.

Typically, MICs, or residential income trusts, incorporate a hurdle rate (preferred return) for investors, after which management shares in profits. We would have liked to see a hurdle rate for this structure as well.

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). If redeeming within the first 5 years, the following redemption schedule applies:

- If notice of 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.

The following is a list of the fees associated with the offering:

- **2.0% annual management fee.** The management fee is paid monthly in arrears at an annual rate of 2% of the net asset value. This fee is in line with average; the range on similar offerings is 1% - 3%. The NAV is calculated by management every quarter.

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

The trust's financials are audited by Johnsen Archer LLP. Johnsen Archer LLP is a Chartered Accountant firm with over 25 years of experience.

Financials

The following table shows a summary of the income statements since inception.

Income Statement	2007 (9M)	2008	2009	2010	2011	2012	2013 (9M)
Revenues							
Interest Income	$59,318	$337,521	$501,656	$702,948	$1,154,458	$1,584,171	$1,688,951
Other Income	2,908	32,125	36,100	72,312	72,792	106,324	$193,710
	$62,226	**$369,646**	**$537,756**	**$775,260**	**$1,227,250**	**$1,690,495**	**$1,882,661**
Expenses							
Audit Fees	2,240	10,000	22,000	40,000	67,275	60,300	$88,908
Bank Charges	826	4,316	1,975	8,048	27,923	30,510	$21,030
Interest on Loan Payable	27,739	70,983	51,773	31,063	84,727	131,177	$220,226
Legal Fees		8,532	5,892	18,681	64,287	72,464	$70,195
Management Fees	2,257	24,539	54,797	97,621	145,619	227,121	$231,416
Provision for Loan Losses	7,963	8,641	14,152	15,380	29,976	91,085	$151,195
Trustee Fees		11,612	10,368	11,852	12,294	16,517	$15,094
	41,025	**138,623**	**160,957**	**222,645**	**432,101**	**629,174**	**798,065**
Net Income	**$21,201**	**$231,023**	**$376,799**	**$552,615**	**$795,149**	**$1,061,321**	**$1,084,596**
Net Asset Value	10.0	10.00	10.00	10.00	10.00	10.00	10.00
Units Outstanding	66,801	292,514	489,475	725,046	1,070,923	1,442,321	1,839,358
Distributions							
Investors	16,961	192,478	339,112	497,354	715,634	955,189	976,136
Management	4,240	38,545	37,687	55,261	79,515	106,132	108,459
Investors' Share	80.0%	83.3%	90.0%	90.0%	90.0%	90.0%	90.0%

: 2008 - the manager waived 50% of their profit share in Q4-2008 - this is the reason why investors' share is 83.3% in 2008

YE – December 31st

Revenues grew from $0.06 million in 2007, to $1.69 million in 2012. Net Income grew from $0.02 million in 2007, to $1.06 million in 2012.

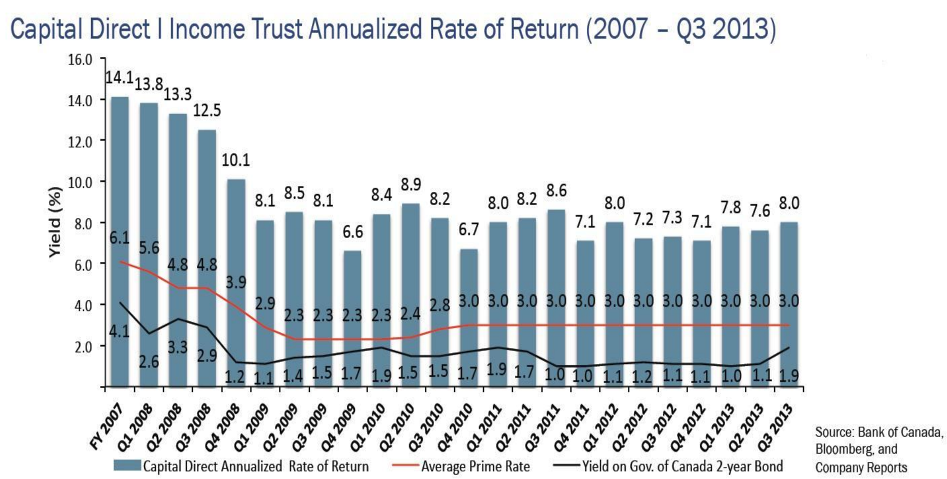
Interest + Other income as a percentage of mortgage receivables dropped from a high of 14.70% in 2008, to 9.71% in the first nine month of 2013. The dividend yield (dividends as a percentage of invested capital) also dropped accordingly from 10.71% to 7.93% - the drop in yields are in line with the drop in lending rates post-recession.

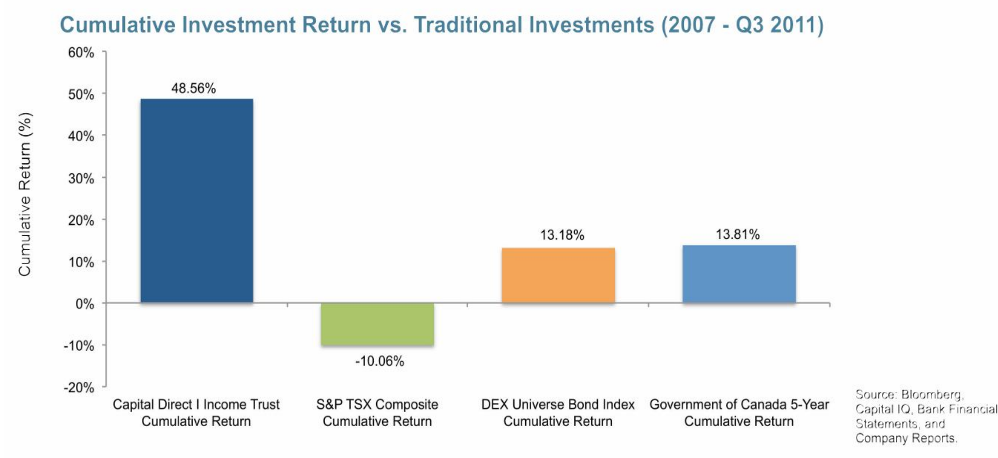
% of Mortgage Receivable	2007 (9M)	2008	2009	2010	2011	2012	2013 (9M)*	Average (2008 - 9M 2013)
Interest Income	3.48%	13.42%	11.49%	10.12%	10.83%	9.71%	8.71%	10.72%
Other Income	0.17%	1.28%	0.83%	1.04%	0.68%	0.65%	1.00%	0.91%
Interest Income + Others	**3.65%**	**14.70%**	**12.32%**	**11.16%**	**11.51%**	**10.36%**	**9.71%**	11.63%
Less:								
Management Fee	-0.13%	-0.98%	-1.25%	-1.41%	-1.37%	-1.39%	-1.19%	-1.26%
G&A Expenses	-0.18%	-1.37%	-0.92%	-1.13%	-1.61%	-1.10%	-1.01%	-1.19%
Provision for Loan Losses	-0.47%	-0.34%	-0.32%	-0.22%	-0.28%	-0.56%	-0.78%	-0.42%
Interest	-1.63%	-2.82%	-1.19%	-0.45%	-0.79%	-0.80%	-1.14%	-1.20%
Net	**1.24%**	**9.19%**	**8.63%**	**7.96%**	**7.46%**	**6.51%**	**5.60%**	7.56%
Investors' Returns (% of Invested Capital)	2.54%	10.71%	8.67%	8.19%	7.97%	7.60%	7.93%	8.51%
2-year GOC	4.19%	2.62%	1.27%	1.53%	1.34%	1.11%	1.11%	1.50%

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.

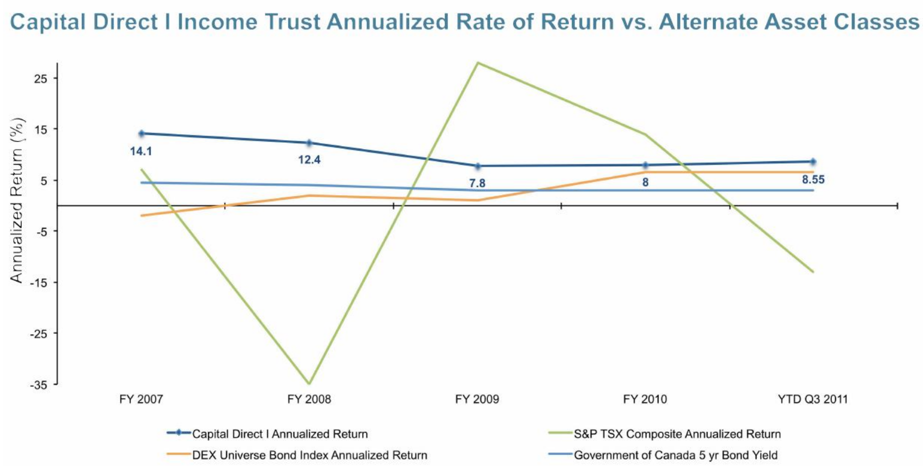
The above table (our estimates) shows that the last five year average yield for investors was 8.5%. Management's calculation is 8.98% p.a.

The following charts show Capital Direct's performance calculations.





Source: Company



Source: Company

Annual provision for loan losses has ranged between 0.22% and 0.78% of the mortgage receivables. The following table shows the actual losses in the portfolio. **Management states that actual historic losses have totaled just $24k.** We believe this is accurate based on our review of the financial statements.

	2007 (9M)	2008	2009	2010	2011	2012	2013 (9M)
Actual Losses	-	84	3	248	66	19,832	4,086
Actual Losses (% of mortgage receivable)	0.000%	0.004%	0.000%	0.007%	0.002%	0.360%	0.070%
Distributions	$16,961	$192,478	$339,112	$497,354	$715,634	$955,189	$976,136
Reinvested	$0	$105,133	$151,708	$232,843	$330,497	$495,024	$485,926
Reinvested (as a % of Distributions)	0%	55%	45%	47%	46%	52%	50%
Redemptions	$0	$62,543	$217,016	$132,798	$10,000	$588,593	$636,516
Redemption (% of invested capital)	0%	3%	6%	2%	0%	5%	4%

Source: FRC and Management

Investors have reinvested about 45% - 55% of the annual distributions so far – which is extremely encouraging. Annual redemptions have ranged between 0% and 6% of invested capital. They key point to note here is that management was able to redeem $0.59 million in 2012, and $0.64 million in the first nine months of 2013, indicating management's ability and willingness to meet redemption requests. According to management, they have never declined any redemption request to date.

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

Balance Sheet	2007	2008	2009	2010	2011	2012	Q3-2013
Assets							
Cash	$75,327	$698,744	$215,007	$121,264	$288,331	$187,552	$621,184
Accounts Receivable			2,333		119,180		367,322
Prepaid Expense				7,500			5,000
Assets held for sale						15,949	
Mortgage Invenstment (net)	1,704,378	3,324,557	5,408,042	8,479,813	12,837,727	19,781,725	31,898,074
	$1,779,705	**$4,023,301**	**$5,625,382**	**$8,608,577**	**$13,245,238**	**$19,985,226**	**$32,891,580**
Liabilities							
Loan Payable	$1,000,000	$1,000,000	$600,000	$1,162,682	$2,183,086	5,083,066	13,904,878
Accounts Payable & Accured Liabilities	111,695	98,161	130,700	195,435	352,925	478,948	593,118
	1,111,695	1,098,161	730,700	1,358,117	2,536,011	5,562,014	14,497,996
Net Asset	668,010	2,925,140	4,894,752	7,250,460	10,709,227	14,423,212	18,393,583
SE + Liabilities	**$1,779,705**	**$4,023,301**	**$5,625,452**	**$8,608,577**	**$13,245,238**	**19,985,226**	**32,891,579**
Debt to Capital	60%	25%	11%	14%	17%	26%	43%
Debt as a % of Mortgage Outstanding	59%	30%	11%	14%	17%	26%	44%
Interest Coverage Ratio	1.8	4.4	8.5	19.2	10.5	9.2	6.0

Total loans issued increased from $1.70 million at the end of 2007, to $31.90 million at the end of Q3-2013 (September 30, 2013). 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 Q3 was $0.62 million.

Line of credit – The trust has an $18 million (prime + 0.75%) line of credit with Canadian Western Bank. The trust cannot withdraw more than 40% of the book value of the outstanding mortgages. As of September 30, 2013, $13.90 million was withdrawn, reflecting debt to capital of 43%, and debt as a percentage of outstanding mortgages of 44%. The interest coverage ratio of the trust is fairly strong, and it is good to see that operating profits generated by the trust can easily cover its annual debt obligation. **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.**

Expected Returns

The following table shows the expected yield, assuming 25% debt to capital. The assumptions used below were based on historic averages.

Capital Raised (gross)	**$100.00**
Sales Commission	$0.00
Debt used	$33.00
Debt to Capital	25%
Total available capital	$133.00
Percentage of available capital deployed	98.50%
Capital Deployed	$131.01

Interest + Other Revenue (10% p.a.)	**$13.10**
Management Fee (2% p.a. of NAV)	-$2.00
Other Expenses (1.2% of Capital Deployed)	-$1.57
Defaults (0.4% of Capital Deployed)	-$0.52
Interest expense (prime + 0.75%)	-$1.24
Net	**$7.77**
Investors' share (80%)	6.99%

Sensitivity Analysis

The sensitivity of expected yields to various factors is shown below:

Annual revenues % of mortgage receivable	8%	9%	**10%**	11%	12%
Investors' Yield	4.63%	5.81%	**6.99%**	8.17%	9.35%
Debt to Capital	0%	15%	**25%**	35%	50%
Investors' Yield	6.27%	6.36%	**6.99%**	7.85%	9.72%
% of Capital Deployed	85%	90%	95.00%	**98.50%**	100%
Investors' Yield	5.63%	6.14%	6.64%	**6.99%**	7.14%
Other Expenses (as a % of mortgage receivable)	0.50%	**1.20%**	1.50%	2%	2.50%
Investors' Yield	7.82%	**6.99%**	6.64%	6.05%	5.46%
Defaults (% of mortgage receivable)	0	**0.40%**	1%	2%	3%
Investors' Yield	7.46%	**6.99%**	6.28%	5.10%	3.92%

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.
- There are redemption fees for the first five years.
- Loans are primarily interest only loans.
- The fund has the ability to use leverage (the current debt to capital is 43%), which would increase the exposure of the fund to negative events.
- The fund can invest in second and third mortgages which carry higher risk.
- Annual redemptions may be limited to 10% of the total invested capital, and may not be paid in cash.

Conclusion

Based on our review of the offering, and management's track record, we have raised our overall rating to 2 (from 2-), and lowered our risk rating to 2 (from 3).

FRC Rating	
Yield (5-year average)	8.98% p.a.
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	24%	Risk - 2	2%
Rating - 3	51%	Risk - 3	30%
Rating - 4	5%	Risk - 4	45%
Rating - 5	5%	Risk - 5	5%
Rating - 6	2%	Suspended	18%
Rating - 7	0%		
Suspended	14%		

Disclaimers and Disclosure

The opinions expressed in this report are the true opinions of the analyst about this company and industry. Any "forward looking statements" are our best estimates and opinions based upon information that was provided and that we believe to be correct, but we have not independently verified with respect to truth or correctness. There is no guarantee that our forecasts will materialize. Actual results will likely vary. The analyst and Fundamental Research Corp. "FRC" does not own any shares of the subject company, does not make a market or offer shares for sale of the subject company, and does not have any investment banking business with the subject company. Fees have been paid by the issuer to FRC to issue this report. The purpose of the fee is to subsidize the high costs of research and monitoring. FRC takes steps to ensure independence including setting fees in advance and utilizing analysts who must abide by CFA Institute Code of Ethics and Standards of Professional Conduct. Additionally, analysts may not trade in any security under coverage. Our full editorial control of all research, timing of release of the reports, and release of liability for negative reports are protected contractually. Distribution procedure: our reports are distributed first to our web-based subscribers on the date shown on this report then made available to delayed access users through various other channels for a limited time. The performance of FRC's research is ranked by Investars. Full rankings and are available at www.investars.com.

To subscribe for real-time access to research, visit http://www.researchfrc.com/subscription.htm for subscription options. This report contains "forward looking" statements. Forward-looking statements regarding the Company and/or stock's performance inherently involve risks and uncertainties that could cause actual results to differ from such forward-looking statements. Factors that would cause or contribute to such differences include, but are not limited to, continued acceptance of the Company's products/services in the marketplace; acceptance in the marketplace of the Company's new product lines/services; competitive factors; new product/service introductions by others; technological changes; dependence on suppliers; systematic market risks and other risks discussed in the Company's periodic report filings, including interim reports, annual reports, and annual information forms filed with the various securities regulators. By making these forward looking statements, Fundamental Research Corp. and the analyst/author of this report undertakes no obligation to update these statements for revisions or changes after the date of this report. A report initiating coverage will most often be updated quarterly while a report issuing a rating may have no further or less frequent updates because the subject company is likely to be in earlier stages where nothing material may occur quarter to quarter.

Fundamental Research Corp DOES NOT MAKE ANY WARRANTIES, EXPRESSED OR IMPLIED, AS TO RESULTS TO BE OBTAINED FROM USING THIS INFORMATION AND MAKES NO EXPRESS OR IMPLIED WARRANTIES OR FITNESS FOR A PARTICULAR USE. ANYONE USING THIS REPORT ASSUMES FULL RESPONSIBILITY FOR WHATEVER RESULTS THEY OBTAIN FROM WHATEVER USE THE INFORMATION WAS PUT TO. ALWAYS TALK TO YOUR FINANCIAL ADVISOR BEFORE YOU INVEST. WHETHER A STOCK SHOULD BE INCLUDED IN A PORTFOLIO DEPENDS ON ONE'S RISK TOLERANCE, OBJECTIVES, SITUATION, RETURN ON OTHER ASSETS, ETC. ONLY YOUR INVESTMENT ADVISOR WHO KNOWS YOUR UNIQUE CIRCUMSTANCES CAN MAKE A PROPER RECOMMENDATION AS TO THE MERIT OF ANY PARTICULAR SECURITY FOR INCLUSION IN YOUR PORTFOLIO. This REPORT is solely for informative purposes and is not a solicitation or an offer to buy or sell any security. It is not intended as being a complete description of the company, industry, securities or developments referred to in the material. Any forecasts contained in this report were independently prepared unless otherwise stated, and HAVE NOT BEEN endorsed by the Management of the company which is the subject of this report. Additional information is available upon request. THIS REPORT IS COPYRIGHT. YOU MAY NOT REDISTRIBUTE THIS REPORT WITHOUT OUR PERMISSION. Please give proper credit, including citing Fundamental Research Corp and/or the analyst, when quoting information from this report.

The information contained in this report is intended to be viewed only in jurisdictions where it may be legally viewed and is not intended for use by any person or entity in any jurisdiction where such use would be contrary to local regulations or which would require any registration requirement within such jurisdiction