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Fundamental Research Corp.
Investment Analysis for Intelligent Investors

August 25, 2016

Capital Direct I Income Trust – Portfolio size surpasses $100M / Key parameters remain healthy

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

Offering Summary	
Issuer	Capital Direct I Income Trust
Date of OM	30-Apr-16
Offering	Maximum of $375M
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	Classes A and C units - penalty of 5% of NAV in year 1, decreasing by 1% every year; no penalty after year 5 / 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

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

Investment Highlights

- Capital Direct I Income Trust (“trust”, “fund”) invests primarily in first and second mortgages secured by residential properties primarily in British Columbia (BC), Ontario (ON), and Alberta (AB).
- The fund is a Mortgage Investment Entity (“MIE”) structured as an income trust which is 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 difference between the two structures is that a MIC is required to hold at least 50% of its holdings in residential mortgages and cash, whereas an income trust does not have such a restriction.
- Mortgage investments (net of provisions) totaled $113 million as of June 30, 2016, up by 110% from $54 million at the end of 2014. Despite the strong growth of the portfolio, the portfolio has maintained its key parameters and risk exposure, indicating management’s ability to efficiently grow the portfolio.
- BC accounted for 48%, and ON accounted for 37% of the portfolio as of June 30, 2016.
- We believe management’s long track record and proactive marketing campaigns give the trust a strong edge over competition.
- The return on Class A units was 8.1% in 2015, versus 7.9% in 2014. The return on Class F units was 8.6% in 2015 versus 7.4% in 2014. In 2016, the trust introduced Class C units, which are intended for investors who purchase units through investment dealers (IIROC and Exempt Market Dealers).
- We are maintaining our overall rating and the risk rating at 2. We are commencing continuous coverage on the trust effective today, implying that we will publish update reports / notes on the trust on a regular basis going forward.

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-values (“LTV”), and higher default risk, as the value of collateral decreases.
- No hurdle rate.
- There are penalties for early redemption of Class A units.
- 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, which carry higher risks. As of June 30, 2016, second and third mortgages accounted for 63% of the portfolio.

Overview

We initiated coverage on Capital Direct I Income Trust on June 12, 2012. The following table shows our rating on the trust units.

	Jun-12	Jan-14	Jan-15	Aug-16
Overall Rating	2-	2	2	2
Risk Rating	3	2	2	2

Since our previous report in January 2015, mortgage investments (net of provisions) have increased by 132%, from $48.56 million in September 2014, to $112.77 million as of June 2016. According to the most recent Offering Memorandum dated April 30, 2016, management's goal is to raise $36 million in the next 12 months.

Manager

The following section provides background on the trust and its 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. ("Capital Direct"), which was incorporated in 1997. The mortgage investments for the trust will be sourced through Capital Direct.

Capital Direct, which is owned by three partners, 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. They currently have approximately 27 employees.

Capital Direct has originated approximately $965 million in mortgages since inception in 1997, and currently originates between $100 and $125 million per year. 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 $159 million in mortgages – which includes $114 million for the trust, and the remaining $45 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 maintains a significant advertising budget, and is a well-known brand, especially in Vancouver. Their long track record and aggressive marketing campaigns, we believe, give them a strong edge over competition, and create barriers to entry for new entrants.

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 interprovincial 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.

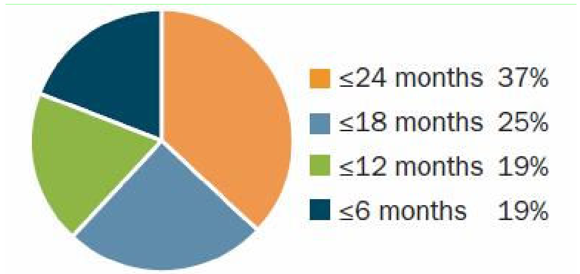
Paul Wylie - Independent member of the Board of Governors
Mr. Wylie's experience includes over 17 years with two leading financial institutions within North America. Most recently Mr. Wylie worked as a Senior Vice-President and Branch Manager with the financial institutions. Throughout his banking career, 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. Paul Wylie is an independent director. The non-independent directors owned 0.7% of the outstanding units as of December 2015. The trust units purchased by the directors were at a price of $10 per unit (the same price as investors).

	Dec-15	% of Total	Jun-15	% of Total	Jun-14	% of Total	Aug-13	% of Total
Richard F.M. Nichols	9,132	0.18%	8,600	0.23%	7,954	0.31%	7,490	0.41%
Derek R. Tripp	14,042	0.27%	13,234	0.35%	12,231	0.48%	11,517	0.63%
Tim Wittig	8,503	0.17%	34,118	0.91%	40,846	1.61%	38,460	2.10%
David Rally	5,192	0.10%	4,889	0.13%	4,522	0.18%	3,026	0.16%
Total	**36,869**	**0.72%**	**60,841**	**1.61%**	**65,554**	**2.58%**	**60,493**	**3.30%**

Current Portfolio

As of June 30, 2016, the trust had $113.67 million in mortgage investments across 1,208 properties, with a duration of up to 24 months. The average remaining term was 15.1 months as of June 30, 2015, versus 14.1 months as of September 30, 2014.



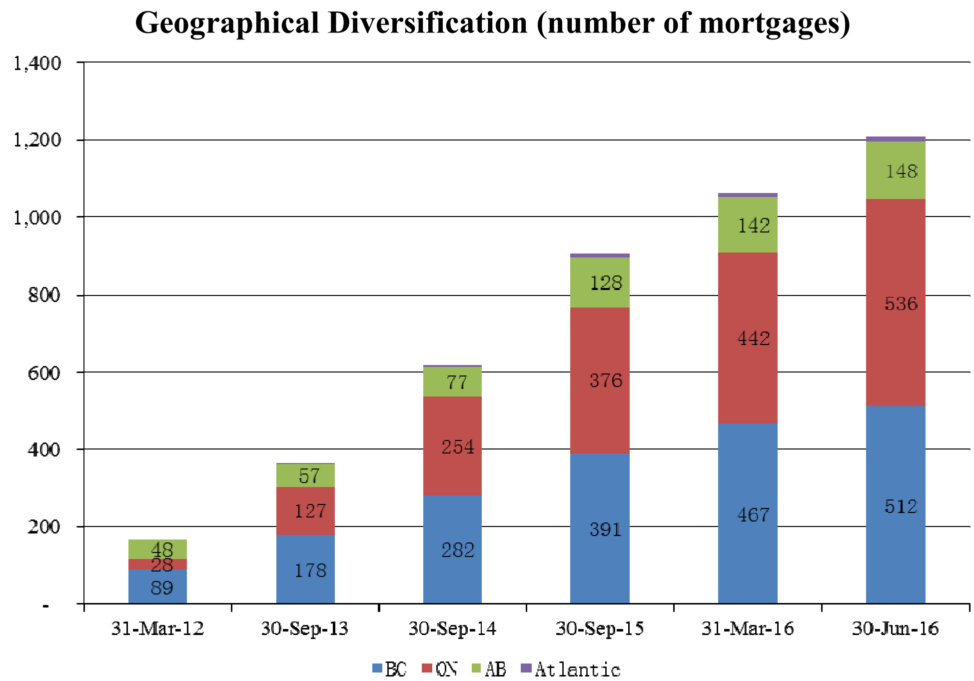
The average loan amount was $94,101 as of June 30, 2016, compared to $79,278 in September 2014. As shown in the table below, the average loan amount has been relatively stable over the past few years.

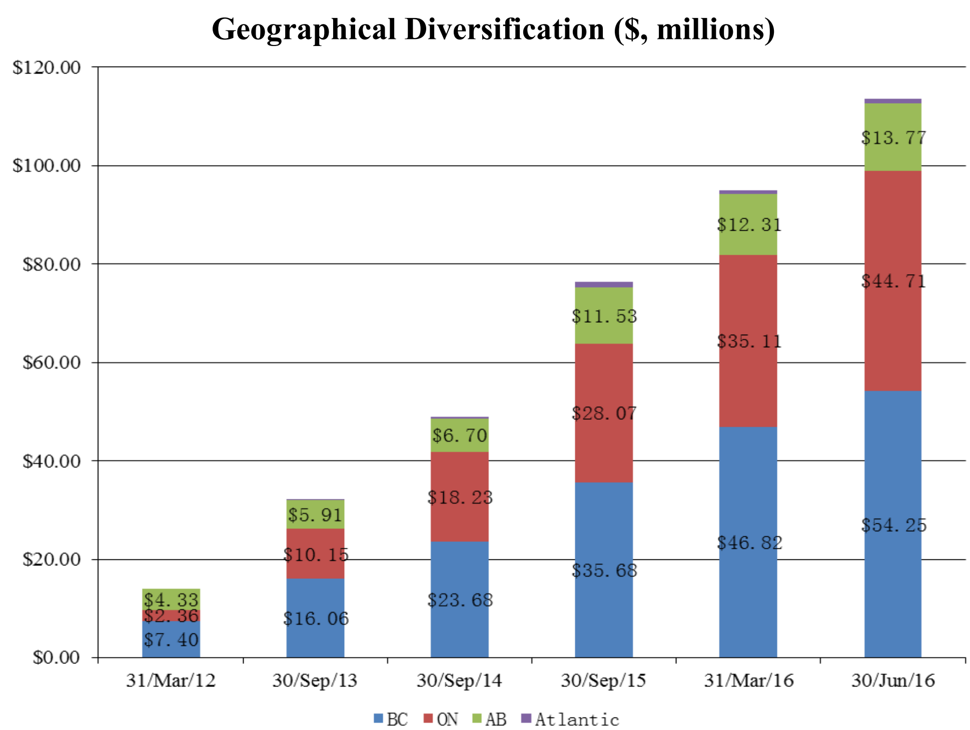
	Mar-12	Sep-13	Sep-14	Sep-15	Mar-16	Jun-16
Average Mortgage	$85,370	$88,526	$79,278	$84,278	$89,528	$94,101

Approximately 48% of the portfolio, as of June 2016, was secured by properties in B.C. Since 2012, the trust had been increasing its exposure to Ontario, while reducing its exposure to Alberta (see table below), 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.

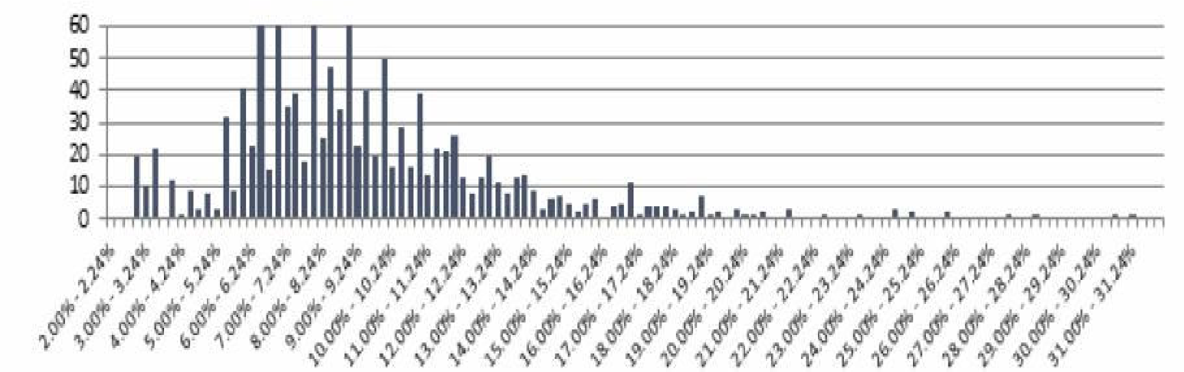
	Mar-12	Sep-13	Sep-14	Sep-15	Mar-16	Jun-16
BC	52.5%	49.7%	48.3%	46.7%	49.2%	47.7%
ON	16.8%	31.4%	37.2%	36.8%	36.9%	39.3%
AB	30.7%	18.3%	13.7%	15.1%	13.0%	12.1%
Atlantic	0.0%	0.6%	0.8%	1.4%	0.9%	0.8%
	100.0%	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Management's primary focus is on single-family residential mortgages. According to management, a majority of the properties are within a 90 km radius of metropolitan areas. Properties close to metropolitan areas, we believe, are less vulnerable to economic downturns. The table below outlines the trust portfolio's distribution of mortgages by province.

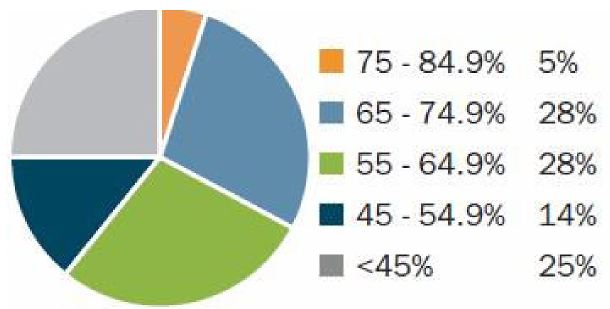




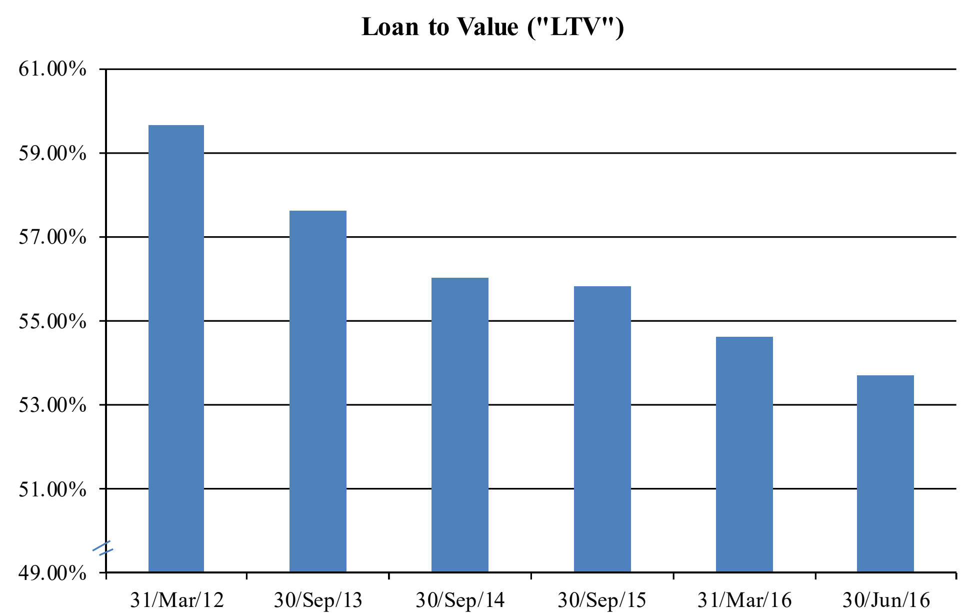
The following chart shows the interest rates charged to the borrowers. The average rate, as of June 30, 2016, was 8.42%, versus 9.77% p.a. as of September 2014.



The portfolio's loan to value ("LTV") dropped slightly YOY from 56.0% in September 2014, to 53.7% by June 2016. Approximately 5% of the mortgages have LTV higher than 75%.



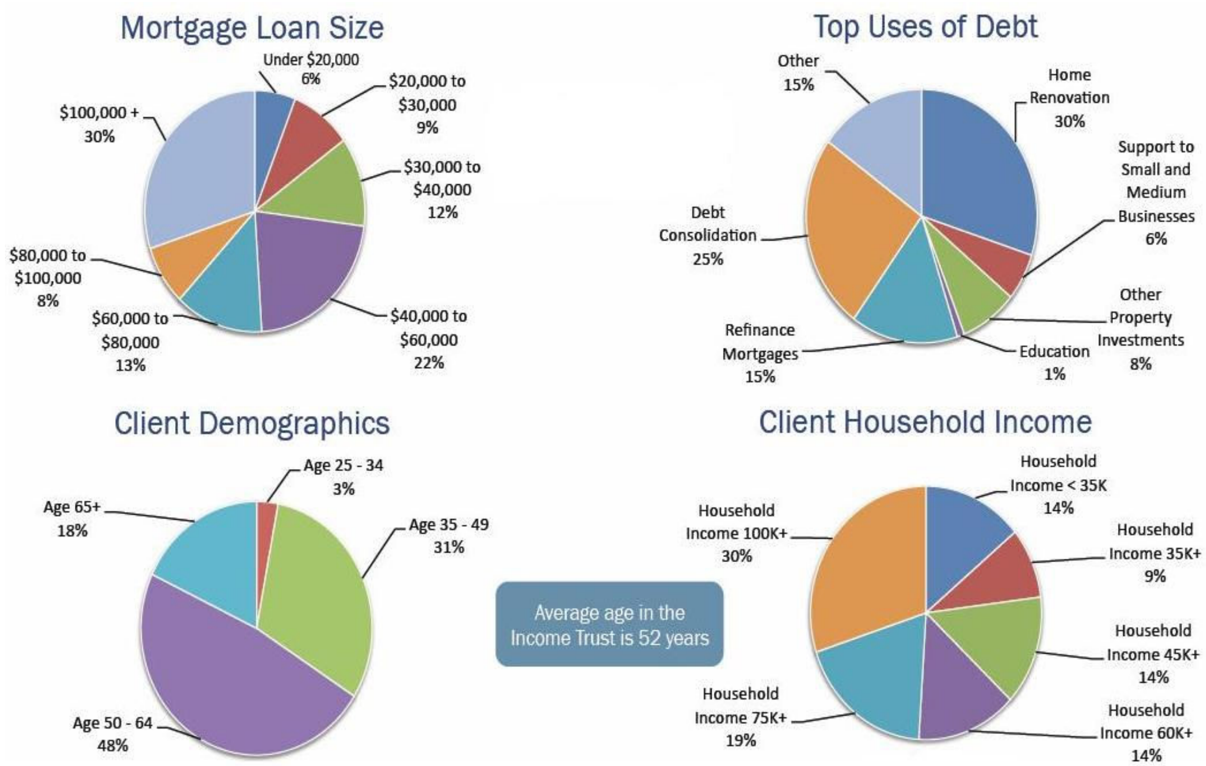
As shown in the following chart, the portfolio's LTV has been decreasing since 2012.



First mortgages accounted for 37% (versus 36% as of September 2014). Second mortgages were at 59% versus 61% as of September 2014.

	Mar-12	Sep-13	Sep-14	Mar-16	Jun-16
1st	29%	39%	36%	37%	37%
2nd	60%	58%	61%	59%	59%
3rd	11%	3%	3%	4%	4%
	100%	**100%**	**100%**	**100%**	**100%**

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

The following table shows the profile of an average borrower / mortgage as of June 2016 versus June 2012.

Profile of average mortgage held	Jun-12	Jun-16
Loan size	$86,502	$94,320
Yield (p.a.)	10.40%	8.42%
Credit score	645	610
LTV	59%	53.70%
Term to maturity	17 months	15 months
Age	46	52
Household income	$45k to $75k	$35k to $100k

Overall, we were pleased to see that the portfolio has maintained its key parameters and risk exposure despite a 132% YOY increase in mortgage investment since our last report, indicating management's ability to efficiently grow the portfolio.

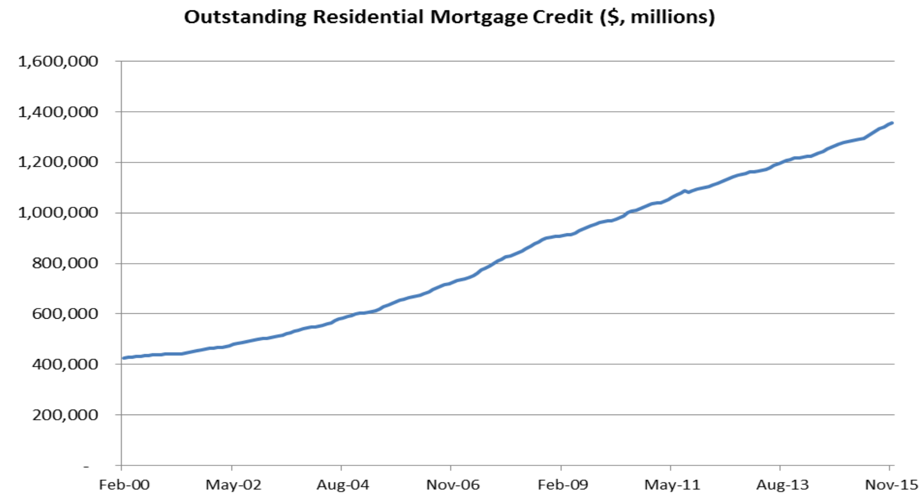
Investment Criteria

Management's investment criteria (listed below) remain 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 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 50% of the book value of the 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.

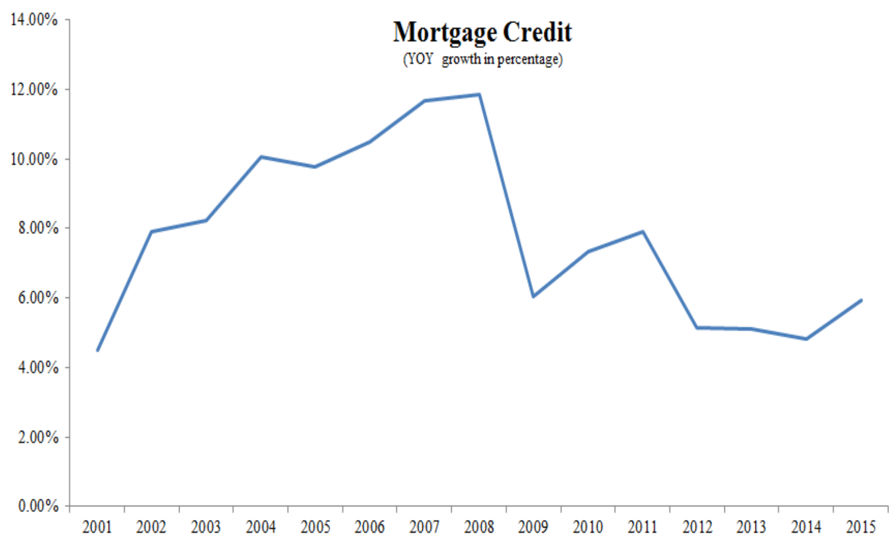
Private Lending Market

The total residential mortgage credit in Canada has increased from $0.42 trillion in 2000, to $1.36 trillion by November 2015, reflecting a compounded annual growth rate ("CAGR") of 7.8%.



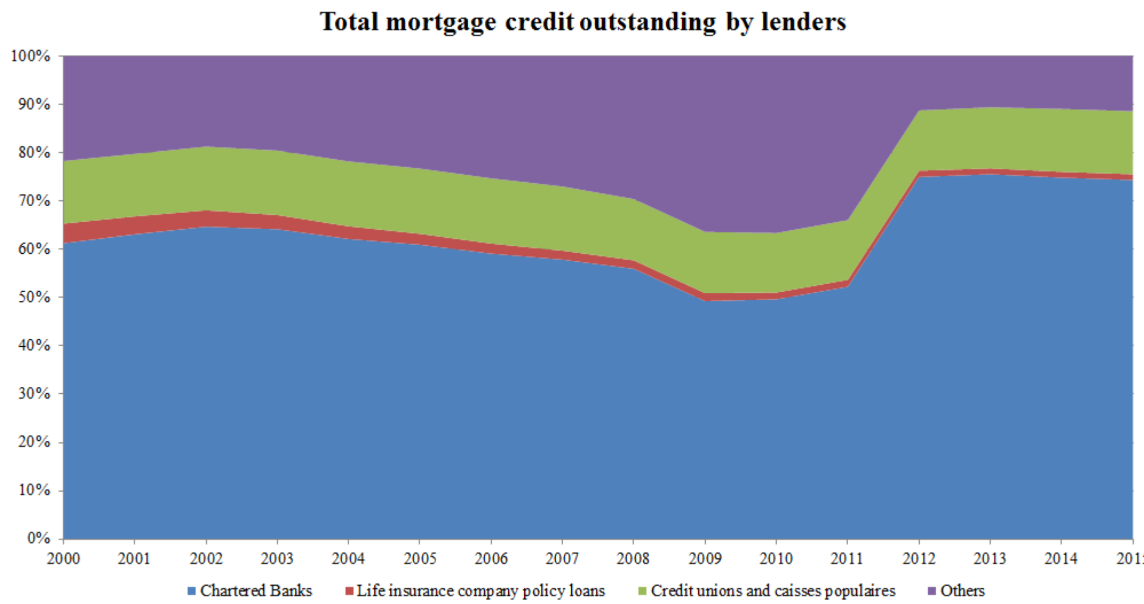
Data Source: Statistics Canada

The YOY growth in credit has declined significantly from pre-recession years, but has been increasing in recent years due to the low interest rate environment.



Data Source: Statistics Canada

Chartered banks, credit unions, life insurance companies, pension funds and related entities accounted for 93.34% of total mortgage credit as of August 2015. The remainingg loans (approximately $89 billion) were from trust, mortgage companies, and non-depository credit intermediaries.



In a study we conducted for the CMHC in 2015, we built a database of 72 entities that operate as MIEs (such as MICs and Income Trusts) across the country through management interviews, surveys, public filings, company websites, etc. We estimate there may be 200 to 300 MIEs in the country. We estimate the total outstanding mortgages of the 72 MIEs to be approximately $6.74 billion, reflecting 0.5% of the total mortgages outstanding in Canada. Since our database includes almost all of the larger MIEs, we estimate that our study represents at least 75% of the total mortgages held by the MIE industry.

Factors contributing to increased private lending - Subsequent to the recession in 2008, there have been several changes in mortgage rules in Canada as the government began to tighten mortgages rules in an effort to further strengthen the Canadian housing finance system.

- Minimum down payment increased to at least 5% for home buyers (previously no down payment was required), and to 20% for non-owner occupied properties (investment/speculative properties).

- The maximum amortization period has been reduced to 30 years from 40 years.

- Limiting the maximum gross debt service ("GDS") ratio to 0.39x and the maximum total debt service ("TDS") ratio to 0.44x (as of December 31, 2015). GDS reflects the portion of a homeowner's gross annual income required to meet payments related to housing, such as mortgage principal and interest, property taxes, etc. TDS reflects the portion of a homeowner's gross annual income required to meet all debt payments.

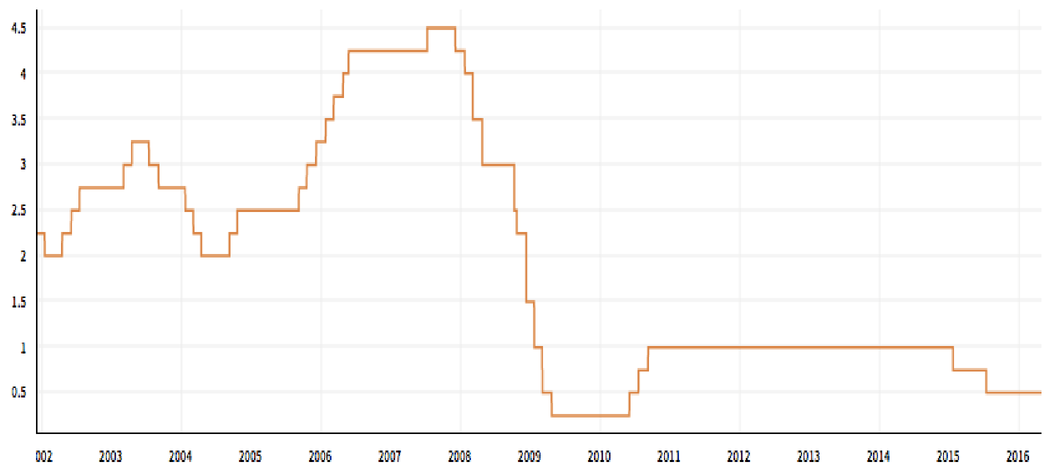
- Government-backed mortgage insurance made available to homes with a price of less than $1 million.

The tighter lending policies set by banks and conventional lenders have been encouraging more and more private lenders to enter the market.

Another factor that is contributing to increased lending is the improving unemployment rate, and the strong growth in housing prices. Data from the major banks show that there was a rise in mortgage arrears during the recession (mid-1990s and 2008-2009). The rate has been dropping since 2010, and is currently at just over 0.3% - which is highly encouraging for lenders.

Historically low interest rates are another factor that is driving lending. The following chart shows the overnight lending rate since 2002.

Overnight Lending Rate (%)

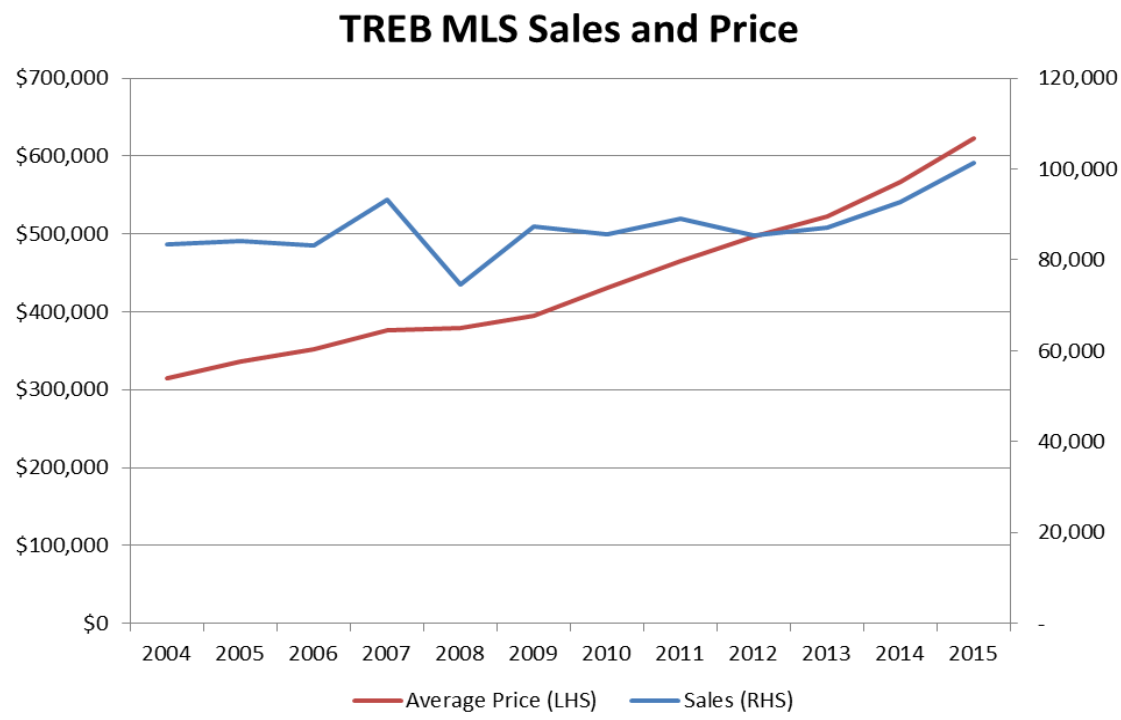


Source: Bank of Canada

The major banks currently offer one-year fixed mortgage rates at about 3% p.a. to borrowers, while rates offered by MIEs range between 5% - 15% p.a.

Toronto Real Estate Market

Although there have been uncertainties about the future of the Toronto real estate market especially due to the rapid rise in price / sales (see chart below), we believe the market is reasonably healthy, and do not expect any major drop in prices.



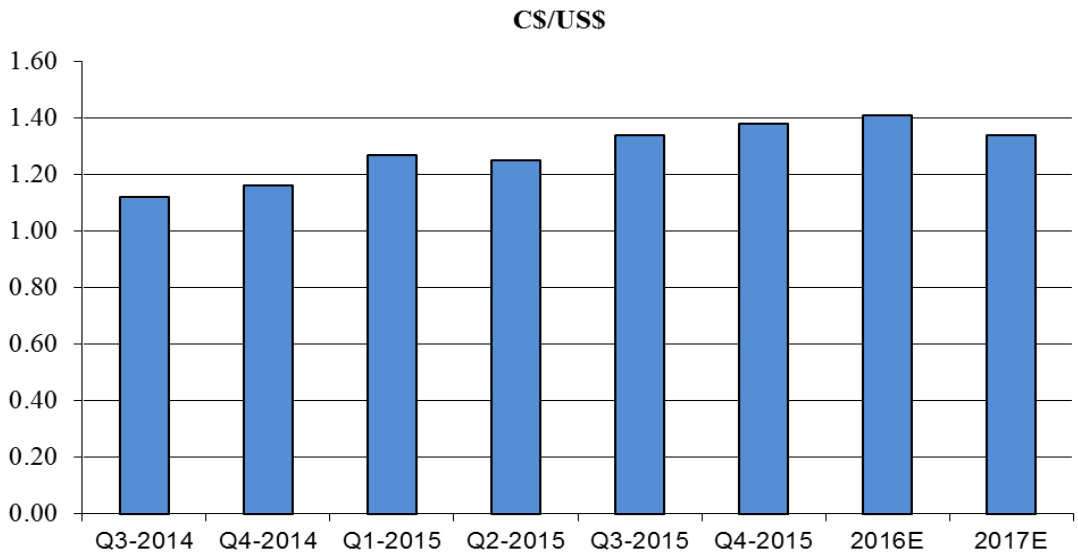
The following table, which shows the Ontario Chamber of Commerce's forecasts, indicates that population growth and unemployment rates in the Toronto Region are expected to stay healthy through 2017.

Regional Economic Summary: Toronto Region

	2013	2014	2015	2016E	2017E
Unemployment Rate	8.20%	8.00%	7.30%	6.90%	6.70%
Population (000s)	6,269	6,358	6,440	6,530	6,626
% ch.	1.4	*1.4*	*1.3*	*1.4*	*1.5*
MLS® Res. Sales	94,588	99,193	107,400	114,300	119,200
% ch.	0.9	*4.9*	*8.3*	*6.4*	*4.3*
MLS® Res. Avg. Price	529,948	573,183	625,800	680,400	730,100
% ch.	5.1	*8.2*	*9.2*	*8.7*	*7.3*
Residential Permits (Units)	40,256	35,136	42,000	46,500	48,500
% ch.	3.6	*-12.7*	*19.5*	*10.7*	*4.3*

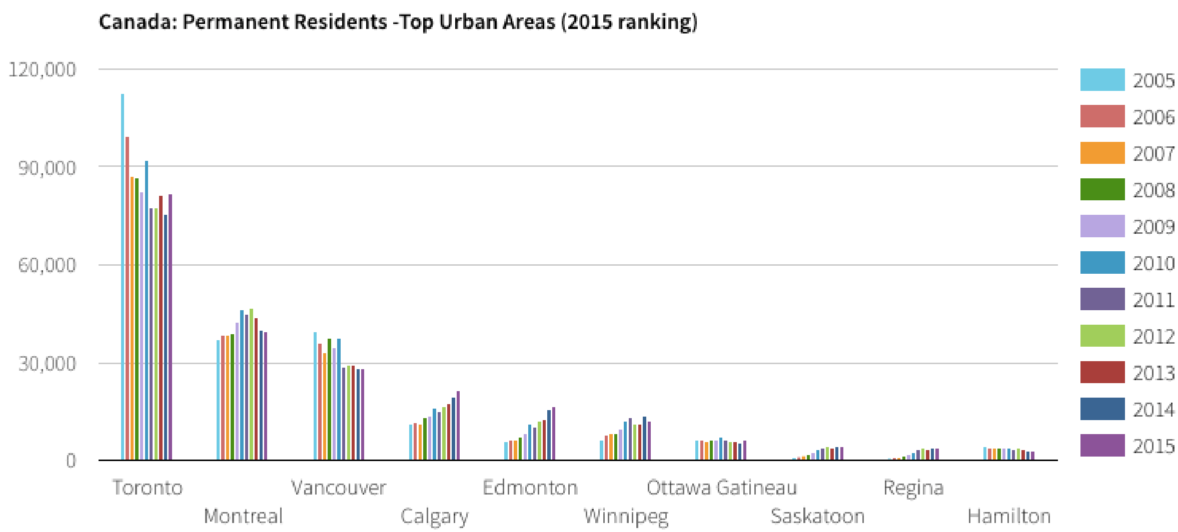
Source: Ontario Chamber of Commerce

The soft oil price environment is expected to keep the C$ weak in the next 12 – 24 months (as shown below), which we believe will continue to encourage international buyers.



Source: TD Economics

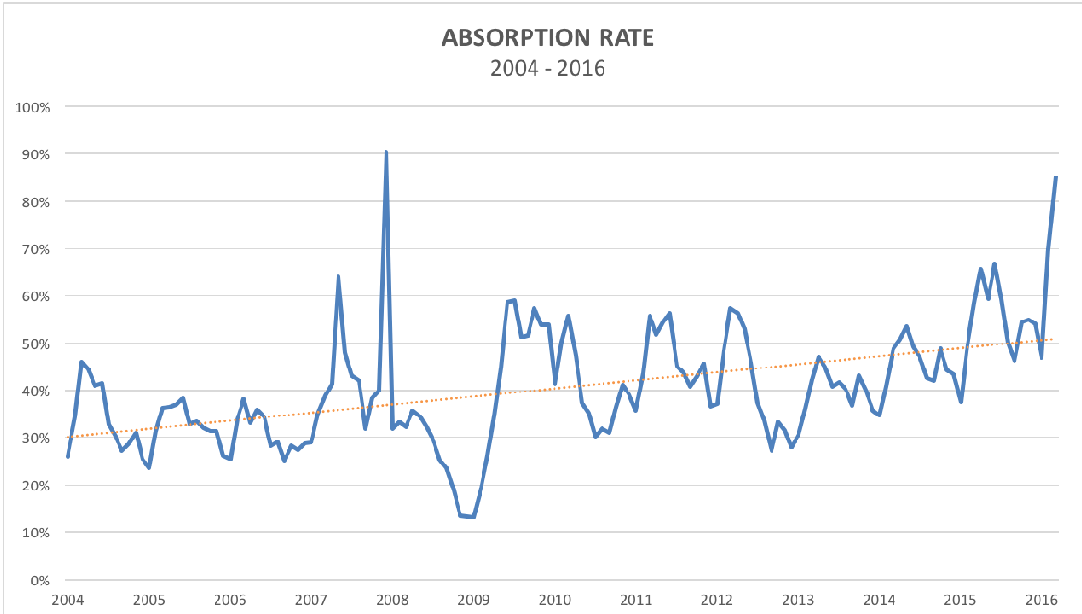
Toronto is expected to continue to be the most popular destination for immigrants. In 2015, approximately 30.2% of the immigrants to Canada chose Toronto.



Source: The Canadian Magazine of Immigration

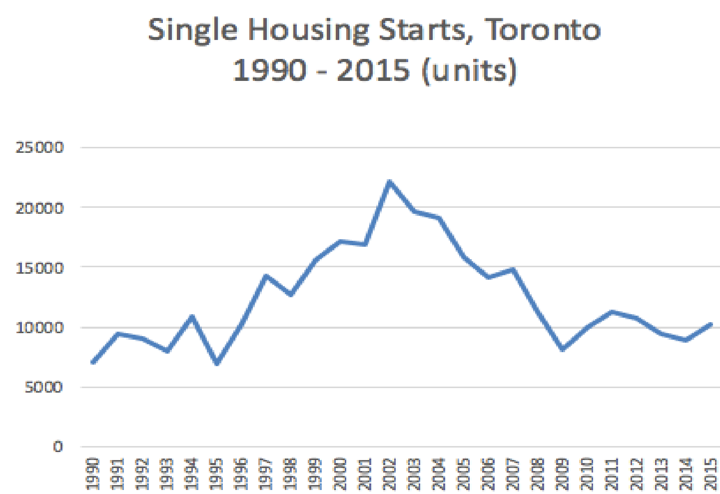
According to the Toronto Real Estate Board ("TREB"), TREB MLS® home sales in Q1-2016 were 22,575, up 16% YOY. The following charts show the strong YOY sales growth and the high sales to new listing ratio. **TREB estimates 2016 will mark a second consecutive record year for home sales.**

The absorption rate, the rate at which houses are sold in a specific period, has steadily increased since 2004.



Source: TREB

According to TREB, there is a persistent lack of inventory for single, semi and townhouses in the GTA, primarily because most of the new supply over the past decade has come from new condominiums. The following chart shows the decline in single housing starts.



Data from: Canadian House Observer

A recent survey conducted by Ipsos indicated that 12% of GTA households are seriously considering purchasing a home in 2016.

All the above factors, along with the historically low interest rate environment, we believe, will keep the GTA real estate market healthy in the near-term.

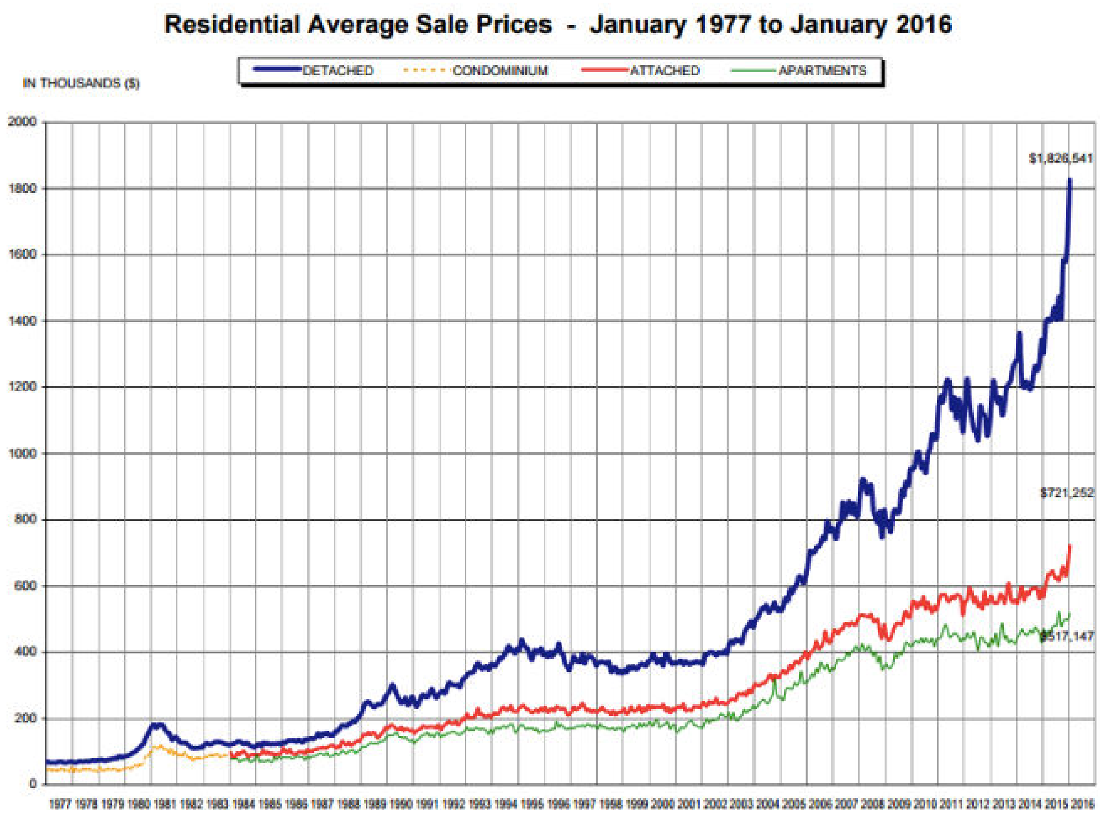
Vancouver Real Estate Market

Vancouver's real estate market continues to remain highly active. Sales volumes have been at record highs so far this year. The following table displays the YOY increase in sales volume.

Sales Volume	2016	2015	YOY Change
January	2,519	1,913	31.70%
February	4,172	3,061	36.30%
March	5,173	4,060	27.40%
April	4,781	4,179	14.40%
May	4,769	4,056	17.60%

Source: REGBV

Excessive housing demand is fuelled by a combination of forces, including foreign investment, immigration, and local buyers. The following chart shows the average price of homes in Greater Vancouver since 1977, as per the Real Estate Board of Greater Vancouver ("REBGV"). Detached properties have had the most notable growth, while condominiums and attached properties experienced more modest figures.



Source: Global News / REGBV

Sales of detached properties in May 2016 totaled 1,865, an increase of 8.2% over 1,723 recorded in May 2015. The average detached home price in Metro Vancouver reached $1.51 million in May 2016, implying a 36.9% YOY increase. The following chart provides

FRC Fundamental Research Corp.

comparative data for the month of May.

Vancouver	May-15	May-16	YOY Change
Apartment			
Sales	1,600	2,150	34.4%
Price	$396,565	$485,000	22.3%
Attached			
Sales	733	754	2.9%
Price	$506,325	$632,400	24.9%
Detached			
Sales	1723	1,865	8.2%
Price	$1,105,770	$1,513,800	36.9%
Total	**4,056**	**4,769**	**17.6%**

Source: REGBV

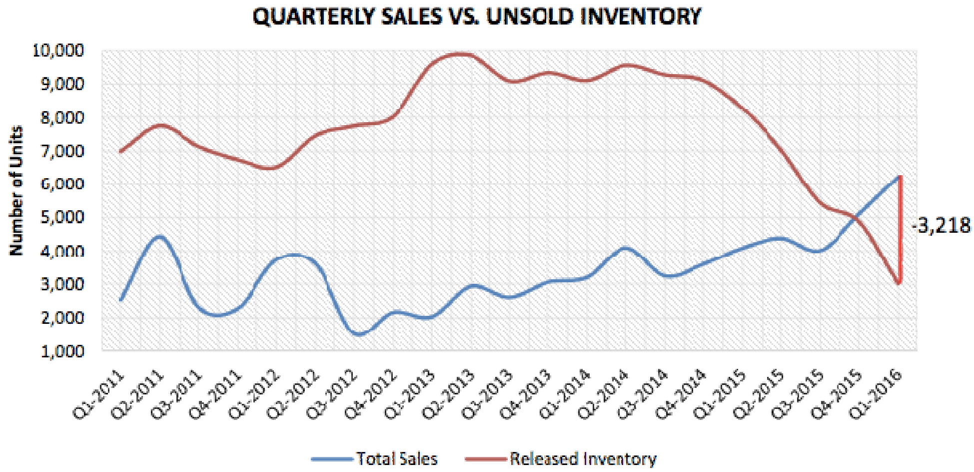
We believe that unaffordability in the detached housing market is driving the multi-family housing market; which includes condominiums, town homes, duplexes, etc. The following chart shows the explosive growth in multi-family housing starts in the City of Vancouver.

Vancouver CMA Preliminary Actual Housing Starts in February

	Feb-15	Feb-16	YOY Change
Singles	95	110	15.8%
Multiples	319	890	179.0%

Source: CMHC

Despite record high levels of housing starts, housing supply has been unable to satisfy demand. In a recent report, Urban Analytics (a provider of industry data for the Vancouver and Calgary real estate market) addressed the inability of Metro Vancouver to respond to the substantial rise in demand. The following chart illustrates that unsold inventory dropped below unit sales for the first time since Q1-2011.

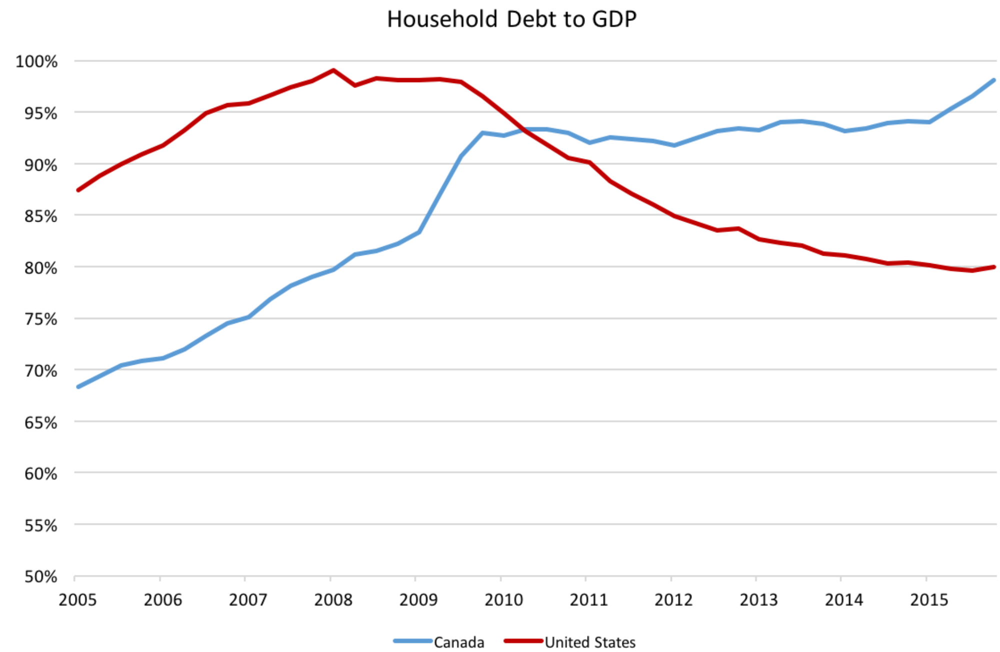


Source: Urban Analytics

Vancouver's real estate market is highly influenced by foreign investment. Currently, there is little data available surrounding foreign investment. The Bank of Canada estimates that Chinese investment accounts for $12.7 billion in real estate sales in Vancouver, representing 33% of the total sales. Economic conditions in BC have been robust despite a slowdown in other regions of Canada. As of May 2016, BC had an unemployment rate of 6.1% (unchanged from May 2015), versus the national rate of 6.9% (6.8% in May 2015). BC experienced a 1.04% YOY increase in population to 4.72 million in Q2-2016 (Source: Statistics Canada).

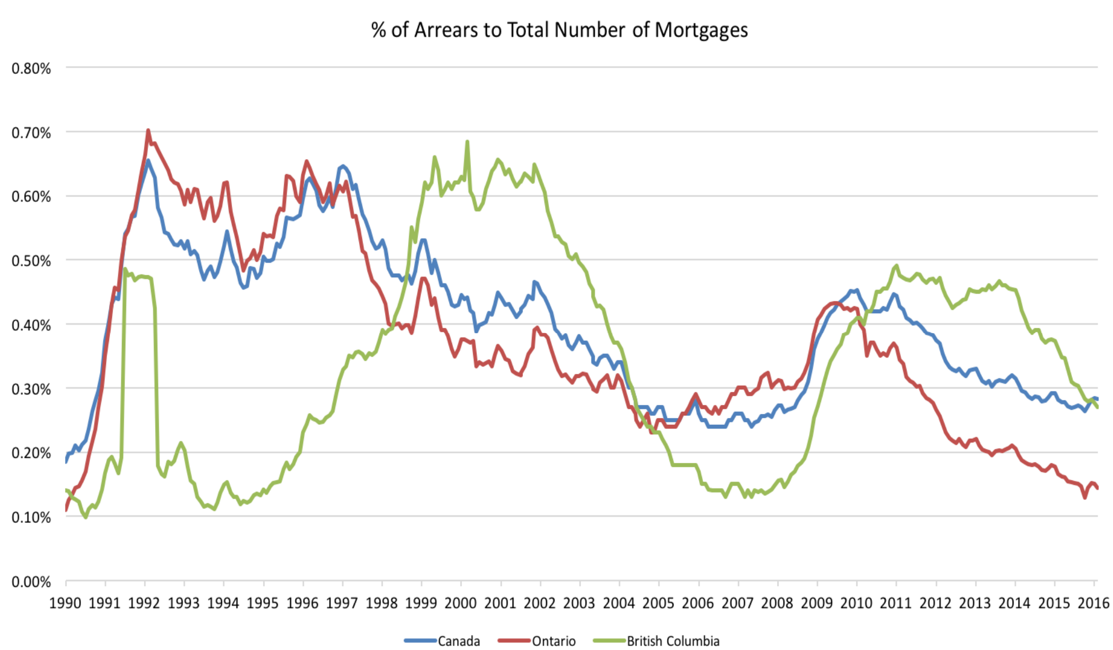
The B.C. government recently introduced legislation to add a 15% property transfer tax on foreign nationals buying real estate in Metro Vancouver – a move, we believe, that is likely to slow foreign investment and eventually lead to a price correction.

A potential area for concern surrounds Canada's rising levels of debt. As shown in the chart below, Canada's household debt to Gross Domestic Product ("GDP") has now approached the levels seen in the U.S. during the 2008-2009 recession.



Source: Federal Reserve Economic Data (FRED)

Despite rising levels of debt, mortgage arrears have been declining in recent years, as shown in the chart below. As of March 2016, approximately 0.27% of mortgages in BC were in arrears versus the national rate of 0.28%. The historic average (from 1990 to March 2016) of BC is 0.34%.



Source: Canadian Bankers Association

In summary, we believe Vancouver's detached 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$. **However, we are taking a more cautious approach to B.C. considering the government's new legislation and will monitor developments very closely.**

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 RRSP, RRIF, TFSA, LIF, RESP, etc. The trust's structure is very similar to a MIC. Both structures allow investors to invest in a pool of diversified mortgages and receive income from them.

The trust is 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. From Q4-2008 to Q3-2015, management distributed 90% of the net income to investors. In Q4-2015, management reversed this to the original 80%.

- The remaining 20% of the aggregate of net income, and net realized capital gains, will be paid to the manager.

In 2014, the trust introduced a new class of units – Class F. These units are intended for funds managed by portfolio managers and other fee-based investment advisors. In 2016, the trust introduced Class C units, which are intended for investors who purchase units through Dealers (IIROC and Exempt Market Dealers). Class C and F units are currently distributed through several IIROC firms. The following table shows the outstanding units as of June 30, 2016.

as of June 30, 2016	Units Outstanding
Class A	4,965,122
Class C	583,621
Class F	2,340,499
Total	**7,889,242**

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

FRC Fundamental Research Corp.

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

- **2.0% of NAV in annual management fee 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.

- 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.

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 statement since inception.

Income Statement	2007 (9M)	2008	2009	2010	2011	2012	2013	2014	2015	2015 (6M)	2016 (6M)
Revenues											
Interest Income	$59,318	$337,521	$501,656	$702,948	$1,154,458	$1,584,171	$2,561,432	$3,948,088	$6,155,599	$2,623,462	$4,145,160
Other Income	$2,908	$32,125	$36,100	$72,312	$72,792	$106,324	$173,377	$303,728	$661,990	$313,137	$546,054
	$62,226	**$369,646**	**$537,756**	**$775,260**	**$1,227,250**	**$1,690,495**	**$2,734,809**	**$4,251,816**	**$6,817,589**	**$2,936,599**	**$4,691,214**
Expenses											
Audit Fees	$2,240	$10,000	$22,000	$40,000	$67,275	$60,300	$55,000	$75,250	$94,134	$68,890	$76,700
Bank Charges	$826	$4,316	$1,975	$8,048	$27,923	$30,510	$59,395	$94,370	$131,609	$13,710	$13,346
Interest on Loan Payable	$27,739	$70,983	$51,773	$31,063	$84,727	$131,177	$350,013	$689,472	$1,051,910	$493,552	$521,178
Legal Fees		$8,532	$5,892	$18,681	$64,287	$72,464	$109,644	$174,877	$216,601	$72,622	$51,961
Management Fees	$2,257	$24,539	$54,797	$97,621	$145,619	$227,121	$321,564	$461,707	$647,100	$287,202	$531,438
Loan Loss Provision	$7,963	$8,641	$14,152	$15,380	$29,976	$91,085	$242,195	$488,142	$916,110	$483,842	$220,347
Trustee Fees		$11,612	$10,368	$11,852	$12,294	$16,517	$60,781	$70,494	$68,618	$16,897	$18,234
	$41,025	**$138,623**	**$160,957**	**$222,645**	**$432,101**	**$629,174**	**$1,198,592**	**$2,054,312**	**$3,126,082**	**$1,436,715**	**$1,433,204**
Net Income	**$21,201**	**$231,023**	**$376,799**	**$552,615**	**$795,149**	**$1,061,321**	**$1,536,217**	**$2,197,504**	**$3,691,507**	**$1,499,884**	**$3,258,010**
Net Asset Value	$10.00	$10.00	$10.00	$10.00	$10.00	$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	2,041,233	2,778,432	5,120,201	3,768,401	7,889,242
Distributions											
Investors	16,961	192,478	339,112	497,354	715,634	955,189	1,382,595	1,977,754	3,215,496	1,349,896	2,606,409
Management	4,240	38,545	37,687	55,261	79,515	106,132	153,622	219,750	476,011	149,988	651,602
Investors' Share	80.0%	83.3%	90.0%	90.0%	90.0%	90.0%	90.0%	90.0%	87.1%	90.0%	80.0%

: 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 by 56% YOY in 2015 to $6.16 million. In the first half of 2016, revenues grew by 58% YOY to $4.42 million. Net Income grew by 68% YOY to $3.69 million in 2015, and by 117% YOY to $3.26 million in the first half of 2016.

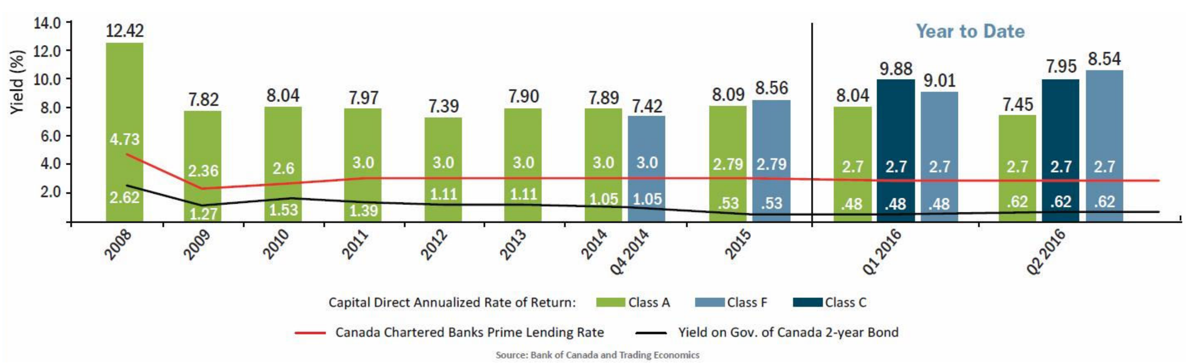
Interest + Other income as a percentage of mortgage receivables was 9.58% p.a. in 2015, and 9.32% in the first half of 2016. The dividend yield (dividends as a percentage of invested capital) was8.14% p.a. and 8.01% p.a., respectively.

% of Mortgage Receivable	2007 (9M)	2008	2009	2010	2011	2012	2013	2014	2015	2015 (6M)*	2016 (6M)*
Interest Income	3.48%	13.42%	11.49%	10.12%	10.83%	9.71%	9.16%	8.80%	8.65%	8.56%	8.23%
Other Income	0.17%	1.28%	0.83%	1.04%	0.68%	0.65%	0.62%	0.68%	0.93%	1.02%	1.08%
Interest Income + Others	**3.65%**	**14.70%**	**12.32%**	**11.16%**	**11.51%**	**10.36%**	**9.78%**	**9.47%**	**9.58%**	**9.58%**	**9.32%**
Less:											
Management Fee	-0.13%	-0.98%	-1.25%	-1.41%	-1.37%	-1.39%	-1.15%	-1.03%	-0.91%	-0.94%	-1.06%
G&A Expenses	-0.18%	-1.37%	-0.92%	-1.13%	-1.61%	-1.10%	-1.02%	-0.92%	-0.72%	-0.56%	-0.32%
Loan Loss Provision	-0.47%	-0.34%	-0.32%	-0.22%	-0.28%	-0.56%	-0.87%	-1.09%	-1.29%	-1.58%	-0.44%
Interest	-1.63%	-2.82%	-1.19%	-0.45%	-0.79%	-0.80%	-1.25%	-1.54%	-1.48%	-1.61%	-1.03%
Net	1.24%	9.19%	8.63%	7.96%	7.46%	6.51%	5.49%	4.90%	5.19%	4.89%	6.47%
Investors' Returns (% of Invested	**2.54%**	**10.71%**	**8.67%**	**8.19%**	**7.97%**	**7.60%**	**7.94%**	**8.21%**	**8.14%**	**8.25%**	**8.01%**
2-year GOC	4.19%	2.62%	1.27%	1.53%	1.34%	1.11%	1.30%	1.05%	0.54%	0.48%	0.62%

** annualized*

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:



In 2015, the trust reported approximately $0.51 million in realized losses, or 0.72% of the total portfolio. This compares to a loss of $0.47 million in 2014, or 1.04% of the portfolio. The realized loss in the first half of 2016 was $0.38 million, or 0.38% of the portfolio. **At the end of Q2-2016, the trust had a general loan loss provision of $0.55 million, or 0.48% of the portfolio.** The trust had assigned a provision of 0.80% at the end of 2015, and 0.58% at the end of 2014. We estimate that comparable MIEs typically assign 0.8% - 1.0% of their portfolios as loan loss provisions.

	2007 (9M)	2008	2009	2010	2011	2012	2013	2014	2015	2015 (6M)	2016 (6M)
Actual Losses	-	-	-	-	-	17,030	106,052	465,260	511,711	268,899	384,342
Actual Losses (% of mortgage receivable)	0.00%	0.00%	0.00%	0.00%	0.00%	0.10%	0.38%	1.04%	0.72%	0.44%	0.38%
Distributions	$16,961	$192,478	$339,112	$497,354	$715,634	$955,189	$1,382,595	$1,977,754	$3,215,496	$1,349,896	$2,606,409
Reinvested	$0	$105,133	$151,708	$232,843	$330,497	$495,024	$690,083	$1,118,084	$1,612,711	$667,143	$1,276,017
Reinvested (as a % of Distributions)	0%	55%	45%	47%	46%	52%	50%	57%	50%	49%	49%
Redemptions	$0	$62,543	$217,016	$132,798	$10,000	$588,593	$636,516	$1,661,741	$1,419,586	$0	$0
Redemption (% of invested capital)	0%	3%	6%	2%	0%	5%	4%	7%	4%	0%	0%

Investors continue to reinvest a significant portion of the distributions (49% in the first six months of 2016) – which, we believe, is a very positive sign and shows their confidence in the investment.

Redemptions totaled $1.42 million in 2015, or 4% of the average invested capital. Note that the trust has redeemed approximately 5% of the invested capital every year since 2012 – 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	2007	2008	2009	2010	2011	2012	2013	2014	2015	Q2-2016
Assets										
Cash	$75,327	$698,744	$215,007	$121,264	$288,331	$187,552	$569,309	$556,175	$194,106	$762,651
Accounts Receivable			$2,333		$119,180			$120,045	$142,589	$532,139
Prepaid Expense				$7,500						
Assets held for sale						$15,949				
Mortgage Investments (net)	$1,704,378	$3,324,557	$5,408,042	$8,479,813	$12,837,727	$19,781,725	$36,139,391	$53,633,836	$88,672,929	$112,772,704
	$1,779,705	**$4,023,301**	**$5,625,382**	**$8,608,577**	**$13,245,238**	**$19,985,226**	**$36,708,700**	**$54,310,056**	**$89,009,624**	**$114,067,494**
Liabilities										
Loan Payable	$1,000,000	$1,000,000	$600,000	$1,162,682	$2,183,086	$5,083,066	$15,631,451	$24,911,835	$35,619,549	$33,018,631
Accounts Payable & Accured Liabilities	$111,695	$98,161	$130,700	$195,435	$352,925	$478,948	$664,922	$1,613,901	$2,188,061	$2,156,436
	$1,111,695	$1,098,161	$730,700	$1,358,117	$2,536,011	$5,562,014	$16,296,373	$26,525,736	$37,807,610	$35,175,067
Net Asset	$668,010	$2,925,140	$4,894,752	$7,250,460	$10,709,227	$14,423,212	$20,412,327	$27,784,320	$51,202,014	$78,892,427
SE + Liabilities	**$1,779,705**	**$4,023,301**	**$5,625,452**	**$8,608,577**	**$13,245,238**	**$19,985,226**	**$36,708,700**	**$54,310,056**	**$89,009,624**	**$114,067,494**
Debt to Capital	60%	25%	11%	14%	17%	26%	43%	47%	41%	30%
Debt as a % of Mortgage Outstanding	59%	30%	11%	14%	17%	26%	43%	46%	40%	29%
Interest Coverage Ratio	1.8	4.3	8.3	18.8	10.4	9.1	5.4	4.2	4.5	7.3

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 Q1-2016 was $0.50 million.

Line of credit – The trust's line of credit (prime + 0.75%) with Canadian Western Bank has increased from $30 million to $40 million since our previous report. Management indicates that the trust will not withdraw more than 50% of the book value of outstanding mortgages. As of June 30, 2016, $33 million was withdrawn, reflecting debt to capital of 30%. **The interest coverage ratio, in the first six months of 2016, of 7.3x 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. 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.
- There are penalties for early redemption of Class A units.
- Like most mortgage lending companies, loans are primarily interest only loans.
- 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	36%
Rating - 4	9%	Risk - 4	38%
Rating - 5	4%	Risk - 5	10%
Rating - 6	1%	Suspended	12%
Rating - 7	0%		
Suspended	11%		

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