

CAPSTONE MORTGAGE OPPORTUNITIES FUND

Q2 Commentary

CAPSTONE
ASSET MANAGEMENT™

AT A GLANCE

JUNE 30, 2022

- Construction and development mortgages in Canada
- Diversified by developer and development type
- Terms are 3 to 36 months
- Low to no correlation to bond and equity markets
- Liquidity is accommodated twice per year (January and July) with 90 days' notice
- \$105 MM AUM
- Current price: 104.8912 (Class O)

MARKET & FUND UPDATE

The Capstone Mortgage Opportunities Fund generates interest income for investors by providing construction financing to reputable Canadian developers known for quality projects and providing achievable business plans. The mortgaged properties in this portfolio are located in the provinces of Ontario and B.C., with their primary concentration in the Greater Toronto Area (GTA).

Between March 31st and June 30th of this year, the Capstone Mortgage Opportunities Fund Class O returned 1.95% to investors which is in line with this fund's historical annual average of 9.17%. During this same period, the real estate market in Canada began to soften in response to rising interest rates. At the end of June, home prices dropped 1.9% compared to May, but it is worth noting that prices are still 14.89% higher than June of last year. Additionally, while sales activity dropped 23.9% since reaching the all-time high of June 2021, the sales volume during this quarter is still on trend with pre-2020 levels. Therefore, while the real estate market is certainly slowing compared to the past year, we need to keep in mind the massive increase in home sales and prices that was experienced from June 2020 to present. These unprecedented increases are unsustainable and, while the rapid interest rate increases may cause a bit of a bumpy road at first, they will also more than likely bring the market back into a much healthier balance.

Because we have recognized that a real estate correction could happen at any point, over the past few years we at Capstone have increased our due diligence requirements and been more selective than ever in new mortgage initiations. While we have seen increased delays in the construction real estate space since the spring of 2020, we are now beginning to see a smaller than usual pipeline for good quality mortgage opportunities. Expanding the mortgage exposure into B.C. this year has been a great start to widen the scope of the Fund. However, if the slowdown of opportunities continues, investors should expect to see cash becoming more prevalent in the Fund, which would result in a drag on return. Additionally, since the adoption of IFRS 9 in 2018, all of Capstone's portfolio strategies are required to include a loan loss provision (bad debt fund) to mitigate default risks. If the market outlook becomes worse, investors should expect a higher percentage of interest profits to be directed to this bad debt fund. If the market outlook improves, then there will be a reversal with a portion of the reserve being directed back to unit values.

All in all, this mortgage portfolio continues to perform in line with expectations and this year we have not seen any new defaults or significant issues with our existing mortgages. While there is a positive relationship between rising interest rates and profits to investors, this may be mitigated in the short term as we navigate the current market conditions. That said, we are still anticipating a typical annual return in the region of 9%.

If you would like to find out more about this Fund, please talk to your Portfolio Manager.

This is not an offer to sell securities. The Subscription Documents and Information Memorandum should be read carefully as they contain important facts about risks, liquidity, fees, and expenses. Past performance may not be repeated.

PERFORMANCE

Performance figures are those of Class O units as of June 30, 2022. Performance is annualized for periods longer than one year. Class O units do not include Management Fees or Administration Fees.



1 MO.	3 MO.	6 MO.	1 YR.	3 YR.	5 YR.	INCEPTION*
0.57%	1.95%	3.59%	8.24%	8.97%	8.52%	9.17%

* Annualized as of first trade date July 15, 2014