CAPSTONE MORTGAGE POOL

Q4 Commentary

CAPSTONE ASSET MANAGEMENT™

AT A GLANCE

DECEMBER 31, 2022

- Construction and development mortgages in Canada
- Diversified by developer and development type
- Mortgage terms are 3 to 36 months
- Low to no correlation to bond and equity markets
- Liquidity is accommodated monthly with 30 days' notice
- $279 MM AUM
- Current price: $9.7836 (Series I)

MARKET & POOL UPDATE

In 2022, the Capstone Mortgage Pool (I series) returned 7.43% to investors whereas the broad fixed income market in Canada yielded -11.67% (represented by the XBB iShares Universal Bond Index ETF). While the Capstone Mortgage Pool certainly exceeded the returns available in the traditional arena, in 2022 the Pool did not achieve its historical average of 8.94%. The greatest detractors from performance were higher-than-typical cash positions and an increased allocation to its loan loss reserve.

This past year saw significantly greater delays in mortgage executions as well as a reduced pipeline of good quality mortgage opportunities in Ontario. Industry delays that began in the spring of 2020 have yet to fully resolve and once interest rates really began to move through late spring, extended timelines became the norm. In the early fall when developers felt more certain about the direction of interest rates, we did see balance return to this space and business activity improved. The strategy of expanding the Pool's mortgage exposure into B.C. this year has been a significant benefit to the portfolio. However, fewer opportunities combined with greater industry delays (especially through the summer of 2022) caused more cash to build in the portfolio, producing a commensurate drag on returns.

Since the adoption of the IFRS 9 accounting standard in 2018, all of Capstone's mortgage portfolios are required to include a loan loss provision (bad debt allowance) to mitigate default risk. While the higher interest rates are likely to reward investors over time, they are punitive to developers and may cause some to experience credit challenges. In these cases, Capstone increases the loan loss provision to ensure that the mortgage portfolio is fairly valued for the given period. If the market outlook becomes worse, investors should expect a higher percentage of interest income to be directed to this bad debt fund. Market improvement will produce a reversal with a portion of the reserve being directed back to investors. This mechanism ensures that the valuation of the portfolio is current throughout the year, but it can cause additional distribution fluctuations that were not experienced in prior years of the Pool.

With the expectation that the Canadian real estate market could correct at any time, we at Capstone have spent the past few years expanding our due diligence procedures while taking a conservative approach to our lending criteria. We believe that our prudence will provide excellent value to our investors in both the long term as well as during shorter periods when the real estate market may be more volatile. Furthermore, while a higher interest rate environment does take some time to be reflected in this portfolio's holdings, we are beginning to see new mortgages with higher rates than were achieved historically. This investment continues to carry a medium risk profile and it is an excellent complement to a traditional investment portfolio.

For more information on this Pool, please contact your Portfolio Manager.

PERFORMANCE (Gross of Fees)

Performance figures are those of Series I units as of December 31, 2022. Performance is annualized for periods longer than one year.

1 MO.	3 MO.	6 MO.	1 YR.	3 YR.	5 YR.	10 YR.	INCEPTION*
0.34%	1.39%	3.10%	7.43%	8.30%	8.28%	9.02%	8.94%

** Annualized as of first trade date April 30, 2012*