First National Mortgage Investment Fund

Annual Management Report of Fund Performance
Annual Audited Financial Statements
For the period ended December 31, 2012

Management's Responsibility for Financial Reporting

March 8, 2013

The accompanying financial statements of First National Mortgage Investment Fund (the "**Fund**") are the responsibility of the management of the Fund. They have been prepared in accordance with Canadian generally accepted accounting principles using information available to March 8, 2013 and management's best estimates and judgments.

The management of the Fund is responsible for the information and representations contained in these Annual Financial Statements and the Annual Management Report of Fund Performance. Management is also responsible for the selection of the accounting principles that are most appropriate for the Fund's circumstances and for the judgments and estimates made in the financial statements. The management of the Fund maintains appropriate processes to ensure that accurate, relevant and reliable financial information is produced.

These financial statements have been approved by the management of the Fund and have been audited by Deloitte LLP, Toronto, Chartered Accountants, on behalf of the unitholders. The auditors' report outlines the scope of their audit and their opinion on the financial statements.

Richard G. Stone
Chief Executive Officer
Stone Asset Management Limited

James A. Elliott
Chief Financial Officer
Stone Asset Management Limited

First National Mortgage Investment Fund

Annual Management Report of Fund Performance for the period

December 19, 2012 to December 31, 2012

Fund:
First National Mortgage Investment Fund

Units:
Listed TSX: FNM.UN

Period:
December 19, 2012 (commencement of operations) to December 31, 2012

Manager:
Stone Asset Management Limited
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Notes:

1. This Annual Management Report of Fund Performance contains financial highlights but does not contain the complete Annual Financial Statements of the Fund. You can get a copy of the Annual Financial Statements at your request, and at no cost, by contacting us (contact information above) or on SEDAR at www.sedar.com. Securityholders may also contact us to request a free copy of the Fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.
2. This report may contain forward looking statements. Forward looking statements involve risks and uncertainties and are predictive in nature and actual results could differ materially from those contemplated by the forward looking statements.
3. Unless otherwise indicated all information is as at December 31, 2012.
4. None of the websites that are referred to in this Annual Management Report of Fund Performance, nor any of the information on any such websites, are incorporated by reference in this Annual Management Report of Fund Performance.

Investment Objectives and Strategies

First National Mortgage Investment Fund (the "**Fund**") is a non-redeemable investment fund established under the laws of the Province of Ontario that issued units of the Fund (the "**Units**") at a price of $10.00 per Unit (the "**Offering**") settled on December 19, 2012.

The investment objectives of the Fund are to:

(i) provide holders of the Units ("**Unitholders**") with tax-advantaged monthly cash distributions; and

(ii) preserve capital.

The Fund was created to obtain exposure to a diversified portfolio (the "**Portfolio**") of Mortgages originated by First National Financial LP (the "**Mortgage Advisor**" or "**First National**"), a wholly owned subsidiary of First National Financial Corporation.

The Fund obtains economic exposure to the Portfolio through a forward agreement (the "**Forward Agreement**"). The return to the Fund will, by virtue of the Forward Agreement, be based on the performance of FN Mortgage Investment Trust (the "**Mortgage Trust**"), an investment trust created to hold the Portfolio. As the Fund will partially settle the Forward Agreement to fund distributions, such distributions will be comprised primarily of returns of capital and capital gains and accordingly, such distributions are described as tax-advantaged.

The Mortgage Trust will seek to accomplish its investment objectives through prudent investments in short term Mortgages (typically 12-36 months) primarily on multi-unit residential and commercial mortgages across Canada. Mortgages will be secured primarily by income producing Real Property where the principal and interest can be serviced from cash flow generated by the underlying Real Property.

Results of Operations

The Fund completed an initial public offering ("IPO") of 5,520,000 units (4,600,000 Class A units and 920,000 Class H units, together the "Unit Offering") on December 19, 2012, raising $55,200,000 in gross proceeds. The proceeds of the offering, net of underwriters' fees of $2,415,000 and $690,000 of other offering expenses on the Class A units, were use to purchase a basket of common shares as described below. Subsequent to the Fund's year end, the over-allotment option was exercised on January 7, 2013, such that an additional 290,000 Units were issued for $2,900,000 million in gross proceeds. The proceeds of the offering, net of underwriters' fees of $152,250 and $43,500 of other offering expenses, were use to purchase an additional basket of common shares. In total, 58,100,000 units have been issued at $10 per Unit.

The Fund's net assets were $52.0 million as at December 31, 2012. Although the Fund closed on December 19, 2012, because of timing on the transaction of the Forward Agreement, statutory holidays in the period, the first portfolio of mortgages was purchased by the Mortgage Trust on December 28, 2012. Accordingly, the Mortgage Trust earned revenue from the Portfolio for 4 days in the fiscal period and there are insufficient financial results to assess the performance of the Portfolio. The statement of operations was more significantly affected by an unrealized loss on the revaluation of the common share basket of $127,147 offset by an unrealized appreciation on the Forward Agreement of $88,830.

As at December 31, 2012, net assets per unit of the Fund's Class A units were $9.31 compared to the NAV upon the IPO of $9.32. For the short period ended December 31, 2012, the Fund recorded a net decrease in net assets from operations of $71,193 or approximately $0.01 per unit. The return of the Fund is, by virtue of the Forward Agreement, based on the return of the Mortgage Trust, which, in turn, is based on the performance of the Portfolio.

The following Manager's Commentary relates to the Fund's exposure to the performance of the Portfolio held in the Mortgage Trust.

During the short period ended December 31, 2012, the Mortgage Trust invested in eight mortgages with an aggregate carrying value of $22,837,434 with an average effective interest rate of 8.68%. The portfolio consists of first, subordinated first, and second mortgages with an average term to maturity of sixteen months. The Mortgage Trust's return was driven primarily by interest income on these mortgages.

Because of the short period between the IPO and year end, the asset mix was weighted more heavily toward cash as there was insufficient time to originate the mortgages as specified in the prospectus. At year end, there was $29,201,949 invested in cash and cash equivalents awaiting investment in appropriate mortgage assets.

The composition of the Portfolio at year end was consistent with the investment objectives and strategy of the Fund. Portfolio capital was deployed primarily in floating rate loan positions with an average loan to value ratio of 68.4% that are typically with large borrowers with whom the Mortgage Advisor has a history of experience.

Recent Developments

Global macroeconomic concerns continue to dominate financial headlines and weigh on investor sentiment. The Manager expects these issues will continue to draw attention for some time with markets intermittently focusing on the latest developments resulting in periods of higher volatility. The Mortgage Advisor believes this volatility will keep interest rates low in Canada. Accordingly, real estate financing will continue to be cheap in comparison to the typical interest rate environment in Canada over the past twenty-five years. This environment will provide incentive for real estate developers to take on new transactions and require the type of mortgage lending which the Fund is offering.

International Financial Reporting Standards

On December 12, 2011, the Canadian Accounting Standards Board (''AcSB'') made a decision to extend the deferral of the adoption of International Financial Reporting Standards (''IFRS'') by investment companies for an additional year to January 1, 2014. This extends the previous two-year deferral of IFRS to three years as compared to other publicly accountable entities. Consequently, IFRS will be applicable to the Fund for the fiscal year beginning January 1, 2014. At the transition date the prior fiscal year financial statements will require restatement to IFRS for comparative purposes.

The deferral is to provide time for the International Accounting Standards Board (''IASB'') to finalize its guidance on investment entities such that a final standard could be issued after January 1, 2013, the previously established changeover date for investment companies in Canada.

The Fund has reviewed the existing body of IFRS against its current policies under Canadian GAAP and has noted certain policy differences, the most notable is the requirement to consolidate the financial results of the Fund with the Mortgage Trust. Currently, investment entities would have to follow the consolidation requirements as set out in IFRS 10 Consolidated Financial Statements because IFRS does not differentiate between them and other entities. As a result, they would have to consolidate their financial statements with that of an entity they are investing in if they control that entity. As part of a project on consolidated financial statements, the IASB published an Exposure Draft (''ED'') for Investment Entities on August 25, 2011, that proposes an exception to the principle in IFRS that an entity consolidates all controlled entities. Instead, the ED would require an entity that meets the criteria to be an investment entity to measure all controlled investments at fair value, with changes recognized in profit or loss. On October 31, 2012 the IASB finalized IFRS 10; under IFRS 10 Investment Entities are exempt from consolidating financial statements provided that the entity meets the criteria of an Investment Entity. The Manager has reviewed the guidance and has determined that the Fund qualifies for the exemption from consolidation given that the Fund has the following typical characteristics of an Investment Entity. The Fund has more than one investment in its portfolio as well as multiple investors who are not related parties of the Fund, and finally the Fund assigns ownership interest in the form of securities.

Apart from this, other major changes identified include the addition of a statement of cash flows and the classification of unitholder's equity (puttable instruments) as a liability unless certain conditions are met, as well as more extensive note disclosure requirements. These changes will not have an impact on the Fund's results of operations or financial position.

The process of evaluating the potential impact of IFRS on the financial statements is ongoing, as the IASB and the AcSB continue to issue new standards and recommendations.

Related Party Transactions

The Manager and the Fund are deemed to be related parties. Please refer to the section titled ''Management Fees'', which outlines the fees paid to the Manager. The Manager and the Fund were not party to any other related party transactions during the period ended December 31, 2012. The Independent Review Committee approved the Mortgage Trust's purchase of any mortgage where there was an identified conflict of interest with the Mortgage Advisor.

Financial Highlights

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance since inception.

THE FUND'S NET ASSETS PER CLASS A UNIT[1]

	For the period ended December 31, 2012	
	Class A	**Class H**
Net Assets, at issuance [2]	**$9.32**	**$10.00**
Increase (decrease) from operations:		
Total revenue	**0.00**	**0.00**
Total expenses	**(0.01)**	**(0.01)**
Unrealized gains (losses) for the period	**0.00**	**0.00**
Total decrease from operations [3]	**(0.01)**	**(0.01)**
Distributions:		
From income (excluding dividends)	**0.00**	**0.00**
From dividends	**0.00**	**0.00**
From capital gains	**0.00**	**0.00**
Return of capital	**0.00**	**0.00**
Total Distributions [4]	**0.00**	**0.00**
Net Assets, end of period	**$9.31**	**$9.99**

Notes:

[1] This information is derived from the Fund's audited annual financial statements.

[2] For 2012, the net assets per unit reflects the issue price of $10.00 (less share issue expenses for Class A).

[3] Net assets and distributions are based on the actual number of units outstanding at the relevant time. The decrease from operations is based on the weighted average number of units outstanding over the financial period.

[4] There were no distributions declared or paid in the period.

RATIOS AND SUPPLEMENTAL DATA

	For the period ended December 31, 2012	
	Class A	**Class H**
Total Net Asset Value [1]	**$42,835,672**	**$9,188,135**
Number of Class A units outstanding [1]	**4,600,000**	**920,000**
Management expense ratio [2]	**8.37%**	**0.79%**
Management expense ratio before waivers or absorptions	**8.37%**	**0.79%**
Trading expense ratio [3]	0.81%	0.81%
Portfolio turnover rate [4]	N/A	N/A
Net Asset Value per Class A unit	**$9.31**	**$9.99**
Closing market price	**$10.00**	**N/A**

Notes:

[1] This information is provided as at December 31 of the year shown.

[2] Management expense ratio is based on total expenses (excluding commissions and other portfolio transaction costs) for the stated period and, except as stated in the following sentence, is expressed as an annualized percentage of daily average net asset value during the period. The MER for the period ended December 31, 2012, include agents' fees and other offering expenses, which are one-time expenses and therefore are not annualized. The MER for the period ended December 31, 2012 excluding agents' fees and offering expenses is 8.37% for the Class A units and 0.79% for the Class H units.

[3] The trading expense ratio represents total commissions, forward agreement fees and other portfolio transaction costs expressed as an annualized percentage of daily average net asset value during the period.

[4] The Fund's return is linked, by virtue of a forward agreement, to the performance of a portfolio comprised primarily of mortgages receivable and, consequently, the portfolio turnover rate does not apply to the Fund.

Management Fees

The Manager is responsible for providing or arranging for all investment advisory and portfolio management services (primarily through the Mortgage Advisor) required by the Fund including, without limitation, managing the Portfolio in a manner consistent with the investment objectives, guidelines and restrictions of the Fund and for arranging for the execution of all portfolio transactions. The Manager is also responsible for the operational and administrative functions of the Fund. As compensation for the management services rendered to the Fund, the Manager is entitled to receive an annual management fee from the Fund in an amount equal to 0.40% of the net asset value of the Fund, which is calculated daily and paid monthly in arrears. The Manager also receives an annual management fee in an amount equal to 0.95% of the net asset value of the Mortgage Trust, which is calculated daily and paid monthly in arrears. From these fees, the Mortgage Advisor is compensated. The Manager will pay to registered dealers a servicing fee equal to 0.40% annually of the net asset value of the Fund per unit for each unit held by clients of the registered dealers, calculated and paid at the end of each calendar quarter commencing on March 31, 2013, plus applicable taxes.

Past Performance

Year-by year returns are not provided, in accordance with security regulations, since the Fund has not been in existence for a period of more than one year.

Summary of Investment Portfolio

The Fund has entered into a forward agreement whereby the Fund obtains exposure to the performance of the Portfolio. Accordingly, these financial statements should be read in conjunction with the financial statements of FN Mortgage Investment Trust. The Management Report of Fund Performance and Financial Statements for FN Mortgage Investment Trust are available to securityholders and can be attained by visiting our website at www.stoneco.com • info@stone.com or by writing to Stone Asset Management Limited, 36 Toronto Street, Suite 710,Toronto, Ontario,M5C 2C5, or on SEDAR at www.sedar.com.

The following is a summary of FN Mortgage Investment Trust's portfolio as at December 31, 2012. This is a summary only and will change due to ongoing portfolio transactions in the Mortgage Trust. A quarterly update will be available on www.stoneco.com.

ALL INVESTMENT HOLDINGS AS AT DECEMBER 31, 2012

Description	Average Effective Interest Rate	% of Net Asset Value of FN Mortgage Trust
Cash		56.12
$5,000,000 Calgary 1st Mortgage	9.04%	9.54
$4,500,000 King City 1st Mortgage	10.54%	8.55
$3,935,500 Hamilton 1st Mortgage	7.32%	7.52
$3,360,000 Brantford 1st Mortgage	6.25%	6.46
$2,817,500 Calgary 1st Mortgage	7.31%	5.38
$2,000,000 Dartmouth 2nd Mortgage	14.00%	3.77
$936,000 Montreal 1st Mortgage	5.75%	1.79
$463,440 Riverview, NB 1st Mortgage	7.86%	0.87
Total Net Asset Value of FN Mortgage Investment Trust	8.68%	**$52,031,128**

Financial Statements of

First National Mortgage Investment Fund

December 31, 2012

Deloitte.

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Independent Auditor's Report

To the Unitholders of
First National Mortgage Investment Fund

We have audited the accompanying financial statements of First National Mortgage Investment Fund, which comprise the statements of net assets and investment portfolio as at December 31, 2012, the statements of operations and changes in net assets for the period December 19, 2012 (commencement) to December 31, 2012 and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audit is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of First National Mortgage Investment Fund as at December 31, 2012, and its financial performance for the period December 19, 2012 (commencement) to December 31, 2012 in accordance with Canadian GAAP.

Deloitte LLP

Chartered Professional Accountants, Chartered Accountants
Licensed Public Accountants
March 8, 2013

FIRST NATIONAL MORTGAGE INVESTMENT FUND
Statement of Net Assets

As at December 31, 2012	$
ASSETS	
Cash and cash equivalents (Note 6)	**645,252**
Common Share Basket (Note 3)	**51,927,850**
Forward Agreement (Note 3)	**88,831**
	52,661,933
LIABILITIES AND NON-CONTROLLING INTEREST	
Accounts payable and accrued liabilities (Note 5)	**638,126**
	638,126
NET ASSETS, REPRESENTING CLASS A AND CLASS H UNITHOLDERS' EQUITY	
Class A Units (Note 4)	**42,835,672**
Class H Units (Note 4)	**9,188,135**
	52,023,807
Outstanding Class A Units (Note 4)	**4,600,000**
Outstanding Class H Units (Note 4)	**920,000**
Net Assets per Class A Unit (Under GAAP and NI-81-106)	**9.31**
Net Assets per Class H Unit (Under GAAP and NI-81-106)	**9.99**

The accompanying notes are an integral part of these financial statements.

FIRST NATIONAL MORTGAGE INVESTMENT FUND

Statement of Operations

For the period December 19, 2012 (commencement) to December 31, 2012	$
REVENUE	-
EXPENSES	
Management fees (Note 5)	**7,734**
Forward Agreement fees	**13,854**
Servicing fees (Note 5)	**5,638**
Audit and other expenses	**5,650**
	32,876
LOSS BEFORE OTHER ITEMS	**(32,876)**
OTHER ITEMS	
Unrealized loss on revaluation of common share basket	**(127,148)**
Unrealized appreciation on Forward Agreement (Note 3)	**88,831**
	(38,317)
NET DECREASE IN NET ASSETS FROM OPERATIONS	**(71,193)**
WEIGHTED AVERAGE NUMBER OF CLASS A AND H UNITS OUTSTANDING	**5,520,000**
NET DECREASE IN NET ASSETS FROM OPERATIONS	
PER CLASS A UNIT	**(0.01)**
PER CLASS H UNIT	**(0.01)**

The accompanying notes are an integral part of these financial statements.

FIRST NATIONAL MORTGAGE INVESTMENT FUND
Statement of Changes in Net Assets
For the period December 19, 2012 (commencement) to December 31, 2012

		Class A		Class H
UNIT CAPITAL				
Units issued (Note 1(a))	$	**46,000,000**	$	**9,200,000**
Issue costs (Note 1(a))		**(3,105,000)**		**-**
Net decrease in net assets from operations		**(59,328)**		**(11,865)**
TOTAL UNITHOLDERS' EQUITY	$	**42,835,672**	$	**9,188,135**
Units issued and outstanding, beginning of period		**4,600,000**		**920,000**
Units issued and outstanding, end of period		**4,600,000**		**920,000**

The accompanying notes are an integral part of these financial statements.

FIRST NATIONAL MORTGAGE INVESTMENT FUND
Statement of Investment Portfolio
As at December 31, 2012

Common Share Basket	Face Value	Number of Shares	Average Cost	Fair Value	% of Net Assets
Equity Shares					
Legacy Oil		638,200	$ 4,326,996	$ 4,352,524	8.37%
New Gold Inc.		414,500	4,327,380	4,534,630	8.71%
Martinrea International		554,200	4,350,470	4,278,424	8.22%
Paramount Resources		133,100	4,327,081	4,249,883	8.17%
Open Text		77,300	4,327,254	4,274,690	8.22%
Osisko Mining		586,200	4,402,362	4,654,428	8.95%
Tourmaline Oil		142,456	4,326,389	4,434,655	8.52%
Tahoe Resources		249,801	4,349,035	4,541,382	8.73%
Athabasca Oil		396,300	4,327,596	4,133,409	7.95%
Catamaran Corp		88,300	4,323,168	4,104,184	7.89%
CGI Group		176,500	4,326,015	4,045,380	7.78%
Lundin Mining		849,560	4,341,252	4,324,261	8.31%
Total Common Share Basket Securities (Note 4)			**$ 52,054,998**	**$ 51,927,850**	**99.82%**

Forward Agreement	Location	Principal	Fair Value	
Fair Value of Forward Agreement				
First Mortgage	Calgary	$ 5,000,000	$ 4,966,785	
First Mortgage*	Montreal	936,000	932,464	
First Mortgage*	Brantford	3,360,000	3,360,000	
First Mortgage*	Calgary	2,817,750	2,801,965	
First Mortgage	Riverview	463,440	453,970	
First Mortgage*	King City	4,500,000	4,451,250	
Second Mortgage*	Dartmouth	2,000,000	1,960,000	
First Mortgage*	Hamilton	3,935,500	3,911,000	
Total fair value of mortgages		**$ 23,012,690**	**$ 22,837,434**	
Add cash and cash equivalents of the Mortgage Trust			**29,201,949**	
Less other net liabilities of the Mortgage Trust			**(8,255)**	
Less Common share basket			**(51,927,850)**	
less accrued forward fees and other			**(14,447)**	
Fair value of forward contract			**$ 88,831**	**0.17%**
Cash and Cash Equivalents (Note 3)			**645,252**	**1.24%**
Other, net[1]			**(638,126)**	**-1.23%**
Total Net Assets			**$ 52,023,807**	**100.00%**

* Mortgages prepayable without penalty

1 - Includes the common share basket, the forward contract and other assets and liabilities. The Manager does not generally view the common share basket and the forward contract as critical from an investor's perspective in understanding the economic risk of the Fund. For further information on the structure please refer to the Fund's prospectus filed on SEDAR.

The accompanying notes are an integral part of these financial statements.

1. NATURE OF OPERATIONS

(a) Background and Rationale of the Corporation

First National Mortgage Investment Fund (the "Fund") was formed on November 27, 2012 and is a non-redeemable investment fund established under the laws of the Province of Ontario.

The Fund actively commenced operations on December 19, 2012, when it was capitalized beyond the initial $10 seed capital. The investment objectives of the Fund are to: (i) provide holders of the units ("Unitholders") with tax-advantaged monthly cash distributions; and (ii) preserve capital.

The Fund has been created to obtain exposure to a diversified portfolio (the "Portfolio") of mortgages originated by First National Financial LP (the "Mortgage Investment Advisor" or "First National"), a wholly owned subsidiary of First National Financial Corporation. The Fund obtains economic exposure to the Portfolio through a forward agreement (the "Forward Agreement"). The return to the Fund will, by virtue of the Forward Agreement, be based on the performance of FN Mortgage Investment Trust (the "Mortgage Trust"), a newly created investment trust, that holds the Portfolio. As the Fund will partially settle the Forward Agreement to fund distributions, such distributions will be comprised primarily of returns of capital and capital gains and accordingly, such distributions are described as tax advantaged.

The Fund completed an initial public offering of 5,520,000 units (4,600,000 Class A units and 920,000 Class H units, together the "Unit Offering") on December 19, 2012, raising $55,200,000 in gross proceeds. The proceeds of the offering, net of underwriters' fees of $2,415,000 and $690,000 of other offering expenses on the Class A units, were used to purchase a basket of common shares as described below. Subsequent to the Fund's year end, the over-allotment option was exercised on January 7, 2013, such that an additional 290,000 Units were issued for $2,900,000 million in gross proceeds. The proceeds of the offering, net of underwriters' fees of $152,250 and $43,500 of other offering expenses, were used to purchase an additional basket of common shares. In total, 5,810,000 units have been issued at $10 per Unit.

(b) Fund Investment Objectives

The Fund's investment objective with respect to the Unitholders is to provide tax-efficient quarterly distributions initially targeted to be 6% per annum which includes the return of the original price of $10 per unit to unitholders through monthly returns of capital. The Class A units are traded on the TSX under the symbol FNM.UN. The Class H units are not listed, held by First National, and are convertible to Class A units as described in Note 4(a). In all other respects, the Class H units have similar features to the Class A units.

The Class A units have no fixed maturity date and currently have a target distribution rate of $0.05 per unit per month or $0.60 per unit per annum. The Fund seeks to provide the unitholders with superior risk-adjusted returns in the form of either net asset value growth or tax-efficient distributions.

(c) The Common Share Basket and Forward Agreement

The Fund obtained economic exposure to the Portfolio through the simultaneous purchase of a basket of Canadian common shares (the "Common Share Basket") and the execution of the Forward Agreement with a subsidiary of a major Canadian Schedule I bank. The Forward Agreement is designed to hedge the Fund's market risk to the Common Share Basket and to provide the economic return of the Portfolio net of any transaction and operating costs.

The Common Share Basket consists of highly liquid non-dividend paying Canadian common shares which are typical of structured transactions of this type.

2. SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

(a) Revenue recognition

Dividend income – Dividends arising from the common share basket are recognized on the ex-dividend date.

(b) Cash and cash equivalents

Cash and cash equivalents are comprised of cash held at the Bank. The Fund had no cash equivalents.

(c) Common Share Basket

The Common Share Basket consists of non-dividend paying publicly listed equities which are valued at fair value using closing bid prices. Unrealized revaluation gains and losses are recognized in the statement of operations.

(d) Forward Agreement

The Forward Agreement is carried at fair value which is based on the valuation methodology as specified in the terms of the Forward Agreement. Unrealized revaluation gains and losses are recognized in the statement of operations.

(e) Accounts payable and accrued liabilities

Accounts payable and accrued liabilities are classified as other liabilities, all of which are carried at amortized cost.

(f) Income taxes

The Fund will be subject to tax in each taxation year under Part I of the Tax Act on the amount of its income for the year, including dividends and net realized taxable capital gains, less the portion thereof that it claims in respect of the amount paid or payable to Unitholders in the year. The Fund intends to make distributions to Unitholders and to deduct, in computing its income in each taxation year, such amount as will be sufficient to ensure that the Fund will not be liable for income tax under Part I of the Tax Act for each year other than such tax on net realized capital gains that will be recoverable by the Fund in respect of such year by reason of the capital gains refund mechanism.

(g) Use of estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

(h) Changes in Accounting Policies and Recent Pronouncements

The Canadian Institute of Chartered Accountants ("CICA") replaced Canadian GAAP for publicly accountable enterprises with International Financial Reporting Standards ("IFRS") effective January 1, 2011 other than for investment companies as defined in the CICA Handbook, for which transition to IFRS has been deferred to January 2014. As a result, the Fund will adopt IFRS for the fiscal period beginning January 1, 2014, and will issue its first interim financial statements in accordance with IFRS, including comparative IFRS information for the previous fiscal period, for the interim period ending June 30, 2014. Management is currently evaluating the impact of the new standards on the financial statements.

3. COMMON SHARE BASKET

As explained in Note 1(c) the Fund obtains the economic exposure to the Mortgage Portfolio through the combination of the Common Share Basket and the Forward Agreement. Although the Fund is the legal owner of the Common Share Basket it considers itself perfectly hedged to the market performance of the Common Share Basket as one component of the Forward Agreement payment (settlement) calculation contemplates the change in the value of the Common Share Basket. That is, if the Common Share Basket has decreased in value the Forward Contract provides an equal but opposite calculation to the Fund on this first component. The second component of the Forward Agreement provides the Fund with the net economic performance of the Mortgage Trust which is primarily invested in cash and cash equivalents and the Mortgage Portfolio. In highly simplified terms this relationship between the Common Share Basket, the Forward Agreement and the Mortgage Trust (which maintains the Mortgage Portfolio) can be expressed as follows: Common Share Basket + Forward Agreement = Economic Performance of the Mortgage Trust (before consideration of any forward fees and other related costs).

The Common Share Basket is comprised of the following securities:

		December 31, 2102	
Investments	**Shares**	**Average Cost**	**Fair Value**
Legacy Oil	638,200	$4,326,996	$4,352,524
New Gold Inc.	414,500	4,327,380	4,534,630
Martinrea International	554,200	4,350,470	4,278,424
Paramount Resources	133,100	4,327,081	4,249,883
Open Text	77,300	4,327,254	4,274,690
Osisko Mining	586,200	4,402,362	4,654,428
Tourmaline Oil	142,456	4,326,389	4,434,655
Tahoe Resources	249,801	4,349,035	4,541,382
Athabasca Oil	396,300	4,327,596	4,133,409
Catamaran Corp	88,300	4,323,168	4,104,184
CGI Group	176,500	4,326,015	4,045,380
Lundin Mining	849,560	4,341,252	4,324,261
		$52,054,998	$51,927,850

The unrealized loss on revaluation of the common share basket is $127,148 as at December 31, 2012. There were no realized gains or losses on the common share basket in the period ended December 31, 2012.

4. UNITHOLDERS' EQUITY

(a) Unitholders' capital

Authorized units:

Unitholders capital comprises an unlimited number of Class A and Class H units (together "Fund Units").

The Fund is authorized to issue an unlimited number of units of an unlimited number of Classes, each of which represents an equal, undivided beneficial interest in the net assets of the Fund attributable to that Class. Commencing no earlier than 120 days after the initial issuance of Class A Units, a holder of Class H Units may convert Class H Units into Class A Units in any month on the second last Business Day of each month (the "Conversion Date") by delivering a notice to the Trustee and surrendering such Class H Units by 5:00 p.m. (Toronto time) at least 10 Business Days prior to the Conversion Date. For each Class H Unit so converted, a holder will receive that number of Class A Units that is equal to the NAV per Class H Unit as of the close of trading on the Conversion Date divided by the NAV per Class A Unit as of the close of trading on the Conversion Date. No fractions of Class A Units will be issued upon any conversion of Class H Units.

Outstanding Units:

The following is a continuity of the unitholders capital of the Fund:

	Class A Units	Class H Units
Issued on initial declaration	1	—
Redeemed on the public offering	(1)	—
Issued on public offering	4,600,000	920,000
As at December 31, 2012	4,600,000	920,000

5. FEES, OPERATING EXPENSES AND MORTGAGE PURCHASES

Management fees

Pursuant to the terms of the Management Agreement, the Fund pays the Manager an annual management fee of 0.40% of the Net Asset Value of the Fund ("Net Asset Value") [plus applicable taxes]. For the period ended December 31, 2012, the Fund expensed $7,734 in management fees including applicable taxes. As at December 31, 2012, $7,734 including applicable taxes in management fees was due to the Manager.

Servicing fees

The Manager collects from the Fund and pays to registered dealers, a servicing fee (calculated and paid at the end of each calendar quarter) equal to 0.40% annually of the Net Asset Value of the Fund.

Counterparty fees

The counterparty charges the Fund for its services in the execution of the Forward Agreement. The counterparty fee under the Forward Agreement is a fee not greater than 0.45% annually on the total assets plus a fee, which may vary, based on the value of the Common Share Basket, payable monthly in arrears. The latter fee is intended to compensate the counterparty for the costs of hedging its exposure under the Forward Agreement and is anticipated to be no greater than 0.30% annually.

Reimbursement of operating costs

The Fund also reimburses the Manager for costs, expenses and liabilities incurred by the Manager on behalf of the Fund including, but not limited to, third party expenses and recovery of allocated salaries. Given the short period of operation for the period ended December 31, 2012, the Fund did not expense any amount for the recovery of mortgage administration costs.

Mortgage purchases

The Mortgage Trust purchases mortgages receivable from the Mortgage Advisor. The Mortgage Advisor may, as part of selecting mortgages for the Mortgage Trust, "prefund" or bridge the mortgage funding and register the mortgage with the Mortgage Trust's custodian, remaining as beneficial owner prior to formal submission to the Mortgage Trust. The mortgage receivables of the Mortgage Trust as at December 31, 2012 were all bridged by the Mortgage Advisor prior to sale to the Mortgage Trust with an effective date of December 31, 2012. The Fund's independent review committee approved the sale of these mortgage receivables to the Mortgage Trust.

6. FINANCIAL INSTRUMENTS

The Fund has classified the significant impacts of its financial instruments as follows:

(a) Financial instruments – carrying values and fair values:

The Fund's investments which include cash and cash equivalents, common share basket and the financial agreement are carried at fair value. The accounts payable and accrued liabilities are classified as other liabilities and carried at amortized cost.

(b) Fair value measurement:

The Fund uses a fair value hierarchy to categorize the inputs used in its valuation of assets and liabilities carried at fair value. The Fund uses unadjusted quoted market prices (Level 1), models using observable market information as inputs (Level 2) and models using unobservable market information (Level 3) in its valuation of assets and liabilities carried at fair value. As at December 31, 2012, cash and the common stock basket were measured with Level 1 support and the Forward Agreement was measured using Level 3 inputs. There were no transfers during the period ended December 31, 2012 between levels.

(c) Changes in fair value measurement for instruments categorized in Level 3

The following table presents the changes in fair value measurements for instruments included in Level 3 of the fair value hierarchy set out in Section 3862 of the CICA Handbook as described in Note 1:

	Opening Fair value	**Investments**	**Unrealized gain recorded in income**	**Payment and amortization**	**Fair value as at December 31, 2012**
	$	$	$	$	$
Financial assets					
Forward Agreement	—	—	**88,831**	—	**88,831**

There have been no transfers between categories during the years ended December 31, 2012.

7. RISK MANAGEMENT AND CAPITAL MANAGEMENT

In the normal course of business the Fund is exposed to a variety of financial risks: credit risk, interest rate risk, credit risk, liquidity risk and market risk. The Fund is not exposed to any currency risk.

Credit risk

Credit risk is the risk of loss associated with a counterparty's inability or unwillingness to fulfill its payment obligations. The Fund's credit risk is mainly related to the value of the Forward Agreement. The Fund mitigates credit risk by dealing with a large reputable schedule one bank for its counterparty on the Forward Agreement. Although the common share basket is susceptible to some credit risk, this risk is mitigated fully in the Forward Agreement which puts this exposure onto the counterparty. The exposure obtained by the Fund through the Forward agreement is to mortgages receivable owned by the Mortgage Trust. The mortgage receivables' credit risk is mainly lending-related in the form of mortgage default. The Mortgage Trust uses stringent underwriting criteria and experienced adjudicators to mitigate this risk. The Mortgage Trust's approach to managing credit risk is based on the consistent application of a detailed set of credit policies and prudent arrears management. The maximum credit exposures of the financial assets are their carrying values as reflected on the statement of net assets. The Mortgage Trust does not have significant concentration of credit risk within any particular geographic region or group of customers.

The Mortgage Trust is at risk that the underlying mortgages default and the servicing cash flows cease. While the current portfolio of individual mortgages is small, the real estate that underlies these assets is diverse in terms of geographical location, borrower exposure and the underlying type of real estate. This and the priority ranking of the Company's rights mitigate the potential size of any single credit loss.

Interest rate risk

Interest rate risk arises when changes in interest rates affect the fair value of financial instruments. The Fund is exposed to interest rate risk to the extent that the value of the Forward Agreement relies on the valuation of the Mortgage Portfolio in the Mortgage Trust. The mortgages in the portfolio are valued at fair value. As interest rates change, the value of the portion of the portfolio that consists of fixed rate mortgages may vary. Typically, as interest rates rise, the value of fixed rate mortgages decrease. The Mortgage Trust's mortgages may not vary directly with changes in interest rates due to their somewhat unusual (mezzanine) nature. The Fund is also exposed to interest rate risk to the extent that significant amounts of cash at the Mortgage Trust level are not invested in mortgages but instead invested in cash or cash equivalents that earn floating rates of interest. As at December 31, 2012, the Mortgage Trust had $29,201,949 of its capital invested in cash and cash equivalents.

The Mortgage Portfolio is not particularly sensitive to small changes in risk-free interest rates and, generally, the Mortgage Portfolio is more sensitive to changes in credit spreads. Management has designed internal valuation models which rely on significant unobservable inputs and management estimates including interest rate and credit spread assumptions. These valuation models indicate that a 1% increase or decrease in combined interest rates and credit spreads will not have any significant affect on the fair value of the Mortgage Portfolio. Changes in excess of a 1% change will increase/decrease the value portfolio by approximately $170,000 for every 1% increment in interest rates.

Liquidity risk

Liquidity risk is the risk that the Fund will be unable to meet its financial obligations as they come due.

The mortgages receivable which comprise the mortgage portfolio are illiquid and have maturities of up to 24 months in the future. The Fund manages liquidity risk under normal operating activities by ensuring sufficient cash flow from fees and interest is generated to cover expenses and distributions. Generally the mortgage portfolio has a relative short maturity duration and maturities will be spread out within a three year period.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates and credit spreads. The level of market risk to which the Fund is exposed varies depending on market conditions, expectations of future interest rates and credit spreads. As the mortgages in the Mortgage Trust typically rely on the development of the underlying real estate by the borrower in order to qualify for traditional mortgage financing, the portfolio is exposed to all the market risks associated with the market for commercial real estate in Canada.

8. SUBSEQUENT EVENT

On January 10, 2013, pursuant to the over-allotment option associated with its initial public offering, an additional 290,000 units were issued for net proceeds of $2,704,250.