Fundamental Research Corp.

Investment Analysis for Intelligent Investors

December 7, 2021

Frontenac Mortgage Investment Corp.

Yield Improves / Reduces Exposure to Impaired Mortgages

Expected Yield (2022): 5.3%
Rating*: 2-
Risk*: 2

Sector / Industry: Mortgage Investment Corporations

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Highlights

- **At the end of Q3-2021, mortgage receivables grew 9% YTD, to $175M.** The MIC had $20M in undeployed capital. Management expects to ramp up lending in Q4, and deploy most of the unused capital in the quarter.
- Remains focused on first mortgages in Ontario, reflecting management's mandate to operate a lower-risk portfolio.
- Over the past few years, the MIC has **raised its average lending rate** by increasing focus on residential properties under construction/development (a higher risk-segment vs already-built properties). As a result, yields increased to 5.44% in 2021 (9M) vs 5.17% in 2020 (12 months). We are expecting yields to be in the 5.3%-5.4% range in 2021 and 2022.
- We believe the **portfolio's risk profile has declined**, due to a significant drop in past-due/impaired mortgages, from $23M (14% of the portfolio) at the end of 2020, to just $2.5M (1.5% of the portfolio) as of December 2021. No realized losses this year. **We consider this to be a major accomplishment by management.**
- Interest rates are expected to remain low over the next six months, and we expect **investors' appetite for high-yield investments (such as Frontenac) to remain strong**.
- Residential real estate transactions have cooled slightly in the past few months. Although the CMHC has a high-risk rating (for market vulnerability) for Toronto, and a low-risk rating for Vancouver, they have assigned a low-risk rating for 'overvaluation' to both cities. The Federal government has proposed initiatives to cool the housing market, while being pro-immigration. We maintain a positive outlook on the residential real estate market. Although the emergence of Omicron has increased uncertainties, we are **expecting a surge in new immigrants and international students** once conditions normalize. Note that Canada is one of the most highly vaccinated countries in the world, and one of the most preferred destinations for immigrations**.**

Sid Rajeev, B.Tech, CFA, MBA
Head of Research

Offering Summary	
Issuer	Frontenac Mortgage Investment Corporation
Securities Offered	Common Shares
Unit Price	NAV
Minimum Subscription	$5,000
Distribution to Investors	Monthly
Redemption	Quarterly
Management Fee	2% of the AUM
Sales Commissions	N/A
Auditor	MNP LLP

*Unlike most private MICs, Frontenac's units are offered by prospectus, which we believe provides more transparency and regulatory oversight

Financial Summary	2017	2018	2019	2020	2021E	2022E
Mortgage Receivables (net)	$189,980,578	$180,967,671	$173,315,185	$160,810,418	$190,000,000	$210,000,000
Debt as % of Mortgage Outstanding	8.8%	7.7%	6.5%	0.0%	0.0%	3.1%
Revenues	$16,178,501	$18,134,892	$15,810,099	$15,086,513	$15,260,253	$17,000,000
Net Income	$8,346,668	$11,332,989	$9,656,983	$9,136,321	$10,128,348	$11,037,208
Investors' Returns (% of Invested Capital)	5.0%	5.6%	5.5%	5.3%	5.4%	5.3%

***See last page for important disclosures, rating and risk definitions. All figures in C$ unless otherwise specified.**

In a study conducted for the Canada Mortgage Housing Corporation/CMHC, we estimated that Assets Under Management ("AUM"), held by MICs across the country, grew 3% YoY to $13.2B by the end of 2020, versus 7% growth in residential mortgages nationwide. At the end of 2020, MICs accounted for 0.80% of total outstanding residential mortgages in Canada ($1.6T).

The following table shows how Frontenac's portfolio compares to its direct comparables (lenders focused on mortgages on single-family residential units). All these entities have over $100M in assets, with mortgages focused almost exclusively on individual borrowers.

Frontenac has higher exposure to first mortgages, and therefore, has a lower risk-profile and yield

Frontenac does not use leverage to enhance returns

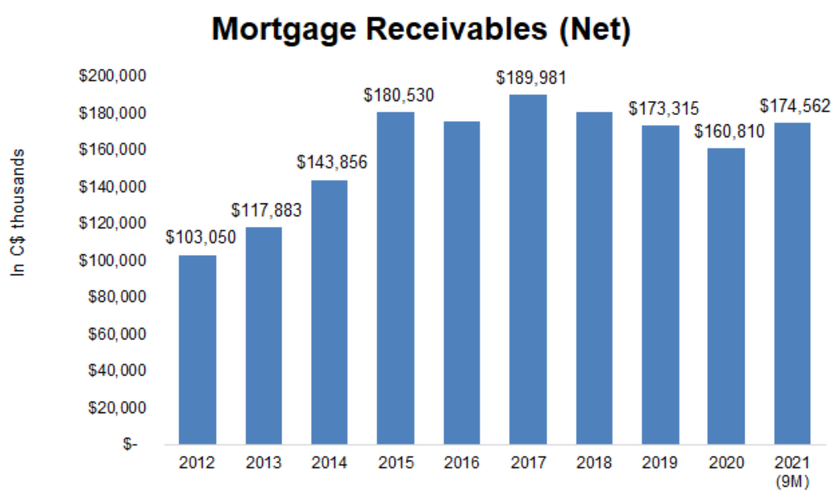
Focused on rural areas/suburban communities in ON

	Frontenac	Average
First Mortgage	99.9%	81%
B.C.	0%	36%
ON	99.9%	49%
AB	0%	8%
Others	0.1%	7%
LTV	N/A	58%
Yield	5.4%	6.9%
Debt to Capital	0%	17%
Average Loan Size	$420,630	$512,666
Actual Loss	0%	0.2%
Provision	2.3%	0.6%

Source: FRC / Various

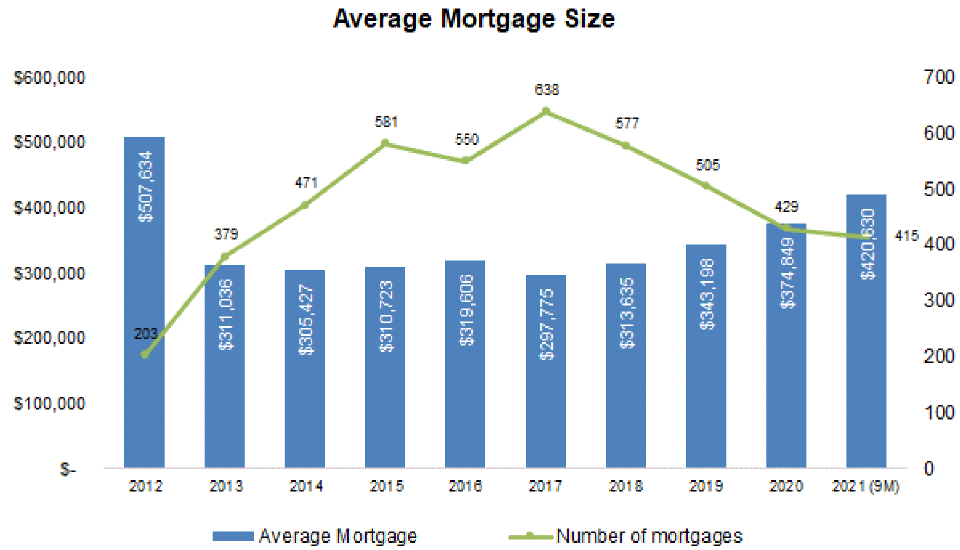
Portfolio Update

Mortgage receivables were up 9% YTD, to $175M by the end of Q3



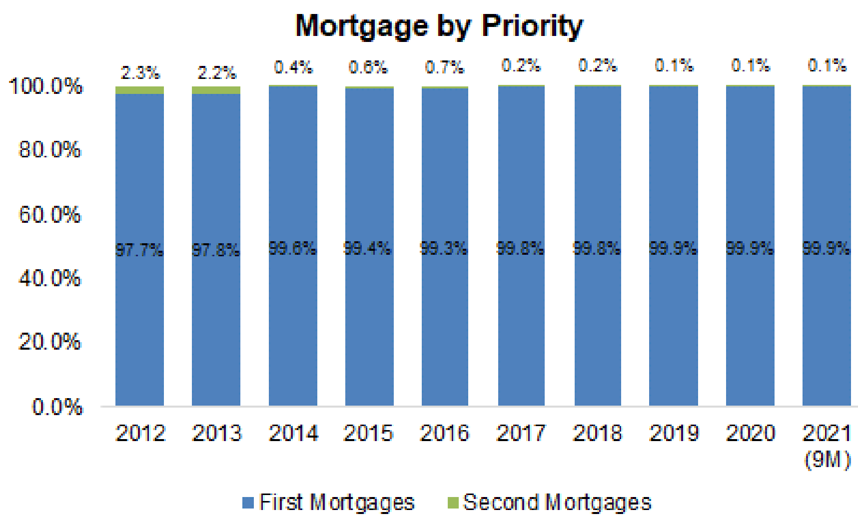
Source: Company / FRC

Average mortgage size increasing (up 12% YTD), but remains below the comparables average due to Frontenac's focus on rural/suburban communities



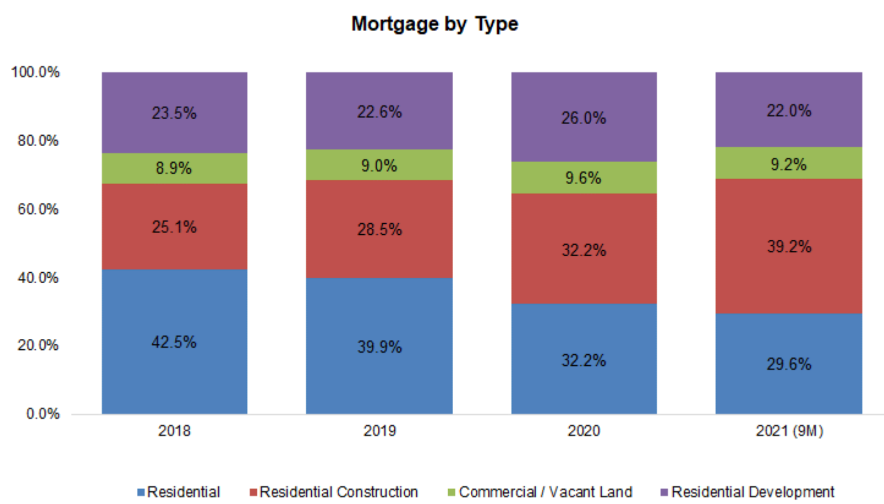
Remains focused on first mortgages, implying management's low risk tolerance

Exposure to residential properties remained relatively flat at 90%



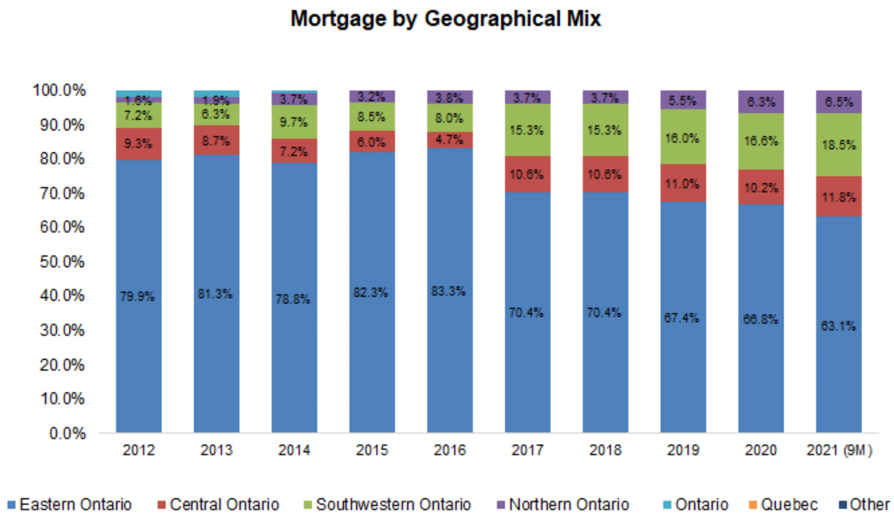
Increasing exposure to residential construction, while reducing exposure to developments and already-built properties

Construction refers to mortgages held by individuals or small developers; management expects to continue lowering exposure to developments (which comprise of larger development projects), which tend to be higher-risk

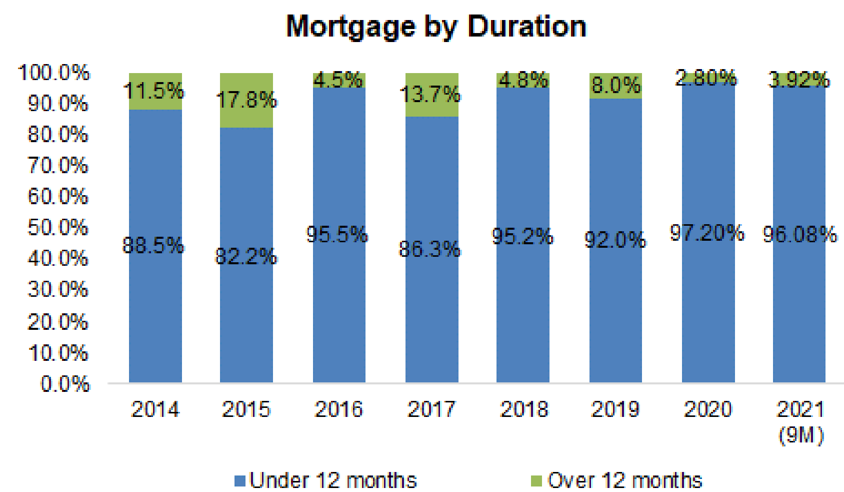


Source: Company / FRC

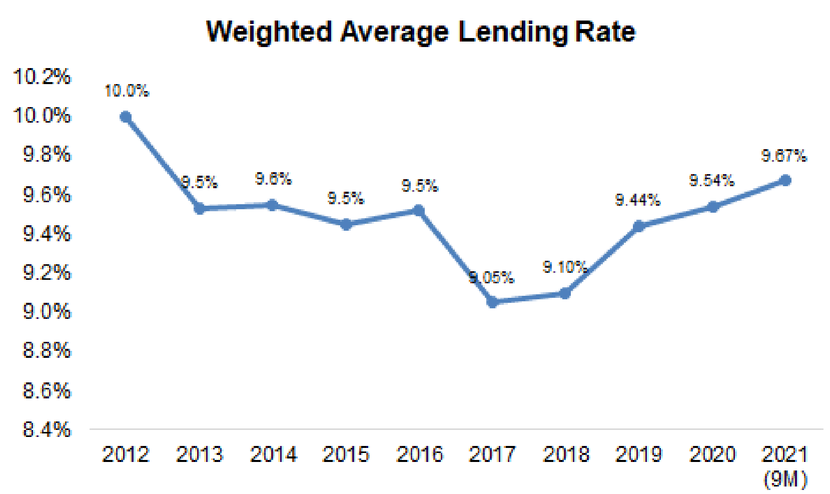
Almost exclusively focused on Ontario; however, the MIC has been diversifying within the province, which is highly encouraging



Duration remains low, as most of the mortgages are due within 12 months; we note that low duration typically implies lower risk



Despite lower market rates, the MIC was able to raise lending rates by increasing exposure to construction mortgages



Source: Company / FRC

No realized losses in 2021

Stage three (impaired) mortgages declined YTD (from 10.6% to 7.3%); subsequent to Q3, stage three declined further to $2.5M (from sales of impaired properties), or 1.5% of mortgage receivables

The MIC has started allowing redemptions once a quarter (previously once a year), which we believe is an attractive feature for investors

	2017	2018	2019	2020	9M-2021
Actual Losses					
Actual Losses	1,071,232	1,142,691	1,238,987	572,776	-
Actual Losses (% of mortgage receivable)	0.59%	0.62%	0.70%	0.34%	0.00%
Distributions	$9,362,668	$10,207,989	$9,656,983	$9,136,319	$7,541,189
Reinvested	$5,182,391	$5,631,065	$5,767,877	$4,314,616	$2,739,142
Reinvested (as a % of Distributions)	55%	55%	60%	47%	36%
Redemptions	$18,459,102	$35,192,790	$34,873,262	$20,450,731	$292,443
Redemption (% of invested capital)	10%	19%	20%	12%	0%
Stage 3			$18,155,907	$17,060,635	$12,806,352
% of Receivable	0.00%	0.00%	10.29%	10.37%	7.17%
Loan Loss Provision	$2,817,427	$738,184	$1,292,201	$1,071,835	$31,569
Loan loss provision (year/quarter ended)	$3,500,195	$3,095,688	$3,148,902	$3,647,961	$4,052,561
Provision % of Receivable	1.84%	1.71%	1.82%	2.27%	2.32%

Past Due / Not Impaired as a % of Mortg Receivable	2018	2019	2020	9M-2021
1 - 30 days	1.54%	1.50%	1.57%	0.28%
31 - 90 days	0.68%	1.30%	0.42%	0.00%
90+ days	0.45%	0.46%	1.67%	0.40%
Total	**2.67%**	**3.26%**	**3.66%**	**0.70%**
Past Due and Impaired	**2018**	**2019**	**2020**	**9M-2021**
#	27	16	9	6
Amount	$22,043,064	$18,155,907	$17,060,636	$12,806,352
% of Mortgage Recivable	12.2%	10.5%	10.6%	7.3%
FV of Collateral	$29,443,500	$21,317,000	$21,026,722	$14,563,000
LTV	74.9%	85.2%	81.1%	87.9%
Past Due and Impaired	**2018**	**2019**	**2020**	**9M-2021**
Commercial	$537,996	$0	$0	$0
Residential	$3,615,332	$2,635,674	$3,012,161	$2,328,922
Residential Construction	$813,584	$339,699	$148,790	
Residential Development	$16,142,873	$14,475,541	$13,713,369	$10,285,761
Vacant Land	$933,278	$704,993	$186,315	$191,669
	$22,043,063	**$18,155,907**	**$17,060,635**	**$12,806,352**
Total Past Due	$26,870,991	$23,807,538	$22,944,325	$13,988,199
% of Mortgage Recivable	14.8%	13.7%	14.3%	8.0%

Source: Company / FRC

The MIC had $20M in undeployed capital at the end of Q3; management has indicated that they have a robust pipeline to deploy most of the unused capital in Q4

Debt to capital was nil; we note that comparable MICs tend to use leverage (typically 20% debt to capital) to enhance yields

Frontenac's focus on first mortgages, and maintaining low debt-levels reflect management's mandate to operate a low-risk portfolio

Balance Sheet	2017	2018	2019	2020	Q3-2021
Assets					
Cash	$0	$45,324	$56,779	$1,142,552	$20,291,660
Due from Administrator in Trust	$574,788	$120,053	$658,402	$73,878	$270,872
Interest Receivable	$10,251,803	$11,194,987	$12,240,090	$10,257,696	$9,756,706
Prepaid Expense	$16,200	$16,200	$16,200	$16,200	$25,115
Mortgage Investments (net)	$189,980,578	$180,967,671	$173,315,185	$160,810,418	$174,561,536
	$200,823,369	**$192,344,235**	**$186,286,656**	**$172,300,744**	**$204,905,889**
Liabilities					
LOC	$16,580,000	$13,880,000	$11,330,000		
Bank Debt	$79,627				
Payable	$621,514	$508,161	$324,490	$611,993	$668,254
Prepaid Mortgage Payments	$316,111	$168,609	$101,614	$47,279	$143,465
	$17,597,252	$14,556,770	$11,756,104	$659,272	$811,719
Net Asset	$183,226,117	$177,787,465	$174,530,552	$171,641,472	$204,094,170
SE + Liabilities	**$200,823,369**	**$192,344,235**	**$186,286,656**	**$172,300,744**	**$204,905,889**
Debt to Capital	8.3%	7.2%	6.1%	0.0%	0.0%
Debt as a % of Mortgage Outstanding	8.8%	7.7%	6.5%	0.0%	0.0%
Interest Coverage Ratio	154.5	17.0	78.4	105.3	9486.8

Source: Company / FRC

In summary, we believe the portfolio's risk profile has declined (despite equal number of green and red signals), due to the significant decrease in past-due/impaired mortgages

Parameter	Risk Profile
Undeployed Capital	↑
Average Mortgage	↑
Diversification	↑
Priority	-
LTV	n/a
Property Type (lower-risk properties)	↓
Default	↓
Debt to Capital	↓

- red (green) indicates an increase (decrease) in risk level

Source: FRC

Financials

2021 (9M) revenue was flat YoY, but net income increased 10% due to lower loan loss provisions

Income Statement	2018	2019	2020	9M-2020	9M-2021	YoY
Revenues						
Interest Income	$18,134,892	$15,810,099	$15,086,513	$11,308,562	$11,275,521	
	$18,134,892	**$15,810,099**	**$15,086,513**	**$11,308,562**	**$11,275,521**	**0%**
Expenses						
G&A	$747,488	$618,686	$910,688	$750,482	$662,957	
Management Fees	$4,608,592	$4,117,383	$3,880,095	$2,906,016	$3,039,011	
Loan Loss Provision	$738,184	$1,292,201	$1,071,835	$724,279	$31,569	
Interest on Loan Payable	$707,639	$124,846	$87,574	$81,708	$795	
	$6,801,903	**$6,153,116**	**$5,950,192**	**$4,462,485**	**$3,734,332**	**-16%**
Net Income	**$11,332,989**	**$9,656,983**	**$9,136,321**	**$6,846,077**	**$7,541,189**	**10%**
Dividends	$10,207,989	$9,656,983	$9,136,319	$6,846,077	$7,541,189	**10%**
Net Asset Value	$30.000	$30.000	$30.000	$30.000	$30.000	**0%**
Shares Outstanding	5,926,249	5,817,686	5,721,384	6,150,049	6,803,141	**11%**

As a result, net income as a percentage of invested capital increased

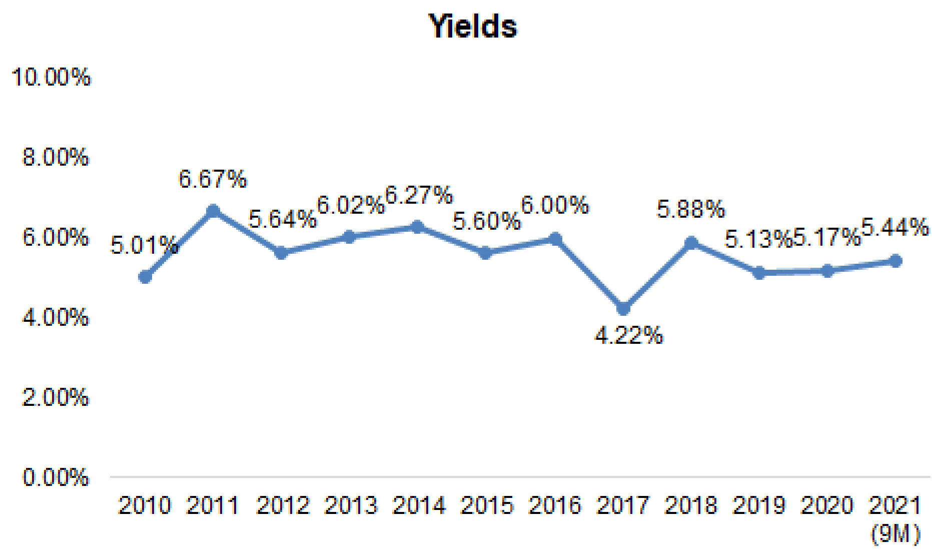
% of Mortgage Receivable	2018	2019	2020	9M-2021*
Interest Income	9.78%	8.93%	9.03%	8.97%
Interest Income + Others	**9.78%**	**8.93%**	**9.03%**	**8.97%**
Less:				
Management Fee	-2.48%	-2.32%	-2.32%	-2.42%
G&A Expenses	-0.40%	-0.35%	-0.55%	-0.53%
Loan Loss Provisions	-0.40%	-0.73%	-0.64%	-0.03%
Interest	-0.38%	-0.07%	-0.05%	0.00%
Net	6.11%	5.45%	5.47%	6.00%
Investors' Returns (% of Invested Capital)	**5.64%**	**5.48%**	**5.28%**	**5.35%**

** annualized*

Note that the above figures may be slightly different from the figures reported by Frontenac 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.

Source: Company / FRC

Yields increased to 5.44% in 2021 (9M) vs 5.17% in 2020 (12 months)



Source: Manager

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.
- Shareholders' principal is not guaranteed, as the NAV per share could decrease from current levels (as a result of loan losses). Shareholders are also not guaranteed minimum distributions.
- Key person risk - Matthew Robinson (CEO) controls 100% of the voting shares of the Manager and the Administrator. However, the MIC has the right to appoint a new Manager and Administrator. Shares held by investors of the MIC have voting rights.
- Although the MIC's primary focus is on first mortgages, it may invest in second mortgages (up to a maximum of 10%) which carry higher risk.

FRC Projections and Rating

We are expecting yields to be in the 5.3%-5.4% range

Financial Summary	2017	2018	2019	2020	2021E	2022E
Mortgage Receivables (net)	$189,980,578	$180,967,671	$173,315,185	$160,810,418	$190,000,000	$210,000,000
Debt as % of Mortgage Outstanding	8.8%	7.7%	6.5%	0.0%	0.0%	3.1%
Revenues	$16,178,501	$18,134,892	$15,810,099	$15,086,513	$15,260,253	$17,000,000
Net Income	$8,346,668	$11,332,989	$9,656,983	$9,136,321	$10,128,348	$11,037,208
Investors' Returns (% of Invested Capital)	5.0%	5.6%	5.5%	5.3%	5.4%	5.3%

Source: FRC

As a result of the steep decline in impaired mortgages, we are raising our overall rating from 3+ to 2-, while maintaining our risk rating at 2. As interest rates are expected to remain low over the next six months, we expect investors' appetite for high-yield investments (such as Frontenac) to remain strong.

FRC Rating	
Expected Yield (2022)	5.30%
Rating	2-
Risk	2

APPENDIX

Income Statement	2018	2019	2020	2021E	2022E
Revenues					
Interest Income	$18,134,892	$15,810,099	$15,086,513	$15,260,253	$17,000,000
	$18,134,892	**$15,810,099**	**$15,086,513**	**$15,260,253**	**$17,000,000**
Expenses					
G&A	$747,488	$618,686	$910,688	$912,107	$1,000,000
Management Fees	$4,608,592	$4,117,383	$3,880,095	$4,073,850	$4,600,000
Loan Loss Provision	$738,184	$1,292,201	$1,071,835	$145,948	$200,000
Interest on Loan Payable	$707,639	$124,846	$87,574	$0	$162,792
	$6,801,903	**$6,153,116**	**$5,950,192**	**$5,131,905**	**$5,962,792**
Net Income	**$11,332,989**	**$9,656,983**	**$9,136,321**	**$10,128,348**	**$11,037,208**
Dividends	$10,207,989	$9,656,983	$9,136,319	$10,128,348	$11,037,208
Net Asset Value	$30.000	$30.000	$30.000	$30.000	$30.000
Shares Outstanding	5,926,249	5,817,686	5,721,384	6,803,141	7,136,474

Balance Sheet	2018	2019	2020	2021E	2022E
Assets					
Cash	$45,324	$56,779	$1,142,552	$3,956,102	$0
Due from Administrator in Trust	$120,053	$658,402	$73,878	$73,878	$73,878
Interest Receivable	$11,194,987	$12,240,090	$10,257,696	$10,770,581	$11,309,110
Prepaid Expense	$16,200	$16,200	$16,200	$17,820	$19,602
Mortgage Investments (net)	$180,967,671	$173,315,185	$160,810,418	$190,000,000	$210,000,000
	$192,344,235	**$186,286,656**	**$172,300,744**	**$204,818,381**	**$221,402,590**
Liabilities					
LOC	$13,880,000	$11,330,000		$0	$6,511,689
Bank Debt					
Payable	$508,161	$324,490	$611,993	$673,192	$740,512
Prepaid Mortgage Payments	$168,609	$101,614	$47,279	$52,007	$57,208
	$14,556,770	$11,756,104	$659,272	$725,199	$7,309,408
Net Asset	$177,787,465	$174,530,552	$171,641,472	$204,093,182	$214,093,182
SE + Liabilities	**$192,344,235**	**$186,286,656**	**$172,300,744**	**$204,818,381**	**$221,402,590**
Debt to Capital	7.2%	6.1%	0.0%	0.0%	3.0%
Debt as a % of Mortgage Outstanding	7.7%	6.5%	0.0%	0.0%	3.1%

Cash Flow Statement	2021E	2022E
Operating Activities		
Net Income	$10,128,348	$11,037,208
Loan Loss Provision		
	$10,128,348	$11,037,208
Chnges in non-cash Working Capital		
Accounts Receivable	-$1,620	-$1,782
Accounts Payable and Accured Liabilities	$65,927	$72,520
Interest Payable	-$512,885	-$538,529
	-$448,578	-$467,791
Cash from Operating Activities	**$9,679,770**	**$10,569,417**
Investing Activities		
Net Puchase of Mortgage Investments	-$29,189,582	-$20,000,000
Cash from Investing Activities	**-$29,189,582**	**-$20,000,000**
Financing Activities		
Debt	$0	$6,511,689
Distribution	-$10,128,348	-$11,037,208
Distribution to Manager		
Cash Received on Subscription	$32,451,710	$10,000,000
Cash from Financing Activities	**$22,323,362**	**$5,474,481**
Net Change in Cash	**$2,813,550**	**-$3,956,102**

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	30%	Risk - 2	8%
Rating - 3	47%	Risk - 3	40%
Rating - 4	9%	Risk - 4	34%
Rating - 5	4%	Risk - 5	8%
Rating - 6	1%	Suspended	10%
Rating - 7	0%		
Suspended	10%		

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