



For the three months ended March 31, 2008

A growth-oriented income trust, Carfinco focuses on providing consumer car loans to borrowers unable to obtain financing through traditional lending sources. A network of select independent and franchise dealerships offer Carfinco's payment plan to their customers who must, along with the vehicle, meet Carfinco's underwriting guidelines. The units of the Fund trade on The Toronto Stock Exchange under the symbol CFN.UN.

## TO OUR UNITHOLDERS

During the first quarter of 2008, significant growth and high demand – particularly from online portals – are presenting some unique accounting challenges for Carfinco in terms of net earnings and book equity. Nonetheless, we are very pleased with the Fund's performance in terms of loan originations, revenue and finance receivables, and we are addressing the challenges that have come with this growth to ensure optimal value creation for our unitholders over the long term.

Carfinco achieved record loan originations in the first quarter of \$20.0 million, an increase of 57.7% from \$12.7 million for the first quarter of 2007, and an increase of 4.8% over the fourth quarter of 2007. These results reflect increasing business from the online portals.

At quarter end, finance receivables were \$100.2 million versus \$73.4 million one year ago, an increase of 36.5%. First quarter revenues were \$7.6 million, up 30.7% compared to \$5.8 million in the first quarter of 2007, continuing Carfinco's quarterly growth momentum, with an increase of 3.7% versus Q4 2007. Prior to non-cash expenses, for loss on derivatives and increases in the allowance for credit losses, earnings for the quarter were \$1.3 million compared to \$1.7 million for the first quarter last year.

Carfinco's growth strategy requires equity to leverage the utilization of the bank credit facility. During the first quarter of 2008, the increased loan originations, primarily in the Fund's regular program, accelerated finance receivable growth. Although the Fund's Regular Program incurs the lowest losses of all its programs, it requires the highest allowance for credit losses. In the first quarter, the allowance for credit losses was increased by a non-cash expense of \$2.2 million recorded through the provision for credit losses versus a decrease of \$97,700 in Q1 2007. Also during the first quarter, a non-cash expense of \$532,789 was recorded for "loss on derivatives" versus nil for Q1 2007. Furthermore, the Fund entered into a swap agreement in August 2007, fixing the interest rate on \$10 million of the outstanding debt facility for three years and \$10 million for five years. These two non-cash items have negatively affected the Fund's net earnings and book equity. As a result, net loss for the quarter was \$1.4 million both basic and diluted.

At the end of the first quarter, the Fund's Board of Trustees unanimously approved changing the Fund's distribution policy to maximize the retention of operating cash flow. The Board believes that it is in the best interests of the Fund to meet its equity requirements through the retention of operating cash flow for at least the next two quarters and issue units in lieu of cash to distribute all, if any, of the Fund's taxable income to its Unitholders. As a result, Carfinco's monthly cash distribution per trust unit will be replaced with a quarterly "in-kind" unit distribution to distribute the Fund's taxable income to its Unitholders. Carfinco anticipates that the next announcement on distribution of taxable income will be on or about June 10 and be payable on June 30, 2008.



During the first quarter, Carfinco announced its credit facility had been increased to \$85 million and that Bank of Montreal joined BoS (USA) Inc. and Bank of America, N.A. as senior lenders of Carfinco. This initiative further diversifies Carfinco's credit facility, and gives the Fund the ability to maintain its current growth rate.

Operationally, the Fund is currently experiencing several short-term challenges, which Management has been actively addressing by implementing changes to both loan origination policies and collection procedures. The challenges include, reduced recovery amounts on repossessed vehicles as a percentage of the principal outstanding on the loan. This is due to lower auction values and the timing of adjustments to Black Book pricing (which dictates the maximum amount the Fund will loan using the vehicle as security). Also affecting higher losses was a rise in delinquencies during Q4 2007 and Q1 2008. During Q2 2008, the delinquencies have decreased, becoming more comparable with historical levels. The higher losses will continue into Q2 2008, as the delinquencies from the previous two quarters flows through the system.

Also during the quarter, Carfinco continued to introduce GPS and "Starter Interrupt" technology to vehicles in its GO Plan. This creates the ability to communicate directly with customers in the vehicle, and provides a significant deterrent to delinquency, which is expected to positively impact portfolio aging over the long term.

Clearly, 2008 is going to be a challenging year for Carfinco as we work through certain growing pains to ensure sustainable value creation. We continue to have proven expertise, a leadership position in our niche, tremendous growth momentum, and are committed to realizing Carfinco's high potential. In the meantime we appreciate the support and patience of our valued unitholders.

Sincerely,

Tracy Graf  
Chief Executive Officer



## MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management's Discussion and Analysis of Carfinco Income Fund (the "Fund") should be read in conjunction with the Fund's audited consolidated financial statements for the years ended December 31, 2007 and 2006, and the accompanying notes to those consolidated financial statements contained in the 2007 Annual Report.

This analysis has been prepared taking into consideration information available to May 15, 2008.

This report contains certain forward-looking statements that involve a number of known and unknown risks, uncertainties and other factors that may cause actual results of events to differ materially from those anticipated in our forward-looking statements.

### OVERVIEW

Carfinco Income Fund is an unincorporated open-end mutual fund trust established under the laws of Ontario by a Deed of Trust made as of August 26, 2002, as amended and restated on April 23, 2004. The Fund owns 100% of Carfinco Holdings Trust, a wholly owned unincorporated trust, established under the laws of Ontario, and 100% of Carfinco Inc., a wholly owned subsidiary, established under the laws of Ontario. Carfinco Holdings Trust holds a 92.39% interest in Carfinco Limited Partnership, and Carfinco Inc. ("Carfinco") holds the remaining 7.61% interest, and is the general partner of Carfinco Limited Partnership. The Fund trades its trust units on The Toronto Stock Exchange under the symbol "CFN.UN."

The Fund, through Carfinco Limited Partnership, purchases loans, originated by select independent and franchise vehicle dealers to consumers buying late-model used automobiles. The Fund targets borrowers who are typically unable to obtain financing from traditional sources.

To fund the acquisition of receivables, the Fund uses its borrowings under its credit facility, and the issuance of debt and equity. The Fund generates interest and fee income on its finance receivables and pays interest expense on borrowings under its credit facility and on outstanding subordinated debentures.

### RECENT EVENTS

On May 15, 2008, the Fund executed the First Amendment to the Amended and Restated Credit Agreement, dated February 13, 2008. Certain terms within the agreement were modified.

On March 31, 2008, the Fund announced a change in the Fund's distribution policy to maximize the retention of operating cash flow. Carfinco's current monthly cash distribution of \$0.027 per trust unit will be replaced with a quarterly "in-kind" unit distribution.

On February 13, 2008, the Fund executed an Amended and Restated Credit Facility. The maximum advance available increased from \$65,000,000 to \$85,000,000, and the maturity date of the credit facility was extended to February 13, 2009. The syndication of lenders increased with the addition of the Bank of Montreal to the existing lenders, BoS (USA) Inc. and the Bank of America, N.A.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### SELECTED ANNUAL INFORMATION AND KEY FINANCIAL RATIOS

(OOOs FOR STATED VALUES, EXCEPT PERCENTAGES AND PER FUND UNIT AMOUNTS)	MARCH 31 2008	MARCH 31 2007
Total revenue (for the three months ended)	\$ 7,576	\$ 5,795
Net (loss) earnings (for the three months ended)	\$ (1,396)	\$ 1,624
Earnings (loss) per fund unit – basic and diluted (for the three months ended)	\$ (0.06)	\$ 0.08
Total assets	\$ 90,836	\$ 68,364
Finance receivables	\$ 100,181	\$ 73,408
Funds advanced on finance receivables (for the three months ended)	\$ 17,889	\$ 11,520
Loan originations	\$ 19,982	\$ 12,668
Allowance for credit losses and dealer reserve	\$ 10,587	\$ 6,050
Allowance and reserve as a percentage of finance receivables	10.6%	8.2%
Bank credit facility	\$ 66,416	\$ 48,217
Unitholders' equity	\$ 20,865	\$ 16,655
Fund units outstanding	23,323	20,528
Book value per fund unit	\$ 0.90	\$ 0.81
Financial leverage ratio	3.16:1	3.10:1
Return on unitholders' equity (annualized)	(24.8)%	39.0%
Return on average finance receivables (annualized)	(5.7)%	8.7%
Cash distributions (for the three months ended)	\$ 1,890	\$ 1,665
Cash distributions per fund unit (for the three months ended)	\$ 0.081	\$ 0.081

### RESULTS OF OPERATIONS

The total revenue for the first quarter of 2008 was \$7,575,964, an increase of \$1,781,282 over the total revenue of \$5,794,682 for the first quarter of 2007. The net loss for the first quarter was \$1,396,047, a decrease of \$3,019,638 from the net earnings of \$1,623,591 for the first quarter of 2007. Earnings per fund unit decreased from \$0.08 for the first quarter of 2007 to a loss per fund unit of \$0.06 in the first quarter of 2008. Overall, total revenue increased 30.7%, net earnings decreased 186.0% and earnings per fund unit decreased 175.0% from the first quarter of 2007 to the first quarter of 2008.

The Fund commenced monthly cash distributions in April 2005 at the rate of \$0.021 (\$0.252 annually) per trust unit held. Prior to this, the Fund issued cash distributions on a quarterly basis. The monthly cash distribution rate increased twice during 2005, to \$0.022 (\$0.264 annually) in July 2005 and to \$0.024 (\$0.288 annually) in October 2005. The monthly cash distribution rate increased three times during 2006, to \$0.025 (\$0.300 annually) in April 2006, to \$0.026 (\$0.312 annually) in July 2006 and to \$0.027 (\$0.324 annually) in September 2006 where it remained through 2007. The Fund intends to continue distributing its taxable income through cash distributions and/or through the issuance of additional trust units.



On March 31, 2008, the Fund announced a change in the Fund's distribution policy to maximize the retention of operating cash flow. Carfinco's current monthly cash distribution of \$0.027 per trust unit will be replaced with a quarterly "in-kind" unit distribution. Distributions settled "in-kind" means that Unitholders will receive additional trust units instead of cash. Trust units will be issued at a deemed price equal to the volume-weighted average price of all trust units traded on The Toronto Stock Exchange on the 10 trading days preceding the applicable record date.

## REVENUES

Revenues increased by \$1,781,282, or 30.7%, from the first quarter of 2007 revenues of \$5,794,682 to the first quarter of 2008 revenues of \$7,575,964.

Interest income increased \$1,637,423, or 30.1%, from \$5,437,703 for the first quarter of 2007 to \$7,075,126 for the first quarter of 2008. The increase in interest income is directly related to the growth in the finance receivable portfolio.

Administration fee income increased \$143,859, or 40.3%, from \$356,979 for the first quarter of 2007 to \$500,838 for the first quarter of 2008.

Revenues are anticipated to move in conjunction with the growth in the finance receivable portfolio. The larger portfolio generates additional interest income and collection activity generates additional administration fee income.

## EXPENSES

The interest expense increased \$262,848, or 32.3%, from \$814,258 for the first quarter of 2007 to \$1,077,106 for the first quarter of 2008. The increase in interest expense is primarily due to an increase in the average outstanding credit facility balance from the first quarter of 2007 to the first quarter of 2008 of 32.7%, combined with an decrease in the average prime rate of 6.9% from the first quarter of 2007 to the first quarter of 2008.

The provision for credit losses increased \$3,372,014, or 209.3%, from \$1,610,789 for the first quarter of 2007 to \$4,982,803 for the first quarter of 2008. The \$4,982,803 (first quarter 2007 – \$1,610,789) provision is composed of \$2,812,803 (first quarter 2007 – \$1,708,489) in net write-offs and a \$2,170,000 (first quarter 2007 – \$97,700 decrease) increase in the allowance for credit losses.

The component for the net write-offs increased 64.6%, while the component for the allowance for credit losses increased 2,321.1%. The significant increase in the allowance for credit losses component is due to finance receivable portfolio growth in the regular program, which requires additions to the allowance for credit losses. Finance receivable portfolio growth in the first quarter of 2007 came primarily from programs that included dealer reserve and did not require increases in the loss reserves.

Amortization expense increased \$2,059, or 7.9%, from \$26,162 for the first quarter of 2007 to \$28,221 for the first quarter of 2008. Purchases of capital assets were \$58,768 during the first quarter of 2008 compared to \$97,902 for the first quarter of 2007. Management does not expect significant capital asset purchases during the remainder of fiscal 2008.

General and administrative expenses increased \$631,210, or 36.7%, from \$1,719,882 for the first quarter of 2007 to \$2,351,092 for the first quarter of 2008. The increase in general and administrative expenses is due to the overall expansion of the operational structure to accommodate the growth in the finance receivable portfolio. Specifically, salaries and benefits costs have increased as a result of higher staffing levels and loan administration costs have increased, due to higher funding volumes and collection activities.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### INCOME TAXES

The Fund is a "mutual fund trust" for income tax purposes. As such, the Fund is taxed on any taxable income not allocated to unitholders. Pursuant to the Deed of Trust, all or virtually all of the taxable income is allocated to unitholders; consequently, there is no tax liability for the Fund. The Fund follows the liability method of accounting for income taxes for future income taxes. Under this method, future tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities, and losses carried forward, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

### ASSET REVIEW

Total assets increased by \$4,272,513, or 4.9%, to \$90,835,958 at March 31, 2008 from \$86,563,445 at December 31, 2007. Non-portfolio assets increased \$185,456, or 17.6%, from \$1,055,914 at December 31, 2007 to \$1,241,370 at March 31, 2008. At March 31, 2008, non-portfolio assets represented 1.4% (December 31, 2007 – 1.2%) of the total assets. The portfolio assets include the finance receivables, the allowance for credit losses and the dealer reserve.

The finance receivables grew during the first quarter of 2008 by \$5,798,041, or 6.1%, to \$100,181,436. Funds advanced on finance receivables during the first quarter of 2008 amounted to \$17,888,780 compared to \$11,519,956 for the first quarter of 2007, an increase of \$6,368,824, or 55.3%. The increase in funding levels can be attributed to the emphasis on geographic and dealer network expansion. The Fund continues to adhere to consistent underwriting standards to achieve portfolio growth.

All finance receivables are secured, under the applicable provincial personal property registry, by motor vehicle collateral. The increase in the size of the finance receivable portfolio is due to the Fund's expansion in the non-prime sector of the auto finance industry. The Fund's strategy continues to be that of the alternative lender to major financial institutions in the higher-risk used vehicle finance market.

The Fund's allowance for credit losses, including dealer reserve, increased \$1,710,984, or 19.3%, to \$10,586,848 at March 31, 2008 from \$8,875,864 at December 31, 2007. Allowance for credit losses, including dealer reserve, as a percentage of finance receivables was 10.6% at March 31, 2008 compared to 9.4% at December 31, 2007. The Fund will continue to monitor its credit loss experience and make additional provisions, as it deems appropriate.

The management of the Fund establishes and maintains an allowance for credit losses, which it considers the best possible estimate of probable credit losses existing in the finance receivable portfolio. The allowance for credit losses consists of accumulated specific and general components, which are deducted from the finance receivable portfolio. In addition to the allowance for credit losses, a dealer reserve has been established to absorb potential credit losses. The dealer reserve is recorded on certain finance receivables purchased by the Fund at a negotiated price that is less than the original principal amount being financed. Under this program, the dealer has a vested interest in the performance of these finance receivables and can receive additional purchase consideration based on the collection performance of these finance receivables.

The Fund's finance receivable portfolio is composed of a large number of homogenous consumer loans, with relatively small balances, originated in the same industry, and as such, the evaluation of the allowance for credit losses is performed collectively for the group after allowance for specific losses. The estimated allowance for credit loss requirements are determined by assessing the individual finance receivables in arrears, the perceived effect of current economic conditions or other circumstances on the remaining finance receivables, the historical industry ratios of write-offs, and the Fund's current write-off and recovery experience.



**DELINQUENCY AND LOSSES**

Credit losses, delinquency and provision as at, and for each of the respective periods, were as follows:

(OOOs FOR STATED VALUES, EXCEPT PERCENTAGES)	MARCH 31 2008	MARCH 31 2007
Finance receivables outstanding at period end	\$ 100,181	\$ 73,408
Average finance receivables for the quarter	\$ 97,282	\$ 74,698
Nonperforming finance receivables at period end (1)	\$ 1,951	\$ 594
Nonperforming percentage at period end	1.9%	0.8%
Delinquent finance receivables at period end (2)	\$ 3,753	\$ 1,812
Delinquent percentage at period end	3.7%	2.5%
Allowance and reserve as a percentage of the finance receivables	10.6%	8.2%
Continuity of allowance for credit losses for the three months ended:		
Allowance, beginning of period	\$ 6,470	\$ 3,860
Provision for credit losses	4,983	1,611
Write-offs	(3,152)	(2,151)
Recoveries	339	442
Allowance, end of period	\$ 8,640	\$ 3,762
Continuity of dealer reserve for the three months ended:		
Reserve, beginning of period	\$ 2,406	\$ 2,701
Reserve on new volume	817	949
Write-offs	(1,424)	(1,623)
Recoveries	148	260
Reserve, end of period	\$ 1,947	\$ 2,287

(1) Nonperforming finance receivables are greater than 90 days contractually past due on their scheduled payments.

(2) Delinquent finance receivables are greater than 60 days contractually past due on their scheduled payments (includes the nonperforming finance receivables amount).

The Fund originates transactions in a relatively high-risk segment of the consumer finance industry; therefore, write-offs are anticipated. The management of the Fund establishes and maintains an allowance for credit losses, which it considers the best possible estimate of probable credit losses existing in the finance receivable portfolio. The Fund reviews static pool loss rates, historical industry ratios of write-offs, current write-off and recovery experience, estimates of the underlying collateral value, and economic conditions and trends to make the necessary judgments as to the appropriateness of the allowance for credit losses. Static pool loss rates are a measure of long-term performance and credit quality of that pool over time by relating a write-off back to its origination date. Although the Fund uses various models and methodologies to assess the adequacy of loss reserves, there is no precise method for estimating the losses existing in the finance receivable portfolio.

**LIABILITY REVIEW**

Total liabilities increased by \$7,506,940, or 12.0%, to \$69,970,893 at March 31, 2008, from \$62,463,953 at December 31, 2007.

The deferred dealer obligation balance decreased by \$12,243, or 0.6%, from \$2,190,247 at December 31, 2007, to \$2,178,004 at March 31, 2008. The Fund purchases certain finance receivables at a negotiated price that is less than the original principal amount being financed. The dealer has a vested interest in the performance of these finance receivables and can receive additional purchase consideration based on the collection performance of these finance receivables. The deferred dealer obligation represents



## MANAGEMENT'S DISCUSSION AND ANALYSIS

the estimated additional purchase consideration owed to the dealers, which is composed of a portion of the accumulated obligations recorded on the origination of these finance receivables, and of charges to interest revenue based on estimates of the obligation balance.

## LIQUIDITY AND CAPITAL RESOURCES

The Fund's primary sources of cash have been cash flows from operating activities, borrowings under its credit facility, and the issuance of debt and equity. The Fund's primary uses of cash have been the funding of advances on finance receivables and the purchase of certain capital assets. Management believes that the resources available to the Fund provide the needed capital to fund the anticipated expansion of the finance receivable portfolio and investments in operating infrastructure for the remainder of fiscal 2008.

The Fund's capitalization at each period end are as follows:

(OOOs FOR STATED VALUES)	MARCH 31 2008	MARCH 31 2007
Bank credit facility	\$ 66,416	\$ 48,217
Accounts payable and accrued liabilities	404	1,020
Deferred dealer obligation	2,178	2,472
<b>Total debt</b>	<b>\$ 68,998</b>	<b>\$ 51,709</b>
Unitholders' equity	\$ 20,865	\$ 16,655
Derivatives	973	-
<b>Total capitalization</b>	<b>\$ 21,838</b>	<b>\$ 16,655</b>
Financial leverage	3.16:1	3.10:1

The Fund's interest coverage ratio for the three months ended is as follows:

(OOOs FOR STATED VALUES)	MARCH 31 2008	MARCH 31 2007
Net (loss) earnings	\$ (1,396)	\$ 1,624
Loss on derivatives	533	-
Amortization of capital assets	28	26
Interest	1,077	814
<b>Interest coverage</b>	<b>\$ 242</b>	<b>\$ 2,464</b>
Interest coverage ratio – quarterly	0.22:1	3.03:1



The interest coverage ratio is calculated as the “interest coverage” divided by the “interest”. During the first quarter of 2008, the minimum interest coverage ratio was 1.50:1 measured on a quarterly basis and the Fund requested and received an amendment to this quarterly test, as the interest coverage ratio was calculated as 0.22:1. The Fund has received an amendment of this covenant for a period of time to allow operational results to improve and to allow additional loss reserves required for portfolio growth to be covered by revenue increases.

The Fund manages its capital resources by maximizing the financial leverage available under the credit facility. When additional capital is required, it is raised from operating cash flows and through subordinated debenture or unit issuances.

#### BANK CREDIT FACILITY

The Fund executed an Amended and Restated Credit Facility on February 13, 2008 with the Bank of America, N.A., BoS (USA) Inc. and the Bank of Montreal as co-lenders. The amount of borrowings available under this facility is \$85,000,000 (December 31, 2007 – \$65,000,000), subject to a defined borrowing base and a maximum financial leverage ratio of 3.75:1. The bank credit facility is the primary source of cash for funding growth in the finance receivable portfolio. As at March 31, 2008, a total of \$66,415,953 (December 31, 2007 – \$58,213,096) was outstanding under the credit facility. The maturity date of the credit facility is February 13, 2009 (December 31, 2007 – October 4, 2008).

#### UNITHOLDERS’ EQUITY

The unitholders’ equity decreased \$3,234,427, or 13.4%, during the first quarter of 2008 from \$24,099,492 at December 31, 2007, to \$20,865,065 at March 31, 2008. The decrease is due primarily to a net loss of \$1,396,047 incurred during the first quarter of 2008, combined with cash distributions of \$1,890,046.

As at March 31, 2008, the following units of the Fund were issued and outstanding:

Units	23,322,566
Units held for unit purchase financing	16,680



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### DISTRIBUTABLE CASH (SEE NON-GAAP MEASURES)

(OOOs FOR STATED VALUES, EXCEPT PER FUND UNIT AMOUNTS AND PERCENTAGES)	MARCH 31 2008	MARCH 31 2007
Cash provided by operating activities	\$ 3,341	\$ 3,354
Add (deduct):		
Long-term unfunded contractual operational obligations (1)	(225)	(75)
Significant non-cash items during the period (2)(3)	(2,280)	(1,658)
<b>Distributable cash</b>	<b>\$ 836</b>	<b>\$ 1,621</b>
Cash distributions paid during the period	\$ 1,890	\$ 1,665
<b>Payout ratio</b>	<b>226.1%</b>	<b>102.7%</b>
Distributable cash per weighted average units outstanding	\$ 0.036	\$ 0.079
Cash distributions per fund unit	\$ 0.081	\$ 0.081
Unit distributions per fund unit	-	-
<b>Total distributions per fund unit</b>	<b>\$ 0.081</b>	<b>\$ 0.081</b>

(1) The Fund records an obligation to dealers that is recorded on the balance sheet as Deferred Dealer Obligation. Provision to fund a portion of such obligations is made through charges to the income statement.

(2) The significant non-cash items during the period are excluded from the calculation of distributable cash, as their inclusion would not properly reflect the cash available for distribution.

(3) The deduction for significant non-cash items during the period has been amended for 2007 to include the portion of the Provision for Credit Losses used to increase the balance of the Allowance for Credit Losses.

Distributable cash for the first quarter of 2008 amounted to \$0.836 million, or \$0.036 per unit, a decrease of \$0.785 million, or 48.4% and \$0.043 per unit from the first quarter of 2007. Cash distributions of \$0.081 per unit were paid to unitholders at a payout ratio of 226.1% for the first quarter of 2008. The distributable cash was lower and the payout ratio was higher compared to the first quarter of 2007 due to a significant change of \$1.050 million in accounts payable and accrued liabilities during the first quarter of 2008. This reduction of operating cash flow is not expected to continue in subsequent quarters.

On March 31, 2008, the Fund announced a change in the Fund's distribution policy to maximize the retention of operating cash flow. Carfinco's current monthly cash distribution of \$0.027 per trust unit will be replaced with a quarterly "in-kind" unit distribution. Distributions settled "in-kind" means that Unitholders will receive additional trust units instead of cash. Trust units will be issued at a deemed price equal to the volume-weighted average price of all trust units traded on the Toronto Stock Exchange on the 10 trading days preceding the applicable record date.

The Fund's distribution policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practices considering requirements for capital expenditures, working capital and other reserves considered advisable by the Trustees of the Fund. All such distributions are discretionary.

Overall, the Fund capitalizes an insignificant amount; therefore, no deduction is made for productive capacity maintenance when calculating distributable cash. The Fund's ability to maintain productive capacity is expensed on an annual basis.



Pursuant to the Deed of Trust of the Fund, the Trustees must distribute all or virtually all of the income of the Fund for the fiscal year, determined in accordance with the *Income Tax Act (Canada)*, to the unitholders of the Fund. If the Fund does not pay cash distributions for the total income of the Fund, determined in accordance with the *Income Tax Act (Canada)*, the remaining income of the Fund is distributed through additional Trust Units having a value equal to the cash shortfall.

The Fund does not intend to repay the existing debt obligation under the bank credit facility. To fund the acquisition of receivables and grow the finance receivable portfolio, the Fund will maximize the financial leverage available under the credit facility. When additional capital is required, it is raised through subordinated debenture or unit issuances.

Although the Fund intends to continue making distributions to its unitholders, cash distributions or “in-kind” unit distributions are not assured. The Fund’s ability to make cash distributions and the actual amount distributed will depend upon, among other things, the Fund’s financial performance, debt covenants and obligations, ability to refinance our debt obligations on similar terms and at similar interest rates, working capital requirements, possible future tax obligations and future capital requirements.

Under the terms of the credit facility, the Fund is restricted from declaring cash distributions and distributing cash if the Fund is in breach of its debt covenants. These include, but are not limited to, a financial leverage ratio, an interest coverage ratio, a loan availability calculation and a taxable income restriction.

There are numerous factors, which affect the Fund’s ability to pay cash distributions or “in-kind” unit distributions to its unitholders and distributions cannot be assured. A description of those risk factors can be found in the section, “Risk Management”, and in the Fund’s Annual Information Form.

## DISTRIBUTIONS

Cash distributions are normally payable by the Fund on a monthly basis to unitholders of record on the 20th business day of each month. Distributions are paid on the last business day of the month. Distributions on units of record during the year ended December 31, 2007 and the three months ended March 31, 2008 are summarized as follows:

RECORD DATE	PAYMENT DATE	CASH DISTRIBUTION PER UNIT	TOTAL CASH DISTRIBUTION
January 18, 2008	January 31, 2008	\$ 0.027	\$ 630,015
February 20, 2008	February 29, 2008	0.027	630,015
March 20, 2008	March 31, 2008	0.027	630,016
Total cash distribution for the three months ended March 31, 2008		\$ 0.081	\$ 1,890,046
January 19, 2007	January 31, 2007	\$ 0.027	\$ 555,033
February 20, 2007	February 28, 2007	0.027	555,033
March 20, 2007	March 30, 2007	0.027	555,034
April 20, 2007	April 30, 2007	0.027	555,155
May 22, 2007	May 31, 2007	0.027	555,155
June 15, 2007	June 29, 2007	0.027	555,155
July 20, 2007	July 31, 2007	0.027	630,015
August 20, 2007	August 31, 2007	0.027	630,015
September 20, 2007	September 28, 2007	0.027	630,016
October 19, 2007	October 31, 2007	0.027	630,015
November 20, 2007	November 30, 2007	0.027	630,015
December 20, 2007	December 31, 2007	0.027	630,016
Total cash distribution for 2007		\$ 0.324	\$ 7,110,657



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### SUMMARY OF QUARTERLY INFORMATION (UNAUDITED)

(000s FOR STATED VALUES, EXCEPT PERCENTAGES AND PER FUND UNIT AMOUNTS)

	Q1-2008	Q4-2007	Q3-2007	Q2-2007	Q1-2007	Q4-2006	Q3-2006	Q2-2006
Total revenue	7,576	7,305	6,746	6,188	5,795	6,089	5,738	5,290
Net earnings	(1,396)	(38)	754	1,506	1,624	1,675	1,649	1,547
Earnings per fund unit – basic and diluted	(0.06)	-	0.03	0.07	0.08	0.09	0.09	0.08
Finance receivables	100,181	94,383	88,552	80,344	73,408	75,989	73,073	68,676
Funds advanced on finance receivables	17,889	17,299	18,940	16,951	11,520	11,053	12,320	12,668
Loan originations	19,982	19,072	21,025	19,286	12,668	12,855	14,389	15,254
Allowance and dealer reserve	10,587	8,876	6,965	6,152	6,050	6,561	6,460	6,278
Allowance and reserve as a % of finance receivables	10.6%	9.4%	7.9%	7.7%	8.2%	8.6%	8.8%	9.1%
Bank credit facility	66,416	58,213	52,173	44,486	48,217	47,393	46,684	43,878
Long-term debt	-	-	-	-	-	-	2,600	1,600
Unitholders' equity	20,865	24,099	26,028	27,164	16,655	16,634	11,684	11,502
Fund units outstanding	23,323	23,306	23,306	23,306	20,528	20,508	18,519	18,519
Basic weighted average fund units	23,306	23,306	23,306	20,805	20,508	19,465	18,662	18,662
Book value per fund unit	0.90	1.03	1.12	1.31	0.81	0.85	0.63	0.62

Total revenue continues to increase proportionately with the increase in finance receivables. Net earnings decreased from Q1 2007 to Q2 2007, due to an increase in the allowance for credit losses, which is recorded through the provision for credit losses, and to an increase in the general and administrative expenses to manage the portfolio growth. Net earnings decreased from Q2 2007 to Q3 2007, primarily due to a non-cash increase of \$855,000 in the allowance for credit losses, to an increase in general and administrative expenses to manage the portfolio growth, and to a non-cash loss of \$250,770 on derivatives. Net earnings decreased from Q3 2007 to Q4 2007, primarily due to a non-cash increase of \$1,755,000 in the allowance for credit losses and to a non-cash loss of \$189,524 on derivatives. Net earnings decreased from Q4 2007 to Q1 2008, primarily due to a non-cash increase of \$2,170,000 in the allowance for credit losses and to a non-cash loss of \$532,789 on derivatives. Earnings per fund unit have decreased in each of the past five quarters, as a result of unit equity issuances in November 2006 and June 2007 and a decrease in net earnings.

The finance receivable portfolio has increased significantly during the last four quarters, due to the implementation of the Curomax and DealerAccess online portals, which increased the consumer applications received by Carfinco. This increase in applications has resulted in increased funding, as reflected in the funds advanced on finance receivables during Q2 2007 through Q1 2008.

The allowance and dealer reserve as a percentage of the finance receivables decreased in the five quarters leading up to Q3 2007, due to the mix of financial components used to assess the adequacy of the Fund's allowance for credit losses on its various programs. Management assesses the adequacy of the allowance for credit losses on a regular basis.



The bank credit facility decreased from Q1 2007 to Q2 2007, due to repayment using net proceeds from the issuance of trust units in June 2007 for gross proceeds of \$11.5 million. The Fund repaid the balance of long-term debt in Q4 2006 using proceeds from the issuance of trust units in November 2006 for gross proceeds of \$6.0 million. The Fund manages its capital resources by maximizing the financial leverage available under the credit facility, and when additional capital is required, it is raised through subordinated debt or unit issuances.

Unitholders' equity increased in Q4 2006 and Q2 2007, due to the unit issuances mentioned above. These unit issuances resulted in an increase in the number of fund units outstanding and in an increase in the book value per fund unit.

#### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management's discussion and analysis of financial condition and results of operations are made with reference to the audited consolidated financial statements for the year ended December 31, 2007. A summary of the Fund's significant accounting policies are presented in Note 2 to these consolidated financial statements. Some of the Fund's accounting policies, as required by generally accepted accounting principles, require management to make subjective, complex judgments and estimates to matters that are inherently uncertain. The Fund believes the following are the most critical accounting estimates that affect its operating results and that would have the most material effect on the financial statements should these policies change or be applied in a different manner.

#### REVENUE RECOGNITION

Interest income is recorded on an accrual basis, where interest is earned over the life of the related finance receivable contract. Accrual of interest income is suspended on finance receivables classified as impaired. Fee income charged to the customer, in excess of the costs incurred, on the origination of finance receivables and fee income charged to the dealer on the origination of finance receivables are recorded as unearned administration fees and are a component of the finance receivable portfolio. These unearned administration fees are recognized into interest income using the effective interest method. Fees charged to the customer during the subsequent servicing of the finance receivables are recognized upon collection of funds to Administration Fees revenue.

#### ALLOWANCE FOR CREDIT LOSSES

The management of the Fund establishes and maintains an allowance for credit losses, which it considers the best possible estimate of probable credit losses existing in the finance receivable portfolio. The allowance for credit losses consists of accumulated specific and general components, which are deducted from the finance receivable portfolio. In addition to the allowance for credit losses, a dealer reserve has been established to absorb potential credit losses. The dealer reserve is recorded on certain finance receivables purchased by the Fund at a negotiated price that is less than the original principal amount being financed. Under this program, the dealer has a vested interest in the performance of these finance receivables and can receive additional purchase consideration based on the collection performance of these finance receivables. The Fund's finance receivable portfolio is composed of a large number of homogenous consumer loans, with relatively small balances, originated in the same industry, and as such, the evaluation of the allowance for credit losses is performed collectively for the group after allowance for specific losses. The estimated allowance for credit loss requirements are determined by assessing the individual finance receivables in arrears, the perceived effect of current economic conditions or other circumstances on the remaining finance receivables, the historical industry ratios of write-offs, and the Fund's current write-off and recovery experience.

#### DEFERRED DEALER OBLIGATION

The Fund purchases certain finance receivables at a negotiated price that is less than the original principal amount being financed. Under this program, the dealer has a vested interest in the performance of these finance receivables, and can receive additional purchase consideration based on the collection performance of these finance receivables. The deferred dealer obligation represents the estimated additional purchase consideration owed to the dealers, which is composed of a portion of the accumulated obligations recorded on the origination of these finance receivables, and of charges to interest revenue based on estimates of the obligation balance.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### RELATED PARTY TRANSACTIONS – PATICA SECURITIES LIMITED

The Fund has an agreement with Patica Securities Limited for services provided on an ongoing basis. These services include general strategic advice, advice on financial structure, advice on senior and/or subordinated debt and equity structure, communication with stakeholders and other general consulting services. Carfinco LP entered into a Consulting Services Agreement with Patica Securities Limited on October 1, 2003, and pursuant to this agreement, Carfinco LP incurs a fixed monthly fee of \$13,375, and a variable monthly fee of one-twelfth of 0.2% of the outstanding principal amount of the finance receivables. During the three months ended March 31, 2008, payments of \$92,265 (three months ended March 31, 2007 – \$79,441) were made to Patica Securities Limited and at March 31, 2008, there was \$31,461 (December 31, 2007 – \$30,401) payable to Patica Securities Limited. Patica Securities Limited is controlled by individuals who are Trustees of the Fund. The related party transactions occurred at the exchange amount, which is the consideration established and agreed to by the related parties.

### DERIVATIVE FINANCIAL INSTRUMENTS

The Fund utilizes derivative financial instruments, in the form of interest rate swap agreements, to reduce the impact of fluctuating interest rates on its bank credit facility. These swap agreements require the monthly exchange of payments without the exchange of the notional principal amount on which the payments are based. Interest expense on the debt is adjusted to include the payments made or received under the interest rate swaps.

A derivative must be designated and effective to be accounted for as a hedge. For cash flow hedges, effectiveness is achieved if the changes in the cash flows of the derivatives substantially offset the changes in the cash flows of the hedged item, and if the timing of the cash flows is similar. Derivatives are classified as “financial asset or financial liabilities held for trading,” and are measured at fair value at each balance sheet date with gains and losses recognized in net earnings if the derivatives are not part of a designated hedging relationship. Gains and losses on derivatives that are part of a designated hedging relationship are recognized in other comprehensive income until such time as the hedging relationship ceases.

On August 23, 2007, the Fund entered into two interest rate swap agreements with a combined notional amount of \$20,000,000. The first agreement has a notional amount of \$10,000,000, a fixed bankers' acceptance rate of 4.92% and a three-year term ending on August 23, 2010. The second agreement has a notional amount of \$10,000,000, a fixed bankers' acceptance rate of 4.99% and a five-year term ending on August 23, 2012.

These interest rate swap agreements have been classified as “held-for-trading financial instruments,” and are measured at fair value with all gains and losses recorded through net earnings. During the first quarter of 2008, a loss of \$532,789 (three months ended March 31, 2007 – \$nil) was expensed as a loss on derivatives, and the fair value of the interest rate swaps at March 31, 2008 was a liability of \$973,083 (December 31, 2007 – liability of \$440,294).

### OFF-BALANCE SHEET ARRANGEMENTS

The Fund has not entered into any off-balance sheet arrangements.

### CONTRACTUAL OBLIGATIONS

The Fund is committed to a long-term operating lease for building space. The minimum annual lease payments plus estimated operating costs required for the remainder of 2008 and the next three years are as follows: \$198,000 for 2008, \$282,000 for 2009, \$289,000 for 2010 and \$297,000 for 2011.



## RISK MANAGEMENT

### General

The operations of the Fund are affected by trends and factors that the Fund may not be able to control. These trends and factors may include changes in the vehicle financing market sector and the state of the domestic and global economy. It is not possible for management to accurately predict the impact of changes in the operating environment, nor to predict their effect on the Fund's financial condition and results of operations.

### Competitive environment

There can be no assurance that the Fund will be able to compete successfully against its current or future competitors, or that such competition will not have a material adverse effect on the financial condition and results of operations of the Fund. Overall, the market for the financial services offered by the Fund is highly competitive and many of the companies operating in this sector have greater financial, technical and marketing resources than the Fund and generate greater revenues. Relatively low barriers to entry into the Fund's markets exist and the Fund expects to face additional competition over time from new entrants into its market sector.

### Reliance on key personnel

The Fund is dependent on the abilities, experience and efforts of its senior management and other key employees. If these individuals become unable or unwilling to continue their employment, there may be a material adverse effect on the Fund's financial condition, results of operations and business prospects.

### Liquidity risk

As is customary in the Fund's industry, the credit facility and subordinated debt instruments must be renewed on a periodic basis. The Fund has been successful in renewing and expanding these facilities. If the Fund were unable to renew these facilities on acceptable terms, there could be a material adverse effect on the Fund's financial position, results of operations and liquidity.

### Credit risk

Credit risk management is the management of the credit risk associated with the total finance receivable portfolio. This is the risk of the loss of principal and/or interest from the failure of debtors, for any reason, to honour the financial or contractual obligations to the Fund. In the event of payment default, the collateral value of the financed vehicle may not cover the outstanding contract balance and costs of recovery.

The Fund originates transactions in a relatively high-risk segment of the consumer finance industry. Therefore, write-offs are anticipated. The management of the Fund establishes and maintains an allowance for credit losses, which it considers the best possible estimate of probable credit losses existing in the finance receivable portfolio.

The Fund reviews static pool loss rates, historical industry ratios of write-offs, current write-off and recovery experience, estimates of the underlying collateral value, and economic conditions and trends to make the necessary judgments as to the appropriateness of the allowance for credit losses. Static pool loss rates are a measure of long-term performance and credit quality, where static pool loss rates are calculated by identifying a pool of assets and tracking the performance of that pool by relating a write-off back to its origination date. Although the Fund uses various models and methodologies to assess the adequacy of loss reserves, there is no precise method for estimating the losses existing in the finance receivable portfolio.

### Interest rate risk

The Fund's earnings are affected by changes in interest rates as a result of its dependence upon a credit facility, which bears interest at a floating rate. The receivable portfolio bears interest at a fixed rate; therefore, the Fund carries the risk of smaller interest rate spreads in the event market interest rates increase.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### Income tax matters

On October 31, 2006, the Minister of Finance announced the proposed Tax Fairness Plan for Canadians that includes a tax on distributions from publicly traded income trusts and limited partnerships. Existing publicly traded income trusts, such as Carfinco Income Fund, would not be subject to the proposed tax until their 2011 taxation year.

On June 22, 2007, the Senate passed the Federal Government's budget implementation bill, which included the taxation of income trusts starting in 2011. As such, the Fund reviewed all temporary differences that were previously not recorded as future income tax assets or liabilities at the trust level. Recognition of these future income tax assets or liabilities is recorded only for temporary differences expected to reverse after the date that the taxation changes take effect, being January 2011. The only such temporary difference relates to fund unit issue costs, which are recorded against fund unit equity and are being deducted against taxable income over a five-year period. At a future income tax rate of 31.50%, an amount of \$51,393 was recorded during the second quarter of 2007 as a future income tax asset.

## ACCOUNTING POLICIES

### Initial Adoption of Accounting Policies

The following is a discussion of relevant changes to accounting policies adopted as a result of Handbook revisions that were released, revised or became effective since the Fund's audited financial statements for the year ended December 31, 2007 were issued.

New CICA Handbook Section 1535, Capital Disclosures, requires the disclosure of both qualitative and quantitative information that enables financial statement users to evaluate the objectives, policies and processes for managing capital. There was no material effect on the Fund's financial statements when the CICA Handbook Section 1535 was adopted on January 1, 2008, other than the addition of required note disclosure. Disclosures recommended by the new handbook section have been included in Note 10 of the interim consolidated financial statements.

New CICA Handbook Section 3862, Financial Instruments – Disclosures, modifies the disclosure requirements for financial instruments that were included in Section 3861, Financial Instruments – Disclosure and Presentation. Section 3863, Financial Instruments – Presentation, carries forward unchanged the presentation requirements of the previous Section 3861, Financial Instruments – Disclosure and Presentation. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. These new standards require disclosures related to the significance of financial instruments on the Fund's financial position and performance and the nature and extent of risk arising from financial instruments in which the Fund is exposed and how the Fund manages the risks. There was no material effect on the Fund's financial statements when the CICA Handbook Section 3862 was adopted on January 1, 2008, other than the addition of required note disclosure. Disclosures recommended by the new handbook section have been included in Note 12 of the interim consolidated financial statements.

## FUTURE ACCOUNTING CHANGES

### International Financial Reporting Standards

The CICA plans to transition Canadian GAAP for publicly accountable companies to International Financial Reporting Standards (IFRS) over a transition period ending in 2011. The impact of the transition to IFRS on the Fund's consolidated financial statements has not yet been determined.



## NON-GAAP MEASURES

### **Distributable cash**

Distributable cash is a non-GAAP measure generally used by Canadian income trusts as an indicator of financial performance, and it should not be seen as a measurement of liquidity, or a substitute for comparable metrics prepared in accordance with GAAP. This measure is commonly used by investors, management and other stakeholders to evaluate the ongoing performance of the Fund. Distributable cash may differ from similar calculations as reported by other entities and, accordingly, may not be comparable to distributable cash as reported by such entities. For reconciliation with GAAP, please refer to the “Distributable Cash” section.

### **Cash distributions per unit and payout ratio**

The Fund reports on cash distributions per unit and payout ratio (actual cash distribution divided by distributable cash) because they are key measures used by investors to value the Fund, assess its performance and provide an indication of the sustainability of distributions. Cash distributions per unit and the payout ratio depend on the Fund’s distributable cash and the Fund’s distribution policy.

The Fund’s policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practices, considering requirements for capital expenditures, working capital, and other reserves considered advisable by the Trustees of the Fund. All such distributions are discretionary.

Cash distributions are normally payable by the Fund on a monthly basis to unitholders of record on the 20th business day of each month. Distributions are paid on the last business day of the month.

### **Disclosure controls and procedures**

The Fund has established and maintains disclosure controls and procedures over financial reporting. The Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Fund’s disclosure controls and procedures (as defined by the Canadian Securities Administrators) as of March 31, 2008, and have concluded that such procedures are adequate and effective to provide reasonable assurance that material information relating to the Fund and its consolidated entities and would be made known to them by others within those entities to allow for accurate and complete disclosures in annual and interim filings or other reports.

It should be noted that while the Fund’s Chief Executive Officer and Chief Financial Officer believe that the Fund’s disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the Fund’s disclosure controls and procedures or internal control over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

### **Internal controls over financial reporting**

Management also concluded that during the quarter ended March 31, 2008, no changes were made to internal controls over financial reporting that would have materially affected, or would be reasonably considered to materially affect, these controls.



## MANAGEMENT'S DISCUSSION AND ANALYSIS

### OUTLOOK

The Fund's strategy is to continue to grow the finance receivable portfolio through the expansion of the dealer network and the partnering with the two online lending portals in Canada. This growth will be attained in a prudent manner without compromising underwriting credit standards. The Fund feels there is significant room for loan portfolio growth by continuing to follow this strategy.

The operational infrastructure needs to be managed in conjunction with the management of the growing finance receivable portfolio. The hiring and retention of the best administrative and collections staff has always been a focus of the Fund. The current labour market in Alberta has a limited number of available qualified applicants, and the Fund has improved hiring practices and employee benefit packages to attract candidates.

The Fund continues to invest in information technology, and recognizes it as the leading contributor to operational efficiency. An Internet-based platform is used to receive credit applications from dealers, to underwrite the customer and to communicate funding stipulations to the dealer. This Internet-based system communicates directly with the Fund's credit bureau providers and integrates with the internal finance system. The internal finance system is specialized to the automotive finance industry and handles the following functions: general ledger, financial reporting, account reporting, accounts payable, automated payment processing, automated deposit processing, account collection administration and repossession processing. The internal finance system is scalable, and will handle the planned growth in the Fund's finance receivable portfolio.

During 2008, the information technology infrastructure will continue to remain a primary focus of management. Projects include improvements to management reporting systems, general upgrades to the hardware and transitioning to a document image storage environment.

### CAUTIONARY STATEMENT

Certain statements contained in this interim report constitute "forward-looking statements". When used in this interim report, the words "may", "would", "could", "will", "intend", "plan", "anticipate", "believe", "estimate", "expect", and similar expressions, as they relate to the Fund, its subsidiaries or their management, are intended to identify forward-looking statements. Such statements reflect our current views with respect to future events and are subject to inherent risks, uncertainties and numerous assumptions, including, without limitation, general economic conditions, reliance on debt financing, dependence on non-prime borrowers, inability to sustain receivables, competition, interest rates, regulation, insurance, failure of key systems, debt service, future capital needs and such other risks or factors described from time to time in reports of Carfinco Income Fund that are filed with securities regulatory authorities.

By their nature, forward-looking statements involve numerous assumptions, known and unknown, risks and uncertainties, both general and specific, which contribute to the possibility that predictions, forecasts, projections and other forms of forward-looking information may not be achieved. Many factors could cause our actual results, performance or achievements to be materially different from any future results, performance or achievements that may be expressed or implied by such forward-looking statements and readers are cautioned that the list of factors in the foregoing paragraph is not exhaustive. Should one or more of these risks or uncertainties materialize, or should assumptions underlying the forward-looking statements prove incorrect, actual results may vary materially from those described herein as intended, planned, anticipated, believed, estimated or expected. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements or interpret or regard forward-looking statements as guarantees of future outcomes.

In addition to the careful consideration of the risks described herein, investors should also consider the risk factors set forth in the most recently filed Annual Information Form of the Fund which is incorporated by reference herein. The Annual Information Form is available through the Internet on the Canadian System for Electronic Document Analysis and Retrieval ("SEDAR"), which can be accessed at [www.sedar.com](http://www.sedar.com).



## CONSOLIDATED BALANCE SHEETS

	<b>MARCH 31 2008</b>	DECEMBER 31 2007
	(UNAUDITED)	(AUDITED)
<b>ASSETS</b>		
Finance receivables (Note 3)	\$ 100,181,436	\$ 94,383,395
Allowance for credit losses (Note 4)	(8,640,000)	(6,470,000)
Dealer reserve (Note 5)	(1,946,848)	(2,405,864)
Finance receivables – net	<u>89,594,588</u>	<u>85,507,531</u>
Cash	235,484	-
Other assets	556,994	637,569
Capital assets	397,499	366,952
Future income taxes	51,393	51,393
	<u>1,241,370</u>	<u>1,055,914</u>
	<u>\$ 90,835,958</u>	<u>\$ 86,563,445</u>
<b>LIABILITIES</b>		
Bank credit facility (Note 6)	\$ 66,415,953	\$ 58,213,096
Bank overdraft	-	165,886
Accounts payable and accrued liabilities	403,853	1,454,430
Deferred dealer obligation (Note 7)	2,178,004	2,190,247
Derivatives (Note 8)	973,083	440,294
	<u>69,970,893</u>	<u>62,463,953</u>
<b>UNITHOLDERS' EQUITY</b>		
Unitholders' capital (Note 9)	29,634,856	29,583,190
Deficit (Note 9)	(8,769,791)	(5,483,698)
	<u>20,865,065</u>	<u>24,099,492</u>
	<u>\$ 90,835,958</u>	<u>\$ 86,563,445</u>

See accompanying notes to the Consolidated Financial Statements.



## CONSOLIDATED STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT

THREE MONTHS ENDED	MARCH 31 2008	MARCH 31 2007
	(UNAUDITED)	(UNAUDITED)
<b>FINANCIAL REVENUE</b>		
Interest	\$ 7,075,126	\$ 5,437,703
Administration fees	500,838	356,979
	<u>7,575,964</u>	<u>5,794,682</u>
<b>FINANCIAL EXPENSE</b>		
Interest	1,077,106	814,258
<b>NET FINANCIAL INCOME BEFORE PROVISION FOR CREDIT LOSSES</b>	<u>6,498,858</u>	<u>4,980,424</u>
Provision for credit losses	4,982,803	1,610,789
<b>NET FINANCIAL INCOME BEFORE OPERATING EXPENSES</b>	<u>1,516,055</u>	<u>3,369,635</u>
<b>OPERATING EXPENSES</b>		
General and administrative	2,351,092	1,719,882
Loss on derivatives	532,789	-
Amortization of capital assets	28,221	26,162
	<u>2,912,102</u>	<u>1,746,044</u>
<b>NET (LOSS) EARNINGS AND COMPREHENSIVE (LOSS) INCOME</b>	<u>\$ (1,396,047)</u>	<u>\$ 1,623,591</u>
<b>DEFICIT, BEGINNING OF PERIOD</b>	<u>\$ (5,483,698)</u>	<u>\$ (2,218,776)</u>
Net (loss) earnings	(1,396,047)	1,623,591
Cash distributions on fund unit equity (Note 9)	(1,890,046)	(1,665,100)
<b>DEFICIT, END OF PERIOD</b>	<u>\$ (8,769,791)</u>	<u>\$ (2,260,285)</u>
<b>EARNINGS (LOSS) PER FUND UNIT</b>		
Basic and diluted	\$ (0.06)	\$ 0.08

See accompanying notes to the Consolidated Financial Statements.



**CONSOLIDATED STATEMENTS  
OF CASH FLOWS**

THREE MONTHS ENDED	MARCH 31 2008	MARCH 31 2007
	(UNAUDITED)	(UNAUDITED)
Increase (decrease) in cash and cash equivalents		
<b>OPERATING</b>		
Net (loss) earnings	\$ (1,396,047)	\$ 1,623,591
Adjustments to reconcile net earnings to net cash from operations:		
Provision for credit losses	4,982,803	1,610,789
Amortization of capital assets	28,221	26,162
Accrued interest	(61,435)	180,962
Deferred dealer obligation	225,000	75,000
Derivatives	532,789	-
Accounts payable and accrued liabilities	(1,050,577)	215,797
Other assets	80,575	(378,238)
	<u>3,341,329</u>	<u>3,354,063</u>
<b>INVESTING</b>		
Funds advanced on finance receivables	(17,888,780)	(11,519,956)
Principal collections on finance receivables	10,181,514	9,015,841
Change in finance receivable reserves and transaction costs	(1,538,402)	(100,223)
Purchase of capital assets	(58,768)	(97,902)
	<u>(9,304,436)</u>	<u>(2,702,240)</u>
<b>FINANCING</b>		
Advances on bank credit facility	9,002,857	2,320,811
Repayments on bank credit facility	(800,000)	(1,400,000)
Repayments on unit purchase financing	51,666	62,000
Fund unit cash distribution	(1,890,046)	(1,665,100)
	<u>6,364,477</u>	<u>(682,289)</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>401,370</b>	<b>(30,466)</b>
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning of period	(165,886)	141,546
End of period	<u>\$ 235,484</u>	<u>\$ 111,080</u>
<b>SUPPLEMENTAL CASH FLOW INFORMATION:</b>		
Interest paid	<u>\$ 1,046,021</u>	<u>\$ 785,368</u>

See accompanying notes to the Consolidated Financial Statements.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2008

### **1** SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Carfinco Income Fund (the “Fund”) is an unincorporated open-end mutual fund trust established under the laws of the Province of Ontario by a Deed of Trust made as of August 26, 2002, as amended and restated on April 23, 2004. The Fund owns 100% of Carfinco Holdings Trust (“CHT”), a wholly owned unincorporated trust, established under the laws of Ontario and 100% of Carfinco Inc. (“CAR”), a wholly owned subsidiary, established under the laws of Ontario. CHT holds 92.39% and is the limited partner of Carfinco Limited Partnership (“Carfinco LP”), and CAR holds the remaining 7.61% and is the general partner of Carfinco LP. Carfinco LP is in the business of providing consumer financing for vehicle purchases. The units of the Fund are publicly traded on The Toronto Stock Exchange, under the symbol “CFN.UN”.

These unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles, and the accounting policies and methods are consistent with those used in the preparation of the Fund’s most recent annual financial statements for the period ended December 31, 2007, except as disclosed in Note 2. While management considers this interim disclosure presented to be adequate, these interim consolidated financial statements and notes should be read in conjunction with the notes included in the Fund’s December 31, 2007 audited consolidated financial statements.

### **2** NEW ACCOUNTING POLICIES

CICA Handbook Section 1535, Capital Disclosures, requires the disclosure of both qualitative and quantitative information that enables financial statement users to evaluate the objectives, policies and processes for managing capital. There was no material effect on the Fund’s financial statements when the CICA Handbook Section 1535 was adopted on January 1, 2008, other than the addition of required note disclosure.

CICA Handbook Section 3862, Financial Instruments – Disclosures, and CICA Handbook Section 3863, Financial Instruments – Presentation replaced CICA Handbook Section 3861, Financial Instruments – Disclosure and Presentations. These sections establish standards for presentation of financial instruments and non-financial derivatives, and identify information that should be disclosed. There is increased emphasis on the disclosure of the risks arising from financial instruments and how the entity manages such exposures. There was no material effect on the Fund’s financial statements when the CICA Handbook Sections 3862 and 3863 were adopted on January 1, 2008, other than the addition of required note disclosure.



## 3 FINANCE RECEIVABLES

Finance receivables consist of conditional sales contracts, which have terms of 12 to 60 months with fixed rates of interest. Each individual finance receivable is collateralized by a vehicle.

The contractual payments, including principal and interest, and the average stated interest rates, are due in the years as follows:

	MARCH 31 2008	AVERAGE STATED INTEREST RATE	DECEMBER 31 2007	AVERAGE STATED INTEREST RATE
2008	\$ 36,703,239	28.6%	\$ 45,691,689	28.5%
2009	45,918,127	28.7%	41,954,932	28.5%
2010	39,434,344	28.7%	34,900,116	28.6%
2011	29,780,042	28.9%	24,415,242	28.8%
2012	14,704,627	29.3%	9,528,542	29.3%
2013	912,289	29.4%	-	
Gross finance receivables	167,452,668		156,490,521	
Unearned interest income	(64,848,726)		(59,965,158)	
Unearned administration fees	(4,072,039)		(3,730,067)	
Principal of finance receivables	98,531,903		92,795,296	
Accrued interest	1,649,533		1,588,099	
Finance receivables	\$ 100,181,436		\$ 94,383,395	

The Fund's experience has shown that the actual contractual payment stream will vary depending on a number of variables. These variables include prepayment rates, write-offs and deferments. Accordingly, the maturities of finance receivables shown in the table above are not to be regarded as a forecast of future cash collections.

The impaired loans and the related allowance for specific credit losses and a summary of the general and specific allowance components are as follows:

	MARCH 31 2008	DECEMBER 31 2007
Impaired loans	\$ 5,627,500	\$ 4,648,600
Specific provisions	(4,775,100)	(3,930,200)
Carrying amount	\$ 852,400	\$ 718,400
Allowance for credit losses – general	\$ 5,891,200	\$ 3,828,200
Allowance for credit losses – specific	2,748,800	2,641,800
Allowance for credit losses	8,640,000	6,470,000
Dealer reserve – general	67,848	1,117,464
Dealer reserve – specific	1,879,000	1,288,400
Dealer reserve	1,946,848	2,405,864
	\$ 10,586,848	\$ 8,875,864



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

### **4 ALLOWANCE FOR CREDIT LOSSES**

THREE MONTHS ENDED	MARCH 31 2008	DECEMBER 31 2007
Allowance, beginning of period	\$ 6,470,000	\$ 4,715,000
Provision for credit losses	4,982,803	3,881,889
Write-offs	(3,151,606)	(2,514,835)
Recoveries	338,803	387,946
Allowance, end of period	\$ 8,640,000	\$ 6,470,000

### **5 DEALER RESERVE**

	MARCH 31 2008	DECEMBER 31 2007
Reserve, beginning of period	\$ 2,405,864	\$ 2,249,823
Reserve on new volume	817,313	1,810,778
Write-offs	(1,424,218)	(1,798,301)
Recoveries	147,889	143,564
Reserve, end of period	\$ 1,946,848	\$ 2,405,864

### **6 BANK CREDIT FACILITY**

	MARCH 31 2008	DECEMBER 31 2007
Bank credit facility	\$ 66,415,953	\$ 58,213,096

The bank credit facility is a demand loan, which is the lesser at any time of: a) \$85,000,000 (December 31, 2007 – \$65,000,000) and b) the total of an advance rate applied to the value of acceptable outstanding finance receivables. The credit facility bears interest at prime plus 1.0%. The Fund also has the option to lock a portion of the outstanding loan balance, for a period of up to 180 days, in bankers' acceptance equivalent loans, which bear interest at the bankers' acceptance rate available at the inception of the equivalent loan, plus 2.5%. A stand-by fee of 0.25% per annum applies to the unused portion of the facility and is calculated, then applied to the outstanding bank credit facility balance, on a monthly basis. The stated maturity date of the credit facility is February 13, 2009 (December 31, 2007 – October 4, 2008). The collateral security lodged by the Fund to support the credit facility is a general security agreement covering all property held by the Fund. The terms of the credit facility provide for certain covenants, all of which the Fund was in compliance with at March 31, 2008.



**6 BANK CREDIT FACILITY (CONTINUED)**

The following table presents components of the outstanding bank credit facility where the interest rate is the bankers' acceptance rate available at the inception of the equivalent loan, plus 2.5%:

	MARCH 31 2008	DECEMBER 31 2007
Bankers' acceptance equivalent loans, interest rate of 7.31%, maturing on February 25, 2008	\$ -	\$ 10,000,000
Prime rate loan	66,622,067	48,273,029
Unamortized transaction costs	(206,114)	(59,933)
	<u>\$ 66,415,953</u>	<u>\$ 58,213,096</u>

**7 DEFERRED DEALER OBLIGATION**

THREE MONTHS ENDED	MARCH 31 2008	DECEMBER 31 2007
Deferred dealer obligation, beginning of period	\$ 2,190,247	\$ 2,704,883
Deferred dealer obligation on new volume	225,000	(257,982)
Advances to dealers	(237,243)	(256,654)
Deferred dealer obligation, end of period	<u>\$ 2,178,004</u>	<u>\$ 2,190,247</u>

**8 DERIVATIVES**

On August 23, 2007, the Fund entered into two interest rate swap agreements with a combined notional amount of \$20,000,000. The first agreement has a notional amount of \$10,000,000, a fixed bankers' acceptance rate of 4.92% and a three-year term ending on August 23, 2010. The second agreement has a notional amount of \$10,000,000, a fixed bankers' acceptance rate of 4.99% and a five-year term ending on August 23, 2012.

These interest rate swap agreements have been classified as "held-for-trading financial instruments," and are measured at fair value with all gains and losses recorded through net earnings. During the first quarter of 2008, a loss of \$532,789 (three months ended March 31, 2007 – \$nil) was expensed as a loss on derivatives, and the fair value of the interest rate swaps at March 31, 2008 was a liability of \$973,083 (December 31, 2007 – liability of \$440,294).



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**9 UNITHOLDERS' EQUITY**

Authorized:

The Fund's Deed of Trust provides that an unlimited number of trust units may be authorized and issued. Each trust unit is transferable, carries the right to one vote and represents an equal undivided beneficial interest in any distribution from the Fund and in the net assets of the Fund in the event of termination or winding-up of the Fund. All trust units are of the same class with equal rights and privileges.

THREE MONTHS ENDED	MARCH 31, 2008		DECEMBER 31, 2007	
	NUMBER	AMOUNT	NUMBER	AMOUNT
Unitholders' equity, beginning of period	23,305,906	\$ 24,099,492	23,305,906	\$ 26,028,097
Unit purchase repayment (financing)	16,660	51,666	-	-
Fund unit distribution (cash distribution)	-	(1,890,046)	-	(1,890,046)
Change in units in the period	16,660	(1,838,380)	-	(1,890,046)
Net loss for the period	-	(1,396,047)	-	(38,559)
Unitholders' equity, end of period	23,322,566	\$ 20,865,065	23,305,906	\$ 24,099,492

Unitholders' capital and deficit consist of the following components:

	MARCH 31 2008	DECEMBER 31 2007
Unitholders' capital		
Fund unit equity	\$ 29,019,494	\$ 28,967,828
Contributed surplus	615,362	615,362
	<u>29,634,856</u>	<u>29,583,190</u>
Deficit		
Accumulated net earnings	16,450,719	17,846,766
Accumulated unit distributions on fund unit equity	(3,681,095)	(3,681,095)
Accumulated cash distributions on fund unit equity	(21,539,415)	(19,649,369)
	<u>(8,769,791)</u>	<u>(5,483,698)</u>
Unitholders' equity	\$ 20,865,065	\$ 24,099,492

Unit purchase financing:

The Fund entered into unit loan agreements on March 31, 2006 with four individuals who are employees of the Fund. The loans have an aggregate principal amount of \$51,666 (December 31, 2007 – \$103,334), bear interest at the prescribed interest rate, as set by the Canada Revenue Agency, and are repayable in full on March 31, 2009. The loans are secured by 16,680 (December 31, 2007 – 33,340) trust units. As at March 31, 2008, the market value of the security was \$38,000 (December 31, 2007 – \$101,687).



## **10** CAPITAL DISCLOSURE

The Fund views its capital as the combination of its long-term debt and unitholders' equity balances, which is used to leverage the debt provided under the Fund's bank credit facility. In general, the overall capital of the Fund is evaluated and determined in the context of its financial objectives and its strategic plan.

While the Fund carries a level of cash on hand, this amount is insignificant in relation to its overall capital and is generally in an amount determined for short-term changes in non-cash working capital balances and to fund finance receivable acquisitions.

The Fund does not intend to repay the existing debt obligation under the bank credit facility. To fund the acquisition of receivables and grow the finance receivable portfolio, the Fund attempts to maximize the financial leverage available under the credit facility and when additional capital is required, it is raised through subordinated debenture or unit issuances. Generally, the Fund has maintained a high level of indebtedness in order to maximize returns on unitholders equity. The Fund has historically distributed a high portion of cash flow and has not focused on reducing indebtedness.

The Fund's indebtedness is subject to a number of covenants and restrictions including the requirement to meet certain financial ratios and financial condition tests at a consolidated level. These include, but are not limited to, a financial leverage ratio, an interest coverage ratio, a loan availability calculation, and a minimum loss reserve requirement.

The maximum financial leverage ratio permitted under these covenants is 3.75:1. This ratio was 3.19:1 at March 31, 2008 (March 31, 2007 – 2.75:1). The Fund maintains minimum loss reserves, as part of normal reporting obligations, while loan availability restrictions can be adjusted using capital infusions.

During the first quarter of 2008, the minimum interest coverage ratio was 1.50:1 measured on a quarterly basis, and the Fund requested and received an amendment to this quarterly test, as the interest coverage ratio was calculated as 0.22:1. The Fund requested and received an amendment of this covenant for a period of time to allow operational results to improve and to allow additional loss reserves required for portfolio growth to be covered by revenue increases. In the current market environment, the Board of Trustees believes that it is in the best interests of the Fund to meet its equity requirements through the retention of operating cash flow and issue units in lieu of cash.

With respect to its equity, the current level of capital is considered adequate in the context of current operations and the present strategic plan of the Fund. The equity component of capital increases or decreases based upon the income of the business less the cash distribution paid. The Fund will also review its level of equity in the context of the change in taxation, which impacts the Fund, commencing in 2011.

## **11** RELATED PARTY TRANSACTIONS

### **Patica Securities Limited**

The Fund has an agreement with Patica Securities Limited for services provided on an ongoing basis. These services include general strategic advice, advice on financial structure, advice on senior and/or subordinated debt and equity structure, communication with stakeholders and other general consulting services. Carfinco LP entered into a Consulting Services Agreement with Patica Securities Limited on October 1, 2003, and pursuant to this agreement, Carfinco LP incurs a fixed monthly fee of \$13,375, and a variable monthly fee of one-twelfth of 0.2% of the outstanding principal amount of the finance receivables. During the three months ended March 31, 2008, payments of \$92,265 (three months ended March 31, 2007 – \$79,441) were made to Patica Securities Limited and at March 31, 2008, there was \$31,461 (December 31, 2007 – \$30,401) payable to Patica Securities Limited. Patica Securities Limited is controlled by individuals who are Trustees of the Fund. The related party transactions occurred at the exchange amount, which is the consideration established and agreed to by the related parties.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

### **12** FINANCIAL INSTRUMENTS

#### **Recognition and measurement**

The Fund's financial instruments consist of cash and cash equivalents, finance receivables, bank credit facility, bank overdraft, accounts payable and accrued liabilities, deferred dealer obligation and derivatives. All financial instruments are classified into one of the following five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments, including derivatives, are included on the consolidated balance sheet and are measured at fair market value, except loans and receivables, investments held-to-maturity and other financial liabilities, which are measured at amortized cost. Subsequent measurement and recognition of changes in fair value of financial instruments depend on their initial classification. Held-for-trading financial investments are measured at fair value and all gains and losses are included in net income in the period in which they arise. Available-for-sale financial instruments are measured at fair value with revaluation gains and losses, net of tax, included in other comprehensive income until the instruments are derecognized or impaired.

The Fund has classified finance receivables as loans and receivables, cash as financial assets held for trading, and the bank credit facility, bank overdraft, accounts payable and accrued liabilities, deferred dealer obligation and long term-debt as other financial liabilities. Derivative instruments are recorded as financial assets or liabilities held for trading and are measured at their fair value unless exempted from derivative treatment as a normal purchase and sale. Certain derivatives embedded in other contracts must also be measured at fair value. The Fund has reviewed all significant contractual arrangements and determined there are no material embedded derivatives that must be separated from the host contract and accounted for separately.

Transaction costs relating to the renewal of the bank credit facility are recorded against the bank credit facility and are amortized over the expected life of the related debt using the effective interest method. Transaction costs relating to finance receivables are added to the initial carrying amount, and recognized into income using the effective interest method.

The estimated fair value of financial instruments has been determined using available market information or other appropriate valuation methodologies. However, considerable judgment is required in developing estimates of fair value. Therefore, estimates may not be indicative of the amounts that could be realized in an arm's length market exchange.

The nature of these instruments and the Fund's operations expose the Fund to interest rate risk and industry credit risk. The Fund manages its exposure to these risks by operating in a manner that minimizes its exposure to the extent practical.

#### **Interest rate risk**

Finance receivables bear interest at a fixed rate. Fixed rate finance receivable are subject to interest rate price risk, as the values will fluctuate, as a result of changes in market rates. The bank credit facility bears interest at a floating rate. The floating rate debt is subject to interest rate cash flow risk, as the required cash flows to service the debt will fluctuate, as a result of changes in market rates. The Fund attempts to mitigate this risk by using bankers' acceptance equivalent loans to lock the interest rate on a portion of the debt for short periods, and by using interest rate swap agreements to lock the interest rate on a portion of the debt for longer periods.



12 FINANCIAL INSTRUMENTS (CONTINUED)

**Liquidity risk**

The Fund depends on the bank credit facility with a syndicate of financial institutions to finance its funding of contracts. The bank credit facility has a maturity date of February 13, 2009. There can be no assurance that future borrowings will be available to the Fund, or available on acceptable terms or at an acceptable amount. If the Fund cannot successfully re-negotiate the loan prior to its due date or is only able to renegotiate on terms less favourable and/or more restrictive terms, the Fund's financial position would be adversely affected. Management, to reduce liquidity risk, has historically renewed the terms of the Fund's indebtedness in advance of its maturity dates.

**Credit risk**

The Fund's finance receivables are a result of transactions within the consumer finance industry and, as such, contain an element of credit risk in the event that the counter parties are unable to meet the terms of the agreements. The Fund secures individual finance receivables by registering a security interest/lien against tangible assets. The Fund performs ongoing credit evaluations of its customers' financial condition and limits the amount of credit extended when deemed necessary. The Fund maintains an allowance for credit losses, and any such losses to date have been within management's expectations.

**13 SUBSEQUENT EVENTS**

On May 15, 2008, the Fund executed the First Amendment to the Amended and Restated Credit Agreement, dated February 13, 2008. Certain terms within the agreement were modified.

**14 COMPARATIVE FIGURES**

Certain of the prior period comparative figures have been reclassified to conform to the current period presentation.



## UNITHOLDER INFORMATION

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David Rosenkrantz  
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Principal, Thales Alternative  
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Maurice Kagan  
President, Sparkle Solutions  
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Simon Serruya  
Owner and COO,  
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### OFFICERS (CARFINCO INC.)

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(General Partner for Carfinco LP)

Troy S.F. Graf  
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Co-lender

Bank of Montreal  
Co-lender

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