



MCAN MORTGAGE CORPORATION

**MANAGEMENT'S DISCUSSION AND
ANALYSIS OF OPERATIONS**

DECEMBER 31, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS OF OPERATIONS

This Management's Discussion and Analysis of Operations ("MD&A") should be read in conjunction with the consolidated financial statements and accompanying notes for the year ended December 31, 2009, which have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") and have been presented in Canadian currency. This MD&A has been prepared as at February 25, 2010.

Additional information regarding MCAN Mortgage Corporation (the "Company", "MCAN" or "we"), including copies of our continuous disclosure materials such as the Annual Information Form, is available on our website at www.mcanmortgage.com or through the System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com.

A NOTE ABOUT FORWARD LOOKING STATEMENTS

This report may contain forward-looking statements, including statements regarding the business and anticipated financial performance of the Company. These forward looking statements can generally be identified as such because of the context of the statements and often include words such as the Company "believes", "anticipates", "expects", "plans", "estimates" or words of a similar nature. These statements are based on current expectations, and are subject to a number of risks and uncertainties that may cause actual results to differ materially from those contemplated by the forward-looking statements. Some of the factors that could cause such differences include legislative or regulatory developments, competition, technology changes, global market activity, interest rates, changes in government and economic policy and general economic conditions in geographic areas where the Company operates. Reference is made to the risk factors disclosed herein and in the Company's 2010 Annual Information Form, which are incorporated herein by reference. These and other factors should be considered carefully and undue reliance should not be placed on the Company's forward-looking statements. Subject to applicable securities law requirements, we do not undertake to update any forward-looking statements.

DESCRIPTION OF THE BUSINESS

MCAN is a public company listed on the Toronto Stock Exchange under the symbol MKP and is a reporting issuer in all provinces and territories in Canada.

Our objective is to generate a reliable stream of income by investing our funds in a portfolio of mortgages (including single family residential, residential construction, non-residential construction and commercial loans), as well as other types of loans and investments, real estate and securitization investments. We employ leverage by issuing term deposits eligible for Canada Deposit Insurance Corporation ("CDIC") deposit insurance up to a maximum of five times capital (on a non-consolidated basis) as permitted by the *Income Tax Act* (Canada) (the "Tax Act"). The term deposits are sourced through a network of independent financial agents. In addition, our regulator, the Office of the Superintendent of Financial Institutions ("OSFI") has provided us with a consolidated regulatory assets to capital limit. As a mortgage investment corporation ("MIC"), we are entitled to deduct from income for tax purposes 50% of capital gains dividends and 100% of non-capital gains dividends paid by the Company. Such dividends are received by our shareholders as capital gains dividends and interest income, respectively.

RESULTS OF OPERATIONS

MCAN reported net income of \$24.7 million for the year ended December 31, 2009, down from \$30.3 million in the prior year. Earnings per share were \$1.73 compared to \$2.14 in the prior year, a decrease of 19%.

Selected Financial Information

(dollars in thousands except for per share amounts)	2009	2008	2007	Change from 2008	
				\$	%
Net investment income	\$ 30,641	\$ 36,082	\$ 18,926	\$ (5,441)	(15.1%)
Operating expenses	<u>5,899</u>	<u>5,734</u>	<u>4,109</u>	<u>165</u>	<u>2.9%</u>
Income before income taxes	24,742	30,348	14,817	(5,606)	(18.5%)
Provision for (recovery of) income taxes	<u>-</u>	<u>-</u>	<u>(26)</u>	<u>-</u>	<u>-</u>
Net income	<u>\$ 24,742</u>	<u>\$ 30,348</u>	<u>\$ 14,843</u>	<u>\$ (5,606)</u>	<u>(18.5%)</u>
Basic and diluted earnings per share	\$ 1.73	\$ 2.14	\$ 1.12	\$ (0.41)	(19.2%)
Dividends per share	\$ 1.44	\$ 0.96	\$ 1.00	\$ 0.48	50.0%
Assets	\$ 506,683	\$ 570,154	\$ 557,425	\$ (63,471)	(11.1%)
Liabilities	383,804	453,545	454,418	(69,741)	(15.4%)
Shareholders' equity	122,879	116,609	103,007	6,270	5.4%
Number of common shares outstanding at year-end	14,321	14,224	14,098	97	0.7%
Book value per common share	\$ 8.58	\$ 8.20	\$ 7.31	\$ 0.38	4.6%
Common share price - close	\$ 13.60	\$ 9.10	\$ 9.96	\$ 4.50	49.5%
Market capitalization	\$ 194,766	\$ 129,438	\$ 140,416	\$ 65,328	50.5%

Net Investment Income

(in thousands)	2009	2008	2007
Investment Income			
Mortgage interest	\$ 27,420	\$ 33,429	\$ 28,669
Interest on loans and investments	3,878	5,617	5,728
Securitization income	7,558	7,761	1,190
Fees	8,024	5,051	3,384
Equity income from MCAP Commercial LP	1,456	3,025	890
Interest on cash and cash equivalents	234	1,109	1,299
Gain on sale of mortgages	-	5,326	22
Marketable securities	-	(97)	956
	48,570	61,221	42,138
Financial Expenses			
Term deposit interest and expenses	13,133	20,684	18,996
Mortgage expenses	2,761	3,524	3,699
Provision for losses	2,035	931	517
	17,929	25,139	23,212
Net Investment Income	\$ 30,641	\$ 36,082	\$ 18,926

Net investment income was \$30.6 million in 2009, a decrease of \$5.5 million from \$36.1 million in 2008. The decrease is primarily due to one-time gains on sales of mortgages from the prior year, increased provisions for losses in the current year and a decrease in equity income from MCAP Commercial LP ("MCLP"), partly offset by higher income in the current year from discounted portfolios of mortgages acquired by both MCAN and MCLP.

During the year, we realized \$4.6 million (2008 - \$2.9 million) relating to the partial recovery of purchase price discounts on MCAN's acquired portfolios, included in mortgage interest income. We also received \$4.9 million (2008 - \$2.1 million) of fees from MCLP from a profit sharing arrangement relating to the aforementioned mortgage portfolios acquired by MCLP.

Mortgage interest income decreased by \$6.0 million from the prior year, primarily due to a \$56 million decrease in the average mortgage portfolio (from \$431 million in 2008 to \$375 million in 2009). The average mortgage yield decreased to 7.48% in 2009 from 7.66% in 2008, as the average prime rate decreased from 4.80% in 2008 to 2.42% in 2009. This decrease has negatively impacted mortgage interest income, as approximately 57% of our mortgages at year end were floating rate, compared to 56% at December 31, 2008. However, the impact of the decrease in the prime rate on the average mortgage yield was largely offset by the aforementioned significant increase in discount income realized on our portfolio of discounted mortgages.

The mortgages in the acquired portfolios have higher effective yields than those in our regular portfolio, as they have been acquired at a discount to their par values. The portion of the discount that we expect to recover is amortized into income over the remaining term of the respective mortgages. Upon the payout of a mortgage, the remaining unamortized discount is recognized as income.

Although we do not accrue interest on impaired mortgages, we include interest owing but not accrued in the mortgage yield calculation to accurately represent the underlying portfolio. Actual interest losses are incorporated into the yield once realized. During the year, interest owing but not accrued on impaired mortgages increased by \$772,000. The mortgage yield would have decreased by 0.20% to 7.28% if interest owing but not accrued was excluded from the yield calculation.

Interest on loans and investments decreased by \$1.7 million from the prior year, primarily due to the aforementioned decrease in the prime rate.

MCAN securitizes insured mortgages through the Canada Mortgage Bonds ("CMB") program. In the current year, we recognized securitization income of \$7.6 million compared to \$7.8 million in the prior year. Current year income consists of an up-front gain from securitization of \$6.4 million (2008 - \$3.3 million), residual securitization income of \$2.4 million (2008 - \$4.7 million) and a write-down on the interest-only strips of \$1.2 million (2008 - \$232,000). The increase in up-front gains from securitization is primarily due to an increase in our economic participation in the CMB program. Residual securitization income decreased as a result of negative fair value adjustments to CMB-related financial instruments of \$2.3 million (2008 - positive impact of \$3.4 million). In general, fair value changes in the interest rate swaps largely offset those in the interest-only strips, however significant fluctuations in the forward rate curve during 2009 had a negative impact to income. Other components of residual securitization income increased from \$1.3 million to \$4.7 million due to an increase in refinancing and renewal gains and a larger CMB portfolio.

During the year, a net write-down of \$1.2 million was recorded on the outstanding interest-only strips. To the time of the write-down, the prepayment level of CMB mortgages was significantly higher than anticipated and decreased expected future cash flows, as the assets in which principal collections are reinvested generally yield less than the securitized mortgages.

Fees increased by \$3.0 million over 2009, primarily due to the increase in fees received from MCLP in regards to the profit sharing arrangement noted above. Fees also include commitment, extension, renewal and letter of credit fees earned on our mortgage portfolio.

Equity income of \$1.5 million from our ownership in MCLP decreased significantly from \$3.0 million in the prior year due to decreases in MCLP's loan origination volumes and one-time gains from sales of mortgages from the acquired portfolios realized in 2008.

Interest on cash and cash equivalents decreased by \$875,000 over the prior year due to a lower average prime rate in 2009.

In 2008, we earned \$5.3 million from sales of mortgages, primarily from the acquired portfolios.

Term deposit interest and expenses decreased by \$7.6 million from 2008. The decrease was due to a \$66 million decrease in the average term deposit balance to \$372 million in 2009 from \$438 million in 2008 and a decrease in the average term deposit rate to 3.12% in 2009 from 4.39% in 2008.

Mortgage expenses, consisting primarily of mortgage servicing expenses, were \$2.8 million compared to \$3.5 million in the prior year, consistent with the decrease in the average mortgage portfolio.

Credit Quality

Provisions for losses in the current and prior year were as follows:

(in thousands)	2009	2008
Mortgages - general provision (recovery)	\$ (497)	\$ (478)
Mortgages - specific provision	2,618	97
Loans and investments - general provision (recovery)	(186)	106
Securitization investments - write-down	100	2,000
Securitization investments - recovery of write-down	-	(794)
	\$ 2,035	\$ 931

Specific provision activity consists of new provisions of \$2.7 million on three residential construction loans and a decrease of \$109,000 relating to uninsured single family mortgages. The construction loans consist of MCAN's 20% participation in a multi-phased land development loan that has experienced slow sales and cost increases, a land loan that has been delayed by municipal negotiations and a small land development loan that has experienced slow sales and cost increases. Given the timeline for repayment and market price point fluctuations, specific provisions have been established for anticipated losses.

Write-offs were 5.2 basis points (\$194,000) on average mortgage balances, compared to 2.3 basis points (\$100,000) in the prior year. The majority of the aforementioned reduction in specific provisions on uninsured single family was due to write-offs recognized during the year.

During 2008, we recorded a \$2.0 million write-down on an investment that was subject to the restructuring of Third Party Structured Asset-Backed Commercial Paper ("ABCP") by the Pan-Canadian Investors Committee (the "Montreal Accord"). The restructuring, which was finalized in early 2009, converted the existing investment into a Master Asset Vehicle II ("MAV II") investment. Following the restructuring, we maintained the \$2.0 million write-down on the MAV II investment, however it was increased to \$2.1 million at year-end based on its fair market value at that time.

Impaired mortgages net of specific allowances are as follows:

(in thousands)	December 31 2009	December 31 2008
Residential construction	\$ 15,815	\$ -
Uninsured single family	1,356	3,438
	\$ 17,171	\$ 3,438
	5.81%	0.80%

Impaired loans increased significantly during 2009, mostly due to the impairment of the aforementioned residential construction loans on which we recorded new specific allowances during the year. We continue to proactively monitor loan arrears and take prudent steps to collect overdue accounts. Although impaired mortgages increased during the year, total mortgage arrears decreased from \$34 million to \$31 million.

Operating Expenses

(in thousands)	2009	2008	2007
Salaries and benefits	\$ 2,587	\$ 2,226	\$ 1,878
General and administrative	3,312	3,508	2,231
	\$ 5,899	\$ 5,734	\$ 4,109

Operating expenses increased by \$165,000 over the prior year. Salaries and benefits increased as a result of an increase in the number of employees, while general and administrative expenses decreased due to one-time expenses relating to the acquired portfolios in 2008.

Income Taxes

(in thousands)	2009	2008	2007
Provision (recovery) against income	\$ -	\$ -	\$ (26)
Charge (recovery) to retained earnings	(679)	6,059	873
	\$ (679)	\$ 6,059	\$ 847

We have taken the position that it is more likely than not that sufficient dividends will be paid to shareholders in future periods to recover current and future taxes. As a result of this, we charge (recover) our current and future tax liabilities directly to retained earnings. The provision for taxes recorded in the consolidated statements of income relates to taxes that cannot be recovered from the payment of future dividends.

During 2009, there was a small recovery of taxes to retained earnings, primarily due to a decrease in the magnitude of the March 31, 2010 dividend compared to 2009. A future tax liability arises due to the fact that this dividend had not yet been paid as of year-end but is deductible from 2009 taxable income. As at December 31, 2009, this liability was significantly lower than the corresponding liability from the prior year due to the lower March 2010 dividend, which led to the recovery of taxes during the year. The current year recovery of taxes was partly offset by the future tax charge to retained earnings that arose from new CMB issuances in 2009, as we recognize up-front gains from securitization for accounting purposes but recognize taxable income as cash is received over the duration of the issuance.

Cash Flows

Operating activities provided cash flows of \$23 million in 2009 and provided \$16 million in 2008. Although net income was lower in the current year, the impact of the non-cash component of income was significantly higher in 2008 than in 2009.

Investing activities provided cash flows of \$94 million in 2009 and provided \$19 million in 2008. The variance is a result of a significant increase in net mortgage inflows in 2009.

Financing activities used cash flows of \$85 million in 2009 and used \$31 million in 2008. The net term deposit outflow increased significantly in 2009, while dividends paid also increased.

Summary of Three Year Results of Operations

Net income in 2009 decreased by \$5.6 million from 2008. Our profitability remained strong as a result of significant securitization income and income from the acquired portfolios. The one-time gains from sale of mortgages in 2008 and the higher provisions for losses in 2009 comprised the majority of the decrease.

The increase in net income in 2008 over 2007 of \$16.0 million was due to significant mortgage interest income, fee income and gains from sales relating to the acquired portfolios. In addition, we had significantly higher securitization income from our participation in the CMB program and an increase in equity income from MCLP.

SUMMARY OF FOURTH QUARTER RESULTS

The Company reported net income for the quarter ended December 31, 2009 of \$6.1 million (\$0.43 per share), down from \$9.9 million (\$0.70 per share) a year earlier as follows:

(in thousands, except for per share amounts)

For the Quarters Ended December 31	2009	2008
Net investment income	\$ 8,056	\$ 11,471
Operating expenses	1,952	1,551
Income before income taxes	6,104	9,920
Provision for income taxes	-	-
Net income	\$ 6,104	\$ 9,920
Basic and diluted earnings per share	\$ 0.43	\$ 0.70
Dividends per share	\$ 0.26	\$ 0.25

Net Investment Income

(in thousands)

For the Quarters Ended December 31	2009	2008
Investment Income		
Mortgage interest	\$ 7,413	\$ 8,643
Interest on loans and investments	910	1,133
Securitization income	1,801	2,765
Fees	1,893	1,783
Equity income from MCAP Commercial LP	523	788
Interest on cash and cash equivalents	34	183
Gain on sale of mortgages	-	1,851
	12,574	17,146
Financial Expenses		
Term deposit interest and expenses	2,525	4,901
Mortgage expenses	615	877
Provision for (recovery of) losses	1,378	(103)
	4,518	5,675
Net Investment Income	\$ 8,056	\$ 11,471

Net investment income decreased by \$3.4 million over the prior year. The decrease is primarily due to a one-time gain on the sale of mortgages in the prior year (\$1.9 million), increased provisions for losses (\$1.5 million) and decreases in mortgage interest income (\$1.2 million) and securitization income (\$964,000), partly offset by a decrease in term deposit interest and expenses (\$2.4 million).

Mortgage interest income decreased by \$1.2 million due to an \$81 million decrease in the average mortgage portfolio, partially offset by a 0.63% increase in the average mortgage yield through the realization of increased discount income. Interest on loans and investments, fee income and equity income from MCLP were comparable to the prior year. Securitization income decreased as a result of current year negative mark-to-market adjustments.

Term deposit interest and expenses decreased by \$2.4 million as a result of a 1.87% decrease in the average interest rate and a \$87 million decrease in the average outstanding balance. Mortgage expenses decreased by \$262,000 on a smaller average portfolio. Provisions for losses of \$1.4 million consisted primarily of the increase of an existing specific mortgage provision by \$1.5 million, compared to recoveries of \$103,000 in 2008.

Operating Expenses

Operating expenses were \$2.0 million for the quarter, up from \$1.6 million last year.

(in thousands)

For the Quarters Ended December 31	2009	2008
Salaries and benefits	\$ 933	\$ 682
General and administrative	1,019	869
	\$ 1,952	\$ 1,551

SELECTED QUARTERLY FINANCIAL DATA

(in thousands, except per share amounts)

	2009				2008			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net investment income	\$7,703	\$6,875	\$8,007	\$8,056	\$6,064	\$6,062	\$12,485	\$11,471
Operating expenses	1,269	1,268	1,410	1,952	922	1,173	2,088	1,551
Income before income taxes	6,434	5,607	6,597	6,104	5,142	4,889	10,397	9,920
Provision for income taxes	-	-	-	-	-	-	-	-
Net income	<u>\$6,434</u>	<u>\$5,607</u>	<u>\$6,597</u>	<u>\$6,104</u>	<u>\$5,142</u>	<u>\$4,889</u>	<u>\$10,397</u>	<u>\$9,920</u>
Basic and diluted earnings per share	\$0.45	\$0.39	\$0.46	\$0.43	\$0.36	\$0.35	\$0.73	\$0.70
Dividends per share								
Regular	\$0.68	\$0.25	\$0.25	\$0.26	\$0.12	\$0.23	\$0.25	\$0.25
Capital gains	-	-	-	-	0.11	-	-	-
Total	<u>\$0.68</u>	<u>\$0.25</u>	<u>\$0.25</u>	<u>\$0.26</u>	<u>\$0.23</u>	<u>\$0.23</u>	<u>\$0.25</u>	<u>\$0.25</u>

After a stable first half of the year, the second half of 2008 had a significant increase in net income due to substantial income from the sale of mortgages and income earned from the acquired portfolios. Securitization income and income from the acquired portfolios remained strong during 2009.

FINANCIAL POSITION

Total assets were down \$63 million from December 31, 2008. This change consisted of decreases of \$98 million in mortgages, \$19 million in loans receivable and other investments and \$12 million in derivative financial instruments, partially offset by increases of \$32 million in cash and \$34 million in securitization investments.

Assets

(in thousands)

	2009		2008		2007	
Cash and cash equivalents	\$ 89,843	17.7%	\$ 58,071	10.2%	\$ 53,804	9.7%
Mortgages	295,415	58.3	393,010	68.9	412,685	74.0
Securitization investments	73,590	14.5	39,743	7.0	36,381	6.5
Loans receivable and other investments	16,885	3.3	35,624	6.2	34,905	6.3
Equity investment in MCLP	17,905	3.5	18,300	3.2	17,095	3.1
Derivative financial instruments	11,490	2.3	23,541	4.2	526	0.1
Other assets	1,555	0.4	1,865	0.3	1,873	0.3
Marketable securities	-	-	-	-	156	-
	\$ 506,683	100.0%	\$ 570,154	100.0%	\$ 557,425	100.0%

Cash equivalents include term deposits and bankers' acceptances. These investments ensure adequate liquidity to meet maturing term deposit and new mortgage commitments. In general, we manage our cash and cash equivalents in the \$20 to \$30 million range, however the year-end balance was extremely high as we received proceeds from significant mortgage sales near the end of 2009.

The composition of our mortgage portfolio at December 31, 2009 and 2008 is as follows:

	2009			2008		
	Principal	Allowance	Net	Principal	Allowance	Net
Single family uninsured	\$ 127,889	\$ 874	\$ 127,015	\$ 189,867	\$ 1,370	\$ 188,497
Single family insured	38,990	-	38,990	28,034	-	28,034
Construction	126,059	3,728	122,331	153,772	1,333	152,439
Commercial	7,207	128	7,079	24,140	100	24,040
	\$ 300,145	\$ 4,730	\$ 295,415	\$ 395,813	\$ 2,803	\$ 393,010

We invest in insured and uninsured single family mortgages in Canada. We believe that the Canadian residential property market continues to exhibit healthy fundamentals. We do not invest in the United States mortgage market. The uninsured mortgages we invest in may not exceed 80% of the value of the real estate securing such loans at the time of funding. For the purposes of this ratio, value is the appraised value of the property as determined by a qualified appraiser at the time of funding. Residential mortgages insured by Canada Mortgage and Housing Corporation or Genworth Financial Mortgage Insurance Company Canada may exceed this ratio.

Uninsured residential construction loans are made to homebuilders to finance residential construction projects. These loans generally have a floating rate of interest and terms of one to two years. Our limit on conventional construction loans is 250% of regulatory capital. Non-residential construction loans may comprise up to one half of this limit. The maximum single conventional construction loan may not exceed the lesser of \$13.5 million or 20% of regulatory capital as per our internal limits.

Mortgages decreased by \$98 million during 2009 (see Note 4 to the consolidated financial statements). The decrease consisted of decreases of \$30 million in construction loans, \$17 million in commercial loans and \$61 million of uninsured single family mortgages, partially offset by an increase of \$11 million in insured single family mortgages. Due to adverse market conditions, we have continued to be selective in our mortgage approvals. Consequently, we have observed significant repayments on our uninsured single family mortgage portfolio. In addition, we have been applying minimum rates on renewed and newly funded construction loans where possible and aggressively managing the repayment of these loans, as they are mostly prime-based and have less attractive yields in the current interest rate environment.

Abnormally low interest rates have contributed to a stabilization of residential property values across Canada. However, weak employment levels have resulted in higher arrears levels. Our account management and that of our mortgage servicers is proactive in managing arrears. We believe that these factors will mitigate loan losses. We continue to regard residential mortgages as a solid investment asset class.

As at December 31, 2009, we held discounted mortgages with a net discount of \$22 million (2008 - \$33 million). We retain 50% of any recoveries of that amount, and we pay the remaining 50% to MCLP. The amount of the discount ultimately recovered is dependent on the value of the real estate securing the mortgage, as well as the financial capacity of the borrower. Additionally, these mortgages have maturity dates ranging from 2010 (for certain fixed rate mortgages) to 2032 (for certain floating rate mortgages). As such, it is difficult to accurately estimate the timing and quantum of the discount ultimately recovered.

Securitization investments consist of investments in securitization programs, the interest-only strips from the CMB program and insured mortgage-backed securities (see Note 5 to the consolidated financial statements). Securitization investments increased by \$34 million in 2009 primarily due to increases of \$28 million in insured mortgage backed securities and \$14 million in CMB interest-only strips, partly offset by a decrease of \$8 million in investments in securitization programs.

Loans receivable and other investments (see Note 6 to the consolidated financial statements) decreased by \$19 million during the year as a result of the full payout of two existing balances and the partial repayment of two additional loans.

Our largest single investment is our minority interest in MCLP. We intend to continue to participate in the mortgage origination and servicing business through our interest in MCLP. MCLP is an originator and servicer of mortgage loans for third party investors in Canada. We outsource our mortgage and loan origination and servicing to MCLP and other third party servicers.

Derivative financial instruments at December 31, 2009 consist of interest rate swaps relating to the CMB program. We have entered into "pay-floating, receive-fixed" swaps to hedge against interest rate risk on reinvested CMB principal collections. The fair market value of the swaps decreased significantly during 2009 as a result of a substantial increase in forward interest rates.

Other assets include capital assets, prepaid expenses, accounts receivable and deferred costs.

Liabilities and shareholders' equity

(in thousands)	2009	2008	2007	Change from	
				2008	2007
Liabilities					
Term deposits	\$ 360,744	\$ 426,663	\$ 445,368	\$ (65,919)	\$ (84,624)
Securitization liabilities	5,048	7,095	-	(2,047)	5,048
Accounts payable and accrued charges	11,001	12,186	8,089	(1,185)	2,912
Future taxes payable	7,011	7,601	961	(590)	6,050
	383,804	453,545	454,418	(69,741)	(70,614)
Shareholders' equity					
Share capital	98,490	97,493	96,370	997	2,120
Contributed surplus	510	510	510	-	-
Retained earnings	22,165	17,313	6,654	4,852	15,511
Accumulated other comprehensive income (loss)	1,714	1,293	(527)	421	2,241
	122,879	116,609	103,007	6,270	19,872
	\$ 506,683	\$ 570,154	\$ 557,425	\$ (63,471)	\$ (50,742)

Term deposit liabilities decreased by \$66 million during the year, consistent with the change in assets.

Securitization liabilities relate to CMB interest-only strips in liability positions, discussed below in the "CMB Program" disclosure.

Total shareholders' equity of \$123 million increased by \$6 million from December 31, 2008. The increase is primarily due to the significant excess of 2009 net income (\$24.7 million) over dividends declared (\$20.6 million). Since we are able to deduct dividends paid up to 90 days after year-end from taxable income, there is sometimes a year-end disconnect between these two components of retained earnings. In addition, there are generally differences between income for accounting purposes and taxable income. We issued \$843,000 of new shares on a quarterly basis under the dividend reinvestment plan at the average closing price for the 20 days preceding such issues. There was also a \$679,000 recovery to retained earnings related to current and future income taxes and a \$421,000 increase in accumulated other comprehensive income.

CMB PROGRAM

We participate in the CMB program, which involves the securitization of insured single family and multi family mortgages. The current year was the first in which we securitized insured multi family mortgages. We participate in the CMB program with MCLP and a private company. For accounting purposes, we recognize an up-front gain on securitization, and at that time we recognize an interest-only strip, which is a retained interest in the securitized mortgages. The interest-only strips consist of the discounted value of future mortgage interest, principal reinvestment interest receipts and penalty income less coupon interest payments. The interest-only strips are generally in asset positions, however they can potentially go into liability positions upon a significant decrease in forward interest rates after issuance, which occurred with certain interest-only strips in 2008. In addition, we recognize liabilities for future mortgage servicing and other costs, which we subcontract to MCLP and the private company that participates in the CMB program. For tax purposes, we recognize CMB-related income on the cash basis, wherein the payment of upfront CMB expenses is a deduction from taxable income at the date of issuance, and the ongoing collection of net CMB cash flows is recognized in taxable income as received over the duration of the issuance. In the early years of a CMB issuance, taxable income is significantly lower than accounting income due to the absence of an upfront gain on securitization for tax purposes to offset upfront cash requirements. However, taxable income significantly exceeds accounting income in the later years of a CMB issuance, in line with the receipt of ongoing CMB cash flows such as mortgage interest and principal reinvestment interest.

In addition, we earn residual securitization income, which includes the net yield earned on the interest-only strips and the CMB liabilities, refinancing and renewal gains, interest rate swap receipts (payments) and fair value changes in the interest-only strips and interest rate swaps.

During the year, we securitized \$836 million of mortgages through the CMB program. We recorded \$10.9 million of interest-only strips and \$1.5 million of liabilities on the respective closing dates.

As part of the CMB program, we enter into "pay-floating, receive-fixed" interest rate swaps. The purpose of these swaps is to hedge interest rate risk on the interest-only strips. We receive interest on reinvested CMB principal collections, the discounted future value of which is included in the interest-only strips.

During the year, we recorded a net write-down of \$1.2 million on the outstanding interest-only strips. To the time of the write-down, the prepayment level of CMB mortgages was significantly higher than anticipated and decreased expected future cash flows, as the assets in which principal collections are reinvested generally yield less than the securitized mortgages. At the time that the write-down was recorded, we revised the calculation of the fair value of the interest-only strips to include the discounted

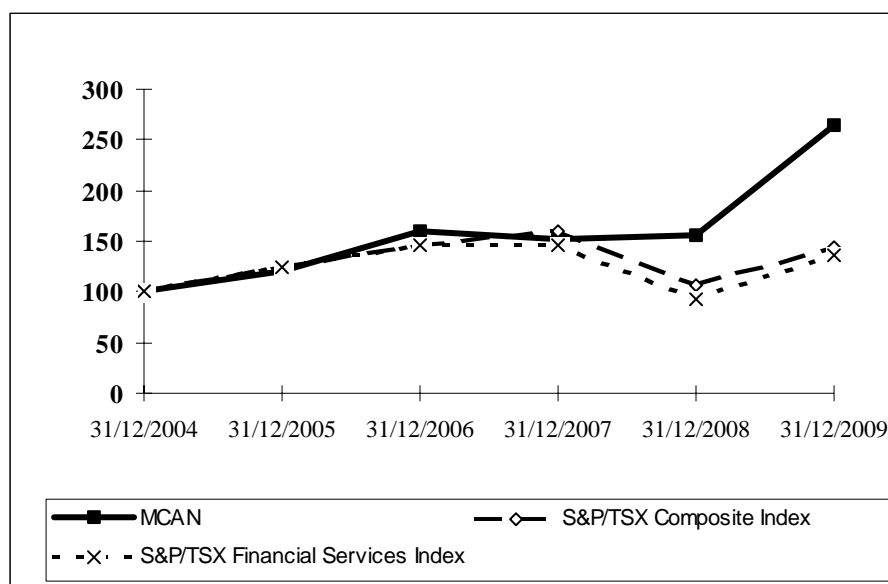
value of future penalty income as a result of a recent significant increase in mortgage liquidations. This revision had a positive impact to income of \$1.0 million, which is included in the net interest-only strip write-down of \$1.2 million.

Our participation in the CMB program may be reduced in the future, as discussed below in "Risk Management".

PERFORMANCE CHARTS

Shareholder Return

The following graph compares MCAN's cumulative total shareholder return (assuming an investment of \$100 on December 31, 2004) on its common shares during the period from January 1, 2005 to December 31, 2009, with the S&P/TSX Composite Index (Total Return) and the S&P/TSX Financial Services Index (Total Return), assuming reinvestment of all dividends.



	Dec 31 2004	Dec 31 2005	Dec 31 2006	Dec 31 2007	Dec 31 2008	Dec 31 2009	Compound Annual Growth
MCAN	100	121	160	153	155	264	21.4%
TSX	100	124	146	160	107	145	7.7%
TSX Financial Services	100	124	147	145	93	136	6.3%

Note: Dividends declared on MCAN's common shares are assumed to be reinvested at the closing price on the payment date.

Ten Year Financial Summary

(in thousands, except per share amounts)

	As at December 31					
	Net Income	Earnings Per Share	Dividends Per Share	Total Assets	Shareholders' Equity	Market Capitalization
2009	\$ 24,742	\$ 1.73	\$ 1.44	\$ 506,683	\$ 122,879	\$ 194,766
2008	30,348	2.14	0.96	570,154	116,609	129,438
2007	14,843	1.12	1.00	557,425	103,007	140,416
2006	15,211	1.23	1.18	498,107	84,611	141,052
2005	14,116	1.18	0.97	434,369	81,164	116,918
2004	11,601	1.12	1.11	454,365	74,965	103,374
2003	8,247	0.84	0.68	369,477	61,741	83,747
2002	5,430	0.58	0.68	327,059	58,383	80,293
2001	6,795	0.85	0.68	222,397	48,149	72,656
2000	6,210	0.80	0.68	243,567	42,945	54,103

DESCRIPTION OF CAPITAL STRUCTURE

The authorized share capital of the Company consists of an unlimited number of common shares with no par value. At December 31, 2009, there were 14,320,980 common shares outstanding. At February 25, 2010 there were 14,334,082 common shares outstanding. Additional information related to the share capital is included in Note 16 to the consolidated financial statements.

DIVIDEND POLICY AND RECORD

Our dividend policy is to pay out substantially all of our taxable income to our shareholders. As a MIC under the Tax Act, we can deduct dividends paid to shareholders during the year and within 90 days thereafter from income for tax purposes. We pay out substantially all of our taxable income to shareholders, whereas other financial institutions generally pay out only a portion of their taxable income to their shareholders. These dividends are taxable in the shareholders' hands as interest. In addition, a MIC can pay certain capital gains dividends which are taxed as capital gains in the shareholders' hands. We intend to continue to declare dividends on a quarterly basis.

Dividends per share over the past three years are as follows:

Fiscal Period	2009	2008	2007
First Quarter - Regular Dividend	\$ 0.25	\$ 0.23	\$ 0.23
First Quarter - Extra Dividend	0.43	-	0.08
Second Quarter	0.25	0.23	0.23
Third Quarter	0.25	0.25	0.23
Fourth Quarter	0.26	0.25	0.23
	\$ 1.44	\$ 0.96	\$ 1.00
Taxable Dividends	\$ 1.44	\$ 0.85	\$ 0.88
Capital Gains Dividends	-	0.11	0.12
	\$ 1.44	\$ 0.96	\$ 1.00

The Board of Directors declared a first quarter dividend of \$0.41 per share to be paid March 31, 2010 to shareholders of record as of March 15, 2010. The dividend comprises the regular quarterly dividend of \$0.26 and a \$0.15 extra dividend.

The March 2010 extra dividend is required to pay out the balance of taxable income to shareholders, despite the fact that taxable income is significantly lower than income for accounting purposes, primarily due to our participation in the CMB program. The March 2009 dividend had a similar relationship between income for accounting and tax purposes. There was no extra dividend distributed to shareholders in March 2008, although we maintained the regular quarterly dividend at that time.

OFF BALANCE SHEET ARRANGEMENTS

We commit to fund mortgages to borrowers in advance of funding at agreed upon interest rates. Substantially all of these commitments relate to floating rate construction loans. At December 31, 2009, outstanding commitments for future fundings of mortgages intended for our portfolio were \$96 million.

Off balance sheet arrangements relating to the CMB program are discussed in the "CMB Program" section above.

CONTRACTUAL OBLIGATIONS

We have contractual obligations to make principal and interest payments on term deposits and an operating lease. In addition, we have outstanding commitments for future fundings of mortgages intended for our own portfolio, as discussed above.

As part of the CMB program, we are required to pay servicing expenses on the securitized mortgages and other ongoing costs.

(in thousands)	Less than one year	One to five years	Over five years	Total
Term deposits	\$ 339,553	\$ 21,191	\$ -	\$ 360,744
Operating lease	171	299	-	470
Mortgage fundings	86,556	9,617	-	96,173
CMB obligations	984	2,268	-	3,252
	\$ 427,264	\$ 33,375	\$ -	\$ 460,639

We outsource our mortgage and loan origination and servicing. We continue to pay servicing expenses as long as the mortgages and loans remain on our balance sheet.

TRANSACTIONS WITH RELATED PARTIES

In 2009, we purchased mortgage origination and administration services and certain corporate services at a cost of \$2.2 million from MCLP while we received fees of \$2.4 million from MCLP. Corporate services include premises and systems. The fees received from MCLP include commitment, extension, renewal and letter of credit fees. We use MCLP's systems, including networks, subsystems, and general ledger. We also receive technology support from MCLP.

In 2009, we paid MCLP \$5.6 million of fees relating to a profit sharing arrangement on a portfolio of discounted mortgages. We received \$4.9 million from MCLP relating to a profit sharing arrangement on a portfolio of discounted mortgages.

In 2004, we entered into an arrangement with MCLP to sublease space at 200 King Street West, Toronto, Ontario, expiring in 2012.

The Company has established an Executive Share Purchase Plan (the "Share Purchase Plan") whereby the Board of Directors can approve loans to key personnel for the purpose of purchasing the Company's shares. The aggregate number of common shares issued pursuant to the Share Purchase Plan may not exceed 480,000, provided that the number of common shares which may be issued pursuant to the Share Purchase Plan together with common shares which may be issued pursuant to any other MCAN share compensation agreements may not exceed 10% of the outstanding common shares, and the common shares which may be issued pursuant to the Share Purchase Plan to any one person may not exceed 5% of the outstanding common shares. At December 31, 2009, \$1.4 million of loans were outstanding. Subsequent to year-end, the approved amount of loans was increased from \$1,620,000 to \$1,720,000, however no new loans were advanced under the Share Purchase Plan. The loans under the Share Purchase Plan bear interest at prime plus 1% and have a five-year term. MCAN, at its discretion, reimburses officers the interest amount in connection with loans provided pursuant to the Share Purchase Plan. Additional information related to the Share Purchase Plan is included in Note 16 to the consolidated financial statements and in our Management Information Circular dated March 12, 2010.

CAPITAL MANAGEMENT

We derive our net investment income from the investment of our equity and the difference or spread between amounts earned on our assets and the cost of the term deposits that we issue to fund such assets. As a MIC under the Tax Act, we are limited to a liabilities to capital ratio of 5:1 (or an assets to capital ratio of 6:1), based on our non-consolidated balance sheet measured at its tax value. As a loan company under the *Trust and Loan Companies Act* (the "Trust Act"), OSFI regulates our consolidated regulatory assets to capital and has granted us a maximum consolidated regulatory assets to capital ratio. We borrow to the extent that we are satisfied that the borrowing and additional investments will increase our overall profitability.

OSFI has issued guidelines to federally regulated companies for capital adequacy, which include meeting a minimum regulatory capital to risk-weighted assets ratio of 10% for total capital and 7% for Tier 1 capital. Our target minimum Tier 1 and Total capital ratios are both 15%.

Our income tax assets and capital, regulatory assets and capital, and maximum assets and ratios over the past three years are as follows:

December 31 (dollar amounts in thousands)	2009	2008	2007
Tax Act Test			
Income Tax Assets	\$ 488,024	\$ 551,589	\$ 552,531
Income Tax Capital	\$ 120,732	\$ 115,998	\$ 100,780
Income Tax Assets to Capital ratio	4.04	4.76	5.48
Maximum Assets (non-consolidated)	\$ 724,392	\$ 695,988	\$ 604,680
Maximum Assets to Capital ratio	6.00	6.00	6.00
Regulatory Test (OSFI)			
Regulatory Assets	\$ 508,351	\$ 578,124	\$ 569,269
Regulatory Capital	\$ 110,231	\$ 107,991	\$ 100,554
Regulatory Assets to Capital ratio	4.61	5.35	5.66
Total Regulatory Capital to Risk-Weighted Assets ratio	27.47%	23.69%	21.53%
Minimum Total Regulatory Capital to Risk-Weighted Assets ratio	10.00%	10.00%	10.00%
Tier 1 Regulatory Capital to Risk-Weighted Assets ratio	27.75%	24.09%	22.16%
Minimum Tier 1 Regulatory Capital to Risk-Weighted Assets ratio	7.00%	7.00%	7.00%

We are limited to the lowest maximum assets amount in the above two asset tests, and the maximum leverage permitted under the Tax Act is more constraining on the Company than the regulatory assets to capital ratio mandated by OSFI. We manage our assets to a level of 5.75 times capital on a tax basis to provide a prudent cushion between the maximum and total actual assets.

We fund the majority of our investments through the issue of term deposits eligible for CDIC deposit insurance with varying maturities in certain provinces of Canada. We do not use capital markets (including asset-backed commercial paper) for liquidity.

For additional information on our capital management, refer to Note 19 to the consolidated financial statements.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

The majority of our consolidated balance sheet consists of financial instruments, and the majority of net income is derived from the related income, expenses, gains and losses. Financial instruments include cash and cash equivalents, mortgages, securitization investments, loans receivable and other investments, term deposits and derivative financial instruments, which are discussed throughout this MD&A.

The use of financial instruments exposes us to interest rate, credit, liquidity and market risk. A discussion of these risks and how these risks are managed is found under "Risk Management", below.

Information on the financial statement classification and amounts of income, expenses, gains and losses associated with the instruments are located in the Results from Operations and Financial Position sections of the MD&A. Information on the determination of the fair market value of financial instruments is located in the Critical Accounting Policies and Estimates section of the MD&A.

LIQUIDITY

We closely monitor our liquidity position to ensure that we have sufficient cash to meet liability obligations as they become due. The Investment Committee of the Board ("ICB") is responsible for the review and approval of liquidity policies. The Asset and Liability Management Committee ("ALCO") is responsible for liquidity management. In general, we maintain a standard level of liquid investments and credit facilities of at least 20% of term deposits maturing within 100 days. In addition, all single family mortgages are readily marketable within a time frame of one to three months, providing us with added flexibility to meet our liquidity needs. We have access to capital through our ability to issue term deposits eligible for CDIC deposit insurance. These term deposits also provide us with the ability to fund asset growth as needed. We also have a \$30 million banking facility in place to fund asset growth or meet short-term funding obligations as required. We believe that our liquidity position and our access to capital markets support our ability to meet current and future commitments. We are not aware of any contingencies or known events that are likely to materially affect our liquidity position.

During 2008, our liquidity management was enhanced with the formalization of a Liquidity Risk Management Framework that included the introduction of multi scenario stress testing. Results of the stress testing are reported to management on a monthly basis and to the ICB on a quarterly basis.

The composition of our liquidity ratios over the last three years is as follows:

As at December 31	2009	2008	2007
Tier 1 liquidity			
Cash and cash equivalents	\$ 89,843	\$ 58,071	\$ 53,804
Less: cash pledged as collateral	(1,642)	-	-
Banking facility	30,000	30,000	30,000
	<u>118,201</u>	<u>88,071</u>	<u>83,804</u>
Tier 2 liquidity			
75% of eligible insured single family mortgages	<u>6,665</u>	<u>9,864</u>	<u>11,001</u>
Total liquidity	<u>\$ 124,866</u>	<u>\$ 97,935</u>	<u>\$ 94,805</u>
100 day term deposit maturities	<u>\$ 111,125</u>	<u>\$ 131,696</u>	<u>\$ 101,634</u>
Liquidity ratios			
Tier 1 liquidity to 100 day term deposit maturities	106%	67%	82%
Total liquidity to 100 day term deposit maturities	<u>112%</u>	<u>74%</u>	<u>93%</u>

We have established and maintain liquidity policies which meet the standards set under the Trust Act and any regulations or guidelines issued by OSFI.

A further analysis of our liquidity risks is found under "Risk Management" below.

RISK FACTORS

We are exposed to a number of risks that can adversely affect our ability to achieve our business objectives or execute our business strategies, and which may result in a loss of earnings, capital or reputation. The risks identified by MCAN may not be the only risks faced by the Company. Other risks of which the Company is not aware of which the Company currently deems to

be immaterial may surface and have a material adverse impact on the Company's business, results from operations and financial condition.

The significant risks to which we are exposed are as follows:

Credit Risk

Credit risk is the risk of financial loss resulting from the failure of a counterparty, for any reason, to fully honour its financial or contractual obligations to the Company, primarily arising from our mortgage and lending activities. Fluctuations in real estate values may increase the risk of default and may also reduce the net realizable value of the collateral property to the Company. These risks may result in defaults and credit losses, which may result in a loss of earnings. Credit losses occur when a counterparty fails to meet its obligations to the Company and the value realized on the sale of the underlying security deteriorates below the carrying amount of the exposure.

Liquidity Risk

Liquidity risk is the risk that cash inflows, supplemented by assets readily convertible to cash, will be insufficient to honour all cash outflow commitments (both on and off-balance sheet) as they come due. The failure of borrowers to make regular mortgage payments increases the uncertainties associated with liquidity management, notwithstanding that we may eventually collect the amounts outstanding, which may result in a loss of earnings or capital, or have an otherwise adverse effect on our financial condition and results of operations.

Interest Rate Risk

Interest rate risk is the potential impact of changes in interest rates on our earnings and net equity. Interest rate risk arises when our assets and liabilities, both on and off-balance sheet, have mismatched repricing dates. Changes in interest rates where we have mismatched repricing dates may have an adverse effect on our financial condition and results of operations. In addition, interest rate risk may arise when changes in the underlying interest rates on assets do not match changes in the interest rates on liabilities. This potential mismatch may have an adverse effect on our financial condition and results of operations.

Economic Conditions

While the economy was in recession during 2009, economic conditions generally improved toward the end of the year, as evidenced by growth in both gross domestic product and employment. Abnormally low interest rates contributed to the stabilization of the housing market.

Higher interest rates or a decline in general economic conditions could cause default rates to increase as creditworthiness decreases for borrowers who are more highly leveraged or as unemployment increases. This decline could negatively affect our net income. In addition, a general decline in economic conditions could slow the pace of housing sales and adversely affect growth in the single family mortgage market, which could adversely affect our ability to grow our mortgage portfolio.

Monetary Policy

Our earnings are affected by the monetary policies of the Bank of Canada. Changes in the supply of money and the general level of interest rates could affect our earnings. Changes in the level of interest rates affect the interest spread between our mortgages, loans and investments, securitization investments and term deposits, and as a result impact our net investment income. Changes to monetary policy and in financial markets in general are beyond our control and are difficult to predict or anticipate.

Outsourcing Risk

Outsourcing risk is the risk incurred when we contract out a business function to a service provider instead of performing the function ourselves, and the service provider performs at a lower standard than we would have under similar circumstances. We outsource all mortgage and loan origination and servicing to MCLP and other third parties.

Reliance on Key Personnel

Our future performance is dependent on the abilities, experience and efforts of our management and other key personnel. There is no assurance that we will be able to continue to attract and retain key personnel, although it remains a key objective of the Company. Should any key personnel be unwilling or unable to continue their employment with MCAN, there may be an adverse effect on our financial condition and results of operations.

Competition Risk

Our operations and income are a function of the interest rate environment and the availability of mortgage products at reasonable yields. The availability of mortgage products for the Company and the yields thereon are dependent on market competition. In the event that we are unable to compete successfully against our current or future competitors, there may be an adverse effect on our financial condition and results of operations.

Regulatory Risk

Changes in laws and regulations, including interpretation or implementation, could affect the Company by limiting the products or services that we can provide and increasing the ability of competitors to compete with our products and services. Also, any failure by the Company to comply with applicable laws and regulations could result in sanctions and financial penalties which could adversely impact our earnings and damage our reputation.

Market Risk

Market risk is the exposure to adverse changes in the value of financial assets. For the Company, market risk factors include interest rates, real estate values, commodity prices and foreign exchange rates, among others. Any changes in these market risk factors may negatively affect the value of our financial assets, which may have an adverse effect on our financial condition and results of operations. We do not undertake trading activities as part of our regular operations, and therefore are not exposed to risks associated with activities such as market making, arbitrage or proprietary trading.

Operational and Infrastructure Risk

We are exposed to many types of operational risks that affect all companies. Such risks include the risk of fraud by employees or others, unauthorized transactions by employees, and operational or human error. We are also exposed to the risk that computer or telecommunication systems could fail, despite efforts to maintain these systems in working order. Shortcomings or failures in internal processes, employees or systems, including any of our financial, accounting or other data processing systems, could lead to financial loss and damage to our reputation. In addition, despite our contingency plans in place, our ability to conduct business may be adversely affected by a disruption in the infrastructure that supports our operations.

Accuracy and Completeness of Information on Customers and Counterparties

In deciding whether to extend credit or enter into other transactions with customers and counterparties, we may rely on information furnished by them, including financial statements and other financial information. We may also rely on the representations of customers and counterparties as to the accuracy and completeness of that information. Our financial condition and results of operations may be negatively affected to the extent that we rely on financial statements and financial information that do not comply with GAAP, that are materially misleading or that do not fairly represent, in all material respects, the financial condition and results of operations of the customers and counterparties.

Environmental Risk

We recognize that environmental hazards are a potential liability. This risk exposure can result from non-compliance with environmental laws either as principal or lender, which may negatively affect our financial condition and results of operations. We aim to mitigate this risk by complying with all environmental laws and by applying a rigorous environmental policy to our commercial and development lending activities.

Changes in Laws and Regulations

Changes to current laws, regulations, regulatory policies or guidelines (including changes in their interpretation, implementation or enforcement), the introduction of new laws, regulations, regulatory policies or guidelines or the exercise of discretionary oversight by regulatory or other competent authorities including OSFI, could adversely affect us, including by limiting the products or services that we provide, restricting the scope of our operations or business lines, increasing the ability of competitors to compete with our products and services or requiring us to cease carrying on business. In addition, delays in the receipt of any regulatory approvals and authorizations that may be necessary to the operation of our business could adversely affect our operations and financial conditions. Our failure to comply with applicable laws and regulations could result in sanctions and financial penalties that could adversely impact our earnings and damage our reputation.

Changes in Accounting Standards and Accounting Policies

We may be subject to changes in the financial accounting and reporting standards that govern the preparation of our financial statements. These changes may materially impact how we record and report our financial condition and results of operations and, in certain circumstances, we may be required to retroactively apply a new or revised standard that results in our restating prior period financial statements. We are required to adopt International Financial Reporting Standards ("IFRS") for the fiscal year commencing January 1, 2011. Among other things, the adoption of IFRS may impact our current accounting policies and critical accounting estimates, as well as the calculation of (and compliance with) our regulatory capital ratios, due to significant recognition and measurement differences between IFRS and current GAAP which could in turn materially impact our financial condition and results of operations, as well as the scope of our operations and business lines. If the IFRS rules regarding securitization are implemented in the form currently proposed, MCAN's assets and liabilities that are subject to securitization will be considered on-balance sheet items. OSFI released a draft advisory in October 2009 with respect to the impact of the currently proposed IFRS rules regarding securitization on regulatory capital ratios. The draft advisory contemplates that the on-balance sheet assets and liabilities that are subject to securitization transactions undertaken after December 31, 2009 (including insured mortgages that are securitized through the CMB program) will be required to be included in the calculation of a regulated financial institution's regulatory capital ratios. Currently, we are not required to reflect securitized assets or liabilities on our balance sheet or include them in the calculation of our regulatory capital ratios. Pursuant to the measures contemplated by the

draft advisory, if the IFRS rules regarding securitization are implemented in their proposed form, beginning with the fiscal year commencing on January 1, 2011, we will be required to include any assets and liabilities that were subject to securitization transactions undertaken as of January 1, 2010 in the calculation of our regulatory capital ratios. We are continuing to identify and assess the impact of the transition to IFRS on our consolidated financial statements and are working to develop a plan to minimize the effect of the transition on our business. However, if the IFRS rules regarding securitization are implemented in the proposed form and if the draft advisory is applied in the form proposed by OSFI, then MCAN's participation in securitization transactions, namely through our participation in the CMB program, may need to be significantly reduced in order for us to comply with our regulatory capital ratios. Although we are reviewing potential alternative structures and arrangements that may permit our continued participation in the CMB program, there can be no assurance that any such alternative structures or arrangements will be available on commercially reasonable terms, or can be implemented in a timely manner.

Leverage

Leverage increases our potential exposure to all risk factors described above.

RISK MANAGEMENT

We operate in changing regulatory and economic environments. As a result, our management and the Board of Directors are particularly diligent in their consideration of issues of risk. Our goal is not to eliminate risk, as this would result in significantly reduced earnings, but rather to be proactive in our assessment and management of risk, as a means to gain a strategic advantage and ultimately enhance shareholder value.

Our senior management is responsible for the quality of processes, policies, procedures and controls and for internal reporting on a day-to-day basis. The Board of Directors is actively involved in the risk management process, providing oversight and guidance on an ongoing basis and at least quarterly. Internal audit is involved in the risk management process to provide validation of its effectiveness, with reports provided to senior management and the Board of Directors.

As discussed above under "Risk Factors," we are exposed to various inherent risks, particularly interest rate risk and credit risk. We mitigate these risks through investment diversification, and by diligent management of assets and liabilities.

Credit and commitment exposure is closely monitored through a reporting process that includes a formal quarterly review involving senior management and the ICB.

Our exposure to credit risk is managed through risk management policies and procedures that emphasize the quality and diversification of our investments. Our policies establish limits on concentration by asset class, risk rating, geographic region, dollar limit and borrower. We use these policies to assess credit risk and portfolio quality. All members of management are subject to limits on their ability to commit the Company to credit risk.

We identify potential risk in our mortgage portfolio by way of regular review of market metrics, which are a key component of semi-annual market reports provided to the Board of Directors. We also undertake site visits of active mortgages. Existing risks in our mortgage portfolio are identified by arrears reporting, portfolio diversification analysis, annual reviews of large loans and risk rating trends of the entire mortgage portfolio. The aforementioned reporting and analysis provides adequate monitoring of and control over our exposure to credit risk. In the current economic environment, we have increased our monitoring of real estate market values for single family mortgages, with independent assessments of value obtained as individual mortgages exceed 90 days in arrears.

We assess a credit score and risk rating for all mortgages at the time of underwriting based on the quality of the borrower and the underlying real estate. Subsequent to the initial mortgage advance, the ongoing monitoring of a mortgage may lead to the downgrading of the status of a mortgage to monitored, in arrears, or impaired.

We closely monitor our liquidity position to ensure that we have sufficient cash to meet liability obligations as they become due. The ICB is responsible for the review and approval of liquidity policies. In general, we maintain liquid investments and credit facilities in excess of 20% of term deposits maturing within 100 days. In addition, all single family mortgages are readily marketable within a time frame of one to three months, thus providing us with added flexibility to meet liquidity needs. We have access to capital through our ability to issue term deposits eligible for CDIC deposit insurance. These term deposits also provide us with the ability to fund asset growth as needed. We also have a \$30 million banking facility in place to fund asset growth or meet short-term obligations as required. We believe that our liquidity position and our access to capital markets in the form of term deposits and the banking facility support our ability to meet current and future commitments.

Management has developed a Liquidity Risk Management Framework that is reviewed and approved annually by the Board of Directors. This framework details the daily, monthly and quarterly analysis that is performed by management. Management monitors changes in cash and cash requirements on a daily basis and formally reports to ALCO on a monthly basis. Management also completes monthly and quarterly stress testing which is reviewed by ALCO and the ICB. Management monitors trends in deposit concentration with significant term deposit brokers on a monthly basis.

We have established and maintain liquidity policies which meet the standards set under the Trust Act and any regulations or guidelines issued by OSFI.

We evaluate our exposure to a variety of changes in interest rates across the term spectrum of our assets and liabilities, including both parallel and non-parallel changes in interest rates. By managing and matching the terms of invested assets and term deposits so that they offset each other, we seek to reduce the risks associated with interest rate changes, and in conjunction with liquidity management policies, we also manage cash flow mismatches. ALCO reviews the Company's interest rate exposure on a monthly basis using interest rate spread and gap analysis as well as interest rate sensitivity analysis based on various scenarios. This information is also formally reviewed by the ICB each quarter. The Company does not currently use derivative financial instruments outside of the CMB program, however the potential use of such instruments for the Company's on-balance sheet assets is analyzed and reported to ALCO on a monthly basis.

All material outsourcing arrangements are required to comply with OSFI guideline B-10, *Outsourcing of Business Activities, Functions and Processes*. Our Enterprise Risk Management Officer and senior management regularly review outsourcing arrangements to provide reasonable assurances that the outsourcing arrangements are in compliance with this guideline. These reviews account for the materiality of the outsourcing arrangement and the status of the risk management program associated with the outsourced arrangement.

Ultimately, risk management is controlled at the highest level of the Company. ALCO reviews and manages these risks on a monthly basis. Our Board of Directors reviews and approves all risk management policies and procedures. Management reports to the Board of Directors on the status of risk management at least quarterly.

PEOPLE

As at December 31, 2009, we had fourteen employees, an increase of two from the prior year.

REGULATORY COMPLIANCE

Our Chief Compliance Officer ensures that management understands the impact of all relevant legislation affecting the business, assesses compliance with current and pending legislation and works with management to address any gaps in policies and procedures. We use a Legislative Compliance Management System that ensures all managers assess their compliance with relevant legislation on a quarterly basis. Senior management liaises with regulators to keep them apprised of Company progress and changes to our business. Our Chief Compliance Officer reports quarterly to the Conduct Review, Corporate Governance & Human Resources Committee of the Board of Directors.

INTERNAL AUDIT

We outsource our Internal Audit function to Protiviti, an independent risk consulting firm. The Internal Audit function has unrestricted access to our operations, records, property and personnel, including senior management and the Chairman of the Audit Committee of the Board of Directors (the "Audit Committee"). Internal Audit formulates an annual risk-based plan for approval by the Audit Committee and then undertakes internal audit reviews throughout the year with regular reporting to senior management and quarterly reporting to the Audit Committee.

OUTLOOK

We continue to carry significant unutilized investment capacity. During the fourth quarter, we recommenced the funding of new uninsured single family mortgages to employ some of this investment capacity. The market for new housing construction has started to improve, so we will also be cautiously growing our residential construction loan portfolio.

While interest rates are expected to remain low for the next few quarters, our average term deposit interest rate has continued to decrease as maturing deposits are replaced by new deposits at significantly lower rates. This decrease should contribute to improved spread income in 2010, compared to 2009.

Arrears in our single family mortgage portfolio remain high due to continued high unemployment levels. Property values have stabilized in most markets in which we invest on rising sales volume. We have not experienced material loan losses resulting from these arrears.

Arrears in our construction loan portfolio also remain high. The large size of these loans causes them to skew our arrears statistics. The nature of these loans also usually results in a more protracted resolution period.

Economic growth and job creation was evident during the last quarter of 2009. As this trend continues, we expect an increase in our mortgage portfolio and lower mortgage arrears.

Management believes that the continuing disruption in the financial markets has not materially affected the capital or liquidity of the Company.

We are in discussions with staff of OSFI in connection with a review being undertaken by OSFI. The review has focused on MCAN's relationship with both MCLP and MCAP Service Corporation ("MSC"), and whether either or both of those entities should be designated as related parties of MCAN in accordance with the Trust Act. MCAN is co-operating with OSFI staff in connection with this review.

MCLP and MSC are not currently related parties of MCAN, and MCAN has made oral and written submissions to OSFI as to why such entities should not be designated as related parties pursuant to the Superintendent's discretion under the Trust Act. At this stage, it is unclear what the results of the review will be. However, MCAN notes that if OSFI, in its discretion, decides to designate MCLP and/or MSC as related parties, any resulting restructuring that may be necessary could have at least a temporary negative impact on MCAN's operations and results.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The notes to our consolidated financial statements provide detailed information on our significant accounting policies, the method of applying those policies, and the material components of the amounts in the consolidated balance sheets and the statements of income, changes in shareholders' equity, comprehensive income and cash flows. The policies discussed below are considered particularly important, as they require management to make judgments involving estimations. We have control procedures to ensure that these policies are applied consistently and that the policies are independently reviewed on at least an annual basis. Changes to accounting policies are made only after an appropriate amount of research and discussion has occurred and independent advice is obtained. Estimates are considered carefully and reviewed at an appropriate level within the Company. We believe that our estimates of the value of our assets and liabilities are appropriate.

Financial Instruments

All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions, and classified based on management's intention. Financial assets are classified as held for trading, held to maturity, available for sale or loans and receivables, and financial liabilities are classified as held for trading or other. Changes in the unrealized fair value of financial instruments classified as held for trading are recognized to income. Changes in the unrealized fair value of available for sale financial assets are recognized in accumulated other comprehensive income, except for those considered to be changes attributable to impairment which are charged to income. Upon disposal, the cumulative change in fair value is transferred to income. Other classifications are subsequently measured at amortized cost. From time to time, the Company may use derivative and non-derivative financial instruments to manage interest rate risk. Hedge accounting is optional, and where it can be applied, it requires the Company to document the hedging relationship and to test the effectiveness of the hedging item to offset changes in value of the underlying hedged item on an ongoing basis. At December 31, 2009, the Company did not have any hedge accounting relationships.

For further details on financial instruments, please refer to Notes 2, 4, 5, 6, 9, 11, 12 and 20 to the consolidated financial statements.

Allowance for Credit Losses

The allowance for credit losses reduces the carrying value of mortgage assets to provide for an estimate of the principal amounts that borrowers may not repay in the future. In assessing the estimated realizable value of assets, we must rely on estimates and exercise judgment regarding matters for which the ultimate outcome is unknown. A number of factors can affect the amount that we ultimately collect, including the quality of our own underwriting process and credit criteria, the diversification of the portfolio, the underlying security relating to the loans and the overall economic environment. Specific provisions include all of the accumulated provisions for losses on particular assets required to reduce the related assets to estimated realizable value. The general provision represents losses that we believe have been incurred but not yet specifically identified. The general provision is established by considering historical loss trends during economic cycles, the risk profile of our current portfolio, estimated losses for the current phase of the economic cycle and historic industry experience. Provisioning rates depend on asset class, as different classes have varying underlying risks. Based on our best judgment, we believe that the general provision is indicative of probable losses within the next two years based on current economic conditions and risk profile. However, future changes in circumstances could materially affect our future provisions for credit losses from those provisions determined in the current year, and there could be a need to increase or decrease the allowance for credit losses.

We complete a review of all provisioning policies at least annually. We continue to monitor asset performance and current economic conditions, focusing on any regionally specific issues to assess the adequacy of the current provisioning policies. Provisioning rates are reviewed on a quarterly basis.

Weak employment levels across Canada are continuing to be reflected in higher arrears levels. However, abnormally low interest rates have contributed to a stabilization of residential property values across Canada. Economic growth and job creation were evident during the fourth quarter, and as this trend continues we expect lower mortgage arrears.

In addition to considering the current economic conditions, we assessed the probability of default, expected loss as a result of default and the loan exposure at the time of default when establishing our general allowance. Based on historical trends, our current mortgage portfolios are performing within an acceptable range that required no further adjustment to our allowance assumptions. Our overall arrears trends remained high during 2009, although losses to date have been insignificant. We continue to review our underwriting and credit requirements on a regular basis, and we have taken measures as warranted by changes in the market and economic conditions.

We believe that we have established adequate provisioning rates given the current economic concerns. Our current provisioning rates consider the impact of a decline in real estate values and anticipated default/loss percentages that are sufficient to offset current and historical loss experiences.

On an ongoing basis, we compare the carrying value of our loans and investments to their fair value, determined on the basis of expected discounted cash flows. When a decline in value is identified as a result of impairment that is other than temporary, the affected carrying amount is written down to its fair value.

Additional details of our accounting policies and balances of the allowances for credit losses can be found in Notes 2, 4 and 6 to the consolidated financial statements.

Securitization

On the closing date of a CMB issuance, we recognize an interest-only strip, which is a retained interest in the securitized mortgages. We require the use of estimates to determine the fair value of the interest-only strips, which represent the present value of expected future cash flows. As a result of this, estimates and assumptions could have a material impact on net income. We review the estimates used to determine the fair value of the interest-only strips on an ongoing basis to ensure their appropriateness. For further information, please refer to Note 7 to the consolidated financial statements, which presents a sensitivity analysis of the current fair value of the interest-only strips to immediate 10% and 20% adverse changes in key assumptions.

Discount Income Recognition

The Company may acquire mortgage portfolios from third parties at fair market value. A mortgage discount will exist to the extent that the fair market value of a mortgage is less than its par value. The discount is allocated between a valuation reserve component and an accretion component. The valuation reserve component represents the risk of credit loss in addition to the general mortgage allowance, while the accretion component represents the part of the discount to be recognized to income over time, thereby adjusting the yield on the mortgage from its face rate to an effective yield. The accretion component is amortized to income over the term of the related mortgage through the application of the effective interest rate method. The valuation reserve component is only recognized into income upon payout, less any realized credit loss.

Income Taxes

As a MIC, we can deduct dividends paid to our shareholders from our calculation of taxable income. We have taken the position that it is more likely than not that future dividends will be sufficient to recover current or future income tax liabilities, and as a result of this, we charge the related provision for future and current taxes directly to retained earnings. The provision for income taxes consists of various taxes that cannot be recovered from the payment of future dividends. Details of our accounting policies and balances relating to income taxes can be found in Notes 2 and 15 to the consolidated financial statements. We will continue to proactively monitor on a quarterly basis that this is an appropriate position.

CHANGES IN ACCOUNTING POLICY

On January 1, 2008, we adopted the new accounting standard of the Canadian Institute of Chartered Accountants ("CICA"), *Capital Disclosures*, which requires the disclosure of qualitative and quantitative information that enables users of financial statements to evaluate the entity's objectives, policies and processes for managing capital.

On January 1, 2008, we adopted the new standards of the CICA, *Financial Instruments - Disclosures* and *Financial Instruments - Presentation*, which enhance the abilities of users of financial statements to evaluate the significance of financial instruments to an entity, related exposures and the management of these risks.

On January 1, 2009, the Company adopted amendments to the standard of the CICA, Section 3862, *Financial Instruments - Disclosures*. These amendments require additional disclosures of fair value measurements of financial instruments and liquidity risk. The additional disclosures include the classification of fair value measurements into one of three levels, as follows: quoted prices in an active market (Level 1), fair value based on observable inputs other than quoted prices (Level 2) and fair value based on inputs that are not based on observable data (Level 3).

On January 1, 2009, the Company adopted EIC 173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. The guideline clarifies how the Company's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative financial instruments. The new guidelines did not have a material effect on the financial position or income of the Company.

On January 1, 2009, the Company adopted amendments to the standard of the CICA, Section 3855, *Financial Instruments - Recognition and Measurement*. Accordingly, held to maturity debt instruments with fixed or determinable payments that are not quoted in an active market were reclassified from held to maturity to loans and receivables.

FUTURE CHANGES IN ACCOUNTING POLICY

International Financial Reporting Standards

The Accounting Standards Board ("AcSB") will require Canadian public companies to prepare their interim and annual financial statements in accordance with IFRS relating to fiscal years beginning on or after January 1, 2011.

For the fiscal year commencing January 1, 2011, we will cease to use GAAP and will adopt IFRS. Financial results for the quarter ended March 31, 2011 will be presented using IFRS.

We have recognized that the conversion to IFRS is complex and requires a significant amount of company resources. As a result of this, we engaged a major accounting firm to advise and assist us with identifying accounting treatment differences between GAAP and IFRS and to provide education and training. We anticipate that this engagement will create efficiencies in MCAN's IFRS conversion process.

Our IFRS conversion plan consists of three key phases, as follows:

1. Scoping and diagnostic phase
2. Assessment of impact of IFRS differences
3. Implementation of conversion plan

The scoping and diagnostic phase, which involved a high-level impact assessment to identify key areas impacted by the conversion to IFRS, has been completed. We have completed our assessment of the impact of differences between GAAP and IFRS on our accounting policies and information systems. During 2010, we will complete our assessment of the impact of IFRS on our financial reporting, control environment and business activities. We have begun the implementation of our conversion plan, which remains on schedule.

We are monitoring the potential impact of changes to financial reporting processes, internal controls over financial reporting and disclosure controls and procedures. As the implications of the conversion are identified, continual requirements for infrastructure, expertise, training and education will be assessed. We will continue to assess the impact of adopting IFRS and will update our MD&A disclosures on a quarterly basis to report on the progress of our IFRS plan.

Most adjustments required as a result of the transition from GAAP to IFRS will be made retrospectively as of January 1, 2010 based on IFRS applicable at that time.

Our assessment of the differences between GAAP and IFRS identified several material differences, as follows:

- **CMB Program:** The most significant IFRS difference for MCAN is the accounting for the securitization of insured mortgages through our participation in the CMB program. Based on IFRS as of the date of transition, we will no longer account for these transactions as sales of mortgages and will reverse all previously recognized up-front gains on securitization through opening retained earnings. This reversal will be partially offset by mortgage interest income, principal reinvestment income and penalty income less coupon interest expense that would have been recognized from the dates of the respective CMB issuances to the date of transition. Our IFRS balance sheet will include mortgages securitized through the CMB program, assets in which principal repayments have been re-invested and a liability to CMB bondholders. On a go-forward basis under IFRS, we will recognize mortgage interest income, principal reinvestment income, penalty income and coupon interest expense on the accrual basis, and we will include any future mortgages securitized through the CMB program on our balance sheet. In regards to our participation in the CMB program, we have not yet quantified the impact of the conversion to IFRS on opening retained earnings.
- **Mortgage Loss Provisions:** Under GAAP, general provisions for mortgage losses are based on expected losses, whereas IFRS collective mortgage provisions are based on an incurred loss model. Although we have not yet quantified the impact of the conversion to IFRS on opening retained earnings in regards to mortgage loss provisions, we expect our general/collective provision to decrease as a result of the conversion to IFRS.
- **Income Taxes:** Under GAAP, we are able to charge our current and future tax liabilities directly to retained earnings instead of recognizing the changes through net income. Based on IFRS as of the date of transition, we will no longer be able to charge current and future taxes directly to retained earnings, which will likely result in increased volatility to net income. In addition, MCAN's future tax position will change to the extent that the accounting values of balance sheet items that have differing values for accounting and tax purposes are impacted by IFRS.
- **Equity investment in MCLP:** To the extent that MCLP's opening retained earnings changes as a result of its conversion to IFRS, MCAN will adjust its investment in MCLP based on its pro-rata share of MCLP's opening retained earnings adjustment, which is not currently quantifiable.

The following table outlines certain elements of our IFRS conversion plan and an assessment of our progress towards the plan as at December 31, 2009. Changes in regulations, economic conditions, business activities or other circumstances could impact the IFRS conversion plan and result in changes to the key activities and deadlines. Our IFRS conversion plan is currently on schedule.

Key Activity	Planned Completion Date	Status
Accounting Policies <ul style="list-style-type: none"> Identify differences in Canadian GAAP and IFRS accounting policies Select ongoing IFRS policies Select IFRS 1 policies and exemptions Quantify impact of transition to IFRS 	Q2 2009 Q4 2009 Q4 2009 Q1 2010	Differences identified and analyzed Policies selected Policies selected Currently unable to quantify
Financial Reporting <ul style="list-style-type: none"> 2011 IFRS financial statement and note disclosure format Identify additional financial statement disclosures Prepare 2010 interim and annual reconciliations from GAAP to IFRS 	Q3 2010 Q3 2010 Quarterly during 2010	Analysis in progress, on schedule Analysis in progress, on schedule Analysis in progress, on schedule
Control Environment <ul style="list-style-type: none"> Assess Internal Controls over Financial Reporting ("ICFR") design and effectiveness implications for all accounting policy changes Implement changes to ICFR Assess Disclosure Controls and Procedures ("DC&P") design and effectiveness implications for all accounting policy changes Implement changes to DC&P 	Q3 2010 Q4 2010 Q3 2010 Q4 2010	Assessment to be completed Assessment to be completed Assessment to be completed Assessment to be completed
Information Systems <ul style="list-style-type: none"> Creation of general ledger for both GAAP and IFRS Program upgrades/modifications One-off calculations (IFRS 1) Gathering data for disclosures 	Q4 2009 Q4 2009 Q4 2009 Q4 2009	Completed Completed Completed Completed
Business Policies <ul style="list-style-type: none"> Assess impact on capital plan Revise capital plan as needed 	Q2 2010 Q3 2010	Assessment to be completed Assessment to be completed

DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

As of December 31, 2009, an evaluation was carried out of the effectiveness of disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer will certify that those disclosure controls and procedures were effective as at the end of the financial year ended December 31, 2009.

Also at December 31, 2009, an evaluation was carried out of the effectiveness of internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and financial statements compliance with GAAP. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer will certify that those internal controls over financial reporting were effective as at the end of the financial year ended December 31, 2009.

These evaluations were conducted in accordance with the standards of the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"), a recognized control model, and the requirements of *National Instrument 52-109 - Certification of Disclosure in Issuers' Annual and Interim Filings*. A Disclosure Committee, comprised of members of senior management, assists the Chief Executive Officer and Chief Financial Officer in their responsibilities.

There were no changes in our internal controls over financial reporting that occurred during the period beginning on January 1, 2009 and ending on December 31, 2009 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.