Fundamental Research Corp.
Investment Analysis for Intelligent Investors

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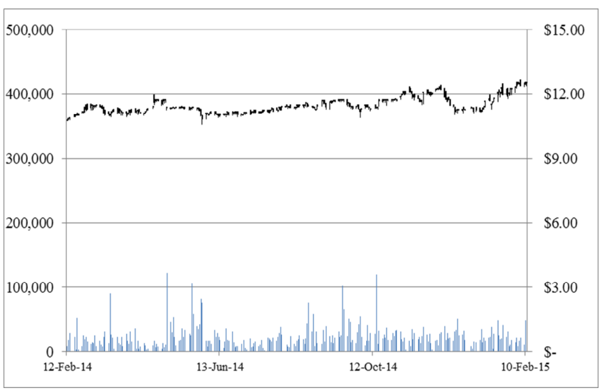
Atrium Mortgage Investment Corporation (TSX: AI) – Record Year

Sector/Industry: Mortgage Investment Corporation **www.atriummic.com**

Market Data (as of February 13, 2015)

Current Price	**C$12.50**
Fair Value	**C$12.80**
Rating*	**BUY**
Risk*	**2**
52 Week Range	C$10.57 - C$12.70
Shares O/S	24.44 million
Market Cap	C$305.56 million
Yield (forward)	7.5%
P/E (forward)	12.8x
P/B	1.2x
YoY change in share price	14.6%
YoY TSX	9.6%

**See back of report for rating and risk definitions*



Highlights

- Atrium Mortgage Investment Corporation ("Atrium", "company") grew its portfolio by 54% YOY to reach $433 million by the end of 2014. Management estimates 2015 will end at approximately $450 million.
- 2014 was a record year for the company as revenues grew by 47% YOY, to $34.96 million.
- Total dividends in 2014 were $0.89 per share, up from $0.85 per share, and were exactly in line with our $0.89 per share estimate. The company has announced it is going to raise its regular dividend to $0.84 per year, or $0.07 per month, reflecting a 2.4% YOY increase. Our forecast for total dividends in 2015 is $0.94 per share.
- First mortgages represented 80.2% of the total portfolio at the end of 2014, down significantly from 90.9% at the end of 2013. Although the decline in first mortgages signals an increase in risk levels, most of the other key portfolio parameters remain unchanged.
- The portfolio's exposure to Western Canada increased from 11.1% at the end of 2013, to 22.9% by the end of 2014.
- Although risk levels of the portfolio have slightly increased, we believe the overall risk profile of the company's portfolio remains reasonable relative to other publicly traded comparable MICs. We also believe that Atrium's weighted average interest rate of 8.81% p.a. (charged to borrowers) is high relative its peers, while maintaining a lower risk portfolio.
- Atrium was the top performing publicly traded MIC in 2014. AI shares produced a total return of 11.25% to investors in 2014.
- <u>Our revised fair value estimate is $12.80 per share, which reflects an overall expected return (including dividends) of 9.9% for investors in 2015.</u>

Key Financials (FYE - Dec 31) (C$)	2011	2012	2013	2014	2015(F)	2016(F)
Mortgage Receivables(net)	$ 157,492,666	$ 201,954,951	$ 281,708,139	$ 432,757,000	$ 474,577,570	$ 499,618,664
Cash	$ 8,330	$ 10,628,383	$ -	$ -	$ 0	$ 0
Revenues	$ 11,414,661	$ 17,235,060	$ 23,759,620	$ 34,956,000	$ 40,090,547	$ 44,909,980
Net Income	$ 9,440,811	$ 13,358,327	$ 17,999,888	$ 21,037,000	$ 24,861,895	$ 28,453,034
EPS	$ 0.88	$ 0.86	$ 0.85	$ 0.91	$ 0.98	$ 1.05
Dividends per Share	$ 0.87	$ 0.85	$ 0.85	$ 0.86	$ 0.98	$ 1.05

Management estimates $450M by the end of 2015

Atrium's portfolio grew by 54% YOY, and 5% QOQ, to $433 million, by the end of 2014. In their Q3 conference call (on October 27, 2014), management had indicated that they expected the year end portfolio to drop to approximately $400 million. Management indicated on their February 11, 2015 call, that the timing of a few large repayments were pushed to early 2015, and therefore, the year-end portfolio ended higher than expected.

The company originated $278 million of mortgages in 2014. **The growth came from the funds raised in a $31.80 million convertible debenture financing in Q1, a $34.61 million equity financing in Q2, and a $40.04 million convertible debenture financing in Q3.**

Management estimates that they expect 2015 to end at approximately $450 million, implying that, at this point, they may not be considering any financings this year. **However, we believe that if the share price stays over $12 per share, management may be encouraged to do a financing.** We have maintained our year end estimate at $475 million. We are introducing our 2016 estimates in this report. Our forecast for 2016 year end is $500 million.

Strong growth in Western Canada

The portfolio's exposure to Western Canada increased from 11.1% at the end of 2013, to 22.9% by the end of 2014, beating management's original estimate of 20%. Western Canada had only accounted for 16.3% at the end of Q3-2014. Although Atrium has fared well so far in most of the key portfolio parameters, diversification had been one of its key challenges compared to its peers. **Therefore, we were very pleased to see the company's ability to geographically diversify its portfolio in such a short time span.** Management expects Western Canada to be approximately 25% by the end of 2015.

	Year ended December 31, 2014			
Location of underlying property	Number of mortgages	Amount	Percentage	Weighted average interest rate
Greater Toronto Area	136	$ 296,405	68.2%	8.81%
Non-GTA Ontario	11	38,716	8.9%	9.66%
Saskatchewan	1	2,880	0.7%	8.50%
Alberta	31	66,325	15.3%	8.47%
British Columbia	11	29,942	6.9%	8.64%
	190	434,268	100.0%	8.81%

	Year ended December 31, 2013			
Location of underlying property	Number of mortgages	Amount	Percentage	Weighted average interest rate
Greater Toronto Area	111	$ 228,391	80.9%	8.64%
Non-GTA Ontario	6	22,465	8.0%	9.10%
Saskatchewan	–	–	–	–
Alberta	7	24,910	8.8%	8.57%
British Columbia	7	6,594	2.3%	10.75%
	131	282,360	100.0%	8.72%

Source: Company

Management has indicated that the recent decline in oil prices have made them more cautious towards the AB market. At the end of 2014, AB accounted for 15% of the total

First mortgages at 80.2%

portfolio, which included 31 mortgages, of which, 97% are first mortgages. The average LTV in AB was 60.3%, lower than the portfolio average LTV of 64.1%, indicating a lower risk profile.

First mortgages represented 80.2% of the total portfolio, down significantly from 90.9% at the end of 2013. We had expected the percentage of first mortgages to decline with portfolio growth. **Although the decline in first mortgages signal an increase in risk levels, most of the other key portfolio parameters remain unchanged (as discussed later), which is encouraging.**

Description	Number of mortgages	Amount	Percentage	Weighted average interest rate
($000s)				
Type of Mortgage				
First mortgages	156	$ 351,310	80.9%	8.50%
Second and third mortgages	34	82,958	19.1%	10.13%
	190	$ 434,268	100.0%	8.81%
Nature of underlying property				
Residential	159	$ 299,278	68.9%	8.87%
Commercial	31	134,990	31.1%	8.68%
	190	434,268	100.0%	8.81%

Source: Company

The percentage of large loans ($7.5+ million) increased YOY from 19.7% (5 mortgages) to 38.9% (16 mortgages). However, the average outstanding mortgage only increased from $2.2 million to $2.3 million.

	December 31, 2014			December 31, 2013		
Mortgage amount	Number	Outstanding amount	% of Portfolio	Number	Outstanding amount	% of Portfolio
(outstanding amounts in $000s)						
$0 - $2,500,000	139	$ 119,655	27.6%	95	$ 98,812	35.0%
$2,500,001 - $5,000,000	26	90,602	20.9%	24	81,090	28.7%
$5,000,001 - $7,500,000	9	54,931	12.6%	7	46,820	16.6%
$7,500,001 +	16	169,080	38.9%	5	55,638	19.7%
	190	$ 434,268	100.0%	131	$ 282,360	100.0%

Source: Company

Although we believe the portfolio's concentration on a few mortgages is slightly high, we believe the company's investment policies (such as the one listed below) ensure that the overall risk profile of the portfolio is not compromised:

"No single borrower may account for more than 15% of our total assets. In addition, any loan or amendment that would result in an exposure to one borrower exceeding the lesser of $50 million or 10% of the portfolio requires approval of the board."

Exposure to property types

The following table shows the outstanding loans by category as of September 30, 2014. The portfolio has had little change in exposure to various property types since the end of Q3.

	December 31, 2014			December 31, 2013		
Mortgage category	Number	Outstanding amount	% of Portfolio	Number	Outstanding amount	% of Portfolio
Commercial/mixed use	31	$ 134,990	31.1%	27	$ 89,475	31.7%
House and apartment	90	93,070	21.4%	59	69,485	24.6%
Low-rise residential	23	85,678	19.7%	17	58,466	20.7%
Construction	17	61,095	14.1%	9	22,093	7.8%
High-rise residential	8	44,048	10.1%	5	32,967	11.7%
Mid-rise residential	8	12,127	2.8%	3	7,440	2.6%
Condominium corporation	13	3,260	0.8%	11	2,434	0.9%
Mortgage portfolio	190	434,268	100.0%	131	282,360	100.0%
Accrued interest receivable		2,177			1,562	
Mortgage discount		(465)			(339)	
Mortgage origination fees		(835)			(724)	
Provision for mortgage losses		(2,388)			(1,151)	
Mortgages receivable		$ 432,757			$ 281,708	

Source: Company

Over the year, exposure to homes and apartments dropped from 24.6% to 21.4%. Housing and apartment mortgages continue to be highly competitive, and therefore, the company was not able to fund as many home and apartment mortgages as it would have liked. The company raised its exposure to relatively higher risk mortgages types, such as construction mortgages (from 7.8% to 14.1%).

Other key parameters

The following highlights the changes in other key portfolio parameters:

The **weighted average interest rate,** excluding lender fees, of the portfolio, was 8.81% p.a. at the end of 2014, versus 8.72% at the end of 2013.

The **weighted average term to maturity was** 13.7 months versus 13.5 months as of December 31, 2013.

The **LTV increased slightly from 64.1% to 64.3%.** Approximately 97.2% of the portfolio, as of December 31, 2014, had LTVs below 75%.

The company reported a **loan loss provision** of $2.39 million in 2014, (0.55% of the total portfolio, up from 0.20% at the end of 2013); all of which are under general provision. **In the conference call, management indicated that the general provision was raised to make it in line with the provisions allocated by their peers.** At the end of 2014, only one mortgage was in default. Management indicated that they do not expect any losses from these loans, which is why they have not assigned any specific loss provision.

Comparables

Although risk levels of the portfolio have slightly increased, we believe the overall risk profile of the company's portfolio remains reasonable relative to the three publicly traded comparable MICs – namely Timbercreek MIC (TSX: TMC), Firm Capital MIC (TSX: FC), and TREZ Capital MIC (TSX: TZZ). **We also believe that Atrium's weighted average interest rate of 8.81% p.a. is higher relative to its peers, with less portfolio risk.**

	Name	LTV	First Mortgages	Geographical Diversification	Interest Rate	Mortgage Oustanding ($, MM)	Debt to Capital
1	Firm Capital MIC*		85%	69% ON, 11% QC, 12% AB and Others	8.45%	$353	41.08%
2	Timbercreek MIC	64.90%	70%	53% ON, 20% QC, 11% AB and 8% BC, and Others	9.17%	$445	26.30%
3	TREZ Capital MIC	69.49%	66%	29% ON, 32% AB, 10% BC and Others	7.73%	$202	8.16%
Group (1)	**Average**	**67.2%**	**73.2%**		**8.45%**		**25.2%**
1	Timbercreek Senior MIC	51.10%	100%	49% ON, 24% QC, 11% BC, 11% SK, and Others	6.21%	$465	37.92%
2	TREZ Capital Senior MIC	40.55%	100%	50% ON, 31% AB, 18% BC, and Others	6.20%	$116	38.38%
Group (2)	**Average**	**45.83%**	**100.00%**		**6.21%**		**38.15%**
	Average of (1) and (2)	**56.51%**	**86.62%**		**7.33%**		**31.66%**
	Atrium MIC	64.10%	80%	77% ON, 7% BC & 15% AB, and 1% SK	8.81%	$433	42.17%

- *As Atrium is the first MIC to announce year end results, the data shown in the above table of the comparable MICS are as of September 30, 3014.*
- *Firm Capital reported that as of September 30, 2014, they had 70% in conventional first mortgages, and 15% in related investments. They define related investments as follows - "Related investments predominantly have first ranking security on the underlying assets securing the loan, and as such, have the same risk profile as the conventional first mortgage investment category."*

47% YOY revenue growth

Revenues grew 47% YOY, to $34.96 million in 2014. Our forecast was $34.06 million.

Net income increased by 17% YOY to $21.04 million (EPS: $0.91). Our forecast was $21.32 million (EPS: $0.92 per share). 2014's EPS was $0.99 per share excluding loss provisions.

Interest income (including lender fees) as a percentage of mortgage receivables: As shown in the table below, interest income as a percentage of mortgage receivables decreased slightly from 9.82% to 9.79% p.a. Net income as a percentage of mortgage receivables dropped from 7.44% to 5.89% p.a. The drop was mainly due to interest expenses due to the increase in leverage. **However, the increase in leverage resulted in improved returns to investors as shown in the table below.**

% of Mortgage Receivables (net) -annualized	2011	2012	2013	2014
Interest Income + Origination	9.84%	9.59%	9.82%	9.79%
Less:				
Management Fee	0.83%	0.87%	1.02%	0.99%
Loan Loss Provision	0.17%	0.11%	0.03%	0.51%
G&A Expenses	0.17%	0.24%	0.27%	0.21%
Interest Expenses	0.53%	0.66%	0.99%	2.11%
Share Based Payments		0.03%	0.08%	0.07%
Net	**8.14%**	**7.69%**	**7.44%**	**5.89%**
Dividends as a Percentage of Book Value	8.21%	7.57%	8.51%	9.06%

**The calculations in the above table are approximates as we used the average of beginning and end of period mortgage receivables outstanding.*

Raising EPS estimate

We expect the average lending rate in the mortgage industry to drop this year due to the recent decision by the Bank of Canada to lower the overnight rate from 1.00% to 0.75%. We are slightly lowering our 2015 revenue estimate from $40.91 million to $40.09 million. Our forecast for 2016 is $44.91 million.

Our revised net income estimate for 2015 is $24.9 million (EPS: $0.98), versus our previous estimate of $25.0 million (EPS: $0.96). Our estimate for 2016 is $28.5 million (EPS: $1.05).

The company distributed an annual regular dividend of $0.82 per share, up from $0.80 per share in 2013. **The total dividends (regular + special) in 2014 were $0.89 per share, up from $0.85 per share, and were exactly in line with our $0.89 per share estimate.** The company has announced it is going to raise its regular dividend to $0.84 per year, or $0.07 per month, reflecting a 2.4% YOY increase. **Our dividend forecast for 2015 is $0.94 per share.**

The table below shows a summary of the balance sheet.

	2011	2012	2013	2014
Mortgages receivable, net	$157,492,666	$201,954,951	$281,708,139	$432,757,000
Cash	$8,330	$10,628,383	-	-
LT debt	-	-	$30,610,763	$100,328,000
Debt	$12,772,211	$205,605	$67,029,130	$181,021,000
Equity	$142,846,412	$210,109,925	$212,018,978	$248,204,000
Total Capital	$155,618,623	$210,315,530	$279,048,108	$429,225,000
Debt to Capital	8.2%	0.1%	24.0%	42.2%
Debt to Asset	8.0%	0.1%	23.8%	41.8%
EBIT/ Interest expense	16.5	12.3	8.6	3.8

Lenders have raised the company’s line of credit from $80 million to $100 million in the past year. The company had a debt to capital of 42% at the end of 2014, versus 24% at the end of 2013. As shown in the comparables table, presented earlier in the report, it is a reasonable practice to maintain a debt level of 35% to 45% for portfolios holding a high percentage of first mortgages. We expect the company to maintain debt between 35% and 45%. The company's lenders require debt to be lower than 50% of assets.

Options and Warrants

The company has no options or warrants outstanding.

Valuation & Rating

The following table shows Atrium's key valuation metrics compared to its peers.

	Name	Ticker	P/E	P/B	Dividend Yield
1	Firm Capital MIC	FC	12.5	1.2	8.0%
2	Timbercreek MIC	TMC	14.3	0.9	8.8%
3	TREZ Capital MIC	TZZ	13.7	0.8	9.9%
Group (1)	**Average**		**13.5**	**1.0**	**8.9%**
1	Timbercreek Senior MIC	MTG	16.1	1.0	6.9%
2	TREZ Capital Senior MIC	TZS	12.5	0.8	6.5%
Group (2)	**Average**		**14.3**	**0.9**	**6.7%**
	Average of (1) and (2)		**13.9**	**0.9**	**7.8%**
	Atrium MIC (trailing)	AI	**13.7**	**1.2**	**7.1%**
	Atrium MIC (2015 forward)	AI	**12.8**	**1.2**	**7.5%**
	Fair Value of AI (based on 2015 est.)		**$13.6**	**$9.5**	**$12.0**

Source: Capital IQ and FRC

Atrium's forward Price to Earnings ("P/E") continues to remain lower than the peer average. However, the forward dividend yield is slightly lower than the peer average. AI's Price to Book ("P/B") continues to remain higher than the peer average.

We continue to base our fair value estimate on AI's shares based on the average of our valuations based on the average P/E and dividend yield, which is now at $12.80 per share (previous estimate - $12.23 per share). **Our revised fair value estimate indicates an expected overall return of 9.9% for investors in 2015 Including dividends). We have maintained our BUY rating (Risk: 2).**

Risks

The following, we believe, are the key risks of the company at this time:

- Diversification - approximately 77% of Atrium's mortgages are secured by properties in Ontario.
- All mortgages are exposed to credit, and interest rate risks.
- Interest rate risks are minimal as most of the mortgages are short-term with fixed rates.
- A downturn in the real estate sector may impact the company's deal flow.
- Timely deployment of capital is critical.
- Investments in mortgages are typically affected by macroeconomic conditions, and local real estate markets.
- Competition is high in the mortgage lending business.
- Like most MICs, the company uses leverage to fund mortgages. Leverage, if not maintained below optimum levels, can have a negative impact.

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Appendix

Income Statement YE - December 31	2011	2012	2013	2014	2015(F)	2016(F)
Revenue						
Mortgage interest and other fees	$11,414,661	$17,235,060	$23,759,620	$34,956,000	$40,090,547	$44,909,980
Total Revenues	**$11,414,661**	**$17,235,060**	**$23,759,620**	**$34,956,000**	**$40,090,547**	**$44,909,980**
Expenses						
G&A	$202,688	886,674	641,260	766,000	875,000	975,000
Mortgage servicing and management fees	$961,359	$1,567,879	2,467,672	3,553,000	4,134,651	4,607,183
Share based payments		$48,176	204,248	248,000	369,507	411,737
Interest + Bank Charges	$609,803	1,180,713	1,318,474	2,908,000	3,354,109	3,606,050
Interest on convertible debenture			1,065,078	4,627,000	6,072,954	6,475,640
Loan loss provision	$200,000	193,291	63,000	1,817,000	422,430	381,336
Provincial capital taxes	-	-	-		-	-
Total Expenses	**$1,973,850**	**$3,876,733**	**5,759,732**	**13,919,000**	**15,228,652**	**16,456,946**
Net Income	**$9,440,811**	**$13,358,327**	**$17,999,888**	**$21,037,000**	**$24,861,895**	**$28,453,034**
EPS	$0.88	$0.86	$0.85	$0.91	$0.98	$1.05

Balance Sheet YE - December 31	2011	2012	2013	2014	2015(F)	2016(F)
Assets						
Cash	$8,330	$10,628,383	-	-	$0	$0
Mortgages receivable, net	$157,492,666	$201,954,951	$281,708,139	$432,757,000	$474,577,570	$499,618,664
Accrued interest receivable	$1,315,017					
Prepaid Expenses		$19,577	$272,615	$370,000	$246,514	$276,148
Receivables						
Total Asset	**$158,816,013**	**$212,602,911**	**$281,980,754**	**$433,127,000**	**$474,824,084**	**$499,894,812**
Liabilities						
Credit facility	$12,600,000	$0	$36,235,930	$80,298,000	$84,543,798	$92,679,972
Account payable and accrued liabilities	$212,546	$460,568	$459,209	$523,000	$911,954	$985,509
Due to related party	$172,211	$205,605	$182,437	$395,000	$395,000	$395,000
Dividend payable	$2,984,844	$1,826,813	$2,473,437	$3,379,000	$2,071,825	$2,371,086
Convertible debenture		$0	$30,610,763	$100,328,000	$114,578,000	$114,578,000
Total Liabilities	**$15,969,601**	**$2,492,986**	**$69,961,776**	**$184,923,000**	**$202,500,577**	**$211,009,568**
Share capital	$142,141,036	$209,383,307	$210,659,880	$245,794,000	$269,544,000	$285,694,000
Contributed surplus	$645,023	$693,199	$898,827	$1,085,000	$1,454,507	$1,866,244
Equity component of convertible debenture		$0	$397,539	$1,062,000	$1,062,000	$1,062,000
Retained Earnings	$60,353	$33,419	$62,732	$263,000	$263,000	$263,000
Total Shareholders Equity	**$142,846,412**	**$210,109,925**	**$212,018,978**	**$248,204,000**	**$272,323,507**	**$288,885,244**
Total Shareholders Equity+Liabilities	**$158,816,013**	**$212,602,911**	**$281,980,754**	**$433,127,000**	**$474,824,084**	**$499,894,812**

Cash Flow Statement YE - December 31	2011	2012	2013	2014	2015(F)	2016(F)
Operating Activities						
Net Income	$9,440,811	$13,358,327	$17,999,888	$21,037,000	$24,861,895	$28,453,034
Add (subtract) non cash item						
Share based payments		$48,176	$205,628	$222,000	$369,507	$411,737
Loan provision	$200,000	$193,291	$63,000	$1,817,000	$422,430	$381,336
Interest capitalized to mortgages	-$641,071	-$693,797	-$1,611,503	-$5,152,000	-	-
Amortization of mortgage discount	-$14,227	-$97,979	-$207,828	-$122,000	-	-
Amortization of mortgage origination fees	-$476,546	-$773,304	-$881,347	-$1,153,000	-	-
Non cash portion of interest on convertible debentures			$148,846	$644,000		
Total	$8,508,967	$12,034,714	$15,716,684	$17,293,000	$25,653,833	$29,246,107
Net changes in non-cash operating items						
Prepaid expenses		-$11,247	-$253,038	-$97,000	$123,486	-$29,634
Accrued interest receivable	-$1,075,751	-$519,018	$1,027,466	-$615,000	-	-
Accounts payable and accrued liabilities	$143,885	$248,023	-$1,359	$63,000	-$918,221	$372,817
Additions to mortgage discount	$0	$407,430	$160,800	$248,000	-	-
Additions to mortgage origination fee	$666,201	$903,128	$961,064	$1,264,000	-	-
Others	-$8,330			$1,093,000		
Cash From Operating Activities	$8,244,633	$13,063,030	$17,611,617	$19,249,000	$24,859,098	$29,589,289
Investing Activities						
Mortgage investments	-$116,424,513	-$129,073,353	-$186,702,516	-$278,319,000		
Repayment of mortgages	$34,045,062	$84,497,520	$107,437,676	$130,983,000		
Interest capitalized to mortgages	$641,071	$693,797				
Mortgage investments(net)	-$81,738,380	-$43,882,036	-$79,264,840	-$147,336,000	-$42,243,000	-$25,422,430
Cash used Investing Activities	-$81,738,380	-$43,882,036	-$79,264,840	-$147,336,000	-$42,243,000	-$25,422,430
Financing Activities						
Credit facility			$35,910,000	$44,062,000	$4,245,798	$8,136,175
Increase/decrease in amounts due to related party	$76,899	$33,394	-$23,168	$213,000	-	-
Issuance of share capital	$55,914,370	$71,130,933	$1,276,573	$36,708,000	$25,000,000	$17,000,000
Share capital issue costs	-$517,757	-$3,888,662	-	-$1,609,000	-$1,250,000	-$850,000
Cash dividends paid during the year	-$8,352,874	-$14,543,292	-$17,323,951	-$19,931,000	-$24,861,895	-$28,453,034
Proceeds from issuance of convertible debentures			$32,500,000	$72,051,000	$15,000,000	
Convertible debenture issue costs			-$1,640,544	-$3,407,000	-$750,000	$0
Cash used in Financing Activities	$59,580,638	$40,132,373	$50,698,910	$128,087,000	$17,383,902	-$4,166,859
Net Increase(Decrease) in Cash	-$13,913,109	$9,313,367	-$10,954,313	$0	$0	$0

Fundamental Research Corp. Equity Rating Scale:
Buy – Annual expected rate of return exceeds 12% or the expected return is commensurate with risk
Hold – Annual expected rate of return is between 5% and 12%
Sell – Annual expected rate of return is below 5% or the expected return is not commensurate with risk
Suspended or Rating N/A— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

Fundamental Research Corp. Risk Rating Scale:
1 (Low Risk) - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

2 (Below Average Risk) - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

3 (Average Risk) - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

4 (Speculative) - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

5 (Highly Speculative) - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues, and may rely on external funding. These stocks are considered highly speculative.

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