CAPREIT

**FINANCIAL REVIEW**
**FOR THE THREE MONTHS ENDED**
**MARCH 31, 2011**

CAPREIT

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May 9, 2011

**Report to Unitholders**

The record operating and financial performance generated in 2010 continued through the first quarter of 2011. Stabilized Net Operating Income (NOI) rose 4.7%, the twenty-first consecutive quarter of stable or improved year-over-year same property growth in NOI. Our strong growth is primarily the result of solid increases in occupancies and average monthly rents from our proven property management strategies, and sustainable reductions in our operating costs from cost management strategies and CAPREIT's ongoing energy-saving initiatives. We are confident this track record of organic growth will continue in the quarters ahead.

For the three months ended March 31, 2011, total operating revenues increased by 3.4% due to the contribution from acquisitions and higher overall average monthly rents across all sectors and geographic regions of the portfolio combined with overall occupancy reaching virtually full levels at 98.3%. The increase in average monthly rent was due to a combination of the acquisition of more luxury-oriented properties and the disposition of affordable properties over the last twelve months, our successful sales and marketing strategies, and continued strength in the residential rental sector in the majority of our markets.

While we increased revenues, we also reduced our operating expenses as a percentage of revenues primarily through lower overall utility costs as a result of our energy-saving initiatives and a revised natural gas supply strategy implemented in 2010. Repair and maintenance costs were higher due to acquisitions and the impact of implementation of the HST in Ontario and British Columbia in July last year.

Solid growth in operating revenues, combined with successful management of our operating costs, resulted in a 6.7% increase in NOI to $46.5 million in the quarter with NOI margins improving to 53.9% compared to 52.3% last year. The first quarter is typically our weakest due to higher costs associated with winter weather.

Normalized Funds From Operations (NFFO) increased by 12.4% for the three months ended March 31, 2011 due to the strong progress made in reducing operating costs, higher average monthly rents and improved occupancy levels, as well as the contribution from recent acquisitions. Importantly, our NFFO payout ratio improved to 92.6% in the quarter from 93.1% last year. Increased participation in our Distribution Reinvestment Plan further improved our effective NFFO payout ratio to 72.5% from 80.1% last year.

Our balance sheet and financial position remained strong at quarter end with debt service ratios well within our guidelines. Coverage ratios also improved and remain conservative with interest coverage exceeding two times. Our weighted average mortgage interest rate declined to 4.74%, and we continue to focus on extending our debt maturities. During the first quarter total financings of $98.3 million were completed, including the renewal of $88.0 million in existing mortgages and $10.3 million in top-up financings. The weighted average interest rate of 5.4% was significantly below the 5.11% for the maturing mortgages. Looking ahead, we expect to renew approximately $144.8 million of the remaining mortgages maturing in 2011, as well as refinancing a significant portion of the $36.9 million in principal repayments. The combined weighted average interest rate for these maturing mortgages is 5.37%, and we expect to renew them at lower rates, further benefiting cash flows in the coming years.

So far this year, we have acquired an 83-suite mid-tier townhome complex in Burlington and five apartment buildings in the Greater Vancouver Region comprising 495 suites. We also sold a non-core affordable property in Hamilton, generating net cash proceeds of $3.6 million. Looking ahead, we remain confident we will meet our goal of acquiring between 1,500 and 2,000 suites this year.

Our acquisition focus remains on finding properties where we can add long-term value through our capital investments and operating programs. We target properties close to current locations in order to build critical mass, pricing power and capitalize on operating synergies. Many acquisition candidates have below-market rents, offering the potential to grow revenues as we apply our proven marketing strategies. And with our highly effective energy supply and pricing strategies, and our national procurement programs and other operating procedures, we believe we can significantly reduce operating costs to grow cash flows.

Looking ahead, we will continue to capitalize on the strong fundamentals in the majority of our markets, and anticipate further growth in the coming quarters.

_(Signed)_
Thomas Schwartz
President and Chief Executive Officer

_(Signed)_
Michael Stein
Chairman

CAPREIT

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

## THREE MONTHS ENDED MARCH 31, 2011

MAY 9, 2011

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**SECTION I**

**FORWARD-LOOKING DISCLAIMER**

The following Management's Discussion and Analysis ("MD&A") of Canadian Apartment Properties Real Estate Investment Trust's ("CAPREIT") results of operations and financial condition for the three months ended March 31, 2011 and 2010 should be read in conjunction with CAPREIT's audited consolidated annual financial statements for the year ended December 31, 2010, contained in CAPREIT's 2010 Annual Report.

Certain statements contained, or contained in documents incorporated by reference, in this MD&A constitute forward-looking information within the meaning of securities laws. Forward-looking information may relate to CAPREIT's future outlook and anticipated events or results and may include statements regarding the future financial position, business strategy, budgets, litigation, projected costs, capital investments, financial results, taxes, plans and objectives of or involving CAPREIT. Particularly, statements regarding CAPREIT's future results, performance, achievements, prospects, costs, opportunities and financial outlook, including those relating to acquisition and capital investment strategy and the real estate industry generally, are forward-looking statements. In some cases, forward-looking information can be identified by terms such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "intend", "estimate", "predict", "potential", "continue" or the negative thereof or other similar expressions concerning matters that are not historical facts. Forward-looking statements are based on certain factors and assumptions regarding expected growth, results of operations, performance and business prospects and opportunities. In addition, certain specific assumptions were made in preparing forward-looking information, including: that the Canadian economy will generally experience growth, however, with specific geographic areas of weakness including Alberta; that inflation will remain low; that interest rates will rise modestly in 2011; that Canada Mortgage and Housing Corporation ("CMHC") mortgage insurance will continue to be available and that a sufficient number of lenders will participate in the CMHC-insured mortgage program to ensure competitive rates; that conditions within the real estate market, including competition for acquisitions, will become more favourable; that the Canadian capital markets will continue to provide CAPREIT with access to equity and/or debt at reasonable rates; that vacancy rates for CAPREIT properties will be consistent with historical norms; that rental rates will grow at levels similar to the rate of inflation on renewal; that rental rates on turnovers will remain stable; that CAPREIT will effectively manage price pressures relating to its energy usage; and, with respect to CAPREIT's financial outlook regarding capital investments, assumptions respecting projected costs of construction and materials, availability of trades, the cost and availability of financing, CAPREIT's investment priorities, the properties in which investments will be made, the composition of the property portfolio and the projected return on investment in respect of specific capital investments. Although the forward-looking statements contained in this MD&A are based on assumptions Management believes are reasonable as of the date hereof, there can be no assurance actual results will be consistent with these forward-looking statements; they may prove to be incorrect. Forward-looking statements necessarily involve known and unknown risks and uncertainties, many of which are beyond CAPREIT's control, that may cause CAPREIT or the industry's actual results, performance, achievements, prospects and opportunities in future periods to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, among other things, risks related to: investment properties, real property ownership, leasehold interests, co-ownerships, investment restrictions, operating risk, energy costs and hedging, environmental matters, insurance, capital investments, indebtedness, interest rate hedging, taxation, harmonization of federal goods and services tax and provincial sales tax, government regulations, controls over financial accounting, International Financial Reporting Standards ("IFRS"), legal and regulatory concerns, the nature of units of CAPREIT ("Trust Units") and of CAPREIT's subsidiary, CAPREIT Limited Partnership ("Exchangeable Units") (collectively, the "Units"), unitholder liability, liquidity and price fluctuation of Units, dilution, distributions, participation in CAPREIT's distribution reinvestment plan, potential conflicts of interest, dependence on key personnel, general economic conditions, competition for residents, competition for real property investments, continued growth and risks related to acquisitions. There can be no assurance that the expectations of CAPREIT's Management will prove to be correct. For a detailed discussion of risk factors, refer to the Risks and Uncertainties section and CAPREIT's latest Annual Information Form. Subject to applicable law, CAPREIT does not undertake any obligation to publicly update or revise any forward-looking information.

## NON-IFRS FINANCIAL MEASURES

CAPREIT prepares and releases unaudited consolidated interim financial statements and audited consolidated annual financial statements in accordance with IFRS. In this MD&A, and in earnings releases and investor conference calls, as a complement to results provided in accordance with IFRS, CAPREIT also discloses and discusses certain financial measures not in accordance with IFRS, including Net Operating Income ("NOI"), Net Rental Revenue Run-Rate, Funds From Operations ("FFO"), Normalized Funds From Operations ("NFFO") and Adjusted Funds From Operations ("AFFO") and applicable per Unit amounts and payout ratios. These non-IFRS measures are further defined and discussed in Section III, under Non-IFRS Financial Measures. Since NOI, Net Rental Revenue Run-Rate, FFO, NFFO and AFFO are not measures determined under IFRS, they may not be comparable to similarly titled measures reported by other issuers. CAPREIT has presented such non-IFRS measures because Management believes these non-IFRS measures are relevant measures of the ability of CAPREIT to earn and distribute cash returns to investors in the Units ("Unitholders") and to evaluate CAPREIT's performance. A reconciliation of non-IFRS measures is provided in Section III, under Non-IFRS Financial Measures. These non-IFRS measures should not be construed as alternatives to net income (loss) or cash flow from operating activities determined in accordance with IFRS as indicators of CAPREIT's performance.

## ADOPTION OF IFRS

In 2008, the Canadian Accounting Standards Board ("AcSB") confirmed that Canadian publicly-listed entities will have to adopt IFRS effective for fiscal years beginning on or after January 1, 2011. Accordingly, the accompanying unaudited consolidated interim financial statements for the three months ended March 31, 2011 have been prepared in accordance with International Accounting Standard ("IAS") 34, Interim Financial Statements and IFRS 1, First-Time Adoption of IFRS, with effect from January 1, 2010, the date of transition. Results for periods prior to January 1, 2010 have not been restated. For the purposes of this MD&A, the term "Canadian GAAP" refers to Canadian generally accepted accounting principles before the adoption of IFRS.

Notes 4 and 5 of the accompanying unaudited consolidated interim financial statements for the three months ended March 31, 2011 contain a detailed description of CAPREIT's conversion to IFRS, including a reconciliation of financial statements prepared under Canadian GAAP to those prepared under IFRS for the three months ended March 31, 2011 and 2010 as well as for the year ended December 31, 2010. Additional details of the transition are disclosed in the Adoption of IFRS section, which also includes line-by-line reconciliations of the consolidated balance sheets at January 1, 2010 and December 31, 2010 as reported under Canadian GAAP to those reported under IFRS. Similar reconciliations of the consolidated statements of income as reported under Canadian GAAP to those reported under IFRS for the three months ended March 31, 2010 and for the year ended December 31, 2010 are also disclosed. Reconciliations of previously reported non-IFRS financial measures to the revised figures as presently reported is provided in the Non-IFRS Financial Measures section of the MD&A.

## OVERVIEW

CAPREIT is an unincorporated open-ended real estate investment trust created by a declaration of trust (the "Declaration of Trust") dated February 3, 1997 under the laws of the Province of Ontario, as most recently amended and restated on November 13, 2009. CAPREIT owns interests in multi-unit residential rental properties, including apartments, townhomes and manufactured home communities located in and near major urban centres across Canada. At March 31, 2011, CAPREIT had ownership interests in a portfolio that included 27,112 residential suites (CAPREIT's share – 25,957 suites), diversified by geographic location and asset type, and two Ontario manufactured home communities ("MHC") comprising 1,325 land lease sites. As at March 31, 2011, CAPREIT had 740 employees (734 employees as at December 31, 2010).

The tables below summarize acquisitions and dispositions of properties for the three months ended March 31, 2011 and for the year ended December 31, 2010:

***Acquisitions Completed During The Three Months Ended March 31, 2011 and subsequent thereto***

| ($ Thousands) | Demographic Sector | Suite or Site Count | Region(s) | Total Acquisition Costs | Mortgage Funding | Interest Rate | Mortgage Maturity Date |
|---|---|---|---|---|---|---|---|
| January 31, 2011 | Mid-tier | 83 | Burlington | $ 9,084 | $ 6,818 | 4.26% | March 1, 2021 |
| *Subsequent to March 31, 2011:* | | | | | | | |
| April 15, 2011 (1) | Mixed (2) | 495 | Greater Vancouver Region | 72,000 | 49,369 | 4.38% | May 1, 2021 |
| Total | | 578 | | $ 81,084 | $ 56,187 | | |

(1) See the Subsequent Event section.
(2) The acquisition comprised of three mid-tier and two luxury properties.

***Acquisitions Completed During the Year Ended December 31, 2010***

| ($ Thousands) | Demographic Sector | Suite or Site Count | Region(s) | Total Acquisition Costs | Mortgage Funding | Interest Rate | Mortgage Maturity Date |
|---|---|---|---|---|---|---|---|
| February 22, 2010 | MHC | 14 | Bowmanville and Grand Bend | $ 912 | $ – (1) | (1) | (1) |
| April 12, 2010 | Luxury | 162 | Vancouver | 38,425 | 22,652 (2) | 4.59% | April 5, 2017 |
| May 14, 2010 | Luxury | 199 | Mississauga | 31,653 | 22,165 | 3.37% | June 1, 2015 |
| July 29, 2010 | Mixed | 307 | Victoria | 47,194 | 26,366 (3) | (3) | (3) |
| December 20, 2010 | MHC | 9 | Bowmanville and Grand Bend | 488 | – (1) | (1) | (1) |
| Total | | 691 | | $ 118,672 | $ 71,183 | | |

(1) The acquisition of MHC land lease sites is funded from CAPREIT's land lease facility (see Liquidity and Financial Condition section).
(2) The mortgage was assumed from the vendor at acquisition.
(3) The acquisition comprised of two affordable, four mid-tier and two luxury properties. Funding for the acquisition comprised of new mortgage financing of $25,580 at 3.67% maturing December 1, 2020 and an assumed mortgage of $786 at a stated rate of 4.73% maturing on February 1, 2016.

***Dispositions Completed During The Three Months Ended March 31, 2011***

| ($ Thousands) | Demographic Sector | Suite Count | Region(s) | Sale Price | Cash Proceeds | Mortgage(s) Repaid |
|---|---|---|---|---|---|---|
| March 29, 2011 | Affordable | 143 | Hamilton | $ 5,975 | $ 3,609 | $ 2,117 |

***Dispositions Completed During the Year Ended December 31, 2010***

| ($ Thousands) | Demographic Sector | Suite Count | Region(s) | Sale Price | Cash Proceeds | Mortgage(s) Repaid |
|---|---|---|---|---|---|---|
| June 3, 2010 | Mid-tier | 88 | Montréal | $ 3,000 | $ 2,831 | $ 1,926 |
| June 9, 2010 | Affordable | 250 | Montréal | 11,750 | 10,568 | 4,014 |
| July 5, 2010 | Affordable | 146 | London | 7,600 | 7,116 | 5,650 |
| July 29, 2010 | Mid-tier | 570 | Mississauga and Kitchener | 45,900 | 42,232 | 20,106 |
| November 24, 2010 | Mid-tier | 56 | Toronto | 6,430 | 6,042 | – |
| Total | | 1,110 | | $ 74,680 | $ 68,789 | $ 31,696 |

## OBJECTIVES

CAPREIT's objectives are to:

- Provide Unitholders with long-term, stable and predictable monthly cash distributions;
- Grow Normalized Funds From Operations, sustainable distributions and Unit value through the active management of its properties, accretive acquisitions and strong financial management; and
- Reinvest capital within the property portfolio in order to ensure life safety of residents and maximize earnings and cash flow potential.

## BUSINESS STRATEGY

To meet its objectives, CAPREIT has established the following strategies:

*Customer Service* – CAPREIT recognizes that it is in a "people business" and strives to be recognized as the Landlord of Choice in all its chosen markets by providing its residents with safe, secure and comfortable homes. It takes a hands-on approach to managing its properties, stressing open and frequent communications to ensure residents' needs are met efficiently and effectively and thereby maintaining a high occupancy level. Numerous initiatives such as newsletters, special events, resident committees and other initiatives help to build a true sense of community at its properties. CAPREIT's strong sales and marketing team continues to execute innovative and highly effective strategies to help attract and retain residents and adapt to changing conditions in specific markets. In addition, CAPREIT's lease administration system improves control of rent-setting by suite, increasing resident service and enhancing the overall profile of its resident base.

*Cost Controls* – While ensuring the needs of its residents are met, CAPREIT also carefully monitors operating costs to ensure it is delivering services to residents both efficiently and cost effectively. CAPREIT strives to capture potential economies of scale and cost synergies arising from past growth. CAPREIT's enterprise-wide procurement system streamlines and centralizes purchasing controls and procedures and is generating reduced costs through national master sourcing contracts, improved pricing and enhanced operating efficiencies.

*Capital Investments* – CAPREIT strives to acquire properties at prices significantly below their current replacement costs, and is committed to improving its operating performance by incurring appropriate capital investments in order to maintain the productive capacity of its property portfolio and to sustain the portfolio's rental income-generating potential over its useful life. CAPREIT continues to invest in environment-friendly and energy-saving initiatives that improve overall net operating income. In 2009, CAPREIT completed a review of its portfolio and developed a five-year capital investment plan that continues to be monitored and re-examined. This plan will allow Management to ensure capital investments extend the useful economic life of CAPREIT's properties, enhance life safety and improve the long-term cash flow potential of its portfolio.

*Portfolio Growth* – CAPREIT will grow its portfolio over the long term through accretive acquisitions that meet its strategic criteria and, where possible, enhance geographic diversification while capturing economies of scale and cost synergies, thereby increasing net operating income. As a component of this growth strategy, CAPREIT will monitor its portfolio and, from time to time, identify certain non-core properties for divestiture. The funds from these divestitures will be used to acquire additional strategic assets better suited to CAPREIT's portfolio composition and property management objectives or to pay down existing debt. Management believes the continued realization and reinvestment of capital is a fundamental component of its growth strategy and demonstrates the success of CAPREIT's capital investment programs and its ability to maximize and manage the earnings and cash flow potential of its property portfolio.

*Financial Management* – CAPREIT takes a conservative approach and strives to manage its exposure to interest rate volatility by proactively managing its mortgage debt portfolio to fix and, where possible, reduce average interest rates, effectively manage the average term to maturity and stagger maturity dates. In addition, CAPREIT strives to maintain a conservative overall liquidity position and achieve a balance in its overall capital resources requirements between debt and equity.

## KEY PERFORMANCE INDICATORS

To assist Management and investors in monitoring and evaluating CAPREIT's achievement of its objectives, CAPREIT has defined a number of key operating and performance indicators ("KPIs") to measure the success of its operating and financial strategies:

*Occupancy* – Management strives, through a focused, hands-on approach to its business, to achieve occupancies that are in line with, or higher than, market conditions in each of the geographic regions in which CAPREIT operates while enhancing the overall qualitative profile of its resident base.

*Average Monthly Rents* – Through its active property management strategies, the lease administration system and proactive capital investment programs, CAPREIT strives to achieve the highest possible average monthly rents in accordance with local market conditions.

*NOI* – As a measure of its operating performance, CAPREIT currently strives to achieve an annual net operating income margin that is in the range of 55% to 57% of operating revenues.

*FFO* and *NFFO* – CAPREIT is focused on achieving steady increases in these metrics. Management believes these measures are indicative of CAPREIT's operating performance and the sustainability of its distributions.

*Payout Ratio* – To help ensure it retains sufficient cash to meet its capital investment objectives, CAPREIT has historically targeted a long-term annual payout ratio of between 85% and 90% of NFFO.

*Portfolio Growth* – Management's objective is to pursue strategic acquisitions of between 1,500 and 2,000 suites on an annual basis, subject to market conditions and available financing, which meet its strategic objectives, serve to accretively increase NFFO and continue to further diversify the portfolio by geography and by sector.

*Financing* – CAPREIT takes a very proactive approach with its mortgage portfolio, striving to manage interest expense volatility risk by achieving the lowest possible average interest rates while mitigating refinancing risk by prudently managing the portfolio's average term to maturity and staggering the maturity dates. For this purpose, CAPREIT strives to ensure its overall leverage ratios and interest and debt service coverage ratios are maintained at a sustainable level. In addition, CAPREIT focuses on maintaining capital adequacy by complying with investment and debt restrictions in its Declaration of Trust and its financial covenants in its credit agreement comprising an acquisition and operating facility ("Acquisition and Operating Facility") and a land lease facility ("Land Lease Facility") (collectively, the "Credit Facilities", as described in Bank Indebtedness and Credit Facilities under Section IV).

## PERFORMANCE MEASURES

The following table presents an overview of certain key IFRS and non-IFRS financial measures and operational results of CAPREIT for the periods ended March 31, 2011 and 2010. Management believes that these measures are useful in assessing CAPREIT's performance vis-à-vis its objectives, business strategy and KPIs. During the period, monthly cash distributions declared to its Unitholders remained constant at $0.09 per Unit.

| **Three Months Ended March 31,** | | **2011** | | **2010** |
|---|---|---|---|---|
| **Portfolio Performance** | | | | |
| Overall Portfolio Occupancy (1) | | **98.3%** | | 97.8% |
| Overall Portfolio Average Monthly Rents (1) | **$** | **978** | $ | 943 |
| Operating Revenues (000s) | **$** | **86,332** | $ | 83,518 |
| NOI (000s) | **$** | **46,564** | $ | 43,643 |
| NOI Margin | | **53.9%** | | 52.3% |
| **Operating Performance** (2) | | | | |
| FFO Per Unit – Basic | **$** | **0.296** | $ | 0.227 |
| NFFO Per Unit – Basic | **$** | **0.301** | $ | 0.302 |
| Cash Distributions Per Unit | **$** | **0.270** | $ | 0.270 |
| FFO Payout Ratio | | **94.4%** | | 123.8% |
| NFFO Payout Ratio | | **92.6%** | | 93.1% |
| **Liquidity and Leverage** | | | | |
| Total Debt to Gross Book Value (1) | | **52.28%** | | 56.04% |
| Total Debt to Gross Historical Cost (1),(3) | | **59.00%** | | 63.22% |
| Weighted Average Mortgage Interest Rate (1) | | **4.74%** | | 5.06% |
| Weighted Average Mortgage Term (years) (1) | | **4.9** | | 4.8 |
| Debt Service Coverage (times) (4) | | **1.34** | | – |
| Interest Coverage (times) (4) | | **2.11** | | – |
| Available Liquidity – Acquisition and Operating Facility (000s) (1) | **$** | **198,032** | $ | 63,509 |
| **Other** | | | | |
| Number of Suites and Sites Acquired | | **83** | | 14 |
| Number of Suites Disposed | | **143** | | – |
| Closing Price of Trust Units (1) | **$** | **19.46** | $ | 14.35 |
| Market Capitalization ($ millions) (5) | **$** | **1,509** | $ | 991 |

(1) As at March 31.
(2) NOI, FFO and NFFO are not defined by IFRS, do not have standard meanings and may not be comparable with other industries or companies (see Non-IFRS Financial Measures).
(3) Based on the historical cost of investment properties.
(4) Based on the trailing four quarters ended March 31, 2011. Prior year comparative ratios have not been restated under IFRS and are therefore not presented. Ratios calculated under Canadian GAAP are available in the MD&A issued for periods prior to 2011.
(5) Defined as the closing price of the Units on the last trading date of the period times the number of Units outstanding on that date (see discussion of Unitholders' equity under the Liquidity and Financial Condition section).

## PROPERTY PORTFOLIO

### Types of Property Interests

CAPREIT's investments in its property portfolio reflect different forms of property interests, including:

*Fee Simple Interests – Apartments and Townhomes* – The majority of CAPREIT's investment in its property portfolio is in the form of fee simple, representing freehold ownership of the properties subject only to typical encumbrances such as mortgages.

*Operating Leasehold Interests* – CAPREIT owns leasehold interests in 15 properties located in the Greater Toronto Area. The leases mature between 2033 and 2037. While separate lease arrangements exist for each property, the general structure is common across all leases: each lease is for a 35-year term and the rent for the entire lease term was fully paid at the time the leasehold interest was acquired. Each lease also provides CAPREIT with a purchase option exercisable between the 26th and 35th year of the lease term. In the case of one of the properties, the purchase option entitles CAPREIT to acquire a prepaid operating leasehold interest in the property maturing in 2072 (see Portfolio of Operating Leasehold Interests in CAPREIT's 2010 Annual Report for additional information).

*Land Leasehold Interests* – CAPREIT owns leasehold interests in two land parcels in Alberta and one land parcel in British Columbia. CAPREIT acquired a residential building on each of the three land parcels and pays ground rent on an annual basis for its use of the land. These land leases mature in 2045, 2068 and 2070. CAPREIT does not have the unilateral right to acquire the land or extend the lease term at the maturity of the respective leases (see Portfolio of Land Leasehold Interests in CAPREIT's 2010 Annual Report for additional information).

*Fee Simple Interests – MHC Land Lease Sites* – CAPREIT has fee simple interests in two MHCs whereby CAPREIT owns sites which it rents to residents under long-term leases of approximately 20 years.

***Portfolio by Type of Property Interest***

| **As at March 31,** | **2011** | % | **2010** (1) | % |
|---|---|---|---|---|
| Fee Simple Interests – Apartments and Townhomes | **22,398** | **78.8** | 22,900 | 79.2 |
| Operating Leasehold Interests | **3,815** | **13.4** | 3,815 | 13.2 |
| Land Leasehold Interests | **899** | **3.2** | 899 | 3.1 |
| Total Residential Suites | **27,112** | **95.4** | 27,614 | 95.5 |
| Fee Simple Interests – MHC Land Lease Sites | **1,325** | **4.6** | 1,316 | 4.5 |
| Total Residential Suites and MHC Land Lease Sites | **28,437** | **100.0** | 28,930 | 100.0 |

(1) Suite count not restated for properties disposed subsequent to March 31, 2010.

### Portfolio Diversification

CAPREIT's property portfolio continues to be diversified by geography and balanced among asset types and demographic sectors. Management's long-term goal is to further enhance the geographic diversification and defensive nature of its portfolio through future acquisitions.

During the fourth quarter of 2010, Management revised the demographic sector classification of certain properties. For the year ended December 31, 2010, the classification of six properties comprising 1,925 suites located in Ontario were reclassified from affordable to mid-tier and two properties comprising 354 suites located in Québec and Ontario were reclassified from mid-tier to luxury. These reclassifications reflect the increases in average monthly rents and the improvements in the quality of the properties and tenant bases resulting from property capital investments completed in 2010 and in prior years.

***Portfolio by Demographic Sector***

| As at March 31, | 2011 | % | 2010 [(1)] | % |
|---|---|---|---|---|
| Affordable | **1,214** | **4.3** | 3,638 | 12.6 |
| Mid-tier | **15,801** | **55.6** | 14,711 | 50.9 |
| Luxury | **10,097** | **35.5** | 9,265 | 32.0 |
| Total Residential Suites | **27,112** | **95.4** | 27,614 | 95.5 |
| MHC Land Lease Sites | **1,325** | **4.6** | 1,316 | 4.5 |
| Total Residential Suites and MHC Land Lease Sites | **28,437** | **100.0** | 28,930 | 100.0 |

(1) Suite count not restated for properties disposed subsequent to March 31, 2010 or for the change in demographic sector classifications effected in the fourth quarter of 2010 (see Portfolio Diversification).

***Portfolio by Geography***

| As at March 31, | 2011 | % | 2010 | % |
|---|---|---|---|---|
| **Ontario** | | | | |
| Greater Toronto Area | **14,184** | **49.9** | 14,178 | 49.0 |
| Ottawa | **1,527** | **5.4** | 1,527 | 5.3 |
| London / Kitchener / Waterloo | **903** | **3.2** | 1,482 | 5.1 |
| Other Ontario | **1,410** | **4.9** | 1,470 | 5.1 |
| Ontario Residential Suites | **18,024** | **63.4** | 18,657 | 64.5 |
| MHC Land Lease Sites | **1,325** | **4.6** | 1,316 | 4.5 |
| Ontario Residential Suites and Land Lease Sites | **19,349** | **68.0** | 19,973 | 69.0 |
| **Québec** | | | | |
| Greater Montréal Region | **2,207** | **7.8** | 2,545 | 8.8 |
| Québec City | **1,909** | **6.7** | 1,909 | 6.6 |
| | **4,116** | **14.5** | 4,454 | 15.4 |
| **British Columbia** | | | | |
| Greater Vancouver Region | **1,453** | **5.1** | 1,291 | 4.5 |
| Victoria | **815** | **2.9** | 508 | 1.8 |
| | **2,268** | **8.0** | 1,799 | 6.3 |
| **Alberta** | | | | |
| Edmonton | **310** | **1.1** | 310 | 1.1 |
| Calgary | **1,070** | **3.8** | 1,070 | 3.7 |
| | **1,380** | **4.9** | 1,380 | 4.8 |
| **Nova Scotia** | | | | |
| Halifax | **1,083** | **3.8** | 1,083 | 3.7 |
| **Saskatchewan** | | | | |
| Saskatoon | **133** | **0.4** | 133 | 0.4 |
| Regina | **108** | **0.4** | 108 | 0.4 |
| | **241** | **0.8** | 241 | 0.8 |
| Total Residential Suites | **27,112** | **95.4** | 27,614 | 95.5 |
| Total Residential Suites and MHC Land Lease Sites | **28,437** | **100.0** | 28,930 | 100.0 |

Through accretive acquisitions, CAPREIT expects to enhance the geographic diversification of its residential suite portfolio. During the first quarter of 2011, CAPREIT acquired a mid-tier townhome complex comprising 83 suites located in Burlington, Ontario. CAPREIT continues to maintain its objective of acquiring between 1,500 and 2,000 suites on an annual basis and Management expects to meet its growth objectives in 2011. During the year ended December 31, 2010, CAPREIT acquired a total of 691 residential suites and sites located across Canada.

Over the past five years, CAPREIT has focused on diversifying its geographic portfolio by increasing its presence in markets with higher growth potential and has also acquired two manufactured home communities while maintaining its strong presence in the Ontario residential suite market. Strategic acquisitions continue to target growth in markets outside

of Ontario; however, Management also continues to believe strategic investments in Ontario will benefit Unitholders as the province's residential market remains strong. CAPREIT continues to look for investment opportunities that meet its investment criteria and that, where possible, will further its diversification strategy. The geographic diversification of its portfolio also enables CAPREIT to mitigate the risks arising from potential downturns in specific markets.

## INVESTMENT PROPERTIES

Investment property is defined as property held to earn rental income or for capital appreciation or both. Investment property is recognized initially at cost. Subsequent to initial recognition, all investment property is measured using the fair value model whereby changes in fair value are recognized for each reporting period in the consolidated statement of income.

Management values each investment property based on the most probable price that a property should be sold for in a competitive and open market as of the specified date under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. This does not contemplate the potential for general declines in real estate markets or sale of assets by CAPREIT under financial or other hardship. Each investment property has been valued on a highest and best use basis, but specifically does not include any portfolio premium that may be associated with economies of scale from owning a large portfolio or the consolidation value of having compiled a large portfolio of properties over a long period of time, many through individual property acquisitions.

Market assumptions applied for valuation purposes do not necessarily reflect the specific history or experience related to CAPREIT, and in many cases, the stabilized cash flows or NOI used for appraisal purposes may not reflect the results ultimately realized during future periods.

The fair value of investment properties is established by a qualified, independent appraiser annually. Each quarter, CAPREIT utilizes market assumptions for capitalization and discount rates provided by the external appraiser to determine the fair value of the investment properties for interim reporting purposes. To the extent that the externally provided capitalization rates or results of operations change from one reporting period to the next, the fair value of the investment properties would increase or decrease accordingly.

Investment properties have been valued using the following methods and key assumptions:

i) *Fee Simple and MHC Land Lease Sites*: CAPREIT utilizes the Direct Income Capitalization ("DC") method. Under this method, capitalization rates are applied to a stabilized NOI representing market-based NOI assumptions (property revenue less property operating expenses). The most significant assumption is the capitalization rate for each specific property.

ii) *Operating Leasehold Interests*: CAPREIT utilizes the Discounted Cash Flow ("DCF") method. Under this method, discount rates are applied to the forecasted cash flows reflecting market-based leasing assumptions for that specific property as well as assumptions as to renewal and new leasing activity. The most significant assumption is the discount rate applied over the initial term of the lease. In the case of one property, a separate liability is recognized for contractual air rights payments and the discount rate used to determine the fair value of the investment property is adjusted for uncertainty relating to the renegotiation of the air rights lease at the end of its term.

iii) *Options to purchase the related operating leases*: CAPREIT utilizes the DC method at the reversion date to estimate the future value, which is then discounted to a present value. Under this method, the stabilized income is adjusted to a projected NOI as at the end of the operating lease term and the capitalization rate is adjusted to a "Reversionary Capitalization Rate" reflecting the incremental risk associated with future uncertainty. The value of the option is then determined based on the difference between the estimated fair value of the property at such date and the option buyout price, discounted back to present value using a risk-adjusted discount rate (the "Option Discount Rate").

iv) *Land Leasehold Interests*: CAPREIT utilizes the DCF method for properties that are subject to land or air rights leases. Under this method, discount rates are applied to the forecasted cash flows reflecting market-based leasing assumptions for that specific property as well as assumptions as to renewal and new leasing activity. The

most significant assumption is the discount rate applied over the initial term of the lease. A separate liability is recognized for contractual land lease payments and discount rates are adjusted for uncertainty relating to the renegotiation of land leases at the end of their terms.

For a discussion of risk factors associated with the valuation of investment properties, refer to the Risks and Uncertainties section. A summary of the fair values of CAPREIT's investment properties along with key market assumptions by geographic region is presented below as at March 31, 2011 and 2010:

***Investment Properties By Geography***

| **As at March 31,** | **2011** | | | **2010** | |
|---|---|---|---|---|---|
| ($ millions) | **Fair Value** | **Weighted Average** | **Change** (1) | Fair Value | Weighted Average |
| **Greater Toronto Area** (2) | **$ 1,614** | | **$ 87** | $ 1,527 | |
| Capitalization rate | | **6.19%** | | | 6.20% |
| Discount rate | | **7.56%** | | | 7.93% |
| **Other Ontario** | **306** | | **(24)** | 330 | |
| Capitalization rate | | **6.12%** | | | 6.29% |
| **Québec** | **345** | | **–** | 345 | |
| Capitalization rate | | **6.28%** | | | 6.43% |
| **British Columbia** (2) | **368** | | **97** | 271 | |
| Capitalization rate | | **4.92%** | | | 4.92% |
| Discount rate | | **7.75%** | | | 7.75% |
| **Alberta** (2) | **234** | | **(1)** | 235 | |
| Capitalization rate | | **5.81%** | | | 5.83% |
| Discount rate | | **7.85%** | | | 7.92% |
| **Nova Scotia** | **139** | | **5** | 134 | |
| Capitalization rate | | **6.70%** | | | 6.74% |
| **Saskatchewan** | **22** | | **–** | 22 | |
| Capitalization rate | | **6.85%** | | | 6.87% |
| **MHC Land Lease Sites** | **89** | | **–** | 89 | |
| Capitalization rate | | **6.25%** | | | 6.25% |
| Gross Value of Investment Properties | **$ 3,117** | | **$ 164** | $ 2,953 | |
| Liabilities Associated with Investment Properties | **(56)** | | **(5)** | (51) | |
| **Investment Properties, Net of Associated Liabilities** | **$ 3,061** | | **$ 159** | $ 2,902 | |

(1) Change in fair value from prior year period.
(2) In the Greater Toronto Area, there is one property that is subject to a contractual air rights lease. In Alberta, there are two properties, and in British Columbia, there is one property with Land Leasehold Interests subject to land leases. These four properties have been reflected at gross fair value, excluding the combined associated liabilities of $56.6 million as at March 31, 2011 (2010 - $50.7 million).

The fair value of investment properties has shown significant movements between the two periods in the Greater Toronto Area, Other Ontario and British Columbia regions.

In the Greater Toronto Area, the fair value increased by $87.0 million including $36.0 million from higher stabilized NOI resulting from higher average monthly rents and $37.0 million from the decrease in the weighted average capitalization rate and discount rate. The remaining increase is mostly due to acquisitions, net of dispositions, for $11.0 million and higher fair value of Operating Leasehold Interests of $2.0 million from the decrease in the time to lease maturity.

In the Other Ontario region, the fair value decreased by $24.0 million primarily due to dispositions net of acquisitions of $34.0 million, which was partially offset by increases of $9.0 million from the decrease in the weighted average capitalization rate and $2.0 million from higher stabilized NOI.

In British Columbia, the fair value increased by $97.0 million primarily due to acquisitions of $87.0 million and by $3.0 million arising from the decrease in the weighted average capitalization rate and higher fair value of Operating Leasehold Interests of $7.0 million from the decrease in the time to lease maturity and changes in estimated cash payments.

The fair value of investment properties for all the other regions remained stable for the three months ended March 31, 2011 and 2010 despite changes in stabilized NOI and capitalization rate.

| **Three Months Ended March 31,**<br>($ Thousands) | | **2011** | **2010** |
|---|---|---|---|
| Balance, Beginning of the Period (1) | | **$ 3,106,548** | $ 2,951,647 |
| Add: | Acquisitions | **9,084** | 912 |
| | Property Capital Investments (2) | **13,020** | 8,411 |
| | Capitalized Leasing Costs (3) | **(78)** | (39) |
| Less: | Dispositions | **(5,730)** | – |
| Unrealized Loss on Remeasurement | | **(5,556)** | (8,364) |
| Investment Properties at Gross Fair Market Value, End of Period | | **$ 3,117,288** | $ 2,952,567 |
| Less: | Liabilities Associated with Investment Properties (1) | **(56,568)** | (50,662) |
| Investment Properties Net of Associated Liabilities, End of Period | | **$ 3,060,720** | $ 2,901,905 |

(1) Includes one Operating Leasehold Interest subject to a contractual air rights lease and three Land Leasehold Interests subject to land leases that have been reflected at gross fair market value and then have been reduced by the liabilities associated with the investment properties. These liabilities represent the present value of the related land leases or air rights payments.
(2) See Property Capital Investments section.
(3) Capitalized leasing costs are comprised of the changes in direct leasing costs, tenant inducements, and straight-line adjustments for the three months ended March 31.

The fair value of CAPREIT's investment properties, excluding the impact of acquisitions and dispositions during the quarter, has increased by a net $7.5 million due to the decrease in capitalization rates and movement in stabilized NOI. The unrealized loss on remeasurement is primarily the result of certain capital investments not having an immediate effect on stabilized NOI and thus not being reflected in the fair value of the investment properties at the measurement date.

As at March 31, 2011, a 25 basis point change in capitalization rates would have the following approximate effect on the fair value of investment properties:

**As as March 31, 2011**

| ($ Thousands) | **Change (basis points) (1)** | **Estimated Increase (Decrease) in Fair Value of Investment Properties** |
|---|---|---|
| Weighted Average Capitalization Rate | +25 | $ (113,000) |
| Weighted Average Capitalization Rate | -25 | $ 136,000 |

(1) For Operating Leasehold Interests and Land Leasehold Interests, CAPREIT applies discount rates to determine the fair value of these properties. However, for the purposes of the above sensitivity analysis, CAPREIT has utilized the implied capitalization rates for Operating Leasehold Interests and Land Leasehold Interests to determine the impact on fair value of the total portfolio.

**SECTION II**

## AVERAGE MONTHLY RENTS AND OCCUPANCY

***Portfolio Average Monthly Rents ("AMR") and Occupancy By Demographic Sector***

| As at March 31, | Total Portfolio | | | | Properties Owned Prior to March 31, 2010 | | | | Properties Acquired Since March 31, 2010 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2011 | | 2010 | | 2011 | |
| | AMR | Occ. % | AMR | Occ. % | AMR | Occ. % | AMR | Occ. % | AMR | Occ. % |
| Affordable | **$ 783** | **97.4** | $ 711 | 97.1 | **$ 789** | **97.7** | $ 711 | 97.1 | $ 709 | 90.0 |
| Mid-tier | **$ 943** | **98.4** | $ 918 | 98.0 | **$ 943** | **98.4** | $ 918 | 98.0 | $ 938 | 97.9 |
| Luxury | **$ 1,101** | **97.9** | $ 1,071 | 97.5 | **$ 1,095** | **98.0** | $ 1,071 | 97.5 | $ 1,221 | 97.1 |
| Average Residential Suites | **$ 997** | **98.2** | $ 960 | 97.7 | **$ 994** | **98.2** | $ 960 | 97.7 | $ 1,101 | 96.9 |
| Average MHC Land Lease Sites | **$ 621** | **99.9** | $ 610 | 99.8 | **$ 620** | **99.9** | $ 610 | 99.8 | $ 588 | 100.0 |
| Overall Portfolio Average | **$ 978** | **98.3** | $ 943 | 97.8 | **$ 975** | **98.3** | $ 943 | 97.8 | $ 1,095 | 97.0 |

Restated for the effects of changes in demographic sector classifications effected in the fourth quarter of 2010 (see Portfolio Diversification).

AMR is defined as actual residential rents, net of vacancies, divided by the total number of suites in the property and does not include revenues from parking, laundry or other sources.

Average monthly rents increased in all sectors of the residential suite portfolio, resulting in a significant 3.9% increase in overall average monthly rent as at March 31, 2011 to $997, compared to $960 in the prior year. The increases in average monthly rents and occupancy levels were due to a combination of the acquisition of mid-tier and luxury properties and the disposition of certain affordable properties during the last twelve months, ongoing successful sales and marketing strategies and continued strength in the residential rental sector in the majority of CAPREIT's regional markets.

Average monthly rents for the residential suite portfolio properties owned prior to March 31, 2010 also increased at March 31, 2011 to $994 from $960 at March 31, 2010, with gains of up to 11.0% in some sectors of the portfolio. Occupancy also increased in most sectors of the residential suite portfolio, resulting in nearly full occupancy at 98.2% compared to 97.7% in the prior year.

For the MHC land lease portfolio, average monthly rents rose to $621 as at March 31, 2011, compared to $610 as at March 31, 2010, while occupancy remained at virtually full levels.

The table below summarizes the changes in the average monthly rent due to suite turnovers and lease renewals compared to the prior year period.

***Suite Turnovers and Lease Renewals***

| For the Three Months Ended March 31, | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|
| | Change in AMR | | % Turnovers | Change in AMR | | % Turnovers |
| | $ | % | & Renewals[(1)] | $ | % | & Renewals[(1)] |
| Suite Turnovers | **7.6** | **0.8** | **6.2** | 4.0 | 0.4 | 5.7 |
| Lease Renewals | **12.8** | **1.3** | **13.1** | 20.7 | 2.1 | 12.9 |
| Weighted Average of Turnovers & Renewals | **11.1** | **1.1** | | 15.5 | 1.6 | |

(1) Percentage of suites turned over or renewed during the period based on the total number of residential suites (excluding co-ownerships) held at the end of the period.

Suite turnovers in the residential suite portfolio (excluding co-ownerships) during the three months ended March 31, 2011 resulted in a $8 or 0.8% increase in average monthly rents compared to an increase of $4 or 0.4% for the same period last year. Although the change in average monthly rents from suite turnovers improved from last year, the effect of aggressive rent discounting in the Alberta market by approximately $24 or 2.3% per suite for the three months ended

March 31, 2011 continues to have an adverse impact. Excluding the impact of the Alberta portfolio, residential suite turnovers would have instead resulted in average monthly rent increases of $11 or 1.1% for the three months ended March 31, 2011.

Pursuant to Management's focus on increasing overall portfolio rents, for the three months ended March 31, 2011, average monthly rents on lease renewals increased by approximately $13 or 1.3% compared to increases of $21 or 2.1% for the same period last year. The lower rate of growth in average monthly rents on lease renewals during the current quarter is due primarily to the Ontario guideline increase of 0.7% for 2011, which compares unfavourably to the permitted Ontario guideline increase of 2.1% in 2010 (see the discussion in the Risks and Uncertainties section of the MD&A contained in CAPREIT's 2010 Annual Report and the discussion of Risk Factors in CAPREIT's latest Annual Information Form). Management is actively pursuing applications for above guideline increases to raise average monthly rents on lease renewals (see discussion in the Future Outlook section).

***Portfolio Average Monthly Rents and Occupancy By Geography***

| **As at March 31,** | **2011** | | **2010** | |
|---|---|---|---|---|
| | **AMR** | **Occ. %** | **AMR** | **Occ. %** |
| **Ontario** | | | | |
| Greater Toronto Area | **$ 1,096** | **98.7** | $ 1,068 | 97.9 |
| Ottawa | **873** | **99.9** | 853 | 99.9 |
| London / Kitchener / Waterloo | **848** | **96.0** | 810 | 96.9 |
| Other Ontario | **1,001** | **97.9** | 930 | 97.1 |
| | **$ 1,065** | **98.6** | $ 1,025 | 97.9 |
| **Québec** | | | | |
| Greater Montréal Region | **$ 681** | **95.6** | $ 657 | 96.9 |
| Québec City | **806** | **97.9** | 796 | 99.2 |
| | **$ 739** | **96.7** | $ 717 | 97.9 |
| **British Columbia** | | | | |
| Greater Vancouver Region | **$ 999** | **98.1** | $ 963 | 99.1 |
| Victoria | **838** | **97.1** | 736 | 92.9 |
| | **$ 941** | **97.7** | $ 899 | 97.3 |
| **Alberta** | | | | |
| Edmonton | **$ 964** | **93.9** | $ 968 | 90.3 |
| Calgary | **1,022** | **98.3** | 1,002 | 97.1 |
| | **$ 1,009** | **97.3** | $ 994 | 95.6 |
| **Nova Scotia** | | | | |
| Halifax | **$ 1,043** | **98.1** | $ 1,001 | 97.2 |
| **Saskatchewan** | | | | |
| Saskatoon | **$ 818** | **98.5** | $ 775 | 97.7 |
| Regina | **876** | **99.1** | 860 | 100.0 |
| | **$ 844** | **98.8** | $ 813 | 98.8 |
| Total Residential Suites | **$ 997** | **98.2** | $ 960 | 97.7 |
| MHC Land Lease Sites | **$ 621** | **99.9** | $ 610 | 99.8 |
| Total Residential Suites and MHC Land Lease Sites | **$ 978** | **98.3** | $ 943 | 97.8 |

Overall average occupancy remained at nearly full levels at 98.3% as at March 31, 2011, compared to 97.8% last year, as CAPREIT's strong portfolio and favourable market conditions enabled Management to continue to focus on improving resident quality, with an emphasis on maintaining or increasing rents in most of the portfolio's core markets, as summarized below:

- Average monthly rents remained stable or increased in all regional markets of the portfolio with the exception of Edmonton, while average occupancy levels improved in all regions in which CAPREIT operates, with the exception of Québec.

- Ontario, whose residential suites represent over 66% of the total residential suite portfolio, experienced a significant increase of 3.9% in average monthly rents and improved occupancy levels to nearly full occupancy at 98.6%, up from 97.9% last year. Management expects the Ontario rental market to remain strong during 2011.
- In Québec, representing over 15% of the total residential suite portfolio, average monthly rents increased 3.1% from the same period last year while occupancy levels decreased slightly to 96.7% from 97.9% over the same period last year partly as a result of the adverse impact of ongoing construction at certain properties. Management expects the Québec City rental market to remain stable and the Greater Montréal Region occupancy levels to improve in 2011.
- The acquisitions completed during 2010 combined with improving industry and economic conditions in British Columbia resulted in a 4.7% increase in average monthly rents while occupancy levels remained at nearly full occupancy at 97.7% compared to 97.3% last year. Management expects British Columbia's rental market to continue to remain strong during the rest of 2011.
- Improving market conditions in Alberta resulted in a 1.5% improvement in average monthly rents on a year-over-year basis while occupancy levels also improved from 95.6% last year to 97.3% at March 31, 2011. Management believes the Alberta market will remain challenging but is expected to improve during 2011.

Overall average monthly rents for the residential suite portfolio as at March 31, 2011 increased by approximately 3.9% as compared to March 31, 2010. Management believes annual occupancies can be maintained in the 97% to 98% range and the trend for gradual increases in average monthly rents will continue, providing the basis for sustainable year-over-year increases in revenues.

Management also believes the defensive characteristics of its nationwide portfolio and its ongoing strategies to further diversify among Canada's major rental markets and by property type will continue to protect Unitholders from downturns in any specific geographic region or demographic sector. This characteristic is demonstrated by CAPREIT's ability to increase overall average monthly rents and maintain high occupancy levels in the course of the soft economic climate experienced over the last few years.

The table below shows the incremental tenant inducements incurred during the period ended March 31, 2011 and 2010 as well as the amortization of tenant inducements and loss from vacancies included in net rental revenue for the same periods.

***Tenant Inducements and Vacancy Loss on Residential Suites and Sites***

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | 2010 |
|---|---|---|
| New Tenant Inducements Incurred | **$ 150** | $ 137 |
| | | |
| Tenant Inducements Amortized | **$ 287** | $ 244 |
| Vacancy Loss Incurred | **1,621** | 1,951 |
| Total Amortization and Loss | **$ 1,908** | $ 2,195 |

## RESULTS OF OPERATIONS

***Total Operating Revenues by Geography***

| For The Three Months Ended March 31, ($ Thousands) | | 2011 | | 2010 [1] |
|---|---|---|---|---|
| **Ontario** | | | | |
| Greater Toronto Area | **$** | **48,868** | $ | 46,628 |
| Ottawa | | **2,137** | | 2,076 |
| London / Kitchener / Waterloo | | **2,357** | | 3,614 |
| Other Ontario | | **4,613** | | 4,288 |
| Ontario Residential Suites | **$** | **57,975** | $ | 56,606 |
| MHC Land Lease Sites | | **2,502** | | 2,441 |
| Ontario Residential Suites and Land Lease Sites | **$** | **60,477** | $ | 59,047 |
| **Québec** | | | | |
| Greater Montréal Region | **$** | **4,651** | $ | 5,255 |
| Québec City | | **4,876** | | 4,786 |
| | **$** | **9,527** | $ | 10,041 |
| **British Columbia** | | | | |
| Greater Vancouver Region | **$** | **4,871** | $ | 4,186 |
| Victoria | | **2,095** | | 1,153 |
| | **$** | **6,966** | $ | 5,339 |
| **Alberta** | | | | |
| Edmonton | **$** | **1,017** | $ | 1,004 |
| Calgary | | **4,081** | | 3,998 |
| | **$** | **5,098** | $ | 5,002 |
| **Nova Scotia** | | | | |
| Halifax | **$** | **3,657** | $ | 3,497 |
| **Saskatchewan** | | | | |
| Saskatoon | **$** | **315** | $ | 309 |
| Regina | | **292** | | 283 |
| | **$** | **607** | $ | 592 |
| Total Residential Suites | **$** | **83,830** | $ | 81,077 |
| Total Residential Suites and MHC Land Lease Sites | **$** | **86,332** | $ | 83,518 |

***Results of Operations***

| Three Months Ended March 31, ($ Thousands) | | 2011 | % [1] | | 2010 | % [1] |
|---|---|---|---|---|---|---|
| Operating Revenues | | | | | | |
| Net Rental Revenues | **$** | **81,552** | **94.5** | $ | 79,592 | 95.3 |
| Other [2] | | **4,780** | **5.5** | | 3,926 | 4.7 |
| Total Operating Revenues | **$** | **86,332** | **100.0** | $ | 83,518 | 100.0 |
| Operating Expenses | | | | | | |
| Realty Taxes | | **11,026** | **12.8** | | 11,105 | 13.3 |
| Utilities | | **12,154** | **14.1** | | 13,362 | 16.0 |
| Other | | **16,588** | **19.2** | | 15,408 | 18.4 |
| Total Operating Expenses | | **39,768** | **46.1** | | 39,875 | 47.7 |
| NOI | **$** | **46,564** | **53.9** | $ | 43,643 | 52.3 |

(1) As a percentage of Total Operating Revenues.
(2) Comprised of ancillary income such as parking, laundry and antenna income.

**Operating Revenues**

For the three months ended March 31, 2011, total operating revenues increased by 3.4% compared to the same period last year due to the contribution from acquisitions, increased average monthly rents and higher occupancies. CAPREIT increased average monthly rents in the residential portfolio to $997 at March 31, 2011, compared to $960 at March 31, 2010, while occupancy improved to 98.2% compared to 97.7% for the same period last year. As CAPREIT continues to enhance the profile of its resident base and increase the level of service to residents, it expects to realize further increases in operating revenues. Ancillary revenues, such as parking, laundry and antenna income, rose by 21.8% for the three months ended March 31, 2011 as Management continued its focus on maximizing the revenue potential of its property portfolio as well as the result of a partially non-recurring item of $0.6 million.

For the three months ended March 31, 2011, overall average residential vacancies as a percentage of operating revenues improved to 1.9% compared to 2.3% for the same period last year. The improvement in occupancies was led by improving recoveries in most geographic markets compared to the prior year.

For the three months ended March 31, 2011, bad debt and tenant inducements remained stable as a percentage of revenues compared to the same period last year at less than 1.0%.

***Estimated Net Rental Revenue Run-Rate***

| **As at March 31,**<br>($ Thousands) | **2011** | **2010** |
|---|---|---|
| Residential Rent Roll [1],[2] | **$ 317,326** | $ 311,353 |
| Commercial Rent Roll [1],[2] | **8,198** | 7,945 |
| Annualized Net Rental Revenue Run-Rate | **$ 325,524** | 319,298 |

(1) Based on rent roll as at March 31, net of vacancy loss, tenant inducements and bad debt for the 12 months ended on such date.
(2) Includes rent roll for all properties held as at March 31.

The table above shows the estimated net rental revenue run-rate, net of average historical vacancy loss, tenant inducements and bad debt and based on the average monthly rents in place and CAPREIT's share of residential suites and sites as at March 31, 2011 and 2010. The estimated annualized net rental revenue run-rate improved by 1.9% to $325.5 million from $319.3 million. Net rental revenue for the twelve months ended March 31, 2011 was $324.7 million (2010 – $316.8 million).

**Operating Expenses**

Operating expenses were negatively impacted during the three months ended March 31, 2011 compared to the same period last year as a result of a combination of: (i) the introduction of harmonized sales tax ("HST") in Ontario and British Columbia, (ii) rising electricity rates in Ontario, and (iii) higher repairs and maintenance ("R&M") costs.

Despite these negative factors, for the three months ended March 31, 2011, total operating expenses declined in comparison to the same period last year due primarily to the success of CAPREIT's energy management and enhanced procurement strategies. These strategies include various energy-saving initiatives and a revised natural gas supply and pricing strategy implemented in 2010 that resulted in lower pricing compared to the unfavourable fixed-price arrangements in effect prior to March 1, 2010 (see Utility Costs below). Improved procurement strategies aim to reduce the negative effects of HST on CAPREIT's operating expenses. These factors resulted in a significant decrease in utility costs despite the impact of property acquisitions and a cooler winter in 2011 compared to last year. As a percentage of revenues, utility costs for the three months ended March 31, 2011 declined significantly to 14.1% from 16.0% for the same period last year.

Other operating expenses as a percentage of revenues also increased for the three months ended March 31, 2011, to 19.2% from 18.4% for the same period last year. Other operating expenses include R&M, wages and benefits, insurance and advertising. A significant portion of the increase was the result of the impact of HST in 2011 as well as from properties acquired since March 31, 2010 though partially offset by the dispositions in the same period.

CAPREIT's utility costs can be highly variable from year to year and can experience significant increases in costs during the winter months as additional resources are consumed to heat the properties. The table below provides CAPREIT's utility costs by type.

***Utility Costs***

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | 2010 |
|---|---|---|
| Electricity | **$ 5,477** | $ 5,157 |
| Natural Gas | **4,484** | 5,812 |
| Water | **2,054** | 2,291 |
| Heating Oil | **139** | 102 |
| Total | **$ 12,154** | $ 13,362 |

Electricity costs increased in 2011 primarily due to an increase in electricity rates and the introduction of the HST in Ontario beginning in July 2010, as well as the impact of cooler weather on CAPREIT's electrically heated properties.

Natural gas costs decreased primarily due to lower commodity costs on the portion of CAPREIT's consumption not subject to unfavourable fixed rates, partially offset by higher consumption during the period as a result of the impact of cooler weather compared to last year.

With the authorization of the Board of Trustees, effective March 1, 2010, Management implemented a revised natural gas supply strategy that, in effect, converted substantially all of the fixed price natural gas commitments to spot pricing arrangements through the amendment of physical delivery contracts and the use of derivative financial instruments. The amendment resulted in the realization of a $4.5 million loss inherent in the physical delivery contracts, which was settled through the use of derivative financial instruments entered into with creditworthy counterparties (see discussion under the Net Income section). The revised strategy eliminated the protection afforded by formerly fixed pricing arrangements; however, Management expects to continue to achieve long-term energy cost savings as a result of historically low natural gas prices, including related commodity tax savings, providing Management with greater flexibility to lock in natural gas prices in the future when deemed appropriate.

Management chose not to apply hedge accounting to these derivative financial instruments, which will be marked-to-market through net income or loss on an ongoing basis. However, the derivatives are structured such that, other than the initial loss recognized on these contracts at inception, Management expects any gains and losses between the derivatives to offset each other and therefore not have a significant impact on CAPREIT's financial performance in the future (see item (ii) *Natural Gas Contracts* under the Net Income section).

In the third quarter of 2010, CAPREIT entered into a floating-to-fixed natural gas financial instrument covering the period from November 2010 through March 2011 ("Winter 2011") and in the fourth quarter of 2010, a second floating-to-fixed natural gas financial instrument was entered into covering the same period (see note 26 to the accompanying unaudited consolidated interim financial statements). The two financial instruments fixed the price of natural gas at $4.32 and $3.58 per gigajoule for 2,700 and 500 gigajoules per day, respectively, which combined, represented approximately 85% of CAPREIT's anticipated Winter 2011 natural gas delivery requirements. These fixed prices compare favourably to the average price per gigajoule at which CAPREIT converted its fixed price natural gas commitments to spot pricing arrangements effective March 1, 2010, of $5.05 per gigajoule and the average price paid by CAPREIT for natural gas from November 2009 through March 2010 of $6.49 per gigajoule.

As a result of the continued decline in the forward pricing curve for natural gas prices, CAPREIT incurred a loss of $141 thousand on the two floating-to-fixed derivative financial instruments for the three months ended March 31, 2011 (see discussion under the Other Comprehensive Income section).

The table below explains the key components of the change in natural gas costs between the three months ended March 31, 2010 and 2011:

**Three Months Ended March 31, 2011**

| ($ Thousands) | | |
|---|---|---|
| Natural Gas Costs - Three Months Ended March 31, 2010 | $ | 5,812 |
| Impact of Change in Consumption | | 422 |
| Impact of Unwinding Fixed Price Commitments | | (759) |
| Impact of Change in Spot Prices on Unhedged Supply | | (907) |
| Net Impact of Property Acquisitions and Dispositions | | (84) |
| Natural Gas Costs - Three Months Ended March 31, 2011 | $ | 4,484 |

## NET OPERATING INCOME

Management believes NOI is a key indicator of operating performance in the real estate industry. NOI includes all rental revenues generated at the property level, less: (i) related direct costs such as utilities, realty taxes, insurance, R&M costs and on-site wages and salaries; and (ii) an appropriate allocation of overhead costs. It may not, however, be comparable to similar measures presented by other real estate trusts or companies.

The following table shows the NOI and the NOI margin attained for each regional market for the periods ended March 31, 2011 and 2010.

***NOI by Geography***

| **For The Three Months Ended March 31,** | **2011** | | | **2010** | |
|---|---|---|---|---|---|
| ($ Thousands) | **NOI** | **NOI Margin (%)** | **Change (%) (1)** | **NOI** | **NOI Margin (%)** |
| **Ontario** | | | | | |
| Greater Toronto Area | **$ 26,651** | **54.5** | **11.9** | $ 23,816 | 51.1 |
| Ottawa | **994** | **46.5** | **(3.5)** | 1,030 | 49.6 |
| London / Kitchener / Waterloo | **1,220** | **51.8** | **(28.7)** | 1,712 | 47.4 |
| Other Ontario | **2,245** | **48.7** | **12.1** | 2,002 | 46.7 |
| Ontario Residential Suites | **$ 31,110** | **53.7** | **8.9** | $ 28,560 | 50.5 |
| MHC Land Lease Sites | **1,413** | **56.5** | **(7.2)** | 1,523 | 62.4 |
| Ontario Residential Suites and Land Lease Sites | **$ 32,523** | **53.8** | **8.1** | $ 30,083 | 50.9 |
| **Québec** | | | | | |
| Greater Montréal Region | **$ 2,150** | **46.2** | **(15.7)** | $ 2,550 | 48.5 |
| Québec City | **2,591** | **53.1** | **(2.2)** | 2,650 | 55.4 |
| | **$ 4,741** | **49.8** | **(8.8)** | $ 5,200 | 51.8 |
| **British Columbia** | | | | | |
| Greater Vancouver Region | **$ 2,765** | **56.8** | **13.8** | $ 2,429 | 58.0 |
| Victoria | **1,216** | **58.0** | **75.5** | 693 | 60.1 |
| | **$ 3,981** | **57.1** | **27.5** | $ 3,122 | 58.5 |
| **Alberta** | | | | | |
| Edmonton | **$ 559** | **55.0** | **(8.4)** | $ 610 | 60.8 |
| Calgary | **2,187** | **53.6** | **5.1** | 2,080 | 52.0 |
| | **$ 2,746** | **53.9** | **2.1** | $ 2,690 | 53.8 |
| **Nova Scotia** | | | | | |
| Halifax | **$ 2,262** | **61.9** | **1.6** | $ 2,226 | 63.7 |
| **Saskatchewan** | | | | | |
| Saskatoon | **$ 135** | **42.9** | **(6.9)** | $ 145 | 46.9 |
| Regina | **176** | **60.3** | **(0.6)** | 177 | 62.5 |
| | **$ 311** | **51.2** | **(3.4)** | $ 322 | 54.4 |
| Total Residential Suites | **$ 45,151** | **53.9** | **7.2** | $ 42,120 | 52.0 |
| Total Residential Suites and MHC Land Lease Sites | **$ 46,564** | **53.9** | **6.7** | $ 43,643 | 52.3 |

(1) Change in NOI from prior year comparable period.

For the three months ended March 31, 2011, overall NOI increased by $2.9 million or 6.7%, while the NOI margin improved significantly to 53.9% from 52.3% for the same period last year. While CAPREIT increased NOI and NOI margins in the majority of its markets, it remains focused on continuing to improve overall NOI through a combination of accretive and value-enhancing acquisitions, successful sales and marketing strategies to improve revenues and investments in capital programs to further reduce costs and enhance the quality and value of its portfolio.

Ontario:

NOI from the Ontario portfolio increased by 8.1% during the three months ended March 31, 2011 compared to the same period last year, primarily due to lower operating costs from a combination of lower prices for natural gas though partially offset by higher R&M costs. As a result, the NOI margin improved to 53.8% for the three months ended March 31, 2011. Management believes the Ontario portfolio will remain strong and generate steady returns in the medium term despite significant challenges imposed by the low guideline increase for 2011 as discussed earlier and the introduction of the HST (see Harmonization of Federal Goods and Services Tax and Provincial Sales Tax discussion under the Risks and Uncertainties section contained in CAPREIT's 2010 Annual Report).

Québec:

The dispositions completed in the Greater Montréal Region during 2010 were the main contributing factor to lower revenues and NOI during three months ended March 31, 2011 compared to the same period last year. For the three months ended March 31, 2011, the NOI margin decreased to 49.8% from 51.8% for the same period last year, primarily due to higher wages and R&M costs. CAPREIT believes the Québec rental market will remain stable and generate steady to improving returns in the medium term.

British Columbia:

Acquisitions completed since the first quarter of last year were the primary contributing factor for the large increase in revenues and NOI for the three months ended March 31, 2011. Certain non-recurring costs associated with the integration of these acquisitions into the portfolio combined with the negative impact of HST resulted in higher operating costs and a lower margin for the British Columbia portfolio for the three months ended March 31, 2011, declining to 57.1% from 58.5% for the same period last year. With its growth in the region, CAPREIT has established the infrastructure and critical mass to build its presence and improve its performance in this market going forward. Management believes the ongoing stabilization of occupancies will enable the British Columbia portfolio to continue to generate improved returns in the medium term. Management believes that the impact of the introduction of the HST in British Columbia will remain more modest than in Ontario as only 8.4% of the portfolio is located in the province.

Alberta:

As expected, the Alberta market is beginning to show signs of improving rental rates and occupancies in 2011. The resulting increase in revenues for the three months ended March 31, 2011 in comparison to last year was, however, offset by increases in overall operating costs. As a result, NOI margin remained stable at 53.9% for the three months ended March 31, 2011, compared to 53.8% for the same period last year. Management believes the Alberta market will remain challenging but should continue to improve over the medium term. The overall impact on CAPREIT will be minimal as only 5% of its overall residential suite portfolio is located in the province.

Nova Scotia:

Increased average monthly rents and occupancy levels offset by higher overall operating costs resulted in the NOI margin decreasing for the three months ended March 31, 2011 to 61.9%, from 63.7% for the same period last year. Management believes its presence primarily in downtown locations will serve to maintain or increase occupancy levels and average monthly rents in the medium term.

Saskatchewan:

The Saskatchewan market continues to perform well with slightly higher average monthly rents and nearly full occupancies resulted in higher revenues compared to last year. However, the NOI margin decreased for the three months ended March 31, 2011 to 51.2%, from 54.4% for the same period last year as a result of higher wages during the current year period compared to last year. However, the overall impact on CAPREIT of changes in operating performance in its Saskatchewan properties is minimal as less than 1% of the overall residential suite portfolio is located in the province. The province's economy remains strong and CAPREIT believes it is well-positioned to maintain or improve current occupancy levels and average monthly rents in the province over the medium term.

## OPERATING PERFORMANCE BY TYPE OF PROPERTY INTEREST

The following table provides a summary of the NOI by type of property interest held by CAPREIT for the three months ended March 31, 2011 and 2010:

***NOI by Type of Property Interest***

| **Three Months Ended March 31,** | | **2011** | | | **2010** | |
|---|---|---|---|---|---|---|
| ($ Thousands) | | | % | | | % |
| Fee Simple Interests - Apartments and Townhomes | $ | **35,849** | **77.0** | $ | 33,710 | 77.2 |
| Operating Leasehold Interests | | **7,323** | **15.7** | | 6,498 | 14.9 |
| Land Leasehold Interests | | **1,979** | **4.3** | | 1,912 | 4.4 |
| Total Residential Suites | $ | **45,151** | **97.0** | $ | 42,120 | 96.5 |
| Fee Simple Interests - MHC Land Lease Sites | | **1,413** | **3.0** | | 1,523 | 3.5 |
| Total | $ | **46,564** | **100.0** | $ | 43,643 | 100.0 |

## STABILIZED PORTFOLIO PERFORMANCE

| **Three Months Ended March 31,** | | **2011** | **% (1)** | | **2010** |
|---|---|---|---|---|---|
| Stabilized Suites and Sites | | **26,531** | | | 26,531 |
| Operating Revenues ($ millions) | **$** | **83.6** | **3.5** | $ | 80.8 |
| Operating Costs ($ millions) | **$** | **39.0** | **2.1** | $ | 38.2 |
| Net Operating Income ($ millions) | **$** | **44.6** | **4.7** | $ | 42.6 |
| Net Operating Income Margin (%) | | **53.3** | **0.6** | | 52.7 |

(1) Change from prior year comparable period.

Stabilized properties for the three months ended March 31, 2011 are defined as all properties owned by CAPREIT continuously since December 31, 2009, and therefore do not take into account the impact on performance of acquisitions or dispositions completed during 2011 and 2010. As at March 31, 2011, stabilized suites and sites represent 97.2% of the overall portfolio.

As of March 31, 2011, CAPREIT has generated 21 consecutive quarters of stable or improved year-over-year NOI growth for stabilized properties. For the three months ended March 31, 2011, operating revenues increased by 3.5% and operating costs increased by 2.1%. As a result, stabilized NOI increased by 4.7% for the three months ended March 31, 2011.

For properties acquired since December 31, 2009, the NOI margin was 61.9% for the three months ended March 31, 2011.

## NET INCOME

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | **2010** |
|---|---|---|
| Net Operating Income | **$ 46,564** | $ 43,643 |
| (Less) Plus: | | |
| Trust Expenses | **(3,605)** | (2,623) |
| Unrealized Loss on Remeasurement of Investment Properties | **(5,461)** | (8,364) |
| Realized Loss on Sale of Investment Property | **(95)** | – |
| Unrealized Loss on Remeasurement of Exchangeable Units | **(954)** | (119) |
| Unit-Based Compensation Expenses | **(5,801)** | (684) |
| Interest on Mortgages Payable | **(19,788)** | (19,576) |
| Interest on Bank Indebtedness | **(748)** | (1,479) |
| Interest on Exchangeable Units | **(111)** | (111) |
| Net Loss on Natural Gas Contracts | **–** | (4,497) |
| Other Income | **465** | 462 |
| Amortization | **(647)** | (651) |
| Severance and Other Employee Termination Costs | **–** | (150) |
| Unrealized Loss on Derivative Financial Instruments | **(156)** | (54) |
| Recovery of Deferred Income Taxes | **–** | 4,875 |
| Net Income | **$ 9,663** | $ 10,672 |

### Trust Expenses

Trust expenses include costs directly attributable to head office, such as salaries, trustee fees, professional fees for legal and advisory services, trustees' and officers' insurance premiums, and other general and administrative expenses. Trust expenses increased for the three months ended March 31, 2011, to $3.6 million from $2.6 million for the same period last year mainly due to higher legal, consulting and compensation costs.

### Unrealized Gain on Remeasurement of Investment Properties

With the adoption of IFRS effective January 1, 2010, CAPREIT elected to recognize its investment properties at fair value at each reporting period, with any unrealized gain or loss upon remeasurement recognized in the consolidated statement of income for the period (see discussion in the Adoption of IFRS section). A description of the key components of the change in the fair value of investment properties is included in the Investment Properties section.

### Unrealized Loss on Remeasurement of Exchangeable Units and Related Interest Expense

With the adoption of IFRS effective January 1, 2010, CAPREIT is required to account for its Exchangeable Units as a financial liability, to remeasure such liability at each reporting period, and to include this remeasurement in the consolidated statement of income (see discussion in the Adoption of IFRS section). As a result of the increase in the market price of CAPREIT's Trust Units for the three months ended March 31, 2011 compared to the same period last year, the remeasurement of Exchangeable Units at fair value resulted in a significantly higher remeasurement expense of $1.0 million compared to $0.1 million for the same period last year. Interest expense remained unchanged at $0.1 million.

### Unit-Based Compensation Expenses

Unit-based compensation benefits are provided to officers, trustees and certain employees and are intended to facilitate long-term ownership of Trust Units and to provide additional incentives by increasing the participants' interest, as owners, in CAPREIT. Unit-based compensation expenses include costs attributable to these incentive plans, namely the Restricted Unit Rights Plan ("RUR Plan"), Unit Option Plan ("UOP"), Deferred Unit Plan ("DUP"), Long-Term Incentive Plan ("LTIP") and Senior Executive Long-Term Incentive Plan ("SELTIP") (see notes 14 and 16 in the accompanying unaudited consolidated interim financial statements for a discussion of these plans).

As a result of CAPREIT being an open-ended mutual fund trust, whereby each Unitholder of the Trust Units is entitled to redeem their Units in accordance with the conditions specified in CAPREIT's Declaration of Trust ("DOT"), under IFRS, the underlying Trust Units relating to the Unit-based compensation awards are not treated as equity and are instead

considered as financial liabilities. As such, these Unit-based compensation awards must be presented as liabilities and remeasured at fair value at each reporting date. Close-ended mutual fund trusts, such as certain of CAPREIT's industry peers, are not required to remeasure their respective Unit-based compensation awards. In such cases, the related expense is limited to the amortization of the fair value of the award over the applicable vesting period.

In order to aid comparability with CAPREIT's peers, the Unit-based compensation expense has been separated into two components: (i) the amortization of the grant date fair value of the award over its vesting period, and (ii) the remeasurement of awards outstanding at period end at fair value.

CAPREIT's Unit-based compensation expense increased significantly for the three months ended March 31, 2011, to $5.8 million from $0.7 million for the same period last year mainly due to the increase in the market price of CAPREIT's Trust Units as well as the issuance of additional DUP and RUR awards. The table below demonstrates the impact of each component of CAPREIT's plans on the total compensation expense.

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | **2010** |
|---|---|---|
| Remeasurement of Unit-Based Compensation Liabilities | **$ 5,474** | $ 384 |
| Amortization of Fair Value on Grant Date of Unit-Based Compensation | **327** | 300 |
| Total | **$ 5,801** | $ 684 |

**Interest on Mortgages Payable**

Interest on mortgages increased for the three months ended March 31, 2011, to $19.8 million from $19.6 million for the same period last year, due to increased top up mortgage financing activity since March 31, 2010. However, as a percentage of operating revenues, mortgage interest expense decreased to 22.9% for the three months ended March 31, 2011 compared to 23.4% for the same period last year as a result of CAPREIT's successful refinancing of mortgages at lower interest rates. Effective January 1, 2010, the amortization of insurance premiums, which relate to mortgages insured by CMHC, has been reclassified from amortization expense to interest on mortgages.

**Interest on Bank Indebtedness**

Interest on bank indebtedness relates to borrowings under the Credit Facilities (see discussion of Bank Indebtedness and Credit Facilities). Interest on bank indebtedness for the three months ended March 31, 2011 decreased significantly to $0.7 million from $1.5 million for the same period last year due to lower borrowings throughout the period as a result of the repayment of a majority of the borrowings from the capital raised in the equity offering completed in the fourth quarter of 2010 (see the Liquidity and Financial Condition section). The weighted average floating interest rate for the amounts drawn under the Acquisition and Operating Facility was 4.05% at March 31, 2011, compared to 3.42% at March 31, 2010. At March 31, 2011, the weighted average floating interest rate for the amounts drawn under the Land Lease Facility was 4.13%, compared to 3.42% at March 31, 2010.

**Net Loss on Natural Gas Contracts**

As previously outlined in the Results of Operations section, effective March 1, 2010, Management implemented a revised natural gas supply strategy that, in effect, converted substantially all of the fixed price natural gas commitments to spot pricing arrangements through the amendment of physical delivery contracts and the use of derivative financial instruments. The amendment resulted in the crystallization of a $4.5 million loss for the period ended March 31, 2010 and settled through the use of derivative financial instruments (see item (ii) *Natural gas contracts* below).

**Other Income**

Other income consists primarily of dividends received from investments (see notes 2(i) and 10 to the accompanying unaudited consolidated interim financial statements).

**Amortization**

These costs represent primarily the amortization of CAPREIT's head office property, plant and equipment on a straight-line basis over their estimated useful lives ranging between three and five years. Also included is the amortization of deferred loan costs associated with the Credit Facilities over their respective terms.

**Severance and Other Employee Termination Costs**

These costs primarily represent employee severance costs incurred in the three months ended March 31, 2010.

**Realized and Unrealized Gains and Losses on Derivative Financial Instruments**

i) *Interest rate contracts for which hedge accounting is being applied:* As at March 31, 2011, CAPREIT has a $55 million interest rate swap agreement fixing the interest rate at 5.706%, maturing in July 2012, to which hedge accounting is being applied. The agreement effectively converts borrowings on a banker's acceptance-based floating rate credit facility to a fixed rate facility for a five-year term. (See notes 17(b) and 18(b) to the accompanying unaudited consolidated interim financial statements).

ii) *Natural gas contracts:* The amended natural gas supply strategy outlined earlier comprises of a physical delivery contract at spot pricing, a floating-to-fixed derivative financial instrument with the natural gas supplier and an offsetting fixed-to-floating derivative financial instrument with a Canadian chartered bank.

Hedge accounting is not being applied to these derivative financial instruments, which will be marked-to-market through net income on an ongoing basis. As at March 31, 2011, a mark-to-market unrealized loss of $2.7 million on the floating-to-fixed derivative financial instrument has been recorded in other liabilities and a mark-to-market unrealized gain of $1.1 million on the fixed-to-floating derivative financial instrument has been recorded in other assets. As a result of the amendment of the fixed price natural gas commitments, the inherent net loss of $4.5 million was crystallized and included in the consolidated statements of income for the three months ended March 31, 2010 (see notes 17(c), 18(c) and 26 to the accompanying unaudited consolidated interim financial statements).

**Deferred Income Taxes**

Amendments enacted in 2007 (the "SIFT Rules") to the Income Tax Act (Canada) (the "Tax Act") modified the federal income tax treatment of certain publicly traded trusts and partnerships that were deemed specified investment flow-through trusts or partnerships ("SIFT"). Under these SIFT Rules, a SIFT such as CAPREIT would generally be taxed in a manner similar to corporations on income from a business carried on in Canada at a rate similar to the combined federal/provincial tax rate of a corporation provided CAPREIT distributed its non-portfolio income. However, the SIFT Rules do not apply until the 2011 taxation year to SIFTs that were publicly traded and were deemed SIFTs as at October 31, 2006. Effective December 24, 2010, based on the guidelines and conditions established under the Tax Act (the "REIT Exception"), CAPREIT became qualified for an exemption from the SIFT Rules (see the Risks and Uncertainties section in CAPREIT's 2010 Annual Report for additional details).

Under IFRS, CAPREIT is unable to assume that it will distribute its non-portfolio income, which means that, had CAPREIT not met the REIT Exception, it would have been subject to tax beginning in 2011 as an inter vivos trust at the highest marginal tax rate applicable to individuals. The transition to IFRS requires that CAPREIT record a deferred income tax provision based on this higher tax rate for the comparative period until the fourth quarter of 2010, at which time CAPREIT satisfied the REIT Exception.

As CAPREIT uses the liability method of accounting for deferred income taxes, the non-cash deferred income tax liability balance represented the cumulative amount of taxes applicable to temporary differences between the carrying amount of assets and liabilities and their carrying amounts for tax purposes expected to reverse on or after January 1, 2011. The deferred income tax liability of $440.5 million recorded as at January 1, 2010 was reversed upon satisfaction of the REIT Exception and recorded as a recovery of $435.7 million to the consolidated statement of income and comprehensive income and a recovery of $4.8 million to other comprehensive income ("OCI") for the year ended December 31, 2010.

**Realized Loss on Disposition of Investment Property**

The realized loss on disposition of investment property of $0.1 million represents the difference between the net proceeds from the disposition of an investment property during the three months ended March 31, 2011 compared to the fair value of the same property as at December 31, 2010.

## OTHER COMPREHENSIVE INCOME

Included in Other Comprehensive Income (Loss) are the following:

i) *Realized loss on derivative financial instruments*: represents the cumulative mark-to-market losses up to October 1, 2008 when hedge accounting ceased to be applied to interest rate forward contracts used to hedge CAPREIT's exposure to the potential rise in interest rates for refinancings of mortgages maturing in 2009 (see note 17 to the accompanying unaudited consolidated interim financial statements).

ii) *Unrealized loss on interest rate swap agreements*: this represents the cumulative mark-to-market loss on an interest rate swap agreement entered into in July 2007, which effectively converts borrowings on a banker's acceptance floating rate credit facility to a fixed rate facility for $55 million for a five-year term. This interest rate swap agreement has been assessed as an effective hedge in accordance with IAS 39, Financial Instruments: Recognition and Measurement. The difference between the effective fixed interest rate and the corresponding three-month banker's acceptance rate is adjusted to interest expense every quarter. Accordingly, the cumulative mark-to-market loss will ultimately reverse over the remaining term of the interest rate swap agreement.

iii) *Unrealized loss on natural gas price swap agreement*: this represents the cumulative mark-to-market loss on a floating-to-fixed price swap agreements entered into in August and October 2010, which effectively converts floating prices for natural gas to a fixed price arrangement for the Winter 2011 period. This swap agreement has been assessed as an effective hedge in accordance with IAS 39. The cumulative mark-to-market loss will ultimately reverse over the remaining term of the swap agreement.

iv) *Change in fair market value of investments*: this represents the cumulative mark-to-market gain or loss for the period on investments accounted for as available-for-sale (see note 2(i) to the accompanying unaudited consolidated interim financial statements).

## SECTION III

## PER UNIT CALCULATIONS

As a result of CAPREIT being an open-ended mutual fund trust, Unitholders are entitled to redeem their Trust Units, subject to certain restrictions. The impact of this redemption feature causes CAPREIT's Trust Units to be treated as financial liabilities. Consequently, all per Unit calculations are considered non-IFRS measures.

The following table explains the number of Units used in calculating non-IFRS financial measures on a per Unit basis:

***Weighted Average Number of Units***

| **Three Months Ended March 31,** | **2011** | **2010** |
|---|---|---|
| Trust Units | **74,359** | 65,951 |
| Exchangeable Units (1) | **411** | 411 |
| Units under the DUP (2) | **74** | 61 |
| Basic Weighted Average Number of Units | **74,844** | 66,423 |
| Plus: | | |
| Dilutive Units under the LTIP (2),(3) | **413** | 148 |
| Dilutive Units under the SELTIP (2),(3) | **146** | 42 |
| Units Rights under the RUR Plan (2) | **115** | 28 |
| Dilutive Unexercised Options under the UOP (2),(4) | **68** | 24 |
| Dilutive Weighted Average Number of Units | **75,586** | 66,665 |

(1) See note 14 to the accompanying unaudited consolidated interim financial statements for details of Exchangeable Units.

(2) See notes 14 and 16 to the accompanying unaudited consolidated interim financial statements for details of CAPREIT's Unit-based compensation plans.

(3) Calculated using the treasury method after taking into account the respective subscriptions receivable (see note 16 to the accompanying unaudited consolidated interim financial statements).

(4) Calculated using the treasury method after taking into account the exercise prices.

## NON-IFRS FINANCIAL MEASURES

### Net Operating Income

NOI is a key non-IFRS financial measure of the operating performance of CAPREIT and is defined and reported in the Results of Operations section.

### Funds From Operations and Normalized Funds From Operations

FFO is a measure of operating performance based on the funds generated by the business before reinvestment or provision for other capital needs. FFO as presented is in accordance with the recommendations of the Real Property Association of Canada, with the exception of the adjustment for the remeasurement at fair value of Unit-based compensation for reasons outlined earlier and the amortization of certain other assets. It may not, however, be comparable to similar measures presented by other real estate trusts or companies in similar or different industries. Management considers FFO to be an important measure of CAPREIT's operating performance.

Payout ratios compare total and net distributions declared to these non-IFRS financial measures. Management considers these ratios to also be important measures of the sustainability of the level of distributions.

***Distribution Reinvestment Plan ("DRIP") and Net Distributions Paid***

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | 2010 |
|---|---|---|
| Distributions Declared on Trust Units | **$ 20,093** | $ 17,813 |
| Distributions Paid on Exchangeable Units | **111** | 111 |
| Distributions Paid on Awards Outstanding Under Unit-Based Compensation Plans (1) | **681** | 751 |
| Total Distributions Declared | **20,885** | 18,675 |
| Less: | | |
| Distributions on Trust Units Reinvested | **(3,847)** | (1,847) |
| Distributions on Unit Awards Reinvested (1) | **(681)** | (751) |
| Net Distributions Paid | **$ 16,357** | $ 16,077 |
| Percent of Distributions Reinvested | **21.7%** | 13.9% |

(1) Comprises: (i) non-cash distributions related to the DUP and the RUR plan, and (ii) retained distributions on LTIP and SELTIP Units (see notes 14 and 16 to the accompanying unaudited consolidated interim financial statements for a discussion of these plans).

Under CAPREIT's DRIP, a participant may purchase additional Units with the cash distributions paid on the eligible Units, registered in the participant's name or held in a participant's account maintained pursuant to the DRIP. Each participant has the right to receive an additional amount equal to 5% of their monthly distributions reinvested pursuant to the DRIP, which shall automatically be paid on each distribution date in the form of additional Units. The price at which Units will be purchased with cash distributions will be the weighted average trading price for CAPREIT's Trust Units on the Toronto Stock Exchange ("TSX") for the five trading days immediately preceding the relevant distribution date.

The average participation rate in the DRIP and other plans under which distributions are reinvested increased for the three months ended March 31, 2011 to 21.7% from 13.9% for the same period last year. Also, as the price of CAPREIT's Units has steadily risen during the period since March 31, 2010, the number of Units issued for a given amount of reinvested distributions has declined. The DRIP participation rate is subject to factors beyond Management's control and varies between investors.

Distributions declared on Units outstanding under the Unit-based compensation plans in these tables are based on all awards granted under the DUP, RUR Plan, LTIP and SELTIP (see notes 14 and 16 to the accompanying unaudited consolidated interim financial statements for a discussion of these plans). When establishing the level of monthly cash distributions to Unitholders, the Board of Trustees relies on cash flow information including forecasts and budgets.

A reconciliation of net income to FFO is as follows:

| **Three Months Ended March 31,**<br>($ Thousands, except per Unit amounts) | **2011** | 2010 |
|---|---|---|
| Net Income | **$ 9,663** | $ 10,672 |
| Adjustments: | | |
| Unrealized Loss on Remeasurement of Investment Properties | **5,461** | 8,364 |
| Realized Loss on Sale of Investment Property | **95** | – |
| Unrealized Loss on Remeasurement of Exchangeable Units | **954** | 119 |
| Remeasurement of Unit-Based Compensation Liabilities | **5,474** | 384 |
| Interest on Exchangeable Units | **111** | 111 |
| Recovery of Deferred Income Taxes | **–** | (4,875) |
| Amortization of Property, Plant and Equipment | **374** | 309 |
| FFO | **$ 22,132** | $ 15,084 |
| FFO Per Unit – Basic | **$ 0.296** | $ 0.227 |
| FFO Per Unit – Diluted | **$ 0.293** | $ 0.226 |
| Total Distributions Declared | **$ 20,885** | $ 18,675 |
| FFO Payout Ratio | **94.4%** | 123.8% |
| Net Distributions Paid | **$ 16,357** | $ 16,077 |
| Excess (Shortfall) FFO over Net Distributions Paid | **$ 5,775** | $ (993) |
| FFO Effective Payout Ratio | **73.9%** | 106.6% |

CAPREIT calculates NFFO by excluding from FFO the effect of the change in fair value of hedging instruments originally put in place for interest rate protection (see note 18(b) to the accompanying unaudited consolidated interim financial statements and the discussion under Realized and Unrealized Gains and Losses on Derivative Financial Instruments in Section II), losses incurred on the amendment of natural gas physical delivery contracts (see note 18(c) to the accompanying unaudited consolidated interim financial statements and discussion under Results of Operations and Net Income sections) and the effect of certain non-recurring items in order to facilitate better comparability to prior period performance and provide a better indicator of its cash flow generation capability.

Management considers NFFO to be the key measure of CAPREIT's operating performance and the primary indicator with respect to the sustainability of CAPREIT's distributions.

A reconciliation of FFO to NFFO is as follows:

| **Three Months Ended March 31,**<br>($ Thousands, except per Unit amounts) | **2011** | 2010 |
|---|---|---|
| FFO | **$ 22,132** | $ 15,084 |
| Adjustments: | | |
| Unrealized Loss on Derivative Financial Instruments | **156** | 54 |
| Amortization of Loss on Derivative Financial Instruments Included in Mortgage Interest | **264** | 274 |
| Net Loss on Natural Gas Contracts | **–** | 4,497 |
| Severance and Other Employee Termination Costs | **–** | 150 |
| NFFO | **$ 22,552** | $ 20,059 |
| NFFO per Unit – Basic | **$ 0.301** | $ 0.302 |
| NFFO per Unit – Diluted | **$ 0.298** | $ 0.301 |
| Total Distributions Declared | **$ 20,885** | $ 18,675 |
| NFFO Payout Ratio | **92.6%** | 93.1% |
| Net Distributions Paid | **$ 16,357** | $ 16,077 |
| Excess NFFO Over Net Distributions Paid | **$ 6,195** | $ 3,982 |
| Effective NFFO Payout Ratio | **72.5%** | 80.1% |

Despite the negative effects of HST and the low guideline increases permitted on lease renewals in Ontario, NFFO for the three months ended March 31, 2011 increased by 12.4% compared to the same period last year primarily due to the contribution from acquisitions, higher average monthly rents and higher occupancy levels, resulting from Management's sales and marketing programs along with reduced operating costs (as discussed under Results of Operations). Basic NFFO per Unit for the three months ended March 31, 2011 remained essentially unchanged from the same period last year.

Management expects FFO and NFFO payout ratios to be negatively affected in the near term as a result of the equity offering completed in December 2010 until such time as the capital raised in the offering is redeployed through acquisitions.

Comparing distributions declared to NFFO, the NFFO payout ratios for the three months ended March 31, 2011 improved to 92.6% compared to 93.1% for the same period last year. The effective NFFO payout ratio, which compares NFFO to net distributions paid to Unitholders, improved significantly for the three months ended March 31, 2011, to 72.5% from 80.1% for the same period last year primarily due to higher participation in the DRIP. Management believes NFFO will be sufficient to fund CAPREIT's distributions on an annualized basis.

**Adjusted Funds From Operations**

AFFO is a supplemental measure of cash generated from operations that is used in the real estate industry to assess the sustainability of future distributions paid to Unitholders after provision for maintenance property capital investments.

Management relies on an industry-based estimate to determine the amount of maintenance property capital investments as significant judgment is required to classify property capital investments as either *maintenance* or *stabilizing or value-enhancing* (see discussion under the Productive Capacity section). Management views AFFO as less reliable or applicable under a gross lease operating structure, as is the case for CAPREIT, because maintenance property capital investments are not clearly identifiable. However, given the current use by investors and other stakeholders of this non-IFRS financial measure, CAPREIT currently intends to continue presenting an estimate of AFFO.

CAPREIT calculates AFFO by deducting from NFFO an industry-based estimate for maintenance property capital investments (see discussion under the Productive Capacity section) and adding back the non-cash compensation costs for LTIP, SELTIP, UOP, DUP and the RUR Plan. In order to determine the AFFO payout ratio, CAPREIT compares distributions declared to AFFO. The effective AFFO payout ratio compares net cash distributions paid to Unitholders to AFFO.

A reconciliation of NFFO to AFFO is as follows:

| **Three Months Ended March 31,**<br>($ Thousands, except per Unit amounts) | | **2011** | | **2010** |
|---|---|---|---|---|
| NFFO | **$** | **22,552** | $ | 20,059 |
| Adjustments: | | | | |
| Provision for Maintenance Property Capital Investments (1) | | **(2,931)** | | (2,977) |
| Amortization of Fair Value on Grant Date of Unit-Based Compensation | | **320** | | 294 |
| AFFO | **$** | **19,941** | $ | 17,376 |
| AFFO per Unit – Basic | **$** | **0.266** | $ | 0.262 |
| AFFO per Unit – Diluted | **$** | **0.264** | $ | 0.261 |
| Distributions Declared | **$** | **20,885** | $ | 18,675 |
| AFFO Payout Ratio | | **104.7%** | | 107.5% |
| Net Distributions Paid | **$** | **16,357** | $ | 16,077 |
| Excess AFFO Over Net Distributions Paid | **$** | **3,584** | $ | 1,299 |
| Effective AFFO Payout Ratio | | **82.0%** | | 92.5% |

(1) Based on an industry estimate of $450 per suite per year and the weighted average number of residential suites during the period (see Productive Capacity section).

The AFFO payout ratios improved for the three months ended March 31, 2011 to 104.7% from 107.5% for the same period last year. The effective AFFO payout ratios for the three months ended March 31, 2011 improved as a result of higher DRIP participation rates period over period.

**Changes in Non-IFRS Financial Measures**

The adoption of IFRS has had a material impact on the presentation of financial results of CAPREIT. However, Management believes the underlying performance of CAPREIT is largely unaffected by the change in accounting principles and, as a result, where possible, Management has adjusted the calculation of its non-IFRS financial measures to exclude substantially the effects of the adoption of IFRS to maintain comparability with prior periods and with CAPREIT's industry peers.

Discussed below are the significant adjustments made by Management to each key non-IFRS financial measure:

Funds From Operations

i) *Fair value adjustment of investment properties*: unrealized gains or losses arising from the fair value remeasurement of investment properties have been adjusted in establishing FFO.

ii) *Fair value adjustment of Exchangeable Units and related interest expense*: although IFRS necessitates the presentation of Exchangeable Units as financial liabilities that must be remeasured at fair value, Management believes these Units are equity in nature. For purposes of comparability, Management has adjusted FFO for the unrealized gains and losses arising from the fair value remeasurement of Exchangeable Units as well the distributions made on these Units, which are treated as interest expense under IFRS.

iii) *Fair value adjustment of Unit-based compensation financial liabilities*: as outlined earlier, the requirement to remeasure at fair value all unsettled award Units at each reporting date is the result of the underlying Trust Units being considered financial liabilities for the purposes of determining the presentation and measurement of Unit-based compensation. This requirement applies only to those open-end trusts with redeemable trust units, such as CAPREIT. As many trusts in CAPREIT's peer group do not fall into this category, Management has elected to adjust the calculation of FFO for the effects of the fair value remeasurement component to maintain comparability.

Adjusted Funds From Operations

i) *Amortization of grant date fair value of Unit-based compensation*: the use of the graded approach to amortize the grant date fair values under IFRS as compared to the straight-line approach under Canadian GAAP for the calculation of this non-cash expense results in a change in the amortization expense added back to arrive at AFFO.

Despite the above adjustments aimed at maintaining comparability with prior periods, certain effects in the adoption of IFRS will impact CAPREIT's non-IFRS financial measures, including the discontinuation of certain types of amortization expenses which were not adjusted for in arriving at FFO.

The tables below reconcile the same non-IFRS financial measures as previously reported to the revised figures as presently reported under IFRS for the three months ended March 31, 2010 and the year ended December 31, 2010.

**For The Three Months Ended March 31, 2010**

| ($ Thousands) | FFO | NFFO | AFFO |
|---|---|---|---|
| **As Previously Reported** | **$ 15,047** | **$ 20,022** | **$ 17,365** |
| Adjustments: | | | |
| Elimination of Amortization of Direct Leasing Costs | 11 | 11 | 11 |
| Change in Calculation of Grant Date Fair Value Amortization of Unit-Based Compensation | 26 | 26 | – |
| **As Presently Reported** | **$ 15,084** | **$ 20,059** | **$ 17,376** |

| For The Year Ended December 31, 2010<br>($ Thousands) | FFO | NFFO | AFFO |
|---|---|---|---|
| **As Previously Reported** | **$ 85,089** | **$ 91,592** | **$ 81,453** |
| Adjustments: | | | |
| Elimination of Amortization of Direct Leasing Costs | 71 | 71 | 71 |
| Change in Calculation of Grant Date Fair Value Amortization of Unit-Based Compensation | 364 | 364 | – |
| **As Presently Reported** | **$ 85,524** | **$ 92,027** | **$ 81,524** |

The following tables reconcile the impact of adopting IFRS on the consolidated statement of income with the calculation of some of CAPREIT's key non-IFRS financial measures for the three months ended March 31, 2010 and the year ended December 31, 2010.

| **For The Three Months Ended March 31, 2010 ($ Thousands)** | **As Previously Reported** | Investment Properties | Exchangeable Units | Unit-Based Compensation | **As Presently Reported** |
|---|---|---|---|---|---|
| **Net (Loss) Income** | **$ (4,790)** | $ 16,051 | $ (230) | $ (359) | **$ 10,672** |
| Depreciation and Amortization | 20,787 | (20,479) | – | – | 308 |
| Unrealized Loss on Remeasurement of | | | | | |
| - Investment Properties | – | 8,364 | – | – | 8,364 |
| - Exchangeable Units | – | – | 119 | – | 119 |
| - Unit-Based Compensation Liabilities | – | – | – | 385 | 385 |
| Interest on Exchangeable Units | – | – | 111 | – | 111 |
| Recovery of Deferred Income Taxes | (950) | (3,925) | – | – | (4,875) |
| **FFO** | **$ 15,047** | $ 11 | $ – | $ 26 | **$ 15,084** |
| Unrealized Loss on Derivative Financial Instruments | 54 | – | – | – | 54 |
| Net Loss on Natural Gas Contracts | 4,497 | – | – | – | 4,497 |
| Severance and Other Employee Termination Costs | 150 | – | – | – | 150 |
| Amortization of Loss on Derivative Financial Instruments Included in Mortgage Interest | 274 | – | – | – | 274 |
| **NFFO** | **$ 20,022** | $ 11 | $ – | $ 26 | **$ 20,059** |
| Provision for Maintenance Property Capital Investments | (2,977) | – | – | – | (2,977) |
| Amortization of Fair Value on Grant Date of Unit-Based Compensation | 320 | – | – | (26) | 294 |
| **AFFO** | **$ 17,365** | $ 11 | $ – | $ – | **$ 17,376** |

| For The Year Ended December 31, 2010 ($ Thousands) | As Previously Reported | Investment Properties | Exchangeable Units | Unit-Based Compensation | As Presently Reported |
|---|---|---|---|---|---|
| **Net Income** | **$ 63,321** | $ 473,219 | $ (1,711) | $ (5,781) | **$ 529,048** |
| Depreciation and Amortization | 84,811 | (83,542) | – | – | 1,269 |
| Unrealized Loss on Remeasurement of | | | | | |
| - Investment Properties | – | (21,857) | – | – | (21,857) |
| - Exchangeable Units | – | – | 1,267 | – | 1,267 |
| - Unit-Based Compensation Liabilities | – | – | – | 6,145 | 6,145 |
| Interest on Exchangeable Units | – | – | 444 | – | 444 |
| Recovery of Deferred Income Taxes | (51,355) | (384,378) | – | – | (435,733) |
| (Gain) Loss on Disposition of Investment Properties | (11,688) | 16,629 | – | – | 4,941 |
| **FFO** | **$ 85,089** | $ 71 | $ – | $ 364 | **$ 85,524** |
| Unrealized Loss on Derivative Financial Instruments | 174 | – | – | – | 174 |
| Net Loss on Natural Gas Contracts | 4,497 | – | – | – | 4,497 |
| Severance and Other Employee Termination Costs | 736 | – | – | – | 736 |
| Amortization of Loss on Derivative Financial Instruments Included in Mortgage Interest | 1,096 | – | – | – | 1,096 |
| **NFFO** | **$ 91,592** | $ 71 | $ – | $ 364 | **$ 92,027** |
| Provision for Maintenance Property Capital Investments | (11,835) | – | – | – | (11,835) |
| Amortization of Fair Value on Grant Date of Unit-Based Compensation | 1,696 | – | – | (364) | 1,332 |
| **AFFO** | **$ 81,453** | $ 71 | $ – | $ – | **$ 81,524** |

## SECTION IV

## PROPERTY CAPITAL INVESTMENTS

CAPREIT capitalizes all capital investments related to the improvement of its properties. These investments have the objective of growing NOI in the future.

An important component of CAPREIT's property capital investment strategy is to acquire properties at values significantly below current replacement costs and improve their operating performance by investing annually in order to sustain and grow the portfolio's future rental income-generating potential over its useful life.

To achieve its property capital investment objectives, taking into account CAPREIT's acquisition history, the soft economic conditions and the availability of competitive pricing from construction trades, in 2009, CAPREIT formulated and embarked on a multi-year capital investment plan that accelerates spending on planned building improvement programs, including upgrading parking garages, balconies and other structural improvements. These investments are closely connected to CAPREIT's property acquisitions, many of which were anticipated at the time of such acquisitions and were included in the acquisition analysis, to ensure such transactions are accretive. Management believes these investments will increase the productive capacity, the useful economic life and the operating capabilities of CAPREIT's properties and enhance their future cash flow generating potential. Management also believes these building improvement programs, combined with existing suite improvement, common area and environment-friendly and energy-saving initiatives, will enable CAPREIT to reposition its portfolio and maintain high occupancy levels throughout any unfavourable economic conditions. These investments are expected to continue to increase average monthly rents while improving life safety and resident services. Management believes strategic investments taken at this time will position the portfolio for improved operating performance as the economy strengthens and over the long term.

During the three months ended March 31, 2011, CAPREIT made property capital investments of $12.8 million as compared to $8.4 million for the same period last year. Property capital investments were higher compared to the prior year period primarily due to the acceleration of building improvement programs, and higher investments in suite improvements, common areas and equipment, which generally tend to increase NOI more quickly. The increased level of investments is in line with the revised capital investment plan for 2011 announced in the fourth quarter of 2010.

In addition, CAPREIT continues to invest in environment-friendly and energy-saving initiatives, including high-efficiency boilers, energy-efficient lighting systems, and water saving programs, which have permitted CAPREIT to mitigate potentially higher increases in utility and R&M costs and have improved overall portfolio NOI significantly as discussed in the Results of Operations section.

A breakdown of property capital investments (excluding head office assets, MHC land lease sites, tenant improvements and signage) is summarized by category below:

***Property Capital Investments by Category***

| **Three Months Ended March 31,**<br>($ Thousands) | | **2011** | **%** | | **2010** | **%** |
|---|---|---|---|---|---|---|
| Building Improvements | $ | **3,332** | **26.1** | $ | 2,044 | 24.3 |
| Suite Improvements | | **4,497** | **35.2** | | 3,296 | 39.2 |
| Common Area | | **2,036** | **16.0** | | 760 | 9.0 |
| Energy-Saving Initiatives | | **271** | **2.1** | | 447 | 5.3 |
| Equipment | | **1,857** | **14.6** | | 1,150 | 13.7 |
| Boiler and Elevators | | **446** | **3.5** | | 423 | 5.0 |
| Appliances | | **317** | **2.5** | | 294 | 3.5 |
| | $ | **12,756** | **100.0** | $ | 8,414 | 100.0 |

Based on a multi-year property capital investment plan, Management expects CAPREIT to complete property capital investments of approximately $100.0 million to $110.0 million during 2011, including approximately $10.5 million in investments in high-efficiency boilers and other energy-saving initiatives.

Set out in the table below is Management's current estimate, established through consultations with an independent engineering firm, of CAPREIT's investments in building improvements for 2011 through 2014 for properties owned as of May 9, 2011. Building improvements represent the most significant category of property capital investment at present, but are expected to decline significantly in the coming years. These estimates exclude the impact of changes in anticipated investment levels resulting from acquisitions and dispositions of properties occurring after May 9, 2011.

***Future Investments in Building Improvements***

| **Year Ending December 31**<br>($ Thousands) | | **Estimated Range** | | | |
|---|---|---|---|---|---|
| 2011 | $ | 58,000 | – | $ | 62,000 |
| 2012 | $ | 37,000 | – | $ | 39,000 |
| 2013 | $ | 32,000 | – | $ | 37,000 |
| 2014 | $ | 14,500 | – | $ | 17,500 |

Excludes property capital investments in other categories, such as suite improvements and common area.

Management believes CAPREIT has sufficient liquidity and access to top up financing opportunities (see the Liquidity and Financial Condition section) to execute the above property capital investment strategy.

## PRODUCTIVE CAPACITY

The primary focus of the following discussion is to differentiate between investments to maintain existing cash flows from the properties and investments incurred in order to achieve CAPREIT's longer term goals of enhanced cash flows and Unit distributions.

*Maintenance property capital investments* vary with market conditions, are partially related to suite turnover and are intended to maintain the earning capacity of the portfolio. Industry estimates for annual overall maintenance capital investments are approximately $450 per residential suite. These maintenance property capital investments are in addition to regular R&M costs, which have historically averaged in the range of $700 to $800 per residential suite annually and are expensed to NOI.

*Stabilizing and value-enhancing property capital investments* are focused on increasing the productivity of the property portfolio. These investments enhance operating effectiveness and profitability and increase revenues or reduce costs to improve NOI over the long term. In addition, they improve the economic life and value of the properties and are mainly long-term in nature.

Owing to the gross lease structure of its portfolio, CAPREIT does not distinguish its property capital investments between the two categories described above. Instead, CAPREIT uses industry guidelines for maintenance property capital investments to estimate its stabilizing and value-enhancing property capital investments as follows:

| **Three Months Ended March 31,**<br>($ Thousands) | **2011** | **2010** |
|---|---|---|
| Total Property Capital Investments (1) | $ **12,756** | $ 8,414 |
| Less: Estimated Maintenance Property Capital Investments (2) | **(2,931)** | (2,977) |
| Stabilizing and Value-Enhancing Capital Investments | $ **9,825** | $ 5,437 |

(1) Excludes capital investments for head office assets, properties disposed as of March 31, MHC land lease sites, tenant improvements and signage.
(2) Based on an industry estimate of $450 per suite per year and the weighted average number of residential suites during the period.

Management believes its increased emphasis on targeted property capital investment programs for its property portfolio is yielding positive results, as significant benefits are being and are expected to continue to be, realized through maintaining high occupancy, increasing average monthly rents and reducing operating costs.

## CAPITAL STRUCTURE

CAPREIT defines capital as the aggregate of Unitholders' equity, debt financing, liabilities associated with investment properties, Unit-based compensation liabilities and Exchangeable Units. CAPREIT's objectives when managing capital are to safeguard its ability to continue to fund distributions to Unitholders, to retain a portion to meet repayment obligations under its mortgages and credit facilities, and to ensure sufficient funds are available to meet capital commitments. Capital adequacy is monitored against investment and debt restrictions contained in CAPREIT's DOT and the Credit Facilities agreement.

CAPREIT's Credit Facilities (see Bank Indebtedness and Credit Facilities) require compliance with the financial covenants shown in the table below. In addition, borrowings must not exceed the borrowing base, calculated as a predefined percentage of the fair value of the investment properties determined on an annual basis.

In the short term, CAPREIT utilizes the Acquisition and Operating Facility to finance its capital investments, which may include acquisitions. In the long term, equity issuances, mortgage financings and refinancings, including top ups, are put in place to finance the cumulative investment in the property portfolio and ensure the sources of financing better reflect the long-term useful lives of the underlying investments.

CAPREIT is in compliance with all the investment and debt restrictions and financial covenants contained in the DOT and in the Credit Facilities. The total capital managed by CAPREIT and the results of compliance with the key covenants are summarized below:

| As at<br>($ Thousands) | Threshold | March 31, 2011 | December 31, 2010 |
|---|---|---|---|
| Mortgages Payable | | $ 1,605,277 | $ 1,603,027 |
| Bank Indebtedness | | 59,362 | 39,358 |
| Liabilities Associated with Investment Properties | | 56,568 | 56,568 |
| Unit-Based Compensation Liabilities | | 21,459 | 16,410 |
| Exchangeable Units | | 8,004 | 7,050 |
| Unitholders' Equity | | 1,351,974 | 1,355,445 |
| Total Capital | | $ 3,102,644 | $ 3,077,858 |
| Total Debt to Gross Book Value (1) | Maximum 70.00% | 52.28% | 51.80% (3) |
| Total Debt to Gross Historical Cost (2) | | 59.00% | 58.87% (3) |
| Tangible Net Worth (4) | Minimum $700,000 | $ 1,351,974 | $ 1,355,445 (3) |

| For the four quarters ended | Threshold | March 31, 2011 | December 31, 2010 |
|---|---|---|---|
| Debt Service Coverage Ratio (times) (5) | Minimum 1.20 | 1.34 | 1.33 (3) |
| Interest Coverage Ratio (times) (6) | Minimum 1.50 | 2.11 | 2.07 (3) |

(1) CAPREIT's DOT limits the maximum amount of total debt to 70% of the gross book value ("GBV") of CAPREIT's total assets. GBV is defined as the historical book value of CAPREIT's assets plus fair value adjustments plus accumulated amortization on property, plant and equipment and deferred loan costs. In addition, the DOT provides for investment restrictions on type and maximum limits on single property investments.
(2) Based on the historical cost of investment properties.
(3) For informational purposes, these financial ratios and tangible net worth, previously calculated under Canadian GAAP have been restated under IFRS.
(4) Tangible net worth is generally represented by Unitholders' equity and is defined as the sum of: i) Units issued; ii) contributed surplus; and iii) retained earnings after adding back the provision for deferred income taxes payable to a maximum limit of $100 million. As at December 31, 2010, this definition includes the sum of accumulated depreciation and amortization and, to a maximum of $50 million, deferred taxes payable on any capital stock based investment transactions.
(5) Debt service coverage ratio is defined as earnings before interest, depreciation, amortization, income taxes and other adjustments including non-cash compensation costs ("EBITDA") less taxes paid divided by principal and interest payments.
(6) Interest coverage ratio is defined as EBITDA less taxes paid divided by interest payments.

## LIQUIDITY AND FINANCIAL CONDITION

### Liquidity and Capital Resources

Management ensures there is adequate overall liquidity by maintaining sufficient amounts of available credit facilities to fund maintenance and property capital investment commitments, distributions to Unitholders and to provide for future growth in its business. CAPREIT finances these commitments through: (i) cash flow from operating activities; (ii) mortgage debt secured by its investment properties; (iii) secured short-term debt financing with two Canadian chartered banks; and (iv) equity. Management's view of CAPREIT's liquidity position going forward continues to be stable based on its evaluation of capital resources as summarized below:

i) CAPREIT's operating business conditions continue to be stable and are expected to generate sufficient cash flow from operating activities to fund the current level of distributions. Management expects the current level of funds reinvested from its DRIP and the retained portion of its annual NFFO will be sufficient to fund its ongoing maintenance property capital investments. For the three months ended March 31, 2011, CAPREIT's NFFO payout ratio was 92.6% compared to 93.1% for the same period last year and the effective NFFO payout ratio was 72.5% compared to 80.1% for the prior year. Historically, CAPREIT has targeted a long-term annual NFFO payout ratio in the 85% to 90% range.

ii) Management believes CAPREIT is well positioned to meet its mortgage renewal and refinancing goals in 2011 due to the continuing availability of CMHC-insured financing. Management does not anticipate any material

difficulties in completing the renewal of mortgages maturing during the remainder of 2011 of approximately $144.8 million, which have an effective interest rate of approximately 5.37%, and refinancing a significant portion of the approximately $36.9 million principal repayments remaining through 2011 with new mortgages at lower interest rates.

iii) Management renewed and amended its Credit Facilities aggregating to $280 million effective June 30, 2010, which comprise a revolving three-year Acquisition and Operating Facility of $270 million, subject to compliance with the various provisions of the Credit Facilities, in order to fund operations, acquisitions, capital improvements, letters of credit and other uses. In addition, the Land Lease Facility of $10 million was renewed for a one-year term maturing on June 30, 2011. The renewal agreement includes amendments to debt covenants to incorporate the effects that IFRS may have on CAPREIT's financial position and also reduces the overall cost of borrowings. The amended Credit Facilities also contemplate converting floating rate charge debentures on certain of CAPREIT's investment properties, which have been pledged as security, into fixed charges.

iv) On November 22, 2010, CAPREIT announced it had agreed to sell, subject to regulatory approval, 7,250,000 Units for $17.30 per Unit for aggregate gross proceeds of $125.4 million on a bought-deal basis with an over-allotment option. The transaction closed on December 10, 2010, and under the over-allotment option, 350,000 additional Units were issued on December 23, 2010. CAPREIT used the total net proceeds of the offering to repay a large portion of the borrowings under its Acquisition and Operating Facility. The additional capital will be used to finance future acquisitions and property capital investments.

In order to maintain and enhance its CMHC-insured financing program, and consistent with CMHC's risk management practices involving large borrowers, CAPREIT entered into an agreement with CMHC (the "Large Borrower Agreement" or "LBA") during the third quarter of 2010. The LBA has not materially affected the manner in which CAPREIT conducts its business or its approach to mortgage financing. The LBA provides for, among other things:

i) Enhanced disclosure to CMHC;
ii) Certain financial covenants and limitations on indebtedness, none of which are inconsistent with CAPREIT's current operating policies;
iii) The posting of a revolving letter of credit with respect to certain capital expenditures on a portfolio, rather than an individual property basis; and
iv) Cross-collateralization of mortgage loans for certain CMHC-insured mortgage lenders.

The available borrowing capacity under CAPREIT's Acquisition and Operating Facility at March 31, 2011 was $198.0 million ($223.5 million as at December 31, 2010). The available borrowing capacity under CAPREIT's Land Lease Facility as at March 31, 2011 was $8.7 million ($8.6 million as at December 31, 2010). The working capital deficiency as presented on CAPREIT's consolidated balance sheet as at March 31, 2011, which includes non-cash Unit-based compensation liabilities, is managed through of the available liquidity under the Credit Facilities as well as the ongoing refinancing of mortgages payable.

The contractual maturities and repayment obligations of CAPREIT's financial liabilities for upcoming periods as at March 31, 2011 are as follows:

| ($ Thousands) | 2011 | 2012 – 2013 | 2014 – 2015 | 2016 onward |
|---|---|---|---|---|
| Mortgages Payable | $ 181,677 | $ 475,329 | $ 418,898 | $ 565,108 |
| Bank Indebtedness | 1,202 | 58,160 | – | – |
| Liabilities Associated with Investment Properties | 2,782 | 5,113 | 4,517 | 44,156 |
| Interest on Mortgages Payable (1) | 53,703 | 108,823 | 67,015 | 89,477 |
| Interest on Bank Indebtedness (1) | 1,788 | 3,521 | – | – |
| Other Liabilities | 44,372 | 1,233 | – | – |
| Unit-Based Compensation Liabilities | 20,868 | 591 | – | – |
| Security Deposits | 19,458 | – | – | – |
| Exchangeable Units | 8,004 | – | – | – |
| Distributions Payable | 6,919 | – | – | – |
| | $ 340,773 | $ 652,770 | $ 490,430 | $ 698,741 |

(1) Based on interest rates in place at March 31, 2011.

**Mortgages Payable**

CAPREIT takes a conservative approach and actively manages its mortgage portfolio to reduce interest costs while ensuring it is not overly exposed to interest rate volatility risk. Management takes a portfolio approach to its mortgage debt, proactively staggering maturities to reduce risk while taking advantage of the current low interest rate environment.

The key liquidity metrics are summarized in the table below:

| As at March 31, | 2011 | 2010 |
|---|---|---|
| Mortgage Debt to Gross Book Value | **50.42%** | 50.10% |
| Total Debt to Gross Book Value | **52.28%** | 56.04% |
| Total Debt to Gross Historical Cost (1) | **59.00%** | 63.22% |
| Total Debt to Total Capitalization | **52.45%** | 62.95% |
| | | |
| Debt Service Coverage Ratio (times) (2) | **1.34** | – |
| Interest Coverage Ratio (times) (2) | **2.11** | – |
| | | |
| Weighted Average Mortgage Interest Rate (%) (3) | **4.74** | 5.06 |
| Weighted Average Mortgage Term to Maturity (years) | **4.9** | 4.8 |

(1) Based on the historical cost of investment properties.
(2) Based on the trailing four quarters ended March 31, 2011. Prior year comparative ratios have not been restated under IFRS and are therefore not presented. Ratios calculated under Canadian GAAP are available in the MD&A issued for periods prior to 2011.
(3) Effective weighted average interest rate includes deferred financing costs and fair value adjustments but excludes the amortization of CMHC premiums. Including the amortization of the realized component of the loss on settlement of $9.9 million included in Accumulated Other Comprehensive Loss ("AOCL"), the effective portfolio weighted average interest rate at March 31, 2011 would be 4.82% (March 31, 2010 - 5.15%).

As at March 31, 2011, the overall leverage represented by the ratio of total debt to gross book value improved to 52.28%, as compared to 56.04% last year, mainly as a result of the repayment of a large portion of the Acquisition and Operating Facility with capital raised from the equity offering completed in December 2010. Due to the rise in CAPREIT's Unit price since March 31, 2010 and overall market capitalization, combined with the equity offering, as at March 31, 2011, CAPREIT's total debt improved to 52.45% of total market capitalization compared to 62.95% last year.

The effective portfolio weighted average interest rate has steadily declined from 5.06% as at March 31, 2010, to 4.74% as at March 31, 2011, which Management expects will result in significant interest rate savings in future years. Management believes that, as CAPREIT's refinancing plan continues to be implemented, there is scope to further reduce the effective portfolio weighted average interest rate based on current market conditions and despite recent and expected increases in interest rates in the medium term. Management is also focused on ensuring the portfolio weighted average term to maturity remains in the five-year range or longer and expects to gradually extend the term.

CAPREIT focuses on multi-unit residential real estate, which is eligible for government-backed insurance for mortgages administered by CMHC, which benefits CAPREIT in two ways:

- CAPREIT obtains lower interest rate spreads for mortgage financing; and
- CAPREIT's overall renewal risk for mortgage refinancings is reduced as the mortgage insurance premium is transferable between approved lenders and is effective for the full amortization period of the underlying mortgage ranging between 25 to 35 years.

At March 31, 2011, 95.7% (March 31, 2010 – 96.2%) of CAPREIT's mortgage portfolio is CMHC-insured (excluding the mortgage on the MHC land lease sites portfolio).

The following table summarizes the changes in the mortgage portfolio during the periods:

| As at March 31,<br>($ Thousands) | | 2011 | 2010 |
|---|---|---|---|
| Balance, Beginning of Period | | **$ 1,603,027** | $ 1,517,206 |
| Add: | New Borrowings | **6,819** | – |
| | Refinanced | **98,339** | – |
| Less: | Mortgage Repayments | **(12,461)** | (12,039) |
| | Mortgages Matured | **(87,964)** | – |
| | Mortgages Repaid on Disposition of Investment Property | **(2,117)** | – |
| | Deferred Financing Costs, Fair Value Adjustments and CMHC Premiums, net | **(366)** | 576 |
| Balance, End of Period | | **$ 1,605,277** | $ 1,505,743 |

Total financings of $110.9 million, including $97.9 million for renewals of existing mortgages and $13.0 million for additional top up financing have been closed or committed up to May 9, 2011, with an average term to maturity of 5.3 years, and at a weighted average interest rate of 3.53%, which is significantly below the weighted average interest rate of mortgages maturing in 2011 of 5.11%. Management expects to raise between $250 million and $275 million in total mortgage renewals and refinancings for 2011.

The following table summarizes refinancings for the three months ended March 31, 2011, and the weighted average interest rates obtained. At March 31, 2011, 97.0% (March 31, 2010 – 99.7%) of CAPREIT's mortgage portfolio bears fixed rates of interest.

| ($ Thousands) | Original Mortgage Amount | Original Interest Rate (1) | New Mortgage Amount | New Interest Rate (1) | Weighted Average Term on New Mortgage (Yrs) | Top Up Financing Amount |
|---|---|---|---|---|---|---|
| First Quarter | $ 87,964 | 4.70% | $ 98,339 | 3.44% | 5.4 | $ 10,375 |

(1) Weighted average.

For purposes of estimating top up financing potential, the following table provides the NOI for those properties with mortgages maturing over the next five years and beyond. A property's full NOI is included in the first year in which a mortgage matures. The balance of mortgages remaining on the same property but maturing in other years is also shown. Based on this mortgage maturity profile, Management believes it will be in a position to achieve its mortgage renewal and refinancing plan for 2011.

**As at March 31, 2011**

($ Thousands)

| Year of Maturity | Mortgage Maturities (1) | Mortgages on the Same Properties Maturing in Other Years (1) | Total Mortgages | NOI of Properties with Maturing Mortgage(s) (2) |
|---|---|---|---|---|
| 2011 | $ 144,823 | $ 24,326 | $ 169,149 | $ 22,638 |
| 2012 | 217,235 | 2,764 | 219,999 | 26,492 |
| 2013 | 173,169 | 46,303 | 219,472 | 32,355 |
| 2014 | 225,136 | 151 | 225,287 | 30,521 |
| 2015 | 134,099 | 16,868 | 150,967 | 17,998 |
| 2016 onward | 444,805 | (90,412) | 354,393 | 61,254 |
| Total | $ 1,339,267 | $ – | $ 1,339,267 | $ 191,258 |

(1) Mortgage balance due upon maturity.
(2) NOI for 12 months ended March 31, 2011.

The breakdown of future principal repayments, including mortgage maturities, and effective weighted average interest rates as at March 31, 2011, is as follows:

| ($ Thousands)<br>Period | | Principal Repayments | | Mortgage Maturities | | Mortgage Balance | % of Total Mortgage Balance | Interest Rate (%) (1) |
|---|---|---|---|---|---|---|---|---|
| Remaining months in 2011 | $ | 36,854 | $ | 144,823 | $ | 181,677 | 11.1 | 5.37 |
| 2012 | | 44,615 | | 217,235 | | 261,850 | 16.0 | 5.10 |
| 2013 | | 40,310 | | 173,169 | | 213,479 | 13.0 | 4.66 |
| 2014 | | 32,053 | | 225,136 | | 257,189 | 15.7 | 4.17 |
| 2015 | | 27,610 | | 134,099 | | 161,709 | 9.9 | 3.82 |
| 2016 | | 22,610 | | 47,094 | | 69,704 | 4.2 | 4.98 |
| 2017 | | 19,375 | | 100,285 | | 119,660 | 7.3 | 4.74 |
| 2018 | | 18,808 | | 52,234 | | 71,042 | 4.3 | 4.69 |
| 2019 | | 16,594 | | 82,760 | | 99,354 | 6.0 | 5.15 |
| 2020 | | 13,806 | | 54,648 | | 68,454 | 4.2 | 4.66 |
| 2021 – 2025 | | 27,603 | | 104,089 | | 131,692 | 8.0 | 5.05 |
| 2026 onward | | 1,507 | | 3,695 | | 5,202 | 0.3 | 5.15 |
| **Total** | **$** | **301,745** | **$** | **1,339,267** | **$** | **1,641,012** | **100.0** | **4.74** (2) |
| Deferred financing costs, fair value adjustments and CMHC premiums, net | | | | | | (35,735) | | |
| **Total** | | | | | **$** | **1,605,277** | | |

(1) Effective weighted average interest rates for maturing mortgages only.

(2) Effective weighted average interest rate includes deferred financing costs and fair value adjustments but excludes CMHC premiums. Including the amortization of the realized component of the loss on settlement of $9.9 million included in AOCL, the effective portfolio weighted average interest rate at March 31, 2011 would be 4.82% (March 31, 2010 - 5.15%).

To ensure CAPREIT is not overly exposed to interest rate volatility risk, Management has been successful in staggering the maturity dates within its mortgage portfolio. During the remainder of 2011, total debt repayments (including maturing mortgages) will be approximately 11.1% of the total mortgage portfolio.

To reduce its interest cost and cost of capital, Management will continue to leverage its balance sheet strength and the stability of its property portfolio to fund acquisitions and its capital investment plan, and to refinance its mortgage principal repayments.

**Bank Indebtedness and Credit Facilities**

Bank indebtedness includes borrowings on the Acquisition and Operating Facility and the Land Lease Facility. As at March 31, 2011, $58.2 million (March 31, 2010 – $176.3 million) was outstanding on the Acquisition and Operating Facility. In addition, at March 31, 2011, letters of credit in the amount of $11.4 million (March 31, 2010 – $6.0 million) were outstanding, which reduce the maximum amount available under the facility. The excess borrowing capacity on the Acquisition and Operating Facility, after taking into account outstanding letters of credit and the hedge liability on an interest rate swap instrument, was $198.0 million (March 31, 2010 – $63.5 million). The increase in the borrowing capacity under CAPREIT's Acquisition and Operating Facility is primarily attributable to the repayment of a large portion of the facility from funds raised in the equity offering completed in December 2010.

The Land Lease Facility of $10 million, established to fund operating, development and acquisition costs for the Bowmanville and Grand Bend manufactured home communities, matures on June 30, 2011. As at March 31, 2011, $1.2 million (March 31, 2010 – $2.2 million) was outstanding on this facility. In addition, letters of credit in the amount of $0.1 million (March 31, 2010 – $0.1 million) were outstanding, which reduce the maximum amount available under the facility.

Refer to the Liquidity and Capital Resources section and Capital Structure section for discussion regarding the renewal of and amendments to the Credit Facilities.

**Unitholders' Equity and Units Awarded Under Unit-Based Compensation Plans**

As previously discussed, under IFRS, unit capital included in Unitholders' equity only represents the issued and outstanding Trust Units, and excludes the Exchangeable Units and any Units issued in connection with Unit-based incentive plans. For

the purposes of the discussion below, Exchangeable Units and Units issued in connection with Unit-based incentive plans are treated as equity as they have claims similar or identical to those of the Trust Units.

On December 10, 2010, CAPREIT issued 7,250,000 Units at $17.30 per Unit on a bought-deal basis for aggregate gross proceeds of $125.4 million. On December 23, 2010, the over-allotment option was exercised and 350,000 additional Units were issued at $17.30 per Unit for aggregate gross proceeds of $6.1 million. The net proceeds of $125.3 million were used to repay a large portion of the borrowings on the Acquisition and Operating Facility.

CAPREIT's market capitalization as at March 31, 2011 was $1,509 million and the total number of Units outstanding as at March 31, 2011 was 77,541,364 (including 2,340,841 LTIP and SELTIP Units, 83,203 Deferred Units, 174,007 RURs and 411,311 Exchangeable Units), of which trustees, officers and other senior managers owned approximately 4.7%. As of March 31, 2011, 453,500 options to acquire Trust Units were outstanding and exercisable.

For the three months ended March 31, 2011, compensation costs related to the DUP, which gives non-executive trustees the right to receive a percentage of their annual retainer in the form of Deferred Units (see note 16(c) to the accompanying unaudited consolidated interim financial statements) of $0.2 million (2010 – $0.2 million) were expensed, excluding remeasurement at fair value, in relation to new Deferred Units under the DUP.

During the first quarter of 2010, CAPREIT introduced the RUR plan as the primary plan through which future long-term incentive compensation will be awarded. The Compensation and Governance Committee of the Board of Trustees may award restricted unit rights ("RURs"), subject to the attainment of specified performance objectives to certain officers and key employees (collectively, "Participants"). The purpose of the RUR plan is to provide Participants with additional incentive and to further align the interests of Participants with Unitholders. Upon vesting, RURs are exercisable for Units issued from treasury.

On February 22, 2011, 99,537 RURs were granted at $18.37 based on the weighted average trading price of the Units for the five trading days prior to the grant date. The fair value of the compensation costs for the Units granted on this day was $1.9 million based on the closing market price of CAPREIT Units on the date of grant. As the RURs vest in their entirety on the third anniversary of the grant date, the compensation costs are amortized on a straight-line basis over the three-year vesting period.

RURs earn notional distributions in respect of each distribution paid on Units commencing from the grant date and such notional distributions are used to calculate additional RURs ("Distribution RURs"), which are accrued for the benefit of the Participants. The Distribution RURs are credited to the Participants only when the underlying RURs upon which the Distribution RURs are earned become vested. For the three months ended March 31, 2011, compensation costs excluding remeasurement at fair value, of $0.1 million (March 31, 2010 – $32 thousand) were expensed in relation to awards granted under the RUR plan.

In February 2010, the President and CEO's employment agreement was amended such that options are to be awarded to acquire three percent (3%) of the number of Units issued by CAPREIT pursuant to any equity offering or acquisition transaction at the then market price and in accordance with the terms of the UOP. In December 2010, in connection with the equity offering and the exercise of the over-allotment option, a total of 228,000 Unit Options under the UOP were granted to the President and CEO at an exercise price of $17.30 with an expiration of December 2020.

**Normal Course Issuer Bid**

On June 22, 2010, CAPREIT announced that the TSX had approved its normal course issuer bid ("NCIB") to acquire up to 6,425,179 Trust Units, representing 10% of the public float at the time, at market prices over the 12-month period ending June 24, 2011. Purchases are made at market prices through the facilities of the TSX. Any Trust Units purchased by CAPREIT are cancelled. CAPREIT believes the ongoing purchase of its outstanding Units may be an appropriate use of its resources from time to time and can provide liquidity to Unitholders who desire to sell their Units. No Trust Units were acquired under this NCIB as of March 31, 2011.

On June 19, 2009, CAPREIT announced that the TSX had approved its NCIB to acquire up to 6,344,344 Trust Units, representing 10% of the public float at the time, at market prices over the 12-month period ending June 24, 2010. No Trust Units were acquired under this NCIB.

**SECTION V**

**SELECTED CONSOLIDATED QUARTERLY INFORMATION**

| ($ Thousands, except per Unit amounts) | | Q1 11 | Q4 10 | Q3 10 | Q2 10 | Q1 10 | Q4 09 (2) | Q3 09 (2) | Q2 09 (2) |
|---|---|---|---|---|---|---|---|---|---|
| Overall Portfolio AMR | | $ 978 | $ 979 | $ 977 | $ 958 | $ 943 | $ 943 | $ 943 | $ 929 |
| Operating Revenues (1) | | $ 86,332 | $ 85,629 | $ 85,057 | $ 84,755 | $ 83,518 | $ 81,329 | $ 80,521 | $ 79,557 |
| NOI (1) | | $ 46,564 | $ 46,592 | $ 49,906 | $ 50,199 | $ 43,643 | $ 43,790 | $ 46,437 | $ 45,359 |
| NOI Margin (1) | | 53.9% | 54.4% | 58.7% | 59.2% | 52.3% | 53.8% | 57.7% | 57.0% |
| Net Income | | $ 9,663 | $ 477,208 | $ 38,534 | $ 2,634 | $ 10,672 | $ 10,192 | $ 950 | $ 9,073 |
| FFO | | $ 22,132 | $ 20,723 | $ 24,885 | $ 24,832 | $ 15,084 | $ 20,639 | $ 21,059 | $ 28,630 |
| NFFO | | $ 22,552 | $ 21,253 | $ 25,227 | $ 25,488 | $ 20,059 | $ 20,178 | $ 23,581 | $ 23,153 |
| Total Debt to Gross Book Value | | 52.28% | 51.80% | 56.64% | 56.93% | 57.28% | 62.75% | 62.97% | 62.42% |
| Net Income Per Unit | - Basic | $ 0.129 | $ 6.943 | $ 0.577 | $ 0.040 | $ 0.161 | $ 0.154 | $ 0.014 | $ 0.138 |
| | - Diluted | $ 0.128 | $ 6.878 | $ 0.573 | $ 0.039 | $ 0.160 | $ 0.153 | $ 0.014 | $ 0.137 |
| FFO Per Unit | - Basic | $ 0.296 | $ 0.302 | $ 0.373 | $ 0.373 | $ 0.227 | $ 0.311 | $ 0.319 | $ 0.434 |
| NFFO Per Unit | - Basic | $ 0.301 | $ 0.309 | $ 0.378 | $ 0.383 | $ 0.302 | $ 0.305 | $ 0.357 | $ 0.351 |
| Weighted Average Units | - Basic | 74,844 | 68,729 | 66,762 | 66,585 | 66,423 | 66,262 | 66,086 | 65,938 |
| | - Diluted | 75,586 | 69,380 | 67,287 | 66,921 | 66,665 | 66,416 | 66,208 | 66,002 |

(1) Includes the results of investment properties owned as at the respective period end.
(2) Not restated for IFRS.
Non-IFRS financial measures are reconciled with IFRS reported amounts in the respective quarterly SEDAR filings.

CAPREIT's operations are affected by seasonal cycles, and operating performance in one quarter may not be indicative of operating performance in any other quarter of the year. The fourth and first quarters of each year tend to typically generate weaker performance due to increased energy consumption during the winter months.

**SECTION VI**

**ACCOUNTING POLICIES AND CRITICAL ESTIMATES**

**Accounting Policies and New Accounting Standards**

CAPREIT adopted IFRS effective January 1, 2010 and the full impact of the change from Canadian GAAP to IFRS is described in the Adoption of IFRS section in addition to the comprehensive discussion under the International Financial Reporting Standards section of the MD&A contained in CAPREIT's 2010 Annual Report.

As of May 9, 2011, the following new or amended IFRS have been issued by the International Accounting Standards Board and are expected to apply for fiscal periods beginning after December 31, 2011: IFRS 1, First-time Adoption of International Financial Reporting Standards; IFRS 7, Financial Instruments: Disclosures; IFRS 9, Financial Instruments; and IAS 12, Income Taxes.

Amendments to IFRS 1 relate to severe hyperinflation environment as well as remove fixed dates for first-time adopters. Amendments to IFRS 7 relate to disclosures with respect to the transfers of financial assets. The new IFRS 9 replaces the current IAS 39 and introduces new requirements for the classification and measurement of financial assets, to be measured at either amortized cost or fair value. The amendments to IAS 12 provide a solution to the issue of assessing whether the recovery of the carrying value of an asset will be through use or through sale when the asset is measured

using the fair value model. The amendment introduces the presumption that recovery of the carrying amount will, normally be through sale. Management is assessing the impact of the above changes but does not expect CAPREIT to be significantly impacted upon adoption in their current form.

**Critical Estimates**

In preparing the accompanying unaudited consolidated interim financial statements in accordance with IFRS, certain accounting policies require the use of estimates, assumptions and judgment that in some cases relate to matters that are inherently uncertain, and which affect the amounts reported in the unaudited consolidated interim financial statements and accompanying notes. Areas of such estimation include, but are not limited to: valuation of investment properties, remeasurement at fair value of financial instruments, valuation of accounts receivable, capitalization of costs, accounting accruals, the amortization of certain assets, accounting for deferred income taxes and Unit-based compensation liabilities. Changes to estimates and assumptions may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited consolidated interim financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could also differ from those estimates under different assumptions and conditions.

Management believes the nature of the business and CAPREIT's portfolio is defensive against economic downturns and, therefore, the current economic conditions have not had as significant an impact on CAPREIT's critical accounting estimates as may have been realized in other industries. However, the current economic conditions impacting the general economy or those more specific to the housing industry or to CAPREIT could have the potential to alter accounting estimates and could impact CAPREIT's financial condition, changes in financial condition or results of operations. Disclosures in the MD&A, including specifically the Property Portfolio, Results of Operations, Property Capital Investments, Liquidity and Financial Condition and Future Outlook sections, outline the risks and both the positive and negative impacts on CAPREIT's performance that have resulted, or may in the future result, from the unusual economic conditions.

During the three months ended March 31, 2011, there were notable changes in the types of assumptions and the nature of estimates deemed by Management to be significant to CAPREIT as a result of the adoption of IFRS. Estimates deemed by Management to be more significant, due to subjectivity, are discussed below.

Valuation of Investment Properties

Investment properties are measured at fair value as at the balance sheet date. Any changes in the fair value are included in the consolidated statements of income and comprehensive income. Fair values are supported by independent external valuations or detailed internal valuations using market-based assumptions, each in accordance with recognized valuation techniques. The techniques used comprise both the capitalized net operating income method and the discounted cash flow method and include estimating, among other things, future stabilized net operating income, capitalization rates, reversionary capitalization rates, discount rates and other future cash flows applicable to investment properties.

In the case of Leasehold Interests, CAPREIT established the fair value of such interests using the discounted cash flow method excluding any future lease payments. A separate liability was recognized for the present value of future lease payments related to these Leasehold Interests. Management's internal assessments of fair value are based on a combination of internal financial information and external market data including components of net operating income and capitalization rates all of which are obtained from an independent appraiser.

Management's internal valuations and the independent appraisals are both subject to significant judgment, estimates and assumptions about market conditions in effect as at the balance sheet date. See note 9 to the accompanying unaudited consolidated interim financial statements for a detailed discussion of valuation methods and the significant assumptions and estimates used.

Valuation of Unit-based Compensation Liabilities

The fair value of Unit-based compensation liabilities are based on assumptions of future events and involve significant estimates. The basis of valuation for CAPREIT's Unit-based compensation liabilities, such as market assumptions, estimates and valuation methodology, is set out in note 16 to the accompanying unaudited consolidated interim financial statements, however, the fair values as at the reporting date may differ materially from how they are ultimately recognized if there is volatility in Trust Unit prices, interest rates or other key assumptions in future periods.

Valuation of Derivative Financial Instruments

The fair value of a derivative financial instrument is based on assumptions of future events and involve significant estimates. The basis of valuation for CAPREIT's derivatives is set out in note 17 to the accompanying unaudited consolidated interim financial statements, however, the fair values of derivatives reported may differ from how they are ultimately recognized if there is volatility in interest rates or energy prices in future periods.

## ADOPTION OF IFRS

As outlined earlier, CAPREIT adopted IFRS for financial reporting purposes with effect from January 1, 2010. The change from Canadian GAAP to IFRS had a significant impact on certain components of CAPREIT's consolidated balance sheets and consolidated statements of income and comprehensive income as well as to the presentation of the consolidated statement of cash flows as a result of necessary reclassifications under IFRS. In addition to the disclosures in notes 4 and 5 in the accompanying unaudited consolidated interim financial statements, discussed below are further details of the impact of IFRS on CAPREIT's financial results. This section should be read in conjunction with the disclosures in the International Financial Reporting Standards section of the MD&A contained in CAPREIT's 2010 Annual Report.

### Consolidated Balance Sheet

The following tables quantify the impact of the significant differences, with the exception of current and non-current classifications, between Canadian GAAP and IFRS on CAPREIT's consolidated balance sheets as at January 1, 2010 and December 31, 2010:

| **As at January 1, 2010 ($ Thousands)** | **Canadian GAAP** | Investment Properties | Exchangeable Units | Unit-Based Compensation | Other Adjustments | **IFRS** |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Investment Properties | $ 2,207,806 | $ 746,921 | $ – | $ – | $ (3,080) | $ 2,951,647 |
| Other Assets | 71,973 | (2,236) | – | – | (25,029) | 44,708 |
| **Total Assets** | $ 2,279,779 | $ 744,685 | $ – | $ – | $ (28,109) | $ 2,996,355 |
| | | | | | | |
| **Liabilities** | | | | | | |
| Liabilities Associated with Investment Properties | $ – | $ 50,662 | $ – | $ – | $ – | $ 50,662 |
| Mortgages Payable | 1,545,315 | – | – | – | (28,109) | 1,517,206 |
| Bank Indebtedness | 146,891 | – | – | – | – | 146,891 |
| Unit-Based Compensation Liabilities | – | – | – | 10,077 | – | 10,077 |
| Deferred Income Tax Liability | 54,059 | 386,448 | – | – | – | 440,507 |
| Other Liabilities | 51,515 | (192) | 37 | – | – | 51,360 |
| Security Deposits | 18,624 | – | | – | – | 18,624 |
| Exchangeable Units | – | – | 5,783 | – | – | 5,783 |
| Distributions Payable | 6,191 | – | (37) | – | – | 6,154 |
| Total Liabilities | $ 1,822,595 | $ 436,918 | $ 5,783 | $ 10,077 | $ (28,109) | $ 2,247,264 |
| | | | | | | |
| **Unitholders' Equity** | | | | | | |
| Unit Capital | $ 889,237 | $ – | $ (8,000) | $ (10,163) | $ – | $ 871,074 |
| Retained Earnings | (409,699) | 309,837 | 2,217 | 86 | – | (97,559) |
| AOCL | (22,354) | (2,070) | – | – | – | (24,424) |
| **Total Untiholders' Equity** | $ 457,184 | $ 307,767 | $ (5,783) | $ (10,077) | $ – | $ 749,091 |
| **Total Liabilities and Equity** | $ 2,279,779 | $ 744,685 | $ – | $ – | $ (28,109) | $ 2,996,355 |

| As at December 31, 2010 ($ Thousands) | Canadian GAAP | Investment Properties | Exchangeable Units | Unit-Based Compensation | Other Adjustments | IFRS |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Investment Properties | $ 2,267,859 | $ 842,073 | $ – | $ – | $ (3,384) | $ 3,106,548 |
| Other Assets | 85,561 | (2,662) | – | – | (27,450) | 55,449 |
| **Total Assets** | $ 2,353,420 | $ 839,411 | $ – | $ – | $ (30,834) | $ 3,161,997 |
| | | | | | | |
| **Liabilities** | | | | | | |
| Liabilities associated with Investment Properties | $ – | $ 56,568 | $ – | $ – | $ – | $ 56,568 |
| Mortgages Payable | 1,633,861 | – | – | – | (30,834) | 1,603,027 |
| Bank Indebtedness | 39,358 | – | – | – | – | 39,358 |
| Unit-Based Compensation Liabilities | – | – | – | 16,410 | – | 16,410 |
| Other Liabilities | 58,194 | (214) | 37 | – | – | 58,017 |
| Security Deposits | 19,227 | – | – | – | – | 19,227 |
| Exchangeable Units | – | – | 7,050 | – | – | 7,050 |
| Distributions Payable | 6,932 | – | (37) | – | – | 6,895 |
| Total Liabilities | $ 1,757,572 | $ 56,354 | $ 7,050 | $ 16,410 | $ (30,834) | $ 1,806,552 |
| | | | | | | |
| **Unitholders' Equity** | | | | | | |
| Unit Capital | $ 1,027,156 | $ – | $ (8,000) | $ (11,885) | $ – | $ 1,007,271 |
| Retained Earnings | (420,223) | 783,057 | 950 | (4,525) | – | 359,259 |
| AOCL | (11,085) | – | – | – | – | (11,085) |
| **Total Unitholders' Equity** | 595,848 | $ 783,057 | $ (7,050) | $ (16,410) | $ – | $ 1,355,445 |
| **Total Liabilities and Equity** | $ 2,353,420 | $ 839,411 | $ – | $ – | $ (30,834) | $ 3,161,997 |

Investment Properties

Under Canadian GAAP, investment properties were identified as income properties and were presented at historical cost less accumulated depreciation. Under IFRS, investment properties are those properties held to earn rental income, for capital appreciation or both and are initially recognized at cost. Subsequent to initial recognition, CAPREIT has elected to measure its investment properties using the fair value model instead of the cost model. As a result, changes in fair value are recognized for each reporting period in the consolidated statement of income. Additionally, corporate head office assets, such as leasehold improvements, corporate and information technology systems, are disclosed in the notes to the accompanying unaudited consolidated interim balance sheets under property, plant and equipment.

As a result of the use of the fair value model, there is a material increase in the carrying value of the investment properties as compared to Canadian GAAP. This translates into an equivalent increase in retained earnings at each reporting date. Marking-to-market resulted in a carrying value, net of the associated liabilities, for CAPREIT's investment properties of approximately $2,901 million as at January 1, 2010, which is approximately $693 million greater than the depreciated cost of $2,208 million reported under Canadian GAAP. As at December 31, 2010, marking-to-market resulted in a carrying value, net of the associated liabilities, for the investment properties of approximately $3,050 million, or approximately $782 million greater than the depreciated cost of $2,268 million reported under Canadian GAAP. With the relative increase in the value of the assets to the liabilities, which did not increase as significantly, certain of CAPREIT's leverage ratios are favourably impacted as a result of the adoption of IFRS.

Additionally, CAPREIT has separately disclosed the fair value of its liability associated with remaining minimum lease payments on the land leasehold interests.

Under IFRS, straight-line rent, direct leasing costs and tenant inducements balances will be included in the carrying amounts of investment properties and the intangible assets and liabilities previously recognized under Canadian GAAP in connection with business combinations are no longer separately recognized under IFRS from the associated investment property.

The increase in the carrying value of CAPREIT's investment properties of approximately $693 million under IFRS from applying the fair value model results in an associated increase in the deferred tax liability as at January 1, 2010 and

March 31, 2010 due to the larger timing differences between the carrying values and the tax bases on the respective reporting dates. Under IFRS, the timing difference is calculated using the income tax rate applicable to inter vivos trusts such as CAPREIT as opposed to the SIFT tax rate that was used in calculating the deferred income tax liability under Canadian GAAP.

As discussed under the Net Income section, CAPREIT satisfied the REIT Exception under the SIFT Rules during the fourth quarter of 2010 and thus is not presently liable for income tax under Part I of the Tax Act. The deferred tax liability under IFRS was reversed during the fourth quarter of 2010.

Exchangeable Units

Exchangeable Units, categorized under Canadian GAAP as equity, are considered a financial liability under IFRS. As these Units are considered to have embedded derivatives, CAPREIT has reported these Exchangeable Units at their fair value at each reporting date. At the date of transition, an adjustment to opening retained earnings for the difference between cost and fair value at the transition date has been recognized and the cumulative distributions on these Exchangeable Units have been reclassified from equity to retained earnings.

Unit-Based Compensation Financial Liabilities

Under Canadian GAAP, all of CAPREIT's Unit-based incentive plans compensation was accounted for as equity-based instruments upon issuance and included in Unitholders' equity with their associated fair value on the grant date amortized over the respective vesting periods and included in the consolidated statement of income. Under IFRS, by virtue of the redemption clause associated with CAPREIT's Trust Units, Unit-based awards that remain unsettled are deemed financial liabilities and not equity, and must be reported as liabilities at fair value on each reporting date with resulting gains or losses recognized in the consolidated statement of income for the period. At the date of transition, a cumulative adjustment to opening retained earnings was recognized for the difference between the cost, including cumulative distributions on Unit-based incentive awards, and the fair value of these awards at the transition date.

**Consolidated Statement of Income**

The following table and discussion quantifies and describe the impact of significant differences between Canadian GAAP and IFRS on CAPREIT's consolidated statements of income.

| **For The Three Months Ended March 31, 2010 ($ Thousands)** | **Canadian GAAP** | Investment Properties | Exchangeable Units | Unit-Based Compensation | Other | **IFRS** |
|---|---|---|---|---|---|---|
| **Revenue from Investment Properties** | **$ 83,515** | $ 3 | $ – | $ – | $ – | **$ 83,518** |
| Realty Taxes | (11,105) | – | – | – | – | (11,105) |
| Property Operating Costs | (28,778) | 8 | – | – | – | (28,770) |
| **Net Operating Income** | **$ 43,632** | $ 11 | $ – | $ – | $ – | **$ 43,643** |
| Trust Expenses | (2,948) | – | – | 325 | – | (2,623) |
| Fair Value Adjustment - Investment Properties | – | (8,364) | – | – | – | (8,364) |
| Fair Value Adjustment - Exchangeable Units | – | – | (119) | – | – | (119) |
| Unit-Based Compensation Costs | – | | – | (684) | – | (684) |
| Interest on Mortgages Payable | (19,239) | – | – | – | (337) | (19,576) |
| Interest on Bank Indebtedness | (1,479) | – | – | – | – | (1,479) |
| Interest on Exchangeable Units | – | – | (111) | – | – | (111) |
| Other Income | 462 | – | – | – | – | 462 |
| Net Loss on Natural Gas Contracts | (4,497) | – | – | – | – | (4,497) |
| Severance and Other Termination Costs | (150) | – | – | – | – | (150) |
| Depreciation | (20,571) | 20,571 | – | – | – | – |
| Amortization | (896) | (92) | – | – | 337 | (651) |
| Unrealized Loss on Derivatives | (54) | – | – | – | – | (54) |
| Recovery of Deferred Income Taxes | 950 | 3,925 | – | – | – | 4,875 |
| **Net (Loss) Income** | **$ (4,790)** | 16,051 | (230) | (359) | – | **$ 10,672** |

| **For The Year Ended December 31, 2010 ($ Thousands)** | **Canadian GAAP** [1] | Investment Properties | Exchangeable Units | Unit-Based Compensation | Other | **IFRS** |
|---|---|---|---|---|---|---|
| **Revenue from Investment Properties** | **$ 339,023** | $ (64) | $ – | $ – | $ – | **$ 338,959** |
| Realty Taxes | (43,438) | – | – | – | – | (43,438) |
| Property Operating Costs | (105,234) | 52 | – | – | – | (105,182) |
| **Net Operating Income** | **$ 190,351** | $ (12) | $ – | $ – | $ – | **$ 190,339** |
| Trust Expenses | (14,012) | – | – | 1,721 | – | (12,291) |
| Fair Value Adjustment - Investment Properties | – | 21,858 | – | – | – | 21,858 |
| Realized Gain on Dispositions | 11,688 | (16,629) | – | – | – | (4,941) |
| Fair Value Adjustment - Exchangeable Units | – | – | (1,267) | – | – | (1,267) |
| Unit-Based Compensation Costs | – | – | – | (7,502) | – | (7,502) |
| Interest on Mortgages Payable | (78,068) | – | – | – | (2,032) | (80,100) |
| Interest on Bank Indebtedness | (6,304) | – | – | – | – | (6,304) |
| Interest on Exchangeable Units | - | – | (444) | – | – | (444) |
| Other Income | 1,854 | – | – | – | – | 1,854 |
| Net Loss on Natural Gas Contracts | (4,497) | – | – | – | – | (4,497) |
| Severance and Other Termination Costs | (736) | – | – | – | – | (736) |
| Depreciation | (83,999) | 83,999 | – | – | – | - |
| Amortization | (4,137) | (375) | – | – | 2,032 | (2,480) |
| Unrealized Loss on Derivatives | (174) | – | – | – | – | (174) |
| Recovery of Deferred Income Taxes | 51,355 | 384,378 | – | – | – | 435,733 |
| **Net Income** | **$ 63,321** | $ 473,219 | $ (1,711) | $ (5,781) | $ – | **$ 529,048** |

(1) Includes results of operations of all properties including those disposed during the year.

Investment Properties

The measurement of investment properties using the fair value model requires the recognition in the consolidated statement of income of an unrealized gain or loss arising from a change in the fair value of investment properties in the period. Also, under the fair value model, depreciation of investment properties is not recorded nor is amortization of the historic intangible balances established under Canadian GAAP in respect of business combinations, all of which are no longer to be separately recognized and accordingly not amortized under IFRS. As a result, CAPREIT recorded an unrealized loss on the remeasurement of its investment properties for the three months ended March 31, 2010 and an unrealized gain for the year ended December 31, 2010. As well, depreciation and amortization recorded under Canadian GAAP was eliminated and there was a corresponding increase in income as a result.

Exchangeable Units

As a result of the classification of Exchangeable Units as financial liabilities being reported at fair value, distributions on these Units are now reported as interest expense instead of accounted for as a component of equity. Additionally, the impact of the remeasurement at fair value of these Units subsequent to the transition date is recognized in the consolidated statement of income for the period.

Unit-Based Compensation Liabilities

The effect of awards under Unit-based compensation plans being deemed liabilities under IFRS has the following significant impacts on the statement of income:

i) *Amortization of grant date fair value*: under IFRS, where a grant is comprised of separate tranches identified by distinct vesting dates, each tranche is deemed a separate grant, and the fair value of each tranche is amortized over its distinct vesting period. Under Canadian GAAP, the fair value of Unit-based compensation is amortized on a combined straight-line basis over the vesting period. This change in amortization methodology increases the amount of Unit-based compensation expense recognized in the initial year of grant and in the earlier portion of the vesting period compared under Canadian GAAP.

ii) *Fair value remeasurement of awards that remain unsettled*: the recognition of the underlying Trust Units as financial liabilities for the purposes of Unit-based compensation necessitates the remeasurement at fair value of all unsettled award Units at each reporting date. Additionally, remeasurement at fair value takes into account the additional impact of distributions on the original awards, which were not required to be expensed under Canadian GAAP.

iii) *Distributions earned/reinvested*: under the RUR Plan and the DUP are reported at fair value and accounted for as part of Unit-based compensation expense whereas under Canadian GAAP they were accounted for as regular distributions.

iv) *Forfeitures*: under IFRS, expected forfeitures are required to be estimated and recognized in the current period, with revisions for actual forfeitures in subsequent periods, however, under Canadian GAAP, forfeitures were recognized as they occurred. Based on historical trends, Management does not expect estimates of forfeitures to have a significant impact on Unit-based compensation expense.

**Key Financial Covenants**

The key covenants under CAPREIT's DOT and Credit Facilities have also been affected by the adoption of IFRS and are discussed below.

Declaration of Trust

The pro forma total debt to gross book value leverage ratio as of January 1, 2010 improves to 55.42% based on carrying values under IFRS compared to CAPREIT's stated leverage ratio of 62.75% based on carrying values under Canadian GAAP. Similarly, the pro forma leverage ratio as of December 31, 2010 improves to 51.80% based on carrying values under IFRS compared to 58.87% based on carrying values under Canadian GAAP. These ratios are well below the borrowing restrictions under the DOT, which requires the total debt to gross book value ratio not to exceed 70%.

Credit Facilities

Under the current definition of EBITDA as defined in the Credit Facilities, all significant impacts of the adoption of IFRS as noted above are accounted for and, therefore, no amendments are needed to the calculation of EBITDA. At present, the various fair value adjustments as described above as well as certain other non-cash or unusual items are excluded from the definition of EBITDA per the Credit Facilities agreement and consequently, the adoption of IFRS has not had a significant impact on Debt Service and Interest Coverage ratios (see the Capital Structure section).

The definition of Tangible Net Worth was amended in the Credit Facilities agreement in light of the changes expected under IFRS. When reporting under Canadian GAAP, the sum of accumulated depreciation and amortization was added back to Unitholder's equity, while under IFRS, Unitholders' equity would take into account investment properties at fair value and therefore mitigates the effect of not adding back accumulated depreciation and amortization. Under IFRS, Tangible Net Worth is generally equal to Unitholders' Equity adjusted for any deferred income tax liability of up to $100 million. The required minimum Tangible Net Worth of $700 million remains unchanged at present.

## CONTROLS AND PROCEDURES

CAPREIT maintains appropriate information systems, procedures and controls to provide reasonable assurance that information disclosed externally is complete, reliable and timely. Pursuant to the Canadian Securities Administrators requirements under National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings, CAPREIT's President and CEO and the Chief Financial Officer have satisfied themselves that as at March 31, 2011, the design of disclosure controls and procedures and the design of internal controls over financial reporting continue to be appropriate.

Over the course of the last two years, as policies were developed in relation to reporting under IFRS, internal controls and financial reporting and disclosure considerations were evaluated as well. Management has designed an adequate and appropriate controls framework for the fair value assessment processes required for reporting under IFRS to ensure values reported accurately reflect market conditions. For the fair value assessment process of investment properties and Unit-based compensation, these controls include a comprehensive review of the assumptions and estimates, including those used by the independent appraiser or third-party on an annual basis, as well as multiple levels of reviews of such key assumptions and data within CAPREIT by Management with final approval by the Board of Trustees on an interim and annual basis.

CAPREIT did not make any other changes to the design of internal controls over financial reporting during the three months ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, the internal controls over financial reporting.

It should be noted that a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. The design of any system of controls is also based in part on certain assumptions about the likelihood of future events, and there can be no assurances that any design will succeed in achieving its stated goals under all potential conditions.

## SECTION VII

## RISKS AND UNCERTAINTIES

There are certain risks inherent in an investment in the Units and the activities of CAPREIT, which investors should carefully consider before investing in Units. Risks and uncertainties in addition to those discussed below are disclosed in CAPREIT's 2010 Annual Report and in CAPREIT's latest Annual Information Form.

### Reporting Investment Property at Fair Value

CAPREIT holds investment property to earn rental income or for capital appreciation or both. All investment property is measured using the fair value model whereby changes in fair value are recognized for each reporting period in the consolidated statement of income. Management values each investment property based on the most probable price that a property should be sold for in a competitive and open market as of the specified date under all conditions requisite to a fair sale, such as the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Each investment property has been valued on a highest and best use basis.

There is a risk that general declines in real estate markets or sale of assets by CAPREIT under financial or other hardship would impact the fair values reported, or the cash flows associated with owning or disposing such properties. Market assumptions applied for valuation purposes do not necessarily reflect CAPREIT's specific history or experience and the conditions for realizing the fair values through a sale may change or may not be realized. Consequently, there is a risk that the actual fair values may differ, and the differences may be material. In addition, there is an inherent risk related to the reliance on and use of a single appraiser, as this approach may not adequately capture the range of fair values that market participants would assign to the investment properties. CAPREIT mitigates this risk by undertaking a detailed review of the assumptions utilized in valuing the properties, including comparing the assumptions to the benchmarks derived from CAPREIT's own observations of market transactions. Certain ratios and covenants could be negatively affected by downturns in the real estate market and could significantly impact CAPREIT's operating revenues, cash flows as well as the fair values of the investment properties.

## RELATED PARTY TRANSACTIONS

For the three months ended March 31, 2011, CAPREIT paid construction management fees of $0.3 million (based on 4.5% of construction costs up to $20.0 million, 3.0% for the next $15.0 million and 1.0% thereafter) in consideration for construction management services provided by a company owned by two trustees and officers of CAPREIT in connection with the capital investment programs for the properties.

CAPREIT leases office space with a company in which one of the trustees and officers has an 18% beneficial interest. The rent paid for the office space (which is based on fair market rents at the date the lease was entered into) for the three months ended March 31, 2011 was $0.2 million including property operating costs, and has been expensed as trust expenses. The lease agreement expires on October 31, 2014 and yearly minimum rental payments are $0.4 million before HST.

## COMMITMENTS AND CONTINGENCIES

From time to time, CAPREIT enters into commitments for fixed price natural gas, hydro and land lease agreements as outlined in note 26 to the accompanying unaudited consolidated interim financial statements.

CAPREIT is contingently liable under guarantees provided to certain of CAPREIT's lenders in the event of defaults and with respect to litigation and claims that arise in the ordinary course of business. These matters are generally covered by insurance. In the opinion of Management, any liability that may arise from such contingencies would not be expected to have a material adverse effect on the consolidated financial statements of CAPREIT.

## SECTION VIII

## SUBSEQUENT EVENT

On April 15, 2011, CAPREIT completed the acquisition of a 495-suite portfolio in Richmond and New Westminster, British Columbia. The purchase price was $72.0 million and was funded through new CMHC-insured mortgages totalling $49.4 million, at an effective interest rate of 4.38%, for ten-year terms, maturing on May 1, 2021 and the balance from the Acquisition and Operating Facility.

## FUTURE OUTLOOK

With an improving national economy, Management believes the multi-unit residential rental business will continue to strengthen in the majority of the markets in which CAPREIT operates. As a result, Management expects to generate modest annual increases in overall average monthly rents while stabilizing average occupancies in the range of 97% to 98% on an annual basis. Management also anticipates operating revenues will benefit from programs over the long term to enhance revenues from parking, commercial leases, laundry, cable, telecommunications and other income sources. In addition, numerous successful cost control initiatives have proven effective, which should lead to stable net operating income over this period.

However, as a result of some continued uncertainty in economic conditions in particular regions, CAPREIT may have to account for an increase in bad debt, experience a reduction in occupancy levels in some markets and tenant inducement costs may increase over the short term. CAPREIT believes the strong defensive characteristics of its property portfolio, due to diversification by both geography and property type, will serve to mitigate some of the negative impact of the unfavourable economic conditions that certain regions are experiencing or may experience. CAPREIT intends to continue to seek opportunities to further diversify its property portfolio. In addition, CAPREIT may also experience difficulty in obtaining long-term financing (i.e., financing for terms of ten years and longer) at acceptable interest rates due to credit market conditions.

In July 2010, the provinces of Ontario and British Columbia harmonized the Federal Goods and Services Tax with their respective Provincial Sales Taxes into one HST applied to the majority of goods and services sold in each province. HST has resulted in a modest increase in CAPREIT's operating costs in these provinces, which cannot immediately be passed on to residents in rental rate increases. CAPREIT has identified and implemented procurement practices to mitigate the higher costs, including HST associated savings with the amendment of some fixed priced physical delivery contracts into spot pricing arrangements (see also Harmonization of Federal Goods and Services Tax and Provincial Sales Tax discussion under Risks and Uncertainties section in CAPREIT's 2010 Annual Report).

In addition, CAPREIT has defined a number of strategies to capitalize on its strengths and achieve its objectives of providing Unitholders with stable and predictable monthly cash distributions while growing distributions and Unit value over the long term.

First, Management will maintain its focus on maximizing occupancy and average monthly rents in accordance with local conditions in each of its markets. Since its inception in May 1997, CAPREIT's hands-on management style, focus on

resident communications and capital investment programs aimed at increasing the long-term value of its properties have contributed to a strong track record of stable portfolio occupancy and average monthly rents.

A significant part of managing CAPREIT's annual rental increases is determined by the annual guideline increases established by certain provincial governments under rent control legislation that CAPREIT must adhere to in setting annual rental rates for renewing tenants. In the Province of Ontario, the guideline increase for 2011 is 0.7%, which compares unfavourably to the 2.1% guideline increase for 2010. The Ontario rent control legislation provides that landlords may apply to the Landlord and Tenant Board (the "Board") to raise rents by more than the approved annual guideline. The Board can allow such an above guideline increase ("AGI") for: (i) eligible capital expenditures; (ii) unusually high increases in property taxes and/or utility costs; and (iii) increases in eligible security costs. The maximum AGI permitted in connection with eligible capital expenditures is three percent per year to a maximum of nine percent over a three-year period. These same limitations do not apply to AGI applications related to unusually high increases in property taxes and/or utilities, or increases in eligible security costs.

In line with its focus to maximize average monthly rents, CAPREIT has begun pursuing above guideline increases where appropriate and to this effect, has filed 90 applications as of March 31, 2011 for completed property capital investments and/or unusually high increases in realty taxes as well as one application relating to an unusually high increase in water costs. In addition, CAPREIT continues to assess the viability of a number of additional AGI applications. The impact of these AGI applications could be significant at the property level, however, it is presently indeterminable due to the inherent uncertainties associated with the adjudication process and the impact of tenant turnover at the affected properties.

The following table summarizes the status of AGI applications filed by CAPREIT as of March 31, 2011:

| | **Number of Applications** | **Number of Impacted Suites and Sites** | **Weighted Average Annual AGI (%)** (1) | **Weighted Average Number of Years** (1),(2) |
|---|---|---|---|---|
| Filed | 91 | 13,602 | 1.9% | 1.4 |
| Withdrawn | (7) | (1,436) | 0.4% | 1.0 |
| Settled | (29) | (3,942) | 2.7% | 1.3 |
| Outstanding | 55 | 8,224 | 1.7% | 1.5 |

(1) Weighted by number of impacted suites and sites.
(2) Represents the number of years over which the AGI application is expected to apply.

Second, Management will continue to focus on reducing its operating costs as a percentage of total revenues. Management is investing in various environment-friendly and energy-saving initiatives including energy-efficient boilers and lighting systems, and is evaluating all energy-purchasing programs to reduce or stabilize overall net energy costs.

Third, Management will continue to direct its efforts on its building infrastructure improvement programs to upgrade properties across the portfolio and to reposition the portfolio by completing value-enhancing capital investments. These investments are expected to enhance the life safety of residents, improve the portfolio's long-term cash flow generating potential and increase its useful life over the long term.

Fourth, CAPREIT will continue to prudently focus on accretive acquisitions that meet its strategic criteria and enhance CAPREIT's geographic diversification. From time to time, CAPREIT will also identify certain non-core assets for sale that do not conform to its current portfolio composition or operating strategies. Management believes the realization and reinvestment of capital are fundamental components of its growth strategy and demonstrate the success of its investment programs.

Fifth, CAPREIT will continue to effectively manage interest costs by leveraging its balance sheet strength and the stability of its property portfolio to reduce borrowings on its credit facilities, while appropriately staggering the maturity dates within its mortgage portfolio to ensure it is not exposed in any one year to a refinancing risk. Management believes that because of the continuing availability of financing insured by CMHC that is at lower cost than is currently available under conventional mortgages, CAPREIT is well positioned to meet its financing and refinancing objectives at reasonable costs over the medium term.

CAPREIT will continue to maintain its conservative approach to its capital structure, leverage and coverage ratios and strive to further improve its distribution payout ratio. Management believes its successful equity financing and mortgage refinancing programs have resulted in CAPREIT possessing one of the strongest balance sheets in its industry, well suited to delivering consistent, stable and secure monthly cash distributions over the long term.

CAPREIT

**CONSOLIDATED FINANCIAL STATEMENTS**
**FOR THE THREE MONTHS ENDED**
**MARCH 31, 2011**
**(Unaudited)**

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## CONSOLIDATED BALANCE SHEETS

(Unaudited - CAD$ Thousands)

| As at | Note | March 31, 2011 | December 31, 2010 | January 1, 2010 |
|---|---|---|---|---|
| **Non-Current Assets** | | | | |
| Investment properties | 5, 9 | **$ 3,117,288** | $ 3,106,548 | $ 2,951,647 |
| Other non-current assets | 10 | **40,438** | 40,307 | 35,060 |
| | | **3,157,726** | 3,146,855 | 2,986,707 |
| **Current Assets** | | | | |
| Other current assets | 10 | **16,900** | 10,792 | 9,648 |
| Cash and cash equivalents | | **–** | 4,350 | – |
| | | **16,900** | 15,142 | 9,648 |
| | | **$ 3,174,626** | $ 3,161,997 | $ 2,996,355 |
| **Non-Current Liabilities** | | | | |
| Liabilities associated with investment properties | 5, 9 | **$ 56,568** | $ 56,568 | $ 50,662 |
| Mortgages payable | 12 | **1,389,761** | 1,323,534 | 1,309,072 |
| Bank indebtedness | 13 | **58,160** | 38,000 | 144,816 |
| Unit-based compensation financial liabilities | 14 | **591** | 355 | – |
| Other non-current liabilities | 11 | **725** | 1,095 | 1,924 |
| Deferred income tax liability | 20 | **–** | – | 440,507 |
| | | **1,505,805** | 1,419,552 | 1,946,981 |
| **Current Liabilities** | | | | |
| Mortgages payable | 12 | **215,516** | 279,493 | 208,134 |
| Bank indebtedness | 13 | **1,202** | 1,358 | 2,075 |
| Unit-based compensation financial liabilities | 14 | **20,868** | 16,055 | 10,077 |
| Accounts payable and accrued liabilities | | **34,862** | 45,913 | 40,908 |
| Other current liabilities | 11 | **10,229** | 11,226 | 8,752 |
| Security deposits | | **19,458** | 19,227 | 18,624 |
| Exchangeable Units | 14 | **8,004** | 7,050 | 5,783 |
| Distributions payable | | **6,708** | 6,678 | 5,930 |
| | | **316,847** | 387,000 | 300,283 |
| | | **$ 1,822,652** | $ 1,806,552 | $ 2,247,264 |
| **Unitholders' Equity** | | | | |
| Unit Capital | | **$ 1,013,038** | $ 1,007,271 | $ 871,074 |
| Accumulated other comprehensive loss | 21 | **(9,893)** | (11,085) | (24,424) |
| Retained earnings | | **348,829** | 359,259 | (97,559) |
| | | **$ 1,351,974** | $ 1,355,445 | $ 749,091 |
| | | **$ 3,174,626** | $ 3,161,997 | $ 2,996,355 |

*See accompanying notes to consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Unaudited - CAD$ Thousands)

| For The Three Months Ended March 31, | Note | 2011 | 2010 |
|---|---|---|---|
| **Operating Revenues** | | | |
| Revenue from investment properties | | **$ 86,332** | $ 83,518 |
| **Operating Expenses** | | | |
| Realty taxes | | **11,026** | 11,105 |
| Property operating costs | | **28,742** | 28,770 |
| | | **39,768** | 39,875 |
| **Income Before the Undernoted** | | **46,564** | 43,643 |
| Trust expenses | | **3,605** | 2,623 |
| Unit-based compensation expenses | 16 | **5,801** | 684 |
| Fair value adjustments of investment properties | 9 | **5,461** | 8,364 |
| Realized loss on disposition of investment properties | 8 | **95** | – |
| Net loss on natural gas contracts | 18 | **–** | 4,497 |
| Severance and other employee termination costs | 22 | **–** | 150 |
| **Operating Income Before the Undernoted** | | **31,602** | 27,325 |
| Amortization | 23 | **647** | 651 |
| Fair value adjustments of Exchangeable Units | 14 | **954** | 119 |
| Unrealized loss on derivative financial instruments | 18 | **156** | 54 |
| Interest on mortgages payable | | **19,788** | 19,576 |
| Interest on bank indebtedness | | **748** | 1,479 |
| Interest on Exchangeable Units | | **111** | 111 |
| Other income | | **(465)** | (462) |
| **Income Before Taxes** | | **9,663** | 5,797 |
| Recovery of deferred income taxes | 20 | **–** | 4,875 |
| **Net Income** | | **$ 9,663** | $ 10,672 |
| | | | |
| **Other Comprehensive Income** | | | |
| Amortization of losses in AOCL to interest on mortgages payable | 21 | **$ 264** | $ 274 |
| Gain on interest rate swap agreements | 18 | **906** | 706 |
| Gain on natural gas derivatives | | **141** | – |
| Loss on amounts designated as cash flow hedges settled in prior years and transferred to interest on mortgages payable | 18 | **(20)** | (33) |
| Unrealized loss on change in fair value of investments | | **(99)** | (1,717) |
| Recovery of deferred income taxes | 20 | **–** | 7 |
| **Other Comprehensive Income (Loss)** | | **$ 1,192** | $ (763) |
| **Comprehensive Income** | | **$ 10,855** | $ 9,909 |

*See accompanying notes to consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF UNITHOLDERS' EQUITY

(Unaudited - CAD$ Thousands)

| | Note | Unit Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Total |
|---|---|---|---|---|---|
| **Unitholders' Equity, January 1, 2011** | | **$ 1,007,271** | **$ 359,259** | **$ (11,085)** | **$ 1,355,445** |
| Unit Capital | | | | | |
| New Units issued | 14 | 366 | – | – | 366 |
| Distribution Reinvestment Plan | 14 | 3,710 | – | – | 3,710 |
| Unit Option Plan | 14, 16 | 1,609 | – | – | 1,609 |
| Employee Unit Purchase Plan | 16 | 82 | – | – | 82 |
| | | 5,767 | – | – | 5,767 |
| Retained Earnings and Other Comprehensive Income | | | | | |
| Net Income | | | 9,663 | – | 9,663 |
| Other comprehensive income | | – | – | 1,192 | 1,192 |
| | | – | 9,663 | 1,192 | 10,855 |
| Distributions on Trust Units | | | | | |
| Distributions declared and paid | 15 | – | (13,385) | – | (13,385) |
| Distributions payable | 15 | – | (6,708) | – | (6,708) |
| | | – | (20,093) | – | (20,093) |
| **Unitholders' Equity, March 31, 2011** | | **$ 1,013,038** | **$ 348,829** | **$ (9,893)** | **$ 1,351,974** |

| | Note | Unit Capital | Retained Earnings | Accumulated Other Comprehensive Loss | Total |
|---|---|---|---|---|---|
| **Unitholders' Equity, January 1, 2010** | | **$ 871,074** | **$ (97,559)** | **$ (24,424)** | **$ 749,091** |
| Unit Capital | | | | | |
| Distribution Reinvestment Plan | 14 | 1,811 | – | – | 1,811 |
| Employee Unit Purchase Plan | 16 | 66 | – | – | 66 |
| | | 1,877 | – | – | 1,877 |
| Retained Earnings and Other Comprehensive Loss | | | | | |
| Net Income | | | 10,672 | – | 10,672 |
| Other comprehensive loss | | – | – | (763) | (763) |
| | | – | 10,672 | (763) | 9,909 |
| Distributions on Trust Units | | | | | |
| Distributions declared and paid | 15 | – | (11,870) | – | (11,870) |
| Distributions payable | 15 | – | (5,942) | – | (5,942) |
| | | – | (17,812) | – | (17,812) |
| **Unitholders' Equity, March 31, 2010** | | **$ 872,951** | **$ (104,699)** | **$ (25,187)** | **$ 743,065** |

*See accompanying notes to consolidated financial statements.*

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited - CAD$ Thousands)

| For the Three Months Ended March 31, | Note | 2011 | 2010 |
|---|---|---|---|
| **Cash Provided By (Used In):** | | | |
| **Operating Activities** | | | |
| Net income | | **$ 9,663** | $ 10,672 |
| Items related to operating activities not affecting cash: | | | |
| Fair value adjustment - investment properties | | **5,461** | 8,364 |
| Fair value adjustment - Exchangeable Units | | **954** | 119 |
| Fair value adjustment - utility contracts | | **(10)** | 2 |
| Loss on sale of investment properties | 8 | **95** | – |
| Unrealized loss on derivative financial instruments | 18 | **156** | 54 |
| Net loss on natural gas contracts | 18 | **–** | 4,497 |
| Recovery of deferred income taxes | 20 | **–** | (4,875) |
| Amortization | 23 | **647** | 651 |
| Amortization of loss on derivative financial instruments in AOCL | 21 | **264** | 274 |
| Unit-based compensation expense | | **5,801** | 684 |
| Straight-line rent adjustment | | **(33)** | (29) |
| | | **22,998** | 20,413 |
| Net income items related to financing and investing activities | 24 | **19,246** | 19,883 |
| Changes in non-cash operating assets and liabilities | 24 | **(7,485)** | (8,905) |
| **Cash Provided By Operating Activities** | | **34,759** | 31,391 |
| | | | |
| **Investing Activities** | | | |
| Acquisition of investment properties | 9 | **(9,084)** | (912) |
| Capital investments | 24 | **(23,792)** | (14,029) |
| Disposition of investment properties | 24 | **3,609** | – |
| Change in restricted cash | | **37** | (192) |
| Investment income received | | **465** | 462 |
| **Cash Used In Investing Activities** | | **(28,765)** | (14,671) |
| | | | |
| **Financing Activities** | | | |
| Mortgage financings | | **105,158** | – |
| Mortgage principal repayments | | **(12,461)** | (12,039) |
| Mortgages repaid on maturity | | **(87,964)** | – |
| Financing costs on mortgages payable | | **(186)** | (49) |
| CMHC premiums on mortgages payable | | **(888)** | – |
| Interest paid on mortgages payable | | **(18,537)** | (18,738) |
| Bank indebtedness | | **20,004** | 31,637 |
| Interest paid on bank indebtedness | | **(1,063)** | (1,496) |
| Interest paid on Exchangeable Units | | **(111)** | (111) |
| Proceeds on issuance of Units | 14 | **2,057** | 66 |
| Net cash distributions to Unitholders | 24 | **(16,353)** | (15,990) |
| **Cash Provided By Financing Activities** | | **(10,344)** | (16,720) |
| | | | |
| **Changes in Cash and Cash Equivalents During the Period** | | **(4,350)** | – |
| **Cash and Cash Equivalents, Beginning of Period** | | **4,350** | – |
| **Cash and Cash Equivalents, End of Period** | | **$ –** | $ – |

*See accompanying notes to consolidated financial statements.*

### 1. Organization of the Trust

Canadian Apartment Properties Real Estate Investment Trust ("CAPREIT") owns interests in multi-unit residential rental properties, including apartments, townhomes and manufactured home communities ("MHC") located in and near major urban centres across Canada. CAPREIT's net assets and operating results are derived from real estate located in Canada where it is also domiciled.

CAPREIT converted from a closed-end real estate investment trust to an open-end trust on January 8, 2008, and is governed under the laws of the Province of Ontario by a Declaration of Trust ("DOT") dated February 3, 1997, as most recently amended and restated on November 13, 2009. CAPREIT commenced active operations on February 4, 1997, when it acquired an initial portfolio of properties and became a reporting issuer on May 21, 1997 pursuant to an initial public offering prospectus dated May 12, 1997.

CAPREIT is listed on the Toronto Stock Exchange ("TSX") under the symbol "CAR.UN" and its registered address is 11 Church Street, Suite 401, Toronto, Ontario, Canada M5E 1W1.

### 2. Significant Accounting Policies

#### *a) Statement of compliance*

Beginning January 1, 2011, CAPREIT prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS"). Accordingly, these are CAPREIT's first consolidated interim financial statements prepared under IFRS. For the purposes of these consolidated interim financial statements, the term "Canadian GAAP" refers to Canadian generally accepted accounting principles before the adoption of IFRS.

These consolidated interim financial statements have been prepared in accordance with IFRS applicable to the preparation of consolidated interim financial statements, including IAS 34, Interim Financial Reporting, and IFRS 1, First-time Adoption of IFRS. Subject to certain transition elections discussed in note 4, CAPREIT has consistently applied the same accounting policies in its opening IFRS consolidated balance sheet as at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 4 discloses the impact of the transition to IFRS on CAPREIT's financial performance, Unitholders' equity and consolidated statements of cash flows, including the nature and effect of significant changes in accounting policies from those employed in CAPREIT's consolidated annual financial statements for the year ended December 31, 2010.

These consolidated interim financial statements, which were approved by CAPREIT's board of trustees on May 9, 2011 have been prepared on the basis of IFRS issued and effective, or available for early adoption, as of March 31, 2011. Any subsequent changes to IFRS effective for CAPREIT's consolidated annual financial statements for the year ending December 31, 2011 could result in restatement of these consolidated interim financial statements, including the transition adjustments recognized on changeover to IFRS.

These consolidated interim financial statements should be read in conjunction with CAPREIT's consolidated annual financial statements for the year ended December 31, 2010 prepared in accordance with Canadian GAAP. Note 5 discloses supplementary information under IFRS for the year ended December 31, 2010 that is relevant to an understanding of these consolidated interim financial statements.

#### *b) Basis of presentation*

These consolidated interim financial statements have been prepared on a going concern basis and historical cost basis except for:

i) Investment properties and certain financial instruments, which are stated at fair value;

ii) Certain Unit-based compensation accounts, which are stated at their fair value; and

iii) Non-current assets classified as held-for-sale, which are stated at fair value.

The accounting policies set out below have been applied consistently to all periods presented in these consolidated interim financial statements, including the opening consolidated balance sheet as at January 1, 2010, as required by IFRS 1.

***c) Principles of consolidation***

i) Controlled entities

These consolidated interim financial statements comprise the assets and liabilities of all controlled entities and the results of all controlled entities for the financial period. CAPREIT and its controlled entities are collectively referred to as CAPREIT in these consolidated interim financial statements. Controlled entities are all entities over which CAPREIT has the power to govern the financial and operating policies, generally accompanying ownership of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable are considered when assessing whether CAPREIT controls another entity.

Controlled entities are fully consolidated from the date control commenced and de-consolidated from the date that control ceased.

ii) Co-ownerships

CAPREIT has co-ownership interests in and joint control of a number of properties through unincorporated co-ownerships and through co-ownership entities. CAPREIT's proportionate share of revenues, expenses, assets and liabilities under both types of co-ownership interests are included in their respective descriptions on the consolidated balance sheets and consolidated statements of income and comprehensive income. In general, CAPREIT has recourse against all of the assets of the co-ownerships in the event that CAPREIT is called upon to pay liabilities in excess of its proportionate share.

All balances and effects of transactions between co-ownerships and CAPREIT have been eliminated to the extent of CAPREIT's interest in the co-ownership. Where co-ownerships adopt accounting policies which differ from CAPREIT, adjustments have been made so as to ensure consistency within the reported financial information.

***d) Investment properties***

CAPREIT considers its income properties to be investment properties under IAS 40, Investment Property ("IAS 40"), and has chosen the fair value model to account for its investment properties in the consolidated interim financial statements. Fair value represents the amount at which the properties could be exchanged between a knowledgeable and willing buyer and a knowledgeable and willing seller in an arm's length transaction at the date of valuation.

CAPREIT's investment properties have been valued on a highest and best use basis, but do not include any portfolio premium that may be associated with economies of scale of owning a large portfolio or the consolidation value of having compiled a large portfolio of properties over a long period of time, many through individual property acquisitions.

Investment properties comprise investment interests held in land and buildings (including integral equipment) held for the purpose of producing rental income, capital appreciation, or both. CAPREIT's investments in its property portfolio reflect different forms of property interests, including (i) Fee Simple Interests – Apartments and Townhomes, (ii) Operating Leasehold Interests, (iii) Land Leasehold Interests and (iv) Fee Simple Interests – Manufactured Home Communities Land Lease Sites. These four forms of property interests meet the definition of investment property and are classified and accounted for as such. All investment properties are recorded at their fair value at their respective acquisition dates and are subsequently stated at fair value at each balance sheet date with any gain or loss arising from a change in fair value recognized in the consolidated statements of income and comprehensive income for the period. For Operating Leasehold Interests, all of which are held under a prepaid operating lease, CAPREIT has accounted for all such interests as finance leases, including the fair value of options to purchase and are accounted for and presented as investment property.

Obligations associated with certain investment properties such as future minimum lease payments on land leasehold interests are presented as liabilities separately from the investment property assets.

The fair value of investment properties is determined by a qualified external appraiser annually. Management regularly undertakes a review of its investment property valuation between external appraisal dates to assess the continuing validity of the underlying assumptions such as cash flows, capitalization rates and discount rates. These assumptions are tested against market information obtained from an independent appraiser. Where increases or decreases are warranted, the carrying values of CAPREIT's investment properties are adjusted. See note 3 and note 9 for a detailed discussion of the significant assumptions, estimates and valuation methods used.

***e) Property asset acquisitions***

Identifiable assets acquired and liabilities assumed in an asset acquisition are measured initially at their fair values at the acquisition date. Acquisition-related transaction costs are capitalized to the property.

***f) Presentation of non-current assets classified as held-for-sale***

Investment properties are reclassified to assets held-for-sale when criteria set out in IFRS 5, Non-Current Assets Held-For-Sale and Discontinued Operations, are met. CAPREIT presents non-current assets classified as held-for-sale and their associated liabilities separately from other assets and liabilities on the balance sheet and in the notes beginning from the period in which they were first classified as 'for sale'. The sale of one or a group of investment properties by CAPREIT will generally be presented as non-current asset held-for-sale and not discontinued operations. If a group of assets for sale are considered to meet the definition of a discontinued operation then income or expense recognized in the consolidated statements of income and comprehensive income relating to that group of assets is presented separately from continuing operations. A discontinued operation is a component of operations that represents a separate major line of business or geographical area of operations that has been disposed of or is held-for-sale, or is a subsidiary acquired exclusively with a view to resale.

***g) Property, plant and equipment***

Property, plant and equipment are stated at historical cost less accumulated depreciation and mainly comprise of head office and regional offices leasehold improvements, corporate and information technology systems and are presented within other non-current assets on the consolidated balance sheet. These items are amortized on a straight-line basis over their estimated useful lives ranging from three to five years, or, in the case of leasehold improvements, are amortized over the leasehold improvement lease term ranging from 5 to 15 years.

***h) Tenant inducements***

Incentives such as cash, rent free periods and move-in allowances may be provided to lessees to enter into a lease. These incentives are capitalized and amortized on a straight line basis over the term of the lease as a reduction of rental revenue. The carrying amounts of the tenant inducements are included in the fair value of investment properties.

***i) Financial instruments***

**Financial assets and financial liabilities**

Financial assets and financial liabilities are initially recognized at fair value and are subsequently accounted for based on their classification as described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics and CAPREIT's designation of such instruments. The standards require that all financial assets and financial liabilities be classified as f*air value through profit or loss, loans and receivables, available-for-sale, other liabilities* or *held-to-maturity*.

### Classification of financial instruments

The following summarizes the classification and measurement CAPREIT has elected to apply to each of its significant categories of financial instruments:

| Type | Classification | Measurement |
|---|---|---|
| **Financial assets** | | |
| Cash and cash equivalents | FVTPL | Fair value |
| Restricted cash | FVTPL | Fair value |
| Other receivables | Loans and receivables | Amortized cost |
| Investments | Available-for-sale | Fair value |
| **Financial liabilities** | | |
| Mortgages payable | Other liabilities | Amortized cost |
| Bank indebtedness | Other liabilities | Amortized cost |
| Accounts payable and other liabilities | Other liabilities | Amortized cost |
| Unit-based compensation liabilities | Other liabilities | Amortized cost |
| Security deposits | Other liabilities | Amortized cost |
| Exchangeable Units | Other liabilities | Amortized cost |

**Fair Value Through Profit or Loss ("FVTPL")**
Cash and cash equivalents acquired with the intention of generating profits in the near term, as well as restricted cash held by CAPREIT, are accounted for at fair value. Interest earned or accrued on these financial assets is included in other income. Derivatives are also categorized as FVTPL unless designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Gains and losses arising from changes in fair value are presented in the consolidated statements of income and comprehensive income in the period in which they arise. Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the balance sheet date, which is classified as non-current.

**Loans and receivables**
Such receivables arise when CAPREIT provides services to a third-party, such as a tenant, and are included in current assets, except for those with maturities more than twelve months after the balance sheet date, which are classified as non-current assets. Loans and receivables are included in other assets in the balance sheet and are accounted for at amortized cost.

**Available-for-sale**
Investments are measured at fair value at each balance sheet date and the difference between the fair value of the asset and its cost basis is included in other comprehensive income. Differences included in accumulated other comprehensive loss are transferred to net income when the asset is removed from the balance sheet or an impairment loss on the asset has to be recognized. Income on available-for-sale investments is recognized as earned and included in other income.

**Other liabilities**
Such financial liabilities are recorded at amortized cost and include all liabilities other than derivatives or liabilities, which are designated to be accounted for at fair value.

**Transaction costs**
Transaction costs related to financial assets classified as FVTPL are expensed as incurred. Transaction costs related to loans and receivables and other liabilities are netted against the carrying value of the asset or liability and amortized over the expected life of the instrument using the effective interest rate method or over the amortization period of the

mortgage. Transaction costs relating to *available-for-sale* financial assets are included in the cost of the asset on initial recognition.

**Determination of fair value**
The fair value of a financial instrument on initial recognition is generally the transaction price, which is the fair value of the consideration given or received. Subsequent to initial recognition, the fair value of financial instruments are remeasured based on relevant market data. CAPREIT classifies the fair value for each class of financial instrument based on the fair value hierarchy in accordance with IFRS 7. The fair value hierarchy distinguishes between market value data obtained from independent sources and CAPREIT's own assumptions about market value. See note 17 for a detailed discussion of valuation methods used for financial instruments quoted on an active market and instruments valued using observable data.

**Derivatives**
Derivatives are measured at fair value with changes therein recognized in the consolidated statements of income and comprehensive income in property operating costs or other comprehensive income ("OCI"), except for those contracts that are designated for CAPREIT's own use. Derivatives not part of a hedging relationship are presented as part of other current assets or liabilities and those expected to be realized or paid beyond twelve months of the balance sheet date, are presented under other non-current assets or liabilities.

**Embedded derivatives**
Derivatives embedded in other financial instruments or contracts are separated from their host contracts and accounted for as derivatives when their economic characteristics and risks are not closely related to those of the host contract; the terms of the embedded derivative are the same as those of a free standing derivative; and the combined instrument or contract is not measured at fair value. These embedded derivatives are measured at fair value with changes therein recognized in the consolidated statement of income and comprehensive income.

CAPREIT has concluded the Units outstanding of its subsidiary, CAPREIT Limited Partnership ("CAPLP"), include embedded derivatives under IFRS, and has elected to account for the combined instrument at fair value. As a result, the host and embedded derivatives are presented under the single classification "Exchangeable Units". CAPREIT does not have any other outstanding contracts or financial instruments with embedded derivatives that require bifurcation.

***j) Hedging relationships***

CAPREIT has applied cash flow hedging accounting to certain derivatives, wherein the effective portion of the change in the fair value of the hedging derivative is recognized in OCI, while the ineffective portion is recognized in net income. Should a hedging relationship become ineffective and/or hedge accounting become no longer appropriate, previously unrealized gains and losses remain within accumulated other comprehensive loss ("AOCL") and are amortized to the relevant item in the consolidated statements of income and comprehensive income in the same periods during which the hedged items affect earnings, while future changes in the fair value of the hedging derivatives are recognized in the consolidated statement of income and comprehensive income.

***k) Mortgages payable and bank indebtedness***

Mortgages payable are recognized at amortized cost using the effective interest rate method. Under the effective interest rate method, any transaction fees, costs and discounts directly related to the mortgage are recognized in the consolidated statement of income and comprehensive income over the expected term of the mortgage. Mortgage maturities and repayments due more than twelve months after the balance sheet date are classified as non-current.

Fees and insurance premiums paid to the Canada Mortgage and Housing Corporation ("CMHC") are presented within the non-current portion of mortgages payable. They are amortized over the remaining amortization period of the underlying mortgage loans (initial amortization period is typically 25 to 35 years) and are included in interest expense on mortgages payable in the consolidated statements of income and comprehensive income. Any unamortized amounts are expensed completely when the underlying mortgage loan has been discharged or fully repaid.

***l) Exchangeable Units***

Issued and outstanding Units of CAPLP are exchangeable on demand for Trust Units ("Exchangeable Units"). As the Trust Units are redeemable at the holder's option, the Exchangeable Units are classified as current liabilities. The distributions on the Exchangeable Units are recognized in the consolidated statements of income and comprehensive income as interest expense under IFRS and the interest payable at the reporting date is reported under other current liabilities on the balance sheet. These Exchangeable Units are remeasured at each reporting date at their amortized cost, which approximates fair value as they are considered to be puttable instruments under IAS 32 with changes in the carrying amount recognized in the consolidated statements of income and comprehensive income for the period.

***m) Comprehensive income***

Comprehensive income includes net income and other comprehensive income (loss). Other comprehensive income (loss) includes changes in the fair value of investments and the effective portion of cash flow hedges less any amounts reclassified to mortgage interest expense in the period.

***n) Accumulated Other Comprehensive Loss ("AOCL")***

AOCL is included in the consolidated balance sheet as Unitholders' Equity and includes the unrealized gains and losses of the changes in the fair market value of cash flow hedges, derivatives and investments. The components of accumulated other comprehensive loss are disclosed in note 21.

***o) Revenue recognition***

CAPREIT recognizes rental revenue using the straight-line method whereby the total amount of rental revenue to be received from all leases is accounted for on a straight-line basis over the term of the related leases. The difference between the rental revenue recognized and the amounts contractually due under the lease agreements are accrued as rent receivable, which is included as a component of investment properties on the consolidated balance sheet.

Other income includes interest, dividends and other income. Interest and dividend income is recognized as earned.

***p) Borrowing costs and interest on mortgages payable***

Mortgage interest expense includes mortgage interest expense at the effective interest rate and the amortization of insurance premiums and fees included in the carrying amount of mortgages payable. Transaction costs incurred in connection with the revolving credit facilities are capitalized and shown as other non-current assets and amortized over the term of the facility to which they relate.

***q) Distributions***

Distributions represent the monthly cash distributions on outstanding Trust Units.

***r) Unit-based compensation and incentive plans***

Unit-based compensation benefits are provided to officers, trustees and certain employees and are intended to facilitate long-term ownership of Trust Units and provide additional incentives by increasing the participants' interest, as owners, in CAPREIT. Where CAPREIT has the unconditional right to defer settlement of vested awards, Unit-based compensation liabilities are classified as current except for the portion expected to be realized or paid beyond twelve months of the consolidated balance sheet date, including amounts which are classified as non-current.

CAPREIT accounts for its Unit-based compensation plans using the fair value based method under which compensation expense is recognized over the vesting period. The key drivers of recognition and measurement of compensation expense are summarized as follows:

| Incentive Plan (1) | Type | Vesting Period | Type of Amortization | Distributions applied to | Mark-to-Market until: |
|---|---|---|---|---|---|
| LTIP | Issued Units | 2 years (2) | Accelerated | Secured loan | Loan repaid |
| SELTIP | Issued Units | 2 years (2) | Accelerated | Secured loan | Loan repaid |
| DUP | Rights | Grant date | Immediate | Additional Units | Issued |
| RUR Plan | Rights | 3 years | Straight line | Additional Units | Issued |
| UOP | Options | Grant date | Immediate | N/A | Exercised |

(1) For definitions of these plans, refer to note 14.
(2) Vesting one-third on grant date, and one-third on each of the subsequent two grant anniversary dates.

***s) Consolidated Statements of Cash flows***

Cash and cash equivalents consist of cash on hand, balances with banks, and investments in money market instruments with an original term to maturity of 90 days or less at acquisition. Investing and financing activities that do not require the use of cash or cash equivalents are excluded from the consolidated statements of cash flows and are disclosed separately in the notes to the consolidated interim financial statements.

***t) Income taxes***

CAPREIT is taxed as a Mutual Fund Trust for income tax purposes and intends to distribute its income for income tax purposes each year to Unitholders to such an extent that it would not be liable for income tax under Part I of the *Income Tax Act (Canada)* ("Tax Act"). Accordingly, no provision for current income taxes payable is required. For a comprehensive discussion of CAPREIT's liability for tax purposes, see note 20.

At the end of 2010, CAPREIT and its wholly owned subsidiaries satisfied certain conditions available to REITs (the "REIT Exeption") under amendments to the Tax Act, intended to permit a corporate income tax rate of nil as long as the specified conditions continue to be met. Without satisfying these conditions, CAPREIT would have been liable for income taxes beginning in the 2011 taxation year. As a result, a provision for income taxes is included in the consolidated interim financial statements for periods prior to CAPREIT satisfying the REIT Exception.

***u) Earnings per Unit***

As a result of the redemption feature of CAPREIT's Trust Units, these Units are considered financial liabilities under IAS 33 and they may not be considered equity for the purposes of calculating net income on a per Unit basis. Consequently, CAPREIT has elected not to report an Earnings per Unit calculation, as permitted under IFRS.

***v) Future accounting changes***

As of May 9, 2011, the following new or amended IFRS have been issued by the International Accounting Standards Board and are expected to apply for fiscal periods beginning after December 31, 2011: IFRS 1, First-time Adoption of International Financial Reporting Standards; IFRS 7, Financial Instruments: Disclosures; IFRS 9, Financial Instruments; and IAS 12, Income Taxes.

Amendments to IFRS 1 relate to severe hyperinflation environments and remove fixed dates for first-time adopters. Amendments to IFRS 7 relate to disclosures with respect to the transfers of financial assets. The new IFRS 9 replaces the current IAS 39 and introduces new requirements for the classification and measurement of financial assets, to be measured at either amortized cost or fair value. The amendments to IAS 12 provide a solution to the issue of assessing whether the recovery of the carrying value of an asset will be through use or through sale when the asset is measured using the fair value model. The amendment introduces the presumption that recovery of the carrying amount will, normally be through sale. CAPREIT is assessing the impact of the above changes but does not expect CAPREIT to be significantly impacted upon adoption in their current form.

***w) Comparative figures***

Certain comparative figures have been reclassified to conform to the current consolidated financial statement presentation.

## 3. Critical Accounting Estimates, Assumptions and Judgements

The preparation of consolidated interim financial statements in accordance with IFRS requires the use of estimates, assumptions and judgement that in some cases relate to matters that are inherently uncertain, and which affect the amounts reported in the consolidated interim financial statements and accompanying notes. Areas of such estimation include, but are not limited to: valuation of investment properties, remeasurement at fair value of financial instruments, valuation of accounts receivable, capitalization of costs, accounting accruals, the amortization of certain assets, accounting for deferred income taxes and Unit-based compensation financial liabilities. Changes to estimates and assumptions may affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated interim financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could also differ from those estimates under different assumptions and conditions.

The estimates deemed to be more significant, due to subjectivity and the potential risk of causing a material adjustment within the next financial year to the carrying amounts of assets and liabilities are discussed below.

i) Valuation of investment properties

Investment properties are measured at fair value as at the balance sheet date. Any changes in the fair value are included in the consolidated statements of income and comprehensive income. Fair value is supported by independent external valuations or detailed internal valuations using market-based assumptions, each in accordance with recognized valuation techniques. The techniques used comprise both the capitalized net operating income method and the discounted cash flow method and include estimating, amongst other things, future stabilized net operating income, capitalization rates, reversionary capitalization rates, discount rates and other future cash flows applicable to investment properties.

CAPREIT's internal assessments of fair value are based upon a combination of internal financial information and external market data including components of net operating income and capitalization rates all which are obtained from an independent industry expert.

CAPREIT's internal valuations and the independent appraisals are both subject to significant judgement, estimates and assumptions about market conditions in effect as at the balance sheet date. See note 9 for a detailed discussion of valuation methods and the significant assumptions and estimates used.

ii) Valuation of financial instruments

The fair value of derivative assets and liabilities are based on assumptions that involve significant estimates. The basis of valuation for CAPREIT's derivatives are set out in note 17, however, the fair values of derivatives reported may differ from how they are ultimately recognized if there is volatility in interest rates or energy prices between the valuation date and settlement date.

iii) Unit-based compensation

The fair values of Unit-based compensation financial liabilities are based on assumptions that involve significant estimates. The basis of valuation for CAPREIT's Unit-based compensation liabilities are set out in note 14, however, the fair values as at the reporting date may differ materially from how they are ultimately recognized if there is volatility in listed Unit prices, interest rates or other key assumptions between the valuation date and settlement date. Market assumptions, estimates and valuation methodology are discussed in note 16, Unit-based Compensation Expense.

### 4. Transition to IFRS

These are CAPREIT's first consolidated interim financial statements prepared in accordance with IFRS. In preparing the opening consolidated balance sheet as at January 1, 2010 and comparative information for the year covered by the December 31, 2010 consolidated annual financial statements, amounts previously reported and prepared in accordance with Canadian GAAP were adjusted to be in accordance with IFRS by applying those standards identified as effective for years ending December 31, 2011 or earlier. Accordingly, the opening consolidated balance sheet at January 1, 2010 and December 31, 2010, as well as the consolidated statements of income and comprehensive income for the three months ended March 31, 2010 and the reporting periods subsequent to December 31, 2010, are prepared in accordance with IFRS effective for years ending December 31, 2011.

The effects of the transition to IFRS are summarized as follows:

***a) Transition elections made under IFRS 1 and other applicable standards***

**Business combinations**

As part of its transition to IFRS, CAPREIT has elected not to restate those business combinations that occurred prior to January 1, 2010. Accordingly, acquisition-related transaction costs associated with business combinations completed prior to January 1, 2010 continue to be capitalized.

**Other transitional exemptions and guidance**

IFRS 1 allows for certain other optional exemptions; however, such exemptions were not deemed to be significant to CAPREIT's adoption of IFRS.

**Mandatory exceptions**

In preparing these consolidated interim financial statements in accordance with IFRS 1, CAPREIT applied certain mandatory exceptions from full retrospective application of IFRS. The significant mandatory exceptions applied from full retrospective application of IFRS were as follows:

Only hedging relationships that satisfied the hedge accounting criteria as of the transition date are reflected as hedges in CAPREIT's results under IFRS. Any derivatives not meeting the IAS 39 criteria for hedge accounting are recorded as non-hedging derivative financial instruments.

In accordance with IFRS 1, hindsight was not used to create or revise estimates and, accordingly, the estimates previously made by CAPREIT under Canadian GAAP were consistently applied under IFRS.

***b) Reconciliation of the consolidated statements of Unitholders' equity as previously reported under Canadian GAAP to IFRS as at January 1, 2010, March 31, 2010 and December 31, 2010:***

| | Ref | December 31, 2010 | March 31, 2010 | January 1, 2010 |
|---|---|---|---|---|
| **Unitholders' Equity as reported under Canadian GAAP** | | $ 595,848 | $ 435,898 | $ 457,184 |
| IFRS adjustments | | | | |
| Opening cumulative adjustments | | 291,907 | 291,907 | - |
| Fair value adjustment of investment properties | *(i)* | 5,229 | (8,364) | 694,215 |
| Depreciation | | 83,624 | 20,479 | - |
| Other leasing costs | | (12) | 11 | - |
| Deferred income taxes | *(ii)* | 386,448 | 3,930 | (386,448) |
| Exchangeable Units – cost | *(iii)* | - | - | (8,000) |
| Exchangeable Units – fair value adjustments | *(iii)* | (1,267) | (119) | 1,106 |
| Exchangeable Units – cumulative distributions | *(iii)* | - | - | 1,111 |
| Unit-based compensation and financial liabilities | *(iv)* | (7,477) | (677) | (10,077) |
| Increase in equity upon settlement of Units | *(v)* | 1,145 | - | - |
| **Unitholders' Equity as reported under IFRS** | | $ 1,355,445 | $ 743,065 | $ 749,091 |

(i) **Fair value adjustment of investment properties** – CAPREIT considers its income properties to be investment properties under IAS 40. Investment properties include land and buildings held primarily to earn rental income or for capital appreciation or both, rather than for use in the production or supply of goods or services or for sale in the ordinary course of business. Similar to Canadian GAAP, investment properties are initially recorded at cost under IAS 40. However, subsequent to initial recognition, IFRS requires that an entity choose either the cost or fair value model to account for investment properties. CAPREIT has elected to use the fair value model. These adjustments to retained earnings represent the cumulative unrealized gain in respect of the investment properties relating to the fair value adjustments and the reversal of accumulated depreciation on the investment properties, net of any de-recognition of related intangible assets and liabilities, which are inherently reflected in the fair value of the investment properties, and the reclassification of straight-line rent receivable, direct leasing costs and tenant inducements.

(ii) **Deferred income taxes** – the increase in deferred income tax liability under IFRS compared with Canadian GAAP primarily relates to the increased carrying values of CAPREIT's investment properties and the increase in the tax rate being applied to timing differences. The deferred income tax liability under IFRS is determined by applying tax rates to temporary differences that are consistent with CAPREIT's expectation that the method of realization will be through owning and operating its properties rather than through sale. IFRS does not allow the assumption that taxable income will be distributed to Unitholders in the future when determining the tax rate to apply, thus the use of the SIFT rate is not an allowable presumption. CAPREIT has assumed, regardless of intentions to distribute, the future taxable income would be taxed at the top marginal personal tax rate when determining its future tax liability. The impact of the change in CAPREIT's tax status from a SIFT to a qualified REIT is disclosed separately in the consolidated statements of income and comprehensive income.

(iii) **Exchangeable Units** – these Units were issued by CAPLP for $8.0 million and are exchangeable on demand for Trust Units, at the holder's option. As such, these Units have been reclassified from equity at historic cost under Canadian GAAP to current liabilities presented at amortized cost, which approximates fair value under IFRS. As a result, equity has been adjusted for (i) the historical cost of the Exchangeable Units previously issued, (ii) the impact on retained earnings from the cumulative fair value adjustment of the liability, and (iii) distributions, which are classified as interest expense under IFRS. These Units are remeasured at each reporting date at amortized cost with changes in their carrying amounts recognized in the consolidated statements of income and comprehensive income for the period.

(iv) **Unit-based compensation and financial liabilities** – Units, Unit rights and Unit options issued as part of CAPREIT's incentive plans for its officers, trustees and certain employees have been reclassified from equity at historic cost under Canadian GAAP to current and non-current liabilities presented at fair value under IFRS. Under Canadian GAAP, compensation cost was only measured once at grant date whereas under IFRS, the Units, Unit rights and Unit options are required to be remeasured each reporting period until settled. As a result, equity under Canadian GAAP has been adjusted for (i) the historical cost of the Units, Unit rights and Unit options previously issued, and (ii) the impact on retained earnings from the cumulative fair value adjustment of the liability. These Units, Unit rights and options are remeasured at each reporting date at fair value and changes in their fair value are recognized in the consolidated statements of income and comprehensive income for the period.

(v) **Increase in equity upon settlement of Units** – represents additional fair value adjustments to Unit capital resulting from the remeasurement of the Unit-based compensation plans for LTIP and DUP Units settled during the period.

***c) Reconciliation of the consolidated statements of income (loss) and comprehensive income (loss) as previously reported under Canadian GAAP to IFRS and related notes for the three months ended March 31, 2010 and the year ended December 31, 2010:***

| | Ref | Year Ended December 31, 2010 | Three Months Ended March 31, 2010 |
|---|---|---|---|
| **Comprehensive income (loss) as reported under Canadian GAAP** | | $ 74,590 | $ (5,558) |
| **IFRS adjustments** | | | |
| Fair value adjustment of investment properties | *(i)* | 5,229 | (8,364) |
| Depreciation on investment properties | *(ii)* | 83,624 | 20,479 |
| Recovery of deferred income tax | *(iii)* | 386,448 | 3,930 |
| Exchangeable Units - fair value adjustments | *(iv)* | (1,267) | (119) |
| Exchangeable Units - interest expense | *(iv)* | (444) | (111) |
| Unit-based compensation expense | *(v)* | (5,781) | (359) |
| Other leasing costs | | (12) | 11 |
| **Comprehensive income as reported under IFRS** | | $ 542,387 | $ 9,909 |

(i) **Fair value adjustment of investment properties** – Upon transition to IFRS, investment properties has been recognized at fair value, whereas under Canadian GAAP, investment properties was measured on a historic cost basis. The adjustments above represent the increase (decrease) in the fair value of the investment properties during the respective periods.

(ii) **Depreciation related to investment properties** – the recognition of investment property at fair value under IAS 40 has the effect of reversing all of the depreciation on the related investment properties previously recognized under Canadian GAAP.

(iii) **Deferred income taxes** – the increase in deferred income tax liability under IFRS compared with Canadian GAAP primarily relates to the increased carrying values of CAPREIT's investment properties and the change in the tax rate being applied.

(iv) **Exchangeable Units** – as a result of these Units being exchangeable on demand for Trust Units, which are redeemable at the holder's option, Exchangeable Units are therefore required to be classified as liabilities whereas under Canadian GAAP, these Units were presented as equity instruments. Exchangeable Units are remeasured at each reporting date at amortized cost with changes in their carrying amounts recognized in the consolidated statements of income and comprehensive income for the period with distributions under Canadian GAAP classified as interest expense under IFRS.

(v) **Unit-based compensation expense** – Under IFRS, CAPREIT accrues the cost of Unit-based payments for the LTIP and SELTIP over the vesting period using the graded accelerated method of amortization rather than the straight-line method, which was CAPREIT's policy under Canadian GAAP. This change in amortization period increased the Unit-based compensation liability and reduced retained earnings at the date of transition and consequently results in accelerated Unit-based compensation amortization expense.

CAPREIT accounts for its Unit-based payments to participants under the liability method, that is, remeasured at fair value each reporting period. Under Canadian GAAP, CAPREIT accounted for these Unit-based payment arrangements by reference to their grant date fair value as a result of being accounted for as equity at historic cost. Under IFRS, the related liability has been adjusted to reflect the remeasured fair value of the outstanding Unit-based payments.

***d) Adjustments to the statement of cash flows***

Although the transition from Canadian GAAP to IFRS had no impact on actual cash flows of CAPREIT, under IFRS, the presentation requirements necessitate the reflection of the changes disclosed in the consolidated statements of income and comprehensive income. These include investment properties and other fair value adjustments presented under cash flow from operating activities, distributions received on investments classified as investing activities and cash flows relating to interest payments presented under financing activities.

***e) Current and non-current classification***

Under IFRS, the consolidated balance sheets have been classified between the current portion and non-current portion of each asset and liability. As a result, each asset and liability line item that is expected to be recovered or settled within no more than 12 months after the consolidated balance sheet date is classified as current, and that which is expected to be recovered or may be settled more than 12 months after the consolidated balance sheet date is classified as non-current. The change in presentation of the consolidated balance sheet has no financial impact on CAPREIT's operating results.

## 5. Additional IFRS disclosures for the year ended December 31, 2010

In addition to comparative transitional information disclosed separately in note 4, the following information, typically reported on an annual basis under IFRS but not required under Canadian GAAP, is important to the understanding of these consolidated interim financial statements and is presented in accordance with IFRS below:

### *a) Reconciliation of investment properties for year ended December 31, 2010*

| **Year Ended December 31, 2010** | | |
|---|---|---|
| Balance at the beginning of the year | $ | 2,951,647 |
| Additions: | | |
| Acquisitions | | 118,672 |
| Property capital investments | | 82,777 |
| Capitalized leasing costs [(1)] | | 400 |
| Dispositions | | (69,770) |
| Realized loss on dispositions of investment properties | | (4,941) |
| Unrealized gain on remeasurement | | 27,763 |
| Total investment property assets at the end of the year | $ | 3,106,548 |
| | | |
| Liabilities associated with investment properties at the beginning of the year | $ | 50,662 |
| Unrealized loss on remeasurement | | 5,906 |
| Total liabilities associated with investment properties at the end of the year | $ | 56,568 |
| | | |
| Total investment properties, net of associated liabilities, at the end of the year | $ | 3,049,980 |

(1) Comprised of tenant inducements, straight-line rent, direct leasing costs and recoverable capital improvements.

### *b) Co-ownerships*

CAPREIT's share of assets, liabilities, revenues, expenses and cash flows from co-ownership activities under IFRS is summarized as follows:

| **As at December 31, 2010** | | |
|---|---|---|
| Assets | $ | 125,585 |
| Liabilities | $ | 68,878 |
| Revenues | $ | 14,083 |
| Expenses | $ | 8,345 |
| Net Income | $ | 5,738 |

| **Year Ended December 31, 2010** | | |
|---|---|---|
| Cash Provided By (Used In): | | |
| Operating Activities | $ | 4,544 |
| Financing Activities | $ | (3,231) |
| Investing Activities | $ | (1,760) |

***c) Fair value re-measurement of Units and Unit Options***

Assumptions and estimates employed in the fair value remeasurement of Units and Unit Options issued under CAPREIT's incentive plans are shown below as at January 1, 2010 and December 31, 2010:

***Unit Option Plan:***

| As at | December 31, 2010 | January 1, 2010 |
|---|---|---|
| Unit options outstanding | 541,000 | 387,200 |
| Weighted average exercise price | $ 15.20 | $ 13.42 |
| Weighted average risk free rate (%) | 2.3 | 1.6 |
| Weighted average distribution yield (%) | 6.3 | 7.7 |
| Weighted average expected years | 5.0 | 2.1 |
| Weighted average volatility (%) | 21.4 | 32.4 |
| Weighted average option value | $ 2.33 | $ 1.87 |

***Long-Term Incentive Plan:***

| As at | December 31, 2010 | January 1, 2010 |
|---|---|---|
| Number of Units | 1,619,187 | 1,672,927 |
| Weighted average loan rate (%) | 4.68 | 4.69 |
| Weighted average issue price | $ 15.49 | $ 15.48 |
| Weighted average loan balance per Unit - current | $ 13.35 | $ 13.76 |
| Weighted average loan balance per Unit - at maturity | $ 9.59 | $ 9.59 |
| Weighted average risk free rate (%) | 2.6 | 3.2 |
| Weighted average distribution yield (%) | 6.3 | 7.7 |
| Weighted average expected years | 6.7 | 7.6 |
| Weighted average volatility (%) | 25.5 | 24.3 |
| Weighted average Unit value | $ 5.38 | $ 3.19 |

***Senior Executive Long-Term Incentive Plan:***

| As at | December 31, 2010 | January 1, 2010 |
|---|---|---|
| Number of Units | 817,914 | 817,914 |
| Weighted average loan rate (%) | 4.96 | 4.96 |
| Weighted average issue price | $ 17.66 | $ 17.66 |
| Weighted average loan balance per Unit - current | $ 15.33 | $ 15.65 |
| Weighted average loan balance per Unit - at maturity | $ 13.40 | $ 13.40 |
| Weighted average risk free rate (%) | 3.1 | 3.6 |
| Weighted average distribution yield (%) | 6.3 | 7.7 |
| Weighted average expected years | 25.4 | 26.4 |
| Weighted average volatility (%) | 27.0 | 27.5 |
| Weighted average Unit value | $ 6.36 | $ 4.49 |

## 6. Significant Matters

In 2010, CAPREIT entered into an agreement with CMHC (the "Large Borrower Agreement" or "LBA"). The LBA provides for, amongst other things: (i) certain financial covenants and limitations on indebtedness; (ii) the posting of a revolving letter of credit with respect to certain capital expenditures on a portfolio rather than an individual property basis; and (iii) cross-collateralization of mortgage loans for certain CMHC-insured mortgage lenders.

## 7. Recent Property Acquisitions

CAPREIT completed the following investment property acquisitions since January 1, 2010, which have contributed to the operating results effective from their respective acquisition dates:

***For the three months ended March 31, 2011:***

| | Suite Count | Region(s) | Total Acquisition Costs | Mortgage Funding | Interest Rate | Maturity Date |
|---|---|---|---|---|---|---|
| January 31, 2011 | 83 | Burlington | $ 9,084 | $ 6,818 | 4.26% | March 1, 2021 |

***For the year ended December 31, 2010:***

| | Suite or Site Count | Region(s) | Total Acquisition Costs | Mortgage Funding | Interest Rate | Maturity Date |
|---|---|---|---|---|---|---|
| December 20, 2010 (1) | 9 | Bowmanville and Grand Bend | $ 488 | $ – (2) | – (2) | – (2) |
| July 29, 2010 (3) | 307 | Victoria | 47,194 | 26,366 (4) | – (4) | – (4) |
| May 14, 2010 | 199 | Mississauga | 31,653 | 22,165 | 3.37% | June 1, 2015 |
| April 12, 2010 | 162 | Vancouver | 38,425 | 22,652 (5) | 4.59% | April 5, 2017 |
| February 22, 2010 (6) | 14 | Bowmanville and Grand Bend | 912 | – (2) | – (2) | – (2) |
| | 691 | | $ 118,672 | $ 71,183 | | |

(1) The December 20, 2010 MHC land lease sites acquisition was comprised of seven sites in Bowmanville and two sites in Grand Bend.
(2) The acquisition of MHC land lease sites is funded from CAPREIT's land lease facility (see note 13(b)).
(3) The acquisition comprised of two affordable, four mid-tier and two luxury properties.
(4) Comprised of new mortgage financing of $25,580 at 3.67% maturing December 1, 2020 and an assumed mortgage of $786 at a stated rate of 4.73% maturing on February 1, 2016.
(5) The mortgage was assumed from the vendor at acquisition.
(6) The February 22, 2010 MHC land lease sites acquisition was comprised of 13 sites in Bowmanville and one site in Grand Bend.

The total purchase consideration including mortgages payable and bank indebtedness is allocated to investment property and other assets acquired based upon the relative fair value of each at the time of purchase.

### 8. Dispositions and Assets and Liabilities Held-For-Sale

The tables below summarize the investment property dispositions completed since January 1, 2010. These dispositions do not meet the definition of discontinued operations under IFRS 5.

***Dispositions Completed During the Three Months Ended March 31, 2011***

| Disposition Date | Suite Count | Region(s) | | Sale Price | | Cash Proceeds | | Mortgage Discharged |
|---|---|---|---|---|---|---|---|---|
| March 29, 2011 | 143 | Hamilton | $ | 5,975 | $ | 3,609 | $ | 2,117 |

***Dispositions Completed During the Year Ended December 31, 2010***

| Disposition Date | Suite Count | Region(s) | | Sale Price | | Cash Proceeds | | Mortgage(s) Repaid |
|---|---|---|---|---|---|---|---|---|
| November 24, 2010 | 56 | Toronto | $ | 6,430 | $ | 6,042 | $ | – |
| July 29, 2010 | 570 | Mississauga and Kitchener | | 45,900 | | 42,232 | | 20,106 |
| July 5, 2010 | 146 | London | | 7,600 | | 7,116 | | 5,650 |
| June 9, 2010 | 250 | Montréal | | 11,750 | | 10,568 | | 4,014 |
| June 3, 2010 | 88 | Montréal | | 3,000 | | 2,831 | | 1,926 |
| Total | 1,110 | | $ | 74,680 | $ | 68,789 | $ | 31,696 |

A loss of $95 was recognized in the three months ended March 31, 2011 (March 31, 2010 - $nil; December 31, 2010 – loss of $4,941) in connection with these property dispositions.

### 9. Investment Properties

***Valuation basis***

Investment properties are carried at fair value, which are the amounts at which the individual properties could be exchanged between willing parties in an arm's length transaction, based on current prices in an active market for similar properties in the same location, considering the highest and best use of the asset and subject to similar leases, with any gain or loss arising from a change in fair value recognized in the consolidated statement of income and comprehensive income for the period. Valuations do not take into account any potential portfolio premium.

The fair values of all of CAPREIT's investment properties are determined by a qualified external appraiser annually. Each quarter, CAPREIT utilizes market assumptions for capitalization and discount rates provided by the external appraiser to determine the fair value of the investment properties. To the extent that the stabilized forecasted cash flows of an investment property change significantly in a quarter, the fair value of the investment property would be re-assessed by the external appraiser and the fair value adjusted accordingly.

Investment properties have been valued using the following methods and key assumptions:

***a) Fee Simple and MHC Land Lease Sites***

CAPREIT utilizes the Direct Income Capitalization ("DC") method. Under this method, capitalization rates are applied to a stabilized net operating income ("NOI") representing market-based NOI assumptions (property revenue less property operating expenses). The most significant assumption is the capitalization rate for each specific property.

***b) Operating Leasehold Interests***

CAPREIT utilizes the Discounted Cash Flow ("DCF") method. Under this method, discount rates are applied to the forecasted cash flows reflecting market-based leasing assumptions for that specific property as well as assumptions as to renewal and new leasing activity. The most significant assumption is the discount rate applied over the initial term of the lease. In the case of one property, the forecasted cash flow is adjusted for contractual air rights payments and the discount rate is adjusted for uncertainty regarding the renegotiation of the air right lease at the end of the term.

***c) Options to Purchase the Related Operating Leasehold Interests***

CAPREIT utilizes the DC method at the reversion date to estimate the future value, which is then discounted to a present value. Under this method, the stabilized income is adjusted to a projected NOI as at the end of the operating lease term and the capitalization rate is adjusted to a "Reversionary Capitalization Rate" reflecting the incremental risk associated with future uncertainty. The value of the option is then determined based upon the difference between the estimated fair value of the property at such date and the option buyout price, discounted back to its present value using a risk-adjusted discount rate (the "Option Discount Rate").

***d) Land Leasehold Interests***

CAPREIT utilizes the DCF method for properties that are subject to land or air rights leases. Under this method, discount rates are applied to the forecasted cash flows reflecting market-based leasing assumptions for that specific property as well as assumptions as to renewal and new leasing activity. The most significant assumption is the discount rate applied over the term of the lease. Forecasted cash flows are adjusted for contractual land lease payments and the discount rates reflect the uncertainty regarding the renegotiation of land lease payments during and at the end of the term of the leases.

***e) Liabilities Associated with Investment Properties***

CAPREIT has contractual minimum lease payments associated with an air rights lease under an Operating Leasehold Interest and land leases under its Land Leasehold Interests. These payments have been reflected at the present value of the related land lease or air rights payments over the term of the respective leases.

A summary of the market assumptions and ranges for each type of property interest along with their fair values are presented below as at January 1, 2010, December 31, 2010 and March 31, 2011:

**As at January 1, 2010**

| **Type of Interest** ($ thousands) | **Fair Value** | **Rate Type** | **Max** | **Min** | **Weighted Average** |
|---|---|---|---|---|---|
| Fee Simple Interests – Apartments and Townhomes | $ 2,304,280 | Capitalization rate | 7.75% | 5.00% | 6.27% |
| MHC Land Lease Sites | 87,940 | Capitalization rate | 6.25% | 6.25% | 6.25% |
| Operating Leasehold Interests (1), (2) | 388,655 | Discount rate (3) | 9.00% | 7.63% | 7.91% |
| Land Leasehold Interests (1) | 170,772 | Discount rate | 8.00% | 7.75% | 7.83% |
| Total Investment Property Assets | $ 2,951,647 | | | | |
| Less: Liabilities Associated with Investment Properties | | | | | |
| Operating Leasehold Interests (1) | 4,910 | Discount rate (3) | 7.75% | 7.75% | 7.75% |
| Land Leasehold Interests (1) | 45,752 | Discount rate | 8.00% | 7.75% | 7.83% |
| Total Liabilities Associated with Investment Properties | $ 50,662 | | | | |
| Total Net Investment Properties | $ 2,900,985 | | | | |

**As at December 31, 2010**

| Type of Interest<br>($ thousands) | Fair<br>Value | Rate Type | Max | Min | Weighted<br>Average |
|---|---|---|---|---|---|
| Fee Simple Interests – Apartments and Townhomes | $ 2,436,001 | Capitalization rate | 7.50% | 4.65% | 6.06% |
| MHC Land Lease Sites | 88,790 | Capitalization rate | 6.25% | 6.25% | 6.25% |
| Operating Leasehold Interests (1), (2) | 399,139 | Discount rate (3) | 8.50% | 7.25% | 7.56% |
| Land Leasehold Interests (1) | 182,618 | Discount rate | 8.00% | 7.50% | 7.80% |
| Total Investment Property Assets | $ 3,106,548 | | | | |
| Less: Liabilities Associated with Investment Properties | | | | | |
| Operating Leasehold Interests (1) | 5,820 | Discount rate (3) | 7.25% | 7.25% | 7.25% |
| Land Leasehold Interests (1) | 50,748 | Discount rate | 8.00% | 7.50% | 7.80% |
| Total Liabilities Associated with Investment Properties | $ 56,568 | | | | |
| Total Net Investment Properties | $ 3,049,980 | | | | |

**As at March 31, 2011**

| Type of Interest<br>($ thousands) | Fair<br>Value | Rate Type | Max | Min | Weighted<br>Average |
|---|---|---|---|---|---|
| Fee Simple Interests – Apartments and Townhomes | $ 2,446,741 | Capitalization rate | 7.50% | 4.65% | 6.08% |
| MHC Land Lease Sites | 88,790 | Capitalization rate | 6.25% | 6.25% | 6.25% |
| Operating Leasehold Interests (1), (2) | 399,139 | Discount rate (3) | 8.50% | 7.25% | 7.56% |
| Land Leasehold Interests (1) | 182,618 | Discount rate | 8.00% | 7.50% | 7.80% |
| Total Investment Property Assets | $ 3,117,288 | | | | |
| Less: Liabilities Associated with Investment Properties | | | | | |
| Operating Leasehold Interests (1) | 5,820 | Discount rate (3) | 7.25% | 7.25% | 7.25% |
| Land Leasehold Interests (1) | 50,748 | Discount rate | 8.00% | 7.50% | 7.80% |
| Total Liabilities Associated with Investment Properties | $ 56,568 | | | | |
| Total Net Investment Properties | $ 3,060,720 | | | | |

(1) The Operating Leasehold Interest subject to a contractual air rights lease and Land Leasehold Interests subject to land leases have been reflected at fair value net of the present value of minimum land lease or air rights payments over the term of the leases. On the balance sheet, these specific properties have been reflected at gross fair value within investment properties and the present value of the related land lease or air rights payments are presented as liabilities.

(2) The fair values of Operating Leasehold Interests include the fair values of the Options to purchase the related operating leases of $14.3 million as at January 1, 2010, $16.6 million as at December 31, 2010 and $16.6 million as at March 31, 2011.

(3) Represents the discount rate used to determine the fair value for Operating Leasehold Interests using the DCF method. A weighted average stabilized NOI growth of 2.5% has been assumed as at January 1, 2010, December 31, 2010 and March 31, 2011.

***Reconciliation of carrying amounts of investment properties***

| **For the Three Months Ended March 31,** | **2011** | **2010** |
|---|---|---|
| **Balance at the beginning of the period,** | **$ 3,106,548** | $ 2,951,647 |
| Additions: | | |
| Acquisitions | **9,084** | 912 |
| Property capital investments | **13,020** | 8,411 |
| Capitalized leasing costs [(1)] | **(78)** | (39) |
| Dispositions | **(5,730)** | - |
| Realized loss on dispositions of investment properties | **(95)** | - |
| Unrealized fair value adjustments | **(5,461)** | (8,364) |
| **Balance of Investment Property Assets as at March 31,** | **$ 3,117,288** | $ 2,952,567 |
| **Less:** | | |
| Liabilities Associated with Investment Properties, at the beginning of the period | **56,568** | 50,662 |
| Unrealized fair value adjustments | **-** | - |
| **Balance of Liabilities Associated with Investment Properties as at March 31,** | **$ 56,568** | $ 50,662 |
| **Net Balance of Investment Properties as at March 31,** | **$ 3,060,720** | $ 2,901,905 |

(1) Comprised of tenant inducements, straight-line rent, direct leasing costs and recoverable capital improvements.

## 10. Other Assets

| **As at** | **Ref** | **March 31, 2011** | **December 31, 2010** | **January 1, 2010** |
|---|---|---|---|---|
| **Other Non-Current Assets** | | | | |
| Property, plant and equipment | (i) | **$ 10,738** | $ 9,937 | $ 8,333 |
| Accumulated amortization of property, plant and equipment | | **(6,336)** | (5,942) | (4,590) |
| Net property, plant and equipment | | **4,402** | 3,995 | 3,743 |
| Investments | | **34,289** | 34,388 | 28,739 |
| Deferred loan costs | (ii) | **1,502** | 1,679 | 1,754 |
| Deposits on purchases | (iii) | **245** | 245 | 824 |
| **Total** | | **$ 40,438** | $ 40,307 | $ 35,060 |
| | | | | |
| **Other Current Assets** | | | | |
| Prepaid expenses | | **$ 2,902** | $ 1,572 | $ 2,110 |
| Other receivables | | **6,159** | 5,669 | 4,359 |
| Restricted cash | | **2,854** | 2,891 | 2,546 |
| Deposits | | **4,985** | 660 | 633 |
| **Total** | | **$ 16,900** | $ 10,792 | $ 9,648 |

(i) Property, plant and equipment consists of head office and regional offices' leasehold improvements, corporate and information technology systems.

(ii) Represents deferred loan costs related to the revolving credit facilities.

(iii) Under the terms of the development agreements entered into concurrently with the acquisition of the MHC land lease sites on July 10, 2007, CAPREIT is required to fund servicing costs on the lands in the land lease communities for future developments. These funded amounts will be deducted from the final purchase price when the MHC land lease sites are acquired by CAPREIT. The Agreements are for a ten-year term and can be extended for an additional ten years.

### 11. Other Liabilities

| As at | March 31, 2011 | December 31, 2010 | January 1, 2010 |
|---|---|---|---|
| **Other Non-Current Liabilities** | | | |
| Hedge liability | **$ 439** | $ 719 | $ 1,924 |
| Accrued loss on natural gas contracts | **286** | 376 | - |
| **Total** | **$ 725** | $ 1,095 | $ 1,924 |
| | | | |
| **Other Current Liabilities** | | | |
| Hedge liability | **$ 1,930** | $ 2,400 | $ 2,926 |
| Accrued loss on natural gas contracts | **2,428** | 3,191 | - |
| Mortgage interest payable | **5,871** | 5,635 | 5,826 |
| **Total** | **$ 10,229** | $ 11,226 | $ 8,752 |

### 12. Mortgages Payable

Mortgages payable bear interest at a weighted average effective rate of 4.82% (December 31, 2010 – 4.90%), and mature between 2011 and 2027. The effective interest rate as at March 31, 2011 includes 0.08% (December 31, 2010 – 0.08%) for the amortization of the realized component of the loss on settlement of derivative financial instruments included in AOCL. All but $49,554 or 3.02% of CAPREIT's mortgages payable are financed at fixed interest rates. The investment properties have been pledged as security. Future principal repayments ending December 31 for the years indicated are as follows:

| As at March 31, 2011 | Principal Amount | % of Total Principal |
|---|---|---|
| Nine Months Remaining in 2011 | $ 181,677 | 11.1 |
| 2012 | 261,850 | 16.0 |
| 2013 | 213,479 | 13.0 |
| 2014 | 257,189 | 15.7 |
| 2015 | 161,709 | 9.9 |
| Subsequent to 2015 | 565,108 | 34.3 |
| | 1,641,012 | 100.0 |
| Deferred financing costs, fair value adjustments and CMHC premiums | (35,735) | |
| | $ 1,605,277 | |
| Represented by: | | |
| Mortgages Payable - current | $ 215,516 | |
| Mortgages Payable - non-current | 1,389,761 | |
| | $ 1,605,277 | |

As at March 31, 2011, unamortized deferred financing costs of $5,299, fair value adjustments of ($940) and prepaid CMHC premiums of $31,376 are netted against mortgages payable.

## 13. Bank Indebtedness

CAPREIT has a credit agreement comprising an acquisition and operating facility ("Acquisition and Operating Facility") and a land lease facility ("Land Lease Facility") (the "Credit Facilities"). Effective June 30, 2010, the Credit Facilities were renewed and amended as summarized below. As part of the renewal, certain aspects of covenants were amended and restated, as further discussed in note 19. The terms governing the Credit Facilities also contemplate converting floating charge debentures on certain of CAPREIT's investment properties, which have been pledged as security, into fixed charges.

### a) *Acquisition and Operating Facility*

The maximum amount available is $270,000, comprising one facility for a three-year term maturing on June 30, 2013, subject to compliance with the various provisions of the credit agreement, in order to fund ongoing working capital requirements, general corporate purposes and acquisition and improvements to the properties. Floating charge debentures on certain investment properties have been provided as security, however, the current agreement provides for converting these floating charges into fixed charges. At March 31, 2011, the weighted average floating interest rate for amounts drawn under this credit facility was 4.05% (December 31, 2010 – 3.95%) and the borrowings outstanding were $58,160 (December 31, 2010 – $38,000). In addition, letters of credit in the amount of $11,439 (December 31, 2010 – $9,687) were outstanding, which reduce the maximum amount available under the facility.

As the Acquisition and Operating Facility is not required to be refinanced during the next 12 months, the facility is reported as a non-current liability.

### b) *Land Lease Facility*

The Land Lease Facility was established (notes 7 and 10) to fund operating, development and acquisition costs associated with the MHC land lease portfolio. The maximum amount of the facility is $10,000 for a one-year term maturing on June 30, 2011. Fixed charge debentures on the MHC land lease properties have been provided as security. At March 31, 2011, the weighted average floating interest rate for amounts drawn under this facility was 4.13% (December 31, 2010 – 4.17%) and the borrowings outstanding were $1,202 (December 31, 2010 – $1,358). In addition, letters of credit in the amount of $84 (December 31, 2010 – $84) were outstanding, which reduce the maximum available under the facility.

As the Land Lease Facility matures within the next 12 months, the facility is reported as a current liability.

## 14. Unitholders' Equity and Unit-based Financial Liabilities

***Unitholders' Equity***

All Trust Units outstanding are fully paid, have no par value and all are voting Trust Units. CAPREIT is authorized to issue an unlimited number of Trust Units. Trust Units represent a Unitholder's proportionate undivided beneficial interest in CAPREIT. No Trust Unit has any preference or priority over another. No Unitholder has or is deemed to have any right of ownership in any of the assets of CAPREIT. Each Unit confers the right to one vote at any meeting of Unitholders and to participate pro rata in any distributions by CAPREIT and, in the event of termination of CAPREIT, in the net assets of CAPREIT remaining after satisfaction of all liabilities. Units will be issued in registered form and are transferable. Issued and outstanding Units may be subdivided or consolidated from time to time by the trustees without Unitholder approval. No certificates for fractional Units will be issued and fractional Units will not entitle the holders thereof to vote.

By virtue of CAPREIT being an open-ended mutual fund trust, Unitholders of Trust Units are entitled to redeem their Units at any time at prices determined and payable in accordance with the conditions specified in the DOT. As a result, under IFRS, Trust Units are defined as financial liabilities; however, for the purposes of financial statement classification and presentation, the Trust Units may be presented as equity instruments as they meet the puttable instrument exemption under IAS 32. For the purposes of presenting earnings on a per Unit basis as well as for Unit-based compensation plans, CAPREIT's Trust Units are not treated as equity instruments.

The number of issued and outstanding Trust Units is as follows:

| For the Three Months Ended March 31, | Ref | 2011 | 2010 |
|---|---|---|---|
| Units outstanding beginning of the period | | | |
| Issued or granted during the period: | | **74,176,908** | 65,884,057 |
| Distribution Reinvestment Plan ("DRIP") | *(a)* | **216,486** | 132,285 |
| Employee Unit Purchase Plan ("EUPP") | *(b)* | **4,512** | 4,629 |
| Unit Option Plan ("UOP") | *(c)* | **87,500** | – |
| Long-Term Incentive Plan ("LTIP") | *(d)* | **46,596** | – |
| Units outstanding March 31, | | **74,532,002** | 66,020,971 |

***a) Distribution Reinvestment Plan ("DRIP")***

The terms of the DRIP grant participants the right to receive an additional amount equal to 5% of their monthly distributions paid in the form of additional Units. The total consideration for Units issued represents the amount of cash distributions reinvested in additional Units.

***b) Employee Unit Purchase Plan ("EUPP")***

The EUPP grants employees the right to receive an additional amount equal to 10% of the Units they acquire, paid in the form of additional Units.

***c) Unit Option Plan ("UOP")***

Under the terms of the UOP, options are granted to trustees, officers and employees based on performance incentive for improved service and enhancing profitability and vest on the date of grant.

***d) Long-Term Incentive Plan ("LTIP")***

During the first quarter of 2011, CAPREIT issued 46,596 Units at $17.16 for a value of $800 to settle 96,260 previously issued LTIP Units.

***Unit-based Financial Liabilities***

Units are issuable pursuant to CAPREIT's Unit-based compensation plans, namely, the UOP, the EUPP, the Unit Purchase Plan, the LTIP, the SELTIP, the DUP and the RUR Plan (each of which is more fully described in note 16). The maximum number of Units issuable under all of CAPREIT's Unit-based incentive plans is 6,000,000 Units. The maximum available for future issuance under all Unit incentive plans as at March 31, 2011 is 371,832 Units (December 31, 2010 - 575,151 Units).

Units, Unit Rights and Unit Options issued or outstanding under CAPREIT's incentive plans as at March 31, 2011 and 2010 are as follows:

| **For The Three Months Ended March 31, 2011** (Number of Units) | **UOP** | **DUP** | **RUR** | **SELTIP/ LTIP (1)** | **Exch. Units (2)** | **Total** |
|---|---|---|---|---|---|---|
| Units, Unit Rights and Unit Options outstanding as of January 1, 2011 | 541,000 | 74,103 | 72,887 | 2,437,101 | 411,311 | 3,536,402 |
| Issued, cancelled or granted during the period: | | | | | | |
| Issued or granted | – | 7,982 | 99,537 | – | – | 107,519 |
| Exercised or settled | (87,500) | – | – | (96,260) | – | (183,760) |
| Distributions reinvested | – | 1,118 | 1,583 | – | – | 2,701 |
| **Units, Unit Rights and Unit options outstanding as of March 31, 2011** | **453,500** | **83,203** | **174,007** | **2,340,841** | **411,311** | **3,462,862** |

| **For The Three Months Ended March 31, 2010** (Number of Units) | **UOP** | **DUP** | **RUR** | **SELTIP/ LTIP (1)** | **Exch. Units (2)** | **Total** |
|---|---|---|---|---|---|---|
| Units, Unit Rights and Unit Options outstanding as of January 1, 2010 | 387,200 | 60,624 | – | 2,490,841 | 411,311 | 3,349,976 |
| Issued, cancelled or granted during the period: | | | | | | |
| Issued or granted | – | 14,214 | 69,552 | – | – | 83,766 |
| Distributions reinvested | – | 1,146 | 439 | – | – | 1,585 |
| Units, Unit Rights and Unit options outstanding as of March 31, 2010 | 387,200 | 75,984 | 69,991 | 2,490,841 | 411,311 | 3,435,327 |

1) The distributions payable on SELTIP and LTIP Units do not increase the number of Units outstanding on said plans but are incorporated into the fair market value of such plans.
2) The outstanding 411,311 Exchangeable Units are entitled to distributions equivalent to distributions on Trust Units, must be exchanged solely for Trust Units on a one-for-one basis, and are exchangeable at any time at the option of the holder. An equivalent number of Special Voting Units were issued at the same time as the Exchangeable Units. The holders of such Units have no entitlement to any share of or interest in the distributions or net assets of CAPREIT. Through Special Voting Units, holders of Exchangeable Units are entitled to an equivalent number of votes at all meetings of Unitholders or in respect of any written resolution of Unitholders equal to the number of Exchangeable Units held. The carrying value of these Units is measured at amortized cost which approximates the closing bid price of the Trust Units.

The table below summarizes the change in the total Unit-based compensation liability for the three months ended March 31, 2011 and 2010 including the reversal of liability as a result of settlement for Trust Units.

| **For the Three Months Ended March 31,** | **2011** | **2010** |
|---|---|---|
| Total Unit-based financial liabilities, beginning of the period | **$ 16,410** | $ 10,077 |
| Unit-based compensation expenses | **5,801** | 684 |
| Settlement of Unit-based compensation awards for Trust Units | **(752)** | – |
| Total Unit-based financial liabilities, end of the period | **$ 21,459** | $ 10,761 |

***Units or Unit-based compensation liabilities held by trustees, officers and other senior management***

As at March 31, 2011, 4.7% (March 31, 2010 – 5.3%) of all Units and Trust-Unit equivalents outstanding were held by trustees, officers and other senior management of CAPREIT.

***Normal course issuer bid ("NCIB")***

On June 22, 2010, CAPREIT announced that the TSX had approved its notice of intention to acquire up to 6,425,179 Units at market prices over the 12-month period ending June 24, 2011. Under this NCIB, no Units were acquired up to March 31, 2011.

On June 19, 2009, CAPREIT announced that the TSX had approved its notice of intention to acquire up to 6,344,344 Units at market prices over the 12-month period ending June 24, 2010. Under this NCIB, no Units were acquired up to March 31, 2010.

### 15. Distributions

CAPREIT paid distributions to its Unitholders in accordance with its DOT. Distributions declared by its Board of Trustees were paid monthly, on or about the 15th day of each month.

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| Distributions declared on Trust Units | **$ 20,093** | $ 17,813 |
| Distributions Per Unit | **$ 0.270** | $ 0.270 |

### 16. Unit-based Compensation Expenses

These costs represent Unit-based compensation amortization, which includes fair value remeasurement at each reporting date amortized over the respective vesting periods for each plan for the three months ended March 31, 2011 and 2010, as follows:

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| UOP | **$ 882** | $ 46 |
| LTIP | **2,900** | 264 |
| SELTIP | **1,426** | 96 |
| DUP | **349** | 238 |
| RUR Plan | **236** | 34 |
| EUPP | **8** | 6 |
| | **$ 5,801** | $ 684 |

#### *a) UOP*

Under the terms of the UOP, options are granted to trustees, officers and employees based on a performance incentive for improved service and enhancing profitability and vest on the date of grant. In February 2010, the President and CEO's employment agreement was amended to provide that during its term, the President and CEO will be awarded options to acquire three percent (3%) of the number of Units issued by the Trust pursuant to any equity offering or acquisition transaction (not including pursuant to any compensation arrangements) at the market price of the Units at the time of completion of each such treasury issuance, in accordance with the terms of the UOP, as amended from time to time. In connection with the Equity Offering, on December 10, 2010, 217,500 options were granted to the President and CEO at an exercise price of $17.30 with an expiration date of December 9, 2020. In connection with the exercise of the over-allotment option, on December 23, 2010, 10,500 options were granted to the President and CEO at an exercise price of $17.30 with an expiration date of December 22, 2020. There were no options granted during 2011.

A summary of Unit option activity for the three months ended March 31, 2011 and 2010 is presented below. All options are exercisable as at March 31, 2011 and 2010.

| For the Three Months Ended March 31, Number of Units | 2011 | 2010 |
|---|---|---|
| Balance, beginning of period | **541,000** | 387,200 |
| Exercised | **(87,500)** | – |
| Balance, end of period | **453,500** | 387,200 |

The fair value of Unit Options is determined as at the grant date and subsequent interim and annual valuations are determined by adjusting market-based valuation assumptions used in arriving at the estimated fair market value. The weighted average assumptions for the grants awarded in the respective periods were as follows:

| As at March 31, | 2011 | 2010 |
|---|---|---|
| Number of Units | **453,500** | 387,200 |
| Weighted average issue price | **$ 15.43** | $ 13.42 |
| Weighted average risk free rate (%) | **2.6** | 1.8 |
| Weighted average distribution yield (%) | **5.6** | 7.5 |
| Weighted average expected years | **5.5** | 1.9 |
| Weighted average volatility (%) | **21.0** | 31.4 |
| Weighted average Unit option value | **$ 3.87** | $ 1.99 |

***b) LTIP and SELTIP***

The Compensation and Governance Committee of the Board of Trustees may award LTIP and SELTIP Units, subject to the attainment of specified performance objectives to certain officers and key employees, collectively the "Participants." SELTIP Units may only be awarded to the Chief Executive Officer and Chief Financial Officer of the Trust. The Participants can subscribe for Units of CAPREIT at a purchase price equal to the weighted average trading price of the Units for five trading days prior to issuance. The purchase price is payable in instalments, with an initial instalment of 5% paid when the Units are issued. The balance represented by Instalment Receipts is due over a term not exceeding ten years for LTIP and 30 years in the case of the SELTIP. Participants are required to pay interest at ten-year and thirty-year fixed rates, respectively, based on the Trust's fixed borrowing rate for long-term mortgage financing and are required to apply cash distributions received by them on these Units toward the payment of interest and the remaining instalments. In the case of the SELTIP, following the tenth anniversary, cash distributions shall be applied to pay interest only and any excess shall be distributed to the Participants. Participants may pre-pay any remaining instalments at their discretion. The Instalment Receipts are non-recourse to the Participants and are secured by the Units as well as the distributions on the Units. If a Participant fails to pay interest and/or principal, CAPREIT may elect to reacquire or sell the Units in satisfaction of the outstanding amounts.

The fair value of LTIP and SELTIP awards is determined by using market-based valuation assumptions to calculate the combination of the intrinsic and put option values.

The intrinsic value at the measurement date is the difference by which the Unit price exceeds the loan value per Unit under the presumption that a participant can repay the loan and exchange the LTIP or SELTIP Unit for a Trust Unit at that date. The intrinsic value is nil if the Unit price falls below the current loan balance per Unit as CAPREIT does not have the right to exchange the LTIP or SELTIP Unit for a Trust Unit and therefore cannot record an asset in such cases.

The non-recourse nature of the loan receivable to CAPREIT effectively provides a participant with a put option as the participant may not repay the loan if, at maturity, the remaining loan balance per Unit exceeds the market value of the underlying Trust Units.

The details of the Units issued under the LTIP and SELTIP are as shown below:

| **Three Months Ended March 31,** | **2011** | | **2010** | |
|---|---|---|---|---|
| (Number of Units) | **LTIP** | **SELTIP** | **LTIP** | **SELTIP** |
| Balance, beginning of period | **1,619,187** | **817,914** | 1,672,927 | 817,914 |
| Settled | **(96,260)** | **–** | – | – |
| Balance, end of period | **1,522,927** | **817,914** | 1,672,927 | 817,914 |

The details of the LTIP and SELTIP Instalment Receipts are as shown below:

| **Three Months Ended March 31,** | **2011** | | **2010** | |
|---|---|---|---|---|
| Installment Receipts | **LTIP** | **SELTIP** | **LTIP** | **SELTIP** |
| Balance, beginning of period | **$ 21,357** | **$ 12,583** | $ 23,103 | $ 12,835 |
| Principal repayments during the period | **(1,070)** | **(67)** | (186) | (64) |
| Balance, end of period | **$ 20,287** | **$ 12,516** | $ 22,917 | $ 12,771 |

The Instalment Receipts are recognized as a deduction from Unit-based compensation liability. During the three months ended March 31, 2011 and 2010, interest payments in the amount of $390 and $422, respectively were applied to the outstanding Unit-based compensation liability. The outstanding balance of the instalment receivable is used in determining the fair value of the Unit and the related fair value adjustments.

The following table summarizes the market-based rates and assumptions as well as projections of certain inputs used in determining the intrinsic value as well as the put option values using the Black-Scholes option pricing model for LTIP and SELTIP Units outstanding at the respective measurement dates.

| **LTIP**<br>**As at March 31,** | **2011** | **2010** |
|---|---|---|
| Number of Units | **1,522,927** | 1,672,927 |
| Weighted average loan rate (%) | **4.66** | 4.69 |
| Weighted average issue price | **$ 15.49** | $ 15.48 |
| Weighted average loan balance per Unit - current | **$ 13.26** | $ 13.65 |
| Weighted average loan balance per Unit - at maturity | **$ 9.56** | $ 9.59 |
| Weighted average risk free rate (%) | **2.9** | 3.2 |
| Weighted average distribution yield (%) | **5.6** | 7.5 |
| Weighted average expected years | **6.5** | 7.4 |
| Weighted average volatility (%) | **25.7** | 24.5 |
| Weighted average Unit value | **$ 7.20** | $ 3.30 |

| **SELTIP**<br>**As at March 31,** | | **2011** | | **2010** |
|---|---|---|---|---|
| Number of Units | | **817,914** | | 817,914 |
| Weighted average loan rate (%) | | **4.96** | | 4.96 |
| Weighted average issue price | **$** | **17.66** | $ | 17.66 |
| Weighted average loan balance per Unit - current | **$** | **15.24** | $ | 15.57 |
| Weighted average loan balance per Unit - at maturity | **$** | **13.40** | $ | 13.40 |
| Weighted average risk free rate (%) | | **3.4** | | 3.6 |
| Weighted average distribution yield (%) | | **5.6** | | 7.5 |
| Weighted average expected years | | **25.2** | | 26.2 |
| Weighted average volatility (%) | | **26.9** | | 27.5 |
| Weighted average Unit value | **$** | **8.11** | $ | 4.61 |

### c) *DUP*

The DUP gives the non-executive trustees the right to receive a percentage of their annual retainer in the form of deferred units ("Deferred Units"). Each trustee who elects to participate may be paid 25%, 50%, 75% or 100% (the "Elected Percentage") of his annual retainer payable in respect of a calendar year (the "Elected Amount"), subject to an annual maximum Elected Percentage established by the Compensation and Governance Committee, in the form of Deferred Units, in lieu of cash. CAPREIT will match the Elected Amount in the form of Deferred Units having a value equal to the volume weighted average price of all Units traded on the TSX for the five trading days immediately preceding the date on which board compensation is payable. The maximum Elected Percentage in respect of 2011 is 100% (2010 - 100%) of a trustee's annual board compensation of $55.

The Deferred Units earn notional distributions based on the same distributions paid on the Units, and such notional distributions are used to acquire additional Deferred Units ("Distribution Units"). The Deferred Units and additional Distribution Units are credited to each trustee's Deferred Unit account and are not issued to the trustee until the trustee elects to withdraw such Units. Each trustee may elect to withdraw up to 20% of the Deferred Units credited to his Deferred Unit account only once in a five-year period. The fair value of the Deferred Units represents the closing price of the Units on the TSX on the distribution date.

On June 21, 2010, in accordance with the DUP, three retiring trustees withdrew 25,585 Deferred Units from the DUP and were issued an equivalent number of Trust Units. In addition, 7,840 Deferred Units were cancelled in consideration for the withholding taxes owed on the Units issued.

On July 14, 2010, in accordance with the DUP, one retired trustee withdrew 1,270 Deferred Units from the DUP and was issued an equivalent number of Trust Units. In addition, 152 Deferred Units were cancelled in consideration for the withholding taxes owed on the Units issued.

The fair value of such Units represents the closing price of the Units on the TSX on the last trading day on which the Units traded prior to the reporting date, representing the fair value of the redemption price.

The details of the Units issued under the DUP are shown below:

| | **March 31, 2011** | | | **March 31, 2010** | | |
|---|---|---|---|---|---|---|
| | **Weighted Avg Issue Price** | **Fair Value per Unit** | **Number of Units** | **Weighted Avg Issue Price** | **Fair Value per Unit** | **Number of Units** |
| Outstanding at period start | **$ 15.34** | **$ 17.14** | **74,103** | $ 15.03 | $ 14.06 | 60,624 |
| Granted during the period | **$ 19.46** | **$ 19.46** | **7,982** | $ 14.35 | $ 14.35 | 14,214 |
| Additional Unit Distributions | **$ 18.09** | **$ 18.09** | **1,118** | $ 14.29 | $ 14.29 | 1,146 |
| Outstanding at period end | **$ 15.78** | **$ 19.46** | **83,203** | $ 14.89 | $ 14.35 | 75,984 |

### *d) RUR Plan*

During the first quarter of 2010, CAPREIT adopted the RUR Plan as the primary plan through which long-term incentive compensation will be awarded. The RUR Plan was approved by Unitholders on May 19, 2010. The Compensation and Governance Committee of the Board of Trustees may award RURs, subject to the attainment of specified performance objectives to certain officers and key employees, collectively the "Participants". The purpose of the RUR Plan is to provide its Participants with additional incentive and to further align the interest of its Participants with Unitholders through the use of RURs which, upon vesting, are exercisable for Units. RUR Plan Units will be issued from treasury upon vesting. The RURs vest in their entirety on the third anniversary of the grant date. The RURs earn notional distributions in respect of each distribution paid on RURs commencing from the grant date and such notional distributions are used to calculate additional RURs ("Distribution RURs"), which are accrued for the benefit of the Participant. The Distribution RURs are credited to the Participants only when the underlying RURs upon which the Distribution RURs are earned become vested. The fair value of the Distribution RURs is based on the closing price of the Units on the TSX on the distribution date.

On February 24, 2010, 69,552 RURs were granted at $14.09 based on the market price equal to the weighted average trading price of the Units for the five trading days prior to the grant date with a fair value of $972.

On October 8, 2010, 743 RURs were cancelled at a fair value of $10.

On February 22, 2011, 99,537 RURs were granted at $18.37 based on the market price equal to the weighted average trading price of the Units for the five trading days prior to the grant date with a fair value of $1,871.

The fair value of such RURs represents the closing price of the Units on the TSX on the last trading day on which the Units traded prior to the reporting date, representing the fair value of the redemption price.

The details of the RURs granted under the RUR Plan (including the Distribution RURs) are as follows:

| | March 31, 2011 | | | March 31, 2010 | | |
|---|---|---|---|---|---|---|
| | Weighted Avg Issue Price | Fair Value per Unit | Number of Units | Weighted Avg Issue Price | Fair Value per Unit | Number of Units |
| Outstanding at period start | **$ 14.19** | **$ 17.14** | **72,887** | $ – | $ 14.06 | – |
| Granted during the period | **$ 18.37** | **$ 18.80** | **99,537** | $ 14.09 | $ 13.97 | 69,552 |
| Additional Unit Distributions | **$ 18.12** | **$ 18.12** | **1,583** | $ 14.32 | $ 14.32 | 439 |
| Outstanding at period end | **$ 16.62** | **$ 19.46** | **174,007** | $ 14.09 | $ 14.35 | 69,991 |

### *e) EUPP*

The EUPP grants employees the right to receive an additional amount equal to 10% of the Units they acquire, paid in the form of additional Units. This additional amount is expensed as compensation upon issuance of the Units.

## 17. Financial Instruments and Risk Management

### *a) Fair value of financial instruments*

The fair value of CAPREIT's financial assets and liabilities, except as noted below and elsewhere in the consolidated interim financial statements, approximate their carrying amount due to the short-term and variable rate nature of those instruments.

At March 31, 2011, the fair value of CAPREIT's mortgages payable is estimated to be $1,696,000 (December 31, 2010 - $1,705,000; January 1, 2010 - $1,568,000) due to changes in interest rates since the dates the individual mortgages were financed and the impact of the passage of time on the primarily fixed rate nature of CAPREIT's mortgages. The fair value of the mortgages payable are based on discounted future cash flows using rates that reflect current rates for similar financial instruments with similar duration, terms and conditions.

CAPREIT has classified and disclosed the fair value for each class of financial instrument based on the fair value hierarchy in accordance with IFRS 7. The fair value hierarchy distinguishes between market value data obtained from independent sources and CAPREIT's own assumptions about market value. The hierarchy levels are defined below:

Level 1 - Inputs based on quoted prices in active markets for identical assets or liabilities;

Level 2 - Inputs based on factors other than quoted prices included in Level 1 and may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates and yield curves that are observable at commonly quoted intervals; and

Level 3 - Inputs which are unobservable for the asset or liability, and are typically based on CAPREIT's own assumptions, as there is little, if any, related market activity.

CAPREIT's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgement, and considers factors specific to the asset or liability.

The following table presents CAPREIT's estimates of assets and liabilities measured at fair value on a recurring basis based on information available to management as of March 31, 2011, and aggregated by the level in the fair value hierarchy within which those measurements fall. These estimates are not necessarily indicative of the amounts CAPREIT could ultimately realize.

| | Level 1<br>Quoted prices in active markets for identical assets and liabilities | Level 2<br>Significant other observable inputs | Level 3<br>Significant unobservable inputs | Total |
|---|---|---|---|---|
| **Assets** | | | | |
| Restricted cash | $ 2,854 (1) | $ – | $ – | $ 2,854 |
| Investments | $ 34,289 (2) | $ – | $ – | $ 34,289 |
| Derivative financial instruments - utilities | $ 1 (3) | $ 1,090 (4) | $ – | $ 1,091 |
| **Liabilities** | | | | |
| Derivative financial instruments - interest | $ – | $ 2,834 (5) | $ – | $ 2,834 |
| Derivative financial instruments - utilities | $ – | $ 2,714 (4) | $ – | $ 2,714 |
| Total | $ 37,144 | $ 6,638 | $ – | $ 43,782 |

(1) CAPREIT's restricted cash is accounted for as FVTPL and measured at fair value.

(2) CAPREIT's investments are accounted for as available-for-sale and are measured at fair value based on the quoted market price in an active market of the asset.

(3) CAPREIT has entered into fixed price supply contract derivatives for the physical delivery of natural gas and hydro, some of which are measured at fair value using quoted spot and forward market prices.

(4) CAPREIT uses certain derivative financial instruments to manage its price risk with respect to energy costs. The valuation of these instruments is determined using widely accepted valuation techniques, netting the future notional cash payments based on the fixed prices specified in the contracts and the expected notional cash receipts, which are estimated using an expectation of future natural gas prices (forward curves) derived from observable market forward pricing curves. CAPREIT also considers the impact of credit valuation adjustments to reflect both its risk and the counterparty's risk in the fair value measurements of CAPREIT's natural gas derivative financial instruments.

(5) CAPREIT uses certain derivative financial instruments to manage its interest rate risk. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of the derivatives. The fair value of the interest rate swap agreement is determined using the market standard methodology of netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves. CAPREIT also incorporates credit valuation adjustments to reflect both its risk and the counterparty's risk in the fair value measurements of CAPREIT's derivative financial instruments.

Although CAPREIT has determined that the majority of the inputs used to value its derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads, to evaluate the likelihood of default by CAPREIT itself. As of March 31, 2011, CAPREIT has assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and has determined that the credit valuation adjustment is not significant to the overall valuation of the derivative. As a result, CAPREIT has determined that the derivative valuations in their entirety should be classified in Level 2 of the fair value hierarchy.

***b) Risk management***

The main risks arising from CAPREIT's financial instruments are interest rate, liquidity and credit risks. CAPREIT's approach to managing these risks is summarized as follows:

***Interest rate risk***

CAPREIT is subject to the risks associated with debt financing, including the risk that mortgages and credit facilities will not be able to be refinanced on terms as favourable as those of the existing indebtedness. In addition, interest on CAPREIT's bank indebtedness is subject to floating interest rates. For the years ended March 31, 2011 and 2010, a 100 basis point change in interest rates would have the following effect:

| | **Change in interest rates (basis points)** | **Increase (decrease) in net income** | | **Increase (decrease) in OCI** | |
|---|---|---|---|---|---|
| | | **2011** | **2010** | **2011** | **2010** |
| Floating rate debt | +100 | **$ (109)** | $ (395) | **$ –** | $ – |
| Floating rate debt | -100 | **$ 109** | $ 395 | **$ –** | $ – |
| Interest rate swap agreements | +100 | **$ –** | $ – | **$ 827** | $ 1,372 |
| Interest rate swap agreements | -100 | **$ –** | $ – | **$ (837)** | $ (1,250) |

CAPREIT's objective of managing interest rate risk is to minimize the volatility of earnings. As at March 31, 2011, interest rate risk has been minimized as all but $49,554 or 3.02% of mortgages payable are financed at fixed interest rates, with maturities staggered over a number of years.

***Liquidity risk***

Liquidity risk is the risk that CAPREIT may encounter difficulties in accessing capital and refinancing its financial obligations as they come due. Approximately 95.7% of CAPREIT's mortgages are CMHC-insured (excluding a $55,000 mortgage on the portfolio of MHC land lease sites), which reduces the risk of mortgage refinancings. CAPREIT's overall risk for mortgage refinancings is further reduced as the unamortized mortgage insurance premiums are transferable between approved lenders and are effective for the full amortization period of the underlying mortgages ranging between 25 to 35 years. To mitigate the risk associated with the refinancing of maturing debt, CAPREIT staggers the maturity dates of its mortgage portfolio over a number of years.

In addition, CAPREIT manages its overall liquidity risk by maintaining sufficient available credit facilities to fund its ongoing operational and capital commitments, distributions to Unitholders and provide future growth in its business. As at March 31, 2011, CAPREIT had undrawn lines of credit in the amount of $198,032 (December 31, 2010 - $223,545).

The contractual maturities and repayment obligations of CAPREIT's financial liabilities as at March 31, 2011 are as follows:

| ($ Thousands) | 2011 | 2012-2013 | 2014-2015 | 2016 onward |
|---|---|---|---|---|
| Mortgages payable | $ 181,677 | $ 475,329 | $ 418,898 | $ 565,108 |
| Bank indebtedness | 1,202 | 58,160 | – | – |
| Mortgage interest (1) | 53,703 | 108,823 | 67,015 | 89,477 |
| Bank indebtedness interest (1) | 1,788 | 3,521 | – | – |
| Liabilities associated with investment properties | 2,782 | 5,113 | 4,517 | 44,156 |
| Other liabilities | 44,372 | 1,233 | – | – |
| Security deposits | 19,458 | – | – | – |
| Unit-based compensation financial liabilities | 20,868 | 591 | – | – |
| Exchangeable Units | 8,004 | – | – | – |
| Distributions payable | 6,919 | – | – | – |
| | $ 340,773 | $ 652,770 | $ 490,430 | $ 698,741 |

(1) Based on current in place interest rates.

***Credit risk***

Credit risk is the risk that: (i) counterparties to contractual financial obligations will default; and (ii) the possibility that CAPREIT's residents may experience financial difficulty and be unable to meet their rental obligations.

CAPREIT monitors its risk exposure regarding obligations with counterparties through the regular assessment of counterparties' credit positions.

CAPREIT mitigates the risk of credit loss with respect to residents by evaluating the creditworthiness of new residents, obtaining security deposits wherever permitted by legislation, and geographically diversifying its portfolio.

CAPREIT monitors its collection experience on a monthly basis and ensures that a stringent policy is adopted to provide for all past due amounts. All residential accounts receivable balances exceeding 30 days are written off to bad debt expense and recognized in the consolidated statements of income and comprehensive income. Subsequent recoveries of amounts previously written off are credited in the consolidated statements of income and comprehensive income. Accordingly, no allowance for doubtful accounts is established.

## 18. Realized and Unrealized Gains and Losses on Derivative Financial Instruments

### a) Contracts for which hedge accounting is no longer effective

During 2005, CAPREIT entered into interest rate forward contracts aggregating to $145,740 (the "Interest Rate Forward Contracts") to hedge its exposure to the potential rise in interest rates for refinancings of mortgages maturing in 2009.

CAPREIT settled these interest rate forward contracts in 2009. The associated cumulative unamortized loss of $9,908 included in AOCL at September 30, 2008 will be amortized to mortgage interest expense over the original terms of the hedged contracts. For the three months ended March 31, 2011 and 2010, $264 and $274, respectively, was amortized from AOCL to mortgage interest expense.

### b) Contracts for which hedge accounting is being applied

As at March 31, 2011, CAPREIT has a $55,000 interest rate swap agreement fixing the interest rate at 5.706%, maturing in July 2012, for which hedge accounting is being applied. The agreement effectively converts borrowings on a bankers' acceptance-based floating rate credit facility to a fixed rate facility for a five-year term. For the three months ended March 31, 2011 and 2010, an unrealized gain of $906 and $706, respectively has been included in OCI (note 21). In addition, for the three months ended March 31, 2011 and 2010, an unrealized loss of $156 and

$54, respectively has been recognized in the consolidated statements of income and comprehensive income for the ineffective portion of the interest rate swap agreement. The mark-to-market cumulative unrealized loss of $2,834 and $3,119 is included in AOCL and has been set up in other liabilities as at March 31, 2011 and December 31, 2010, respectively.

The position of unrealized gains and losses on the interest rate swap agreement has been summarized as follows:

| **As at March 31,** | **2011** | 2010 |
|---|---|---|
| Opening cumulative unrealized loss, beginning of the period | **$ (3,119)** | $ (4,850) |
| Unrealized gain included in OCI | **906** | 706 |
| Unrealized loss included in net income | **(156)** | (54) |
| Closing cumulative unrealized loss, end of the period | **(2,369)** | (4,198) |
| Realized loss included in other current liabilities | **(465)** | (578) |
| Net cumulative loss, end of period | **$ (2,834)** | $ (4,776) |

**c) Natural gas contracts**

Effective March 1, 2010, CAPREIT adopted a natural gas supply strategy that, in effect, converted substantially all of the fixed price natural gas commitments through October 2012 (see note 26) to spot pricing arrangements through the amendment of physical delivery contracts and the use of derivative financial instruments. The amended arrangement is comprised of a physical delivery contract at spot pricing, a floating-to-fixed derivative financial instrument with the natural gas supplier and an offsetting fixed-to-floating derivative financial instrument with a Canadian chartered bank.

CAPREIT has elected not to apply hedge accounting to these derivative financial instruments, which will be marked-to-market through the statement of income on an ongoing basis. As at March 31, 2011, a mark-to-market unrealized loss of $2,714 on the floating-to-fixed derivative financial instrument has been recorded in other liabilities and a mark-to-market unrealized gain of $1,090 on the fixed-to-floating derivative financial instrument has been recorded in other assets.

As a result of the amendment of the fixed price natural gas commitments, for the three months ended March 31, 2011 and 2010, the inherent net loss of $nil and $4,497, respectively has been crystallized and has been included in the consolidated statements of income and comprehensive income.

During the last half of 2010, through the use of floating-to-fixed derivative financial instruments, CAPREIT hedged a significant portion of its variable rate natural gas commitments (see note 26), which will be marked-to-market through OCI on an ongoing basis. During the quarter ended March 31, 2011, the instrument was settled and a mark-to-market gain of $141 on the floating-to-fixed derivative financial instruments was recorded in OCI.

The position of realized and unrealized gains and losses on the natural gas derivative financial instruments has been summarized as follows:

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| Unrealized gain (loss) included in net loss on natural gas contracts | $ 87 | $ (5,878) |
| Unrealized (loss) gain included in net loss on natural gas contracts | (87) | 1,381 |
| Net loss on natural gas contracts included in net income during the period | - | (4,497) |
| Opening cumulative unrealized net loss, beginning of the period | (4,497) | - |
| Net realized gain relating to supply arrangements for the period | 2,732 | 288 |
| Cumulative unrealized net loss included in net income, end of the period | (1,765) | (4,209) |
| Net gain on natural gas contracts included in OCI | 141 | - |
| Closing cumulative unrealized net loss, end of the period | $ (1,624) | $ (4,209) |

| | March 31, 2011 | March 31, 2010 | December 31, 2010 |
|---|---|---|---|
| Unrealized gain included in other assets | $ 1,090 | $ 1,286 | $ 1,360 |
| Unrealized loss included in other liabilities (1) | (2,714) | (5,495) | (3,708) |
| Closing cumulative unrealized net loss, end of the period | $ (1,624) | $ (4,209) | $ (2,348) |

(1) December 31, 2010 includes the mark-to-market unrealized loss of $3,567 on the floating-to-fixed derivative financial instrument for which hedge accounting is not being applied and the $141 unrealized loss on the mark-to-market unrealized loss on the floating-to-fixed derivative financial instrument for which hedge accounting is being applied.

## 19. Capital Management

CAPREIT defines capital as the aggregate of Unitholders' equity, liabilities associated with investment properties, mortgages payable, bank indebtedness, Unit-based compensation financial liabilities, Exchangeable Units and other non-current liabilities. CAPREIT's objectives when managing capital are to safeguard its ability to continue to fund its distributions to Unitholders, to meet its repayment obligations under its mortgages and credit facilities, and to ensure sufficient funds are available to meet capital commitments. Capital adequacy is monitored against investment and debt restrictions contained in CAPREIT's DOT and Credit Facilities.

CAPREIT's Credit Facilities (note 13) require compliance with certain financial covenants. In addition, borrowings must not exceed the borrowing base, calculated at a predefined percentage to the market value of the properties.

In the short term, CAPREIT utilizes the Acquisition and Operating Facility to finance its capital investments, which may include acquisitions. In the long term, equity issuances, mortgage financings and refinancings, including "top ups", are put in place to finance the cumulative investment in the property portfolio and ensure that the sources of financing better reflect the long-term useful lives of the underlying investments.

CAPREIT is in compliance with all its investment and debt restrictions and financial covenants contained in the DOT, the LBA and the Credit Facilities. The covenants were amended effective June 30, 2010 to incorporate changes made under the renewal of the Credit Facilities as discussed in note 13.

The total capital managed by CAPREIT and the results of its compliance with the key covenants are summarized as follows:

| As at | | March 31, 2011 | December 31, 2010 | January 1, 2010 |
|---|---|---|---|---|
| Mortgages payable | | **$ 1,605,277** | $ 1,603,027 | $ 1,517,206 |
| Bank indebtedness | | **59,362** | 39,358 | 146,891 |
| Liabilities associated with investment properties | | **56,568** | 56,568 | 50,662 |
| Unit-based compensation financial liabilities | | **21,459** | 16,410 | 10,077 |
| Exchangeable Units | | **8,004** | 7,050 | 5,783 |
| Unitholders' equity | | **1,351,974** | 1,355,445 | 749,091 |
| Total capital | | **$ 3,102,644** | $ 3,077,858 | $ 2,479,710 |
| | Threshold | | | |
| Total debt to gross book value [1] | Maximum 70.00% | **52.28%** | 51.80% | 55.42% |
| Tangible net worth [2] | Minimum $700,000 [3] | **$ 1,351,974** | $ 1,355,445 | $ 849,091 |
| Debt service coverage ratio (times) [4] | Minimum 1.20 | **1.34** | 1.33 | N/A [5] |
| Interest coverage ratio (times) [6] | Minimum 1.50 | **2.11** | 2.07 | N/A [5] |

(1) CAPREIT's DOT limits the maximum amount of total debt to 70% of the gross book value ("GBV") of CAPREIT's total assets. GBV is defined as the historical book value of CAPREIT's assets plus fair value adjustments plus accumulated amortization on property, plant and equipment and deferred loan costs. In addition, the DOT provides for investment restrictions on type and maximum limits on single property investments.

(2) Tangible net worth is generally represented by Unitholders' Equity and is defined as the sum of: i) Units issued; ii) contributed surplus; and iii) retained earnings after adding back the provision for deferred income taxes payable to a maximum limit of $100,000. Effective June 30, 2010, this definition includes the sum of accumulated depreciation and amortization and, to a maximum of $50,000, deferred taxes payable on any capital Unit-based investment transactions.

(3) Effective June 30, 2010 (January 1, 2010 - $400,000).

(4) Debt service coverage ratio is defined as earnings before interest, income taxes, depreciation and amortization and other adjustments including non-cash compensation costs less income taxes paid divided by principal and interest payments.

(5) This ratio is calculated on a rolling twelve month basis. As the results for the twelve month period ended January 1, 2010 are primarily under Canadian GAAP, the ratio is not calculated on a comparable basis to IFRS and is therefore not disclosed. Actual results may be found in CAPREIT's 2010 Annual Report.

(6) Interest coverage ratio is defined as earnings before interest, income taxes, depreciation and amortization and other adjustments including non-cash compensation costs less income taxes paid divided by interest expense.

### 20. Deferred Income Taxes

Prior to June 22, 2007, no provision for income taxes was recorded in the consolidated financial statements. On June 22, 2007, amendments to the Tax Act were substantively enacted (as a result of tax legislation included in Bill C-52, the *Budget Implementation Act, 2007*), which modified the tax treatment of certain publicly traded trusts and partnerships that are specified investment flow-through trusts or partnerships ("SIFTs"). Under the SIFT Rules, a SIFT will generally be taxed in a manner similar to a corporation on income from a business carried on in Canada by the SIFT and income (other than taxable dividends) or capital gains from non-portfolio properties (as defined in the Tax Act) at a combined federal/provincial tax rate similar to that of a corporation. Allocations or distributions of income and capital gains that are subject to the SIFT Rules will be taxed as a dividend from a taxable Canadian corporation in the hands of the beneficiaries or partners of the SIFT. Subject to the normal growth guidelines issued in a press release by the Department of Finance (Canada) on December 15, 2006 (the "Normal Growth Guidelines"), the SIFT Rules will not apply until the 2011 taxation year to trusts or partnerships that would have been SIFTs on October 31, 2006 if the "SIFT trust" and "SIFT partnership" definitions in the Tax Act had been in force as of that date.

Certain real estate investment trusts that satisfy specified conditions (the "REIT Exception"), including a condition that the trust not exceed the Normal Growth Guidelines, are excluded from the SIFT definition and therefore will not be subject to taxation under the SIFT Rules. As CAPREIT did not meet the REIT Exception prior to January 1, 2010 or March 31, 2010, deferred income tax liability in the amounts of $440,507 and $435,625 were recorded as at those dates, respectively,

based on the temporary differences between the carrying amount of assets and liabilities and their carrying amounts for tax purposes. As at December 31, 2010, CAPREIT qualified for the REIT Exception and is therefore not subject to taxation as a SIFT. As a result, the non-cash deferred tax liability was reversed at December 31, 2010. The change in the deferred income tax liability has been recorded as a recovery to the consolidated statements of income and comprehensive income in the amount of $435,733 for the year ended December 31, 2010 and a recovery to other comprehensive income for $4,774 relating to the unrealized loss on derivative financial instruments and interest rate swap agreements. CAPREIT is not currently taxable and accordingly, no current income taxes have been recorded for 2011 and 2010. Comparative deferred income tax amounts are calculated using the substantively enacted SIFT tax rate applicable as at the reporting date.

A reconciliation of income tax (recovery) expense for the year is as follows:

| **For The Three Months Ended March 31,** | **2011** | **2010** |
|---|---|---|
| Current income taxes at Canadian statutory tax rate | **$ –** | $ – |
| Recovery relating to OCI | **–** | (7) |
| Provision for changes in substantively enacted tax rates for OCI | **–** | – |
| Provision for changes in substantively enacted tax rates | **–** | – |
| Recovery related to timing differences expected to reverse (1) | **–** | (4,875) |
| Deferred income tax recovery | **$ –** | $ (4,882) |

(1) Includes impact of acquisitions and dispositions.

The deferred income tax liability is as follows:

| **As at** | **March 31, 2011** | **December 31, 2010** |
|---|---|---|
| Balance, beginning of period | **$ –** | $ 440,507 |
| Recovery relating to OCI | **–** | (4,774) |
| Recovery (1) | **–** | (435,733) |
| Balance, end of period | **$ –** | $ – |

(1) Includes impact of acquisitions and dispositions.

The components of the deferred income tax liability are as follows:

| **As at** | **March 31, 2011** | **December 31, 2010** | **January 1, 2010** |
|---|---|---|---|
| Carrying value in excess of tax base of investment properties | **$ –** | $ – | $ (429,221) |
| Relating to OCI | **–** | – | (4,774) |
| Other | **–** | – | (6,512) |
| Deferred income tax liability, end of period | **$ –** | $ – | $ (440,507) |

The tax component of each item in OCI is as follows:

| **As at** | **March 31, 2011** | **December 31, 2010** | **January 1, 2010** |
|---|---|---|---|
| Loss on interest rate swap agreements | **$ –** | $ – | $ (966) |
| Loss on amounts designated as cash flow hedges settled in prior years and transferred to mortgage interest expense | **–** | – | (3,808) |
| | **$ –** | $ – | $ (4,774) |

### 21. Accumulated Other Comprehensive Loss

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| **AOCL balance, beginning of period** | **$ (11,085)** | $ (24,424) |
| Amortization of AOCL to mortgage interest (1) | **264** | 274 |
| Gain on interest rate swap agreements | **906** | 706 |
| Recovery of future income taxes | **–** | 7 |
| Gain on natural gas hedges | **141** | – |
| Loss on amounts designated as cash flow hedges settled in prior years and transferred to interest on mortgages payable | **(20)** | (33) |
| Unrealized loss on the change in fair value of investments | **(99)** | (1,717) |
| **Other comprehensive income (loss)** | **1,192** | (763) |
| **AOCL balance, end of period** | **$ (9,893)** | $ (25,187) |

| | March 31, 2011 | December 31, 2010 | January 1, 2010 |
|---|---|---|---|
| AOCL comprised of: | | | |
| Loss on derivative financial instruments | | | |
| Cumulative realized loss (1) | **$ (9,908)** | $ (9,908) | $ (9,908) |
| Accumulated amortization to interest on mortgages payable | **2,128** | 1,864 | 592 |
| Loss on interest rate swap agreements | **(2,781)** | (3,687) | (5,592) |
| Provision for deferred income taxes | **–** | – | (4,774) |
| Loss on natural gas hedges | **–** | (141) | – |
| Unamortized balance of loss on cash flow hedges previously settled | **(109)** | (89) | 31 |
| Unrealized gain on the change in fair value of investments | **777** | 876 | (4,773) |
| AOCL balance, end of period | **$ (9,893)** | $ (11,085) | $ (24,424) |

(1) The cumulative realized loss on derivative financial instruments aggregating to $9,908 before tax will be amortized as mortgage interest expense to the consolidated statements of income and comprehensive income over periods ending in December 2014 to September 2022, being the original terms of the hedged contracts. The estimated amount of the amortization that is expected to be reclassified to net income from AOCL in the next 12 months is $1,075.

### 22. Severance and Other Employee Termination Costs

In the three months ended March 31, 2011 and 2010, $nil and $150, respectively, of severance and other employee termination costs were incurred.

### 23. Amortization

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| Amortization of property, plant and equipment | **$ 394** | $ 329 |
| Amortization of deferred loan costs on credit facilities | **253** | 322 |
| | **$ 647** | $ 651 |

### 24. Supplemental Cash Flow Information

#### *a) Net income items related to investing and financing activities*

| Three Months Ended March 31, | | 2011 | | 2010 |
|---|---|---|---|---|
| Investment income received | $ | (465) | $ | (462) |
| Interest paid on Exchangeable Units | | 111 | | 111 |
| Interest paid on mortgages payable | | 18,537 | | 18,738 |
| Interest paid on bank indebtedness | | 1,063 | | 1,496 |
| | $ | 19,246 | $ | 19,883 |

#### *b) Changes in non-cash operating assets and liabilities*

| Three Months Ended March 31, | | 2011 | | 2010 |
|---|---|---|---|---|
| Prepaid expenses | $ | (1,331) | $ | (1,389) |
| Tenant inducements and direct leasing costs | | 110 | | 107 |
| Other receivables | | 606 | | (555) |
| Other assets | | (76) | | (1) |
| Deposits on purchases | | – | | 491 |
| Deposits | | (4,325) | | (845) |
| Accounts payable and other liabilities | | (2,756) | | (6,872) |
| Security deposits | | 287 | | 159 |
| | $ | (7,485) | $ | (8,905) |

#### *c) Net cash distributions to Unitholders*

| Three Months Ended March 31, | | 2011 | | 2010 |
|---|---|---|---|---|
| Distributions declared to Unitholders | $ | (20,093) | $ | (17,813) |
| Add: Distributions payable at beginning of period | | (6,678) | | (5,930) |
| Less: Distributions payable at end of period | | 6,708 | | 5,942 |
| Less: Distributions to participants in the DRIP | | 3,710 | | 1,811 |
| | $ | (16,353) | $ | (15,990) |

#### *d) Capital investments*

| Three Months Ended March 31, | | 2011 | | 2010 |
|---|---|---|---|---|
| Capital investments | | (13,822) | $ | (8,466) |
| Change in accounts payable and other liabilities | | (9,970) | | (5,563) |
| | $ | (23,792) | $ | (14,029) |

***e) Disposition of investment property***

| Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| Proceeds | $ 5,975 | $ – |
| Closing costs | (249) | – |
| Mortgages assumed by purchasers and discharged | (2,117) | – |
| Net proceeds | $ 3,609 | $ – |

## 25. Related Party Transactions

***a)*** CAPREIT incurred the following transactions with key management personnel and trustees. The loans outstanding from key management personnel and trustees for indebtedness relating to the SELTIP and LTIP at March 31, 2011 were $8,585 and $14,111, respectively (March 31, 2010 - $8,754 and $16,420, respectively). These amounts are included in the Unit Capital of the consolidated balance sheet and are taken into consideration when calculating the fair value of the Unit-based compensation liabilities. Key management personnel are eligible to participate in the EUPP. In addition, certain key management personnel also participate in the RUR and trustees currently participate in the DUP. Pursuant to employee contracts, key management personnel are subject to termination benefits that entitle them to payments up to 36 months of benefits (based on base salary, bonus and other benefits) depending on cause.

Key management personnel and trustee compensation included in trust expenses in the consolidated statements of income and comprehensive income is comprised of:

| For The Three Months Ended March 31, | 2011 | 2010 |
|---|---|---|
| Short-term employee benefits | $ 812 | $ 668 |
| Unit-based compensation - grant date amortization | 268 | 256 |
| Unit-based compensation - fair value remeasurement | 3,545 | 17 |
| Total | $ 4,625 | $ 941 |

***b)*** CAPREIT has entered into construction management agreements with a company that is owned by two trustees and officers of CAPREIT to provide construction management services (based on 4.5% of construction costs up to $20,000, 3% for the next $15,000 and 1% thereafter) to carry out the capital improvements for the properties. The total construction management fees for the three months ended March 31, 2011 and 2010 (excluding HST/GST) amounted to $295 and $222, respectively, and have been capitalized to income properties. At March 31, 2011, there were construction management fees outstanding of $111 (December 31, 2010 - $72) in accounts payable and other liabilities.

***c)*** CAPREIT has a lease for office space with a company in which one of the trustees and officers has an 18% beneficial interest. The rent paid for the office space (which is based on fair market rents at the date the lease was entered into) for the three months ended March 31, 2011 and 2010 was $189 and $176, respectively, including property operating costs and has been expensed as trust expenses. The lease agreement expires on October 31, 2014. Minimum annual rental payments for the next four years are as follows:

| | Remaining in 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|
| **Minimum annual rent** | $ 305 | $ 407 | $ 407 | $ 339 |

### 26. Commitments

***Natural gas and hydro***

Through the combination of fixed and variable price contracts, CAPREIT is committed as at March 31, 2011, in the aggregate amount of $7,501 for its natural gas and $9 for its hydro requirements. These commitments, which range from one to two years, fix the price of natural gas and hydro for a portion of CAPREIT's natural gas and hydro requirements. Certain of these contracts have been designated for CAPREIT's own use. The fixed price component of the natural gas commitments is 7.69% or $577 of the total commitments.

Effective March 1, 2010, through the use of derivative financial instruments, CAPREIT, in effect, converted substantially all of the fixed price natural gas commitments to spot pricing arrangements (see note 17).

During the third quarter of 2010, through the use of floating-to-fixed derivative financial instruments with a Canadian chartered bank, CAPREIT hedged a significant portion of its variable rate natural gas commitments for the period of November 2010 through March 2011 ("Winter 2011") into fixed rate commitments and elected to use hedge accounting. Rates for Winter 2011 have been fixed at $4.32 per gigajoule for 2,700 gigajoules per day.

During the fourth quarter of 2010, CAPREIT entered into a second floating-to-fixed derivative financial instrument with a Canadian chartered bank, hedging a portion of its variable rate natural gas commitments for Winter 2011 into fixed rate commitments and elected to use hedge accounting. Rates for Winter 2011 have been fixed at $3.58 per gigajoule for 500 gigajoules per day.

During 2009, CAPREIT entered into hydro purchase agreements to fix future rates for its Alberta properties. Rates have been fixed for CAPREIT's Edmonton and Calgary properties for the periods covering May 1, 2011 to April 30, 2014 and March 1, 2011 to February 28, 2014, respectively. The new purchase agreements meet the requirement for hedge accounting as they set the minimum quantity requirement at 0% of expected usage and therefore, do not require "net settlement" of unused volume and are not included in the $9 referenced above.

***Land Leasehold Interests***

Three of the properties have ground leases with various expiry dates (subject to revisions at periodic intervals) between March 31, 2045 and March 31, 2070. Generally, each lease provides for annual rent and additional rent calculated from the results of property operations. During the three months ended March 31, 2011 and 2010, total expenses under these three leases were $541 and $542, respectively.

In addition, CAPREIT has two leasehold interests, expiring on September 30, 2013 and May 31, 2014, in land parcels used in conjunction with two of its existing freehold properties. Total expenses under these two leases during the three months ended March 31, 2011 and 2010 were $6 and $2, respectively.

Annual lease payments under these five leasehold interests are included in property operating costs. Minimum annual rent for the next five years under these five leases is as follows:

| | Remaining in 2011 | 2012 | 2013 | 2014 | 2015 | Thereafter |
|---|---|---|---|---|---|---|
| **Minimum annual rent** | $ 968 | $ 1,290 | $ 1,287 | $ 1,274 | $ 1,273 | $ 43,965 |

***Property capital investments***

Commitments primarily related to capital investments in investment properties of $35,140 were outstanding as at March 31, 2011 (December 31, 2010 - $13,624). In addition, under the terms of residential mortgage financing arrangements, CAPREIT is obligated to incur minimum levels of property capital investments and repairs and maintenance costs on its investment properties.

## 27. Contingencies

CAPREIT is contingently liable under guarantees provided to certain of CAPREIT's lenders in the event of default, and with respect to litigation and claims that arise in the ordinary course of business. Matters relating to litigation and claims are generally covered by insurance.

## 28. Subsequent Event

**a)** On April 15, 2011, CAPREIT completed the acquisition of a 495-suite portfolio in Richmond and New Westminster, British Columbia. The purchase price was $72,000 and was funded through new CMHC-insured mortgages totalling $49,369, at an effective interest rate of 4.38%, for ten-year terms, maturing on May 1, 2021 and the balance from the Acquisition and Operating Facility.

# *Unitholder Information*

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**STOCK EXCHANGE LISTING**

Units of CAPREIT are listed on the Toronto Stock Exchange under the trading symbol "CAR.UN."