



**AUTOCANADA INCOME FUND**

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

For the three and six months ended June 30, 2007

As of August 9, 2007

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

The following discussion and analysis should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes (the "Interim Financial Statements") of AutoCanada Income Fund (the "Fund") for the three and six months ended June 30, 2007 and the annual consolidated financial statements and accompanying notes of the Fund for the year ended December 31, 2006. These financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). Results are reported in Canadian dollars unless otherwise stated. Unless otherwise indicated, certain dollar amounts have been rounded to the nearest thousand dollars. References to notes are to the notes of the Interim Financial Statements of the Fund unless otherwise stated.

This Management Discussion and Analysis is dated August 9, 2007.

### **FORWARD LOOKING STATEMENTS**

Certain statements in this management's discussion and analysis may constitute "forward looking" statements that involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward looking statements. These statements relate to future events or future performance and reflect the expectations of management regarding growth, results of operations, performance and business prospects and opportunities. Such forward looking statements reflect current beliefs of management or of the third parties to which they are attributed and are based on information currently available to us. In some cases, the statements use such words as "may", "will", "intend", "should", "expect", "believe", "plan", "anticipate", "estimate", "predict", "potential", "continue" or the negative of these terms or other similar terminology. These statements reflect current expectations regarding future events and operating performance and speak only as of the date of management's discussion and analysis, or in the case of third party statements as of the date on which they were made. Forward looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward looking statements, including, but not limited to, the factors discussed under "Risk Factors". Although the forward looking statements contained in management's discussion and analysis are based upon what management believes are reasonable assumptions, the Fund cannot assure you that actual results will be consistent with these forward looking statements. These forward looking statements are made as of the date of management's discussion and analysis and, except as required by applicable law, the Fund assumes no obligation to update or revise them to reflect new events or circumstances.

### **Non-GAAP Measures**

References to "EBITDA" are to earnings before interest expense (other than interest expense on floorplan financing and other interest), income taxes, depreciation and amortization and references to "distributable cash" are to cash flow provided by operating activities available for distribution to Unitholders' in accordance with the distribution policies of the Fund. Management believes that, in addition to earnings or loss, EBITDA is a useful supplemental measure of both performance and cash available for distribution before debt service, changes in working capital, capital expenditures and income taxes. Distributable cash of the Fund is a measure generally used by Canadian open-ended trusts as an indicator of financial performance. As one of the factors that may be considered relevant by prospective investors is the cash distributed by the Fund relative to the price of the Units, management believes that distributable cash of the Fund is a useful supplemental measure that may assist prospective investors in assessing an investment in the Fund. Distributable cash is calculated as cash flows provided by operating activities, less purchases of non-growth property and equipment.

EBITDA and distributable cash are not earnings measures recognized by GAAP and do not have standardized meanings prescribed by GAAP. Investors are cautioned that EBITDA and distributable cash should not replace net earnings or loss (as determined in accordance with GAAP) as an indicator of the Fund's performance, of its cash flows from operating, investing and financing activities or as a measure of its liquidity and cash flows. The Fund's methods of calculating EBITDA and distributable cash may differ from the methods used by other issuers. Therefore, the Fund's EBITDA and distributable cash may not be comparable to similar measures presented by other issuers.

References to "absorption rate" are to the ratio of gross profits of a franchised automobile dealership from parts, service and collision repair to the fixed operating costs of the dealership. For this purpose, fixed operating costs include fixed salaries and

benefits, administration costs, occupancy costs, insurance expense, utilities expense and interest expense (other than interest expense relating to floor plan financing) of the dealerships only and do not include expenses pertaining to head office. Absorption rate is an operating measure commonly used in the retail automotive industry as an indicator of the performance of the parts, service and collision repair operations of a franchised automobile dealership. Absorption rate is not a measure recognized by GAAP and does not have a standardized meaning prescribed by GAAP. Therefore, absorption rate may not be comparable to similar measures presented by other issuers that operate in the retail automotive industry.

## OVERVIEW OF THE FUND

### Issuance of Fund Units and Acquisition

The Fund is an unincorporated, open-ended trust governed by the laws of the Province of Alberta and a Declaration of Trust dated January 4, 2006 and amended May 10, 2006. The Fund has been created to invest in the franchised automobile dealership industry through an indirect acquisition of substantially all of the assets and undertakings of Canada One Auto Group (“CAG” or the “Vendors”) and such other investments as the Trustees may determine.

**Prior to December 31, 2010, income tax obligations relating to distributions from the Fund are expected to be obligations of unitholders. As a result of new tax legislation, substantively enacted on June 12, 2007, the Fund recognized a non-cash future income tax expense in the quarter ended June 30, 2007. Current income tax does not expect to be recognized until the new tax becomes effective on January 1, 2011 at which point the distributions made by the Fund will be subject to a 31.5% tax to the extent that they are not reduced by available tax deductions. Until that time the new legislated tax does not impact the cash earnings of the business.**

The Fund commenced business operations on May 11, 2006, when it completed an initial public offering (the “IPO”) of 10,209,500 trust units (“Fund Units”), at a price of \$10 per unit, for aggregate gross proceeds of \$102,095. The costs of issuance of the units were \$8,523. Concurrent with the closing of the IPO, the Fund used the net cash proceeds from the IPO to acquire a 50.4% indirect interest in AutoCanada LP which used such net proceeds to acquire, through various limited partnerships, the net assets (the “Acquired Business”) of the Vendors. In connection with this transaction, 10,047,500 Exchangeable Units were issued to the Vendors in the amount of \$10 per unit for a total of \$100,475. On May 31, 2006, the underwriters exercised their over-allotment option for 740,000 additional units for \$7,400 thereby increasing the interest of the Fund to 54.05%.

The Fund has finalized the process of determining the issuance costs and the fair value of the assets acquired and the liabilities assumed as of March 21, 2007. The purchase price allocated to the assets acquired and the liabilities assumed, based on their fair values, is as follows:

(In thousands of dollars)	\$
Consideration	
Cash from the Offering	102,095
Issuance of Exchangeable LP Units	100,475
Issuance costs	(8,523)
	<hr/>
Total purchase price	194,047
	<hr/>
	\$
Allocated as follows:	
Net working capital	26,382
Long-term assets	12,906
Long-term liabilities	(142)
Intangible assets	77,800
Goodwill	77,101
	<hr/>
	194,047
	<hr/>

Additional information concerning the Fund is contained in the final prospectus of the Fund dated May 3, 2006, at SEDAR

([www.sedar.com](http://www.sedar.com)), the Fund's Annual Information Form for the year ended December 31, 2006 and at the Fund's website ([www.autocan.ca](http://www.autocan.ca)). The Fund's Units trade on the Toronto Stock Exchange under the symbol ACQ.UN.

### Basis of Management's Discussion and Analysis ("MD&A")

To provide more meaningful information, this MD&A refers to the operating results for the three-month and six-month periods ended June 30, 2007 of the Fund and compares these periods to the combined operating results of the Fund and CAG for similar operating accounts for the three-month and six-month periods ended June 30, 2006 (See "Non-GAAP Measures" above). We have also included in the MD&A certain historical information with respect to CAG from other periods. Readers should be cautioned that the results of operations of CAG for the period from January 1, 2006 to May 11, 2006 include certain expenses and contractual obligations that are not part of the Fund subsequent to May 11, 2006.

### The Business of the Fund

The Fund is one of Canada's largest multi-location automobile dealership groups, currently operating or managing 18 franchised dealerships in British Columbia, Alberta, Manitoba, Ontario, New Brunswick and Nova Scotia. In 2006, the 16 franchised automobile dealerships currently owned by the Fund, sold approximately 19,350 vehicles and processed approximately 215,000 service and collision repair orders in our 245 service bays. We have grown, and intend to continue to grow, our business through the acquisition of profitable franchised automobile dealerships in key markets, the organic growth of our existing dealerships, the opening of new franchised automobile dealerships, or "Open Points" and the management of franchised automobile dealerships.

Our revenues are derived from the following four inter-related business operations: new vehicle sales; used vehicle sales; parts, service and collision repair; and finance and insurance. While new vehicle sales are our most important source of revenue, they generally result in lower gross profits than used vehicle sales, parts, service and collision repair operations and finance and insurance sales. Our overall gross profit margins increase as revenues from our higher margin operations increase relative to revenues from lower margin operations.

The Fund's geographical profile is illustrated below by number of dealerships owned and managed and revenues by province for the three-month and six-month periods ended June 30, 2007 and June 30, 2006.

(In thousands of dollars except % of total and number of dealerships)	<u>June 30, 2007</u>			<u>June 30, 2006</u>		
	<u>Current Number of Dealerships</u>	<u>Revenue June 30, 2007</u>	<u>% of Total</u>	<u>Number of Dealerships</u>	<u>Revenue June 30, 2006</u>	<u>% of Total</u>
British Columbia	5	78,356	37%	4	60,824	33%
Alberta	9	92,894	43 %	6	88,070	48 %
All other	<u>4</u>	<u>43,461</u>	<u>20%</u>	<u>4</u>	<u>35,786</u>	<u>19%</u>
<b>Total</b>	<u>18</u>	<u>214,711</u>	<u>100%</u>	<u>14</u>	<u>184,680</u>	<u>100%</u>

The following table sets forth the dealerships owned or managed as at June 30, 2007 and the date opened or acquired by the Fund or CAG.

<u>Location of Dealerships</u>	<u>Operating Name</u>	<u>Franchise</u>	<u>Year Opened or Acquired</u>
Victoria, British Columbia	Victoria Hyundai	Hyundai	2006
Maple Ridge, British Columbia	Maple Ridge Chrysler Jeep Dodge	Chrysler	2005
Prince George, British Columbia	Northland Chrysler Jeep Dodge	Chrysler	2002
Prince George, British Columbia	Northland Hyundai	Hyundai	2005
Kelowna, British Columbia	Okanagan Chrysler Jeep Dodge	Chrysler	2003
Grande Prairie, Alberta	Grande Prairie Chrysler Jeep Dodge	Chrysler	1998
Grande Prairie, Alberta	Grande Prairie Hyundai	Hyundai	2005
Grande Prairie, Alberta	Grande Prairie Subaru	Subaru	1998
Grande Prairie, Alberta	Grande Prairie Mitsubishi	Mitsubishi	2007
Grande Prairie, Alberta (managed)	Grande Prairie Nissan	Nissan	2007
Edmonton, Alberta	Crosstown Chrysler Jeep Dodge	Chrysler	1994
Edmonton, Alberta	Capital Chrysler Jeep Dodge	Chrysler	2003
Sherwood Park, Alberta	Sherwood Park Hyundai	Hyundai	2006
Ponoka, Alberta	Ponoka Chrysler Jeep Dodge	Chrysler	1998
Thompson, Manitoba	Thompson Chrysler Jeep Dodge	Chrysler	2003
Woodbridge, Ontario	Colombo Chrysler Jeep Dodge	Chrysler	2005
Moncton, New Brunswick	Moncton Chrysler Jeep Dodge	Chrysler	2001
Dartmouth, Nova Scotia	Dartmouth Chrysler Jeep Dodge	Chrysler	2006

### Seasonality

We have leveled the Fund's monthly distributions to provide a steady stream of cash to Unitholders, although revenues are subject to seasonal fluctuations. The following table illustrates the quarterly variation in the sales of new and used vehicles, based on the combined results of the Fund and CAG for 2006 and the 2005, 2004 and 2003 results of CAG.

	<u>New Vehicle Sales</u>				<u>Used Vehicle Sales</u>				<u>Total Vehicles Sold</u>			
	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
First Quarter	21%	20%	19%	20%	24%	25%	23%	24%	23%	23%	22%	22%
Second Quarter	29%	28%	27%	26%	28%	27%	26%	26%	30%	28%	27%	26%
Third Quarter	28%	30%	32%	29%	27%	26%	25%	27%	26%	27%	28%	28%
Fourth Quarter	22%	22%	22%	25%	21%	22%	26%	23%	21%	22%	23%	24%

The results from operations have been lower in the first and fourth quarters of each year, largely due to consumer purchasing patterns during the holiday season, inclement weather and the reduced number of business days during the holiday season. As a result, our financial performance is generally not as strong during the first and fourth quarters than during the other quarters of each fiscal year. The timing of acquisitions may also cause substantial fluctuations in operating results from quarter to quarter.

On a year over year basis, Chrysler Canada's sales have increased in each of the last eleven months. During the first six months of 2007, Chrysler Canada's sales have increased by 7.5% over the comparable period in the prior year.

## Distributable Cash and Cash Distributions

The Fund's policy is to distribute annually to Unitholders available cash provided by operations after cash required for capital expenditures, working capital reserves, growth capital reserves and other reserves considered advisable by the Trustees of the Fund. The policy allows the Fund to make stable monthly distributions to its Unitholders based on the Fund's estimate of distributable cash for the year. The Fund pays cash distributions on or about the 15th of each month to Unitholders of record on the last business day of the previous month.

The following table summarizes the distributions of the Fund for the period of May 11, 2006 to June 30, 2007:

(In thousands of dollars)

Record date	Payment date	Fund Units		Exchangeable Units		Total	
		Declared \$	Paid \$	Declared \$	Paid \$	Declared \$	Paid \$
May 31, 2006	June 15, 2006	618	618	525	525	1,143	1,143
June 30, 2006	July 17, 2006	912	912	775	775	1,687	1,687
July 31, 2006	August 15, 2006	912	912	775	775	1,687	1,687
August 31, 2006	September 15, 2006	912	912	775	775	1,687	1,687
September 30, 2006	October 16, 2006	912	912	775	775	1,687	1,687
October 31, 2006	November 15, 2006	912	912	775	775	1,687	1,687
November 30, 2006	December 15, 2006	912	912	775	775	1,687	1,687
December 31, 2006	January 15, 2007	912	912	775	775	1,687	1,687
January 31, 2007	February 15, 2007	912	912	775	775	1,687	1,687
February 28, 2007	March 15, 2007	912	912	775	775	1,687	1,687
March 31, 2007	April 16, 2007	912	912	775	775	1,687	1,687
April 30, 2007	May 15, 2007	912	912	775	775	1,687	1,687
May 31, 2007	June 15, 2007	912	912	775	775	1,687	1,687
June 29, 2007	July 16, 2007 (1)	912	-	775	-	1,687	-
		<u>12,474</u>	<u>11,562</u>	<u>10,600</u>	<u>9,825</u>	<u>23,074</u>	<u>21,387</u>

(1) Distributions payable to all Unitholders in the amount of \$1,687 as at June 30, 2007 were paid in July, 2007.

Distributions are paid on Fund Units and Exchangeable Units. As of June 30, 2007 the following numbers of units were outstanding:

Fund Units	10,949,500
Exchangeable Units	<u>9,307,500</u>
	<u>20,257,000</u>

During the three-month and six-month periods ended June 30, 2007, the Fund declared distributions of \$0.250 and \$0.500 respectively per Fund Unit and Exchangeable Unit to Unitholders. The distributions in the period ended June 30, 2007 were funded from cash flow generated from operations. The Fund's IPO prospectus contemplated an initial distribution of \$0.0564 per unit for the month of May, 2006 and thereafter monthly distributions of \$0.0833 per unit or \$1 per year in aggregate. The Fund reviews its distribution policy on a periodic basis.

As of June 30, 2007, there are 894,318 options outstanding under the Fund's Incentive Unit Option Plan for certain employees, officers, directors and trustees. Options issued under the Plan vest at a rate of one third on the three subsequent award date anniversaries. All the options must be exercised over specified periods not to exceed five years from the dates granted. At June 30, 2007, 1,519,275 units remained reserved for issuance under the option plan.

## Distributable Cash per Unit (Fund Units and Exchangeable Units)

The following table summarizes the distributable cash of the Fund for the three-month period ended June 30, 2007 and from the inception of the Fund on January 4, 2006, which includes the results of operations from May 11, 2006 to June 30, 2007.

<b>(In thousands of dollars except unit and per unit amounts)</b>	<b><u>Q2 2007</u></b> <b>April 1, 2007 to</b> <b><u>June 30, 2007</u></b>	<b><u>From Inception</u></b> <b>January 4, 2006</b> <b>to</b> <b><u>June 30, 2007</u></b> <b>(including</b> <b>operations from</b> <b>May 11, 2006</b> <b>to June 30, 2007)</b>
	\$	\$
Cash provided by operating activities	2,368	40,210
Less: Purchase of non-growth property and equipment (1)	<u>(762)</u>	<u>(1,802)</u>
Distributable cash	<u>1,606</u>	<u>38,408</u>
Weighted average units outstanding at the end of period (2)	20,257,000	20,257,000
Distributable cash per unit	0.079	1.896
Distributions declared to unitholders	5,061	23,074
Distributions declared per unit	0.250	1.896
Distributable cash less distributions declared	(3,455)	15,335
Distributable cash less distributions declared per unit	(0.171)	0.757
Basic earnings (loss) per unit	(0.660)	(0.259)
Diluted earnings (loss) per unit	(0.657)	(0.258)

(1) Purchase of non-growth property and equipment is necessary to maintain and sustain the current productive capacity of the Fund's operations and distributable cash (see "Capital Expenditures" on the next page for details). Management believes that maintenance capital expenditures should be funded by cash flow provided by operating activities. Capital spending for the expansion of sales and service capacity is expected to improve future distributable cash and as such is not deducted from cash flow provided by operating activities.

(2) Includes Fund Units and Exchangeable Units

On November 6, 2006, the Canadian Institute of Chartered Accountants released a draft interpretive release regarding the preparation and disclosure of distributable cash for income trusts and other flow-through entities. The definition of distributable cash outlined in this release has been applied by the Fund in calculating distributable cash both for second quarter of 2007 and from inception. On July 18, 2007, the Canadian Institute of Chartered Accountants released a revised interpretive release regarding the preparation and disclosure of distributable cash for income trust and other flow-through entities. The Fund is determining the impact of this release on its calculation of distributable cash.

Distributable cash from April 1, 2007 to June 30, 2007 varies significantly from the results of operations measured by EBITDA of \$6,743 for the same period due primarily to the net change in non-cash operating working capital balances of \$4,287. This decrease

is a result of higher accounts receivable, higher accounts payable and higher inventories net of floorplan financing. These same items will contribute to volatility in distributable cash when compared to EBITDA on a quarterly basis.

For the second quarter of 2007, the Fund generated distributable cash of \$0.079 per unit, including changes in non-cash operating working capital amounts and \$0.291 before changes in non-cash operating working capital balances, and declared distributions of \$0.250 per unit, for a payout ratio of 315% including changes in non-cash working capital amounts and 86% before changes in non-cash working capital balances.

Distributions declared to Unitholders for the period are more than distributable cash generated since the distributions of the Fund are currently \$1 per year or \$0.0833 per month and cash available for distribution will vary in connection with the seasonality and the changes in non-cash working capital balances.

### **Capital Expenditures**

The following table provides a reconciliation of the purchase of property and equipment as reported on the Statement of Cash Flows to the purchase of property and equipment as calculated in the distributable cash on the previous page:

<b>(In thousands of dollars)</b>	<b>April 1, 2007 to June 30, 2007</b>	<b>January 1, 2007 to June 30, 2007</b>
	\$	\$
Purchase of property and equipment from the Statement of Cash Flows	987	2,104
Less: Amounts related to the expansion of sales and service capacity	<u>(225)</u>	<u>(821)</u>
Purchase of non-growth property and equipment	<u>762</u>	<u>1,283</u>

Amounts relating to the expansion of sales and service capacity are considered growth expenditures. Growth expenditures are discretionary, represent cash outlays intended to provide additional future cash flows and are expected to provide benefit in future periods and thus they have been excluded from the calculation of distributable cash. Additional details on the components of non-growth property and equipment purchases are as follows:

<b>(In thousands of dollars)</b>	<b>April 1, 2007 to June 30, 2007</b>	<b>January 1, 2007 to June 30, 2007</b>
	\$	\$
Leasehold improvements	127	136
Machinery and equipment	82	236
Furniture and fixtures	174	202
Computer equipment	125	283
Company vehicles	<u>254</u>	<u>426</u>
	<u>762</u>	<u>1,283</u>

During the three-month and six-month periods ended June 30, 2007 growth capital expenditures of \$225 and \$821 respectively were incurred. These expenditures related primarily to purchases of equipment for our Sherwood Park Hyundai location which opened in November of 2006 and our Prince George Hyundai location which was recently relocated to a new dealership facility with an additional five service bays. Repairs and maintenance expenditures are expensed as incurred and have been deducted from earnings for the period. Repairs and maintenance expense incurred during the three-month and six-month periods ended June 30, 2007, were \$406 and \$834 respectively.

## SELECTED FINANCIAL INFORMATION AND RESULTS FROM OPERATIONS

The following table shows the unaudited results of: CAG for the three-month period ended March 31, 2006, combined results of CAG and the Fund for the three-month period ended June 30, 2006, results of the Fund for the 51-day period ended June 30, 2006, the three-month period ended September 30, 2006, the three-month period ended December 31, 2006, the audited results of the Fund from May 11, 2006 to December 31, 2006, the unaudited results for the three-month period ended March 31, 2007, and the three-month period ended June 30, 2007. The results of operations for these periods are not necessarily indicative of the results of operations to be expected in any given comparable period.

(In thousands of dollars except Operating Data and gross profit %)	The Fund & CAG							
	CAG	The Fund & CAG	The Fund	The Fund	The Fund	The Fund	The Fund	The Fund
	Q1 2006	Q2 2006	Q2 2006	Q3 2006	Q4 2006	2006	Q1 2007	Q2 2007
<b>Income Statement Data</b>								
Revenue	143,091	184,680	105,992	189,861	176,079	471,932	194,379	214,711
New vehicles	70,299	102,431	59,044	106,424	98,970	264,438	109,862	117,204
Used vehicles	47,772	53,546	30,487	53,897	46,425	130,809	53,020	62,389
Parts, service & collision repair	18,081	18,738	10,734	19,632	21,410	51,776	21,908	23,228
Finance, insurance & other	6,939	9,965	5,727	9,908	9,274	24,909	9,590	11,890
Gross profit	24,100	29,265	17,775	30,818	28,930	77,523	31,292	36,777
New vehicles	5,392	6,782	4,190	6,792	6,998	17,980	7,000	8,312
Used vehicle	4,158	4,766	3,294	5,563	3,614	12,471	4,914	6,082
Parts, service & collision repair	7,930	8,712	5,014	8,721	9,514	23,249	10,223	11,305
Finance, insurance & other	6,620	9,005	5,277	9,742	8,804	23,823	9,155	11,078
Gross profit %	16.8%	15.8%	16.8%	16.2%	16.4%	16.4%	16.1%	17.1%
Sales, general & admin expenses	18,492	21,469	12,245	22,481	21,682	56,408	23,634	27,522
Floorplan interest expense	1,683	2,153	1,256	1,854	2,085	5,195	2,069	2,414
Other interest & bank charges	304	93	24	117	405	546	316	326
Future income taxes	-	-	-	-	-	-	-	19,107
Net earnings (1) (5)	3,097	4,761	3,631	5,220	3,623	12,474	4,483	(13,362)
EBITDA(2) (5)	4,160	5,547	4,249	6,366	4,906	15,521	5,424	6,743
<b>Operating Data</b>								
Vehicles (new and used) sold	4,223	5,068	3,023	5,369	4,690	13,082	5,440	6,089
New retail vehicles sold	1,736	2,465	1,515	2,741	2,199	6,455	2,295	2,866
New fleet vehicles sold	440	372	211	371	525	1,107	886	535
Used retail vehicles sold	2,047	2,231	1,297	2,257	1,966	5,520	2,259	2,688
Number of service & collision repair orders completed	48,122	57,372	32,565	54,345	55,393	142,303	57,876	58,157
Absorption rate (3)	n/a	95%	n/a	97%	96%	94%	92%	94%
# of dealerships	14	14	14	14	16	16	17	18
# of service bays at period end	223	223	223	223	245	245	250	256
Same store revenue growth(4)	n/a	5%	n/a	3.8%	10.4%	n/a	24.1%	6.6%
Same store gross profit growth(4)	n/a	21%	n/a	12.5%	6.3%	n/a	20.1%	13.4%
<b>Balance Sheet Data</b>								
Cash and cash equivalents	10,926	20,271	20,271	20,265	20,880	20,880	24,268	21,077
Accounts receivable	28,417	25,875	25,875	30,562	27,742	27,742	31,200	35,980
Inventories	124,607	145,888	145,888	101,252	112,680	112,680	117,034	132,814
Revolving floorplan facility	122,454	146,283	146,283	103,297	113,357	113,357	118,974	133,731

- (1) Net earnings for CAG from January 1, 2006 to May 10, 2006 are net earnings as defined by GAAP plus income taxes, stock-based compensation and shareholder bonuses (including the performance component related to dealership management's compensation) to be consistent with the results of the Fund from May 11, 2006 to December 31, 2006.
- (2) EBITDA has been calculated as described under "Non-GAAP Measures" above. EBITDA for CAG is defined under "Non-GAAP Measures" with the exception that to facilitate comparison to the Fund we have added stock-based compensation and shareholder bonuses (including the performance component related to dealership management's compensation) expensed by CAG.
- (3) Absorption has been calculated as described under "Non-GAAP Measures" above.
- (4) Same store revenue growth & same store gross profit growth is calculated using franchised automobile dealerships that we have owned for at least 2 full years.
- (5) The results from operations have been lower in the first and fourth quarters of each year, largely due to consumer purchasing patterns during the holiday season, inclement weather and the reduced number of business days during the holiday season. As a result, our financial performance is generally not as strong during the first and fourth quarters than during the other quarters of each fiscal year. The timing of acquisitions may also cause substantial fluctuations in operating results from quarter to quarter.

## Second Quarter Operating Results

The three-month period ended June 30, 2007 showed an increase over the comparable period in 2006 in terms of EBITDA. Net earnings decreased by \$18.1 million due to the recognition of non-cash adjustment for future income taxes of \$19.1 million as a result of new tax legislation substantively enacted on June 12, 2007 which is explained in the "Outlook" section below. Excluding the effect of amended Canadian tax rules, net earnings would have increased by 20.7% to \$5.7 million for the second quarter of 2007, compared to \$4.8 million for the same period in 2006. The second quarter, along with the third quarter, are historically the industry's strongest in terms of revenues and EBITDA and the results for the second quarter of 2007 follow this pattern. EBITDA for the three-month period ended June 30, 2007 increased by 21.6% to \$6,743, from \$5,547 when compared to the same period in the prior year. SG&A expenses reduce EBITDA and included in SG&A expenses in the second quarter of 2007 are recruitment costs of approximately \$410 relating to senior executive personnel, public company costs, and unit based compensation of \$135 that would not have been incurred in the comparable period in 2006.

### Revenues

Revenues for the three-month and six-month periods ended June 30, 2007 increased to \$214.7 million and \$409.1 million, respectively from \$184.7 million and \$327.8 million when compared to the same periods in the prior year. The 16.3% and 24.8% year-over-year increases in revenue for the periods arose from \$8.2 million and \$35.5 million increases respectively in same store revenue and \$21.8 million and \$45.8 million increases respectively in revenue from acquired dealerships. For the three-month and six-month periods ended June 30, 2007, the four new dealerships that were acquired or opened during 2005, the three dealerships that were opened or acquired in 2006, and the two dealerships that were opened or acquired in 2007 accounted for approximately 61.4% and 56.3% of the increases in revenues when compared to the same periods in the prior year.

The following table summarizes the results for the three-month and six-month periods ended June 30, 2007 on a same store basis by revenue source for the nine dealerships that were owned and operated for all of 2006 and 2005 and compares these results to the results of these stores for the same period in 2006. An acquired dealership may take as long as two years in order to reach normalized operating results. As a result in order for an acquired dealership to be included in our same store analysis the dealership must be owned and operated by us for two full years.

### Same Store Revenue and Vehicles Sold

(In thousands of dollars except % change and vehicle data)	For the Three Months Ended			For the Six Months Ended		
	June 30, 2007	June 30, 2006	% Change	June 30, 2007	June 30, 2006	% Change
<b>Revenue Source</b>						
New vehicles	72,206	69,938	3.2%	144,733	120,743	19.9%
Used vehicles	38,753	35,136	10.3%	70,642	64,683	9.2%
Parts, service & collision repair	15,518	13,253	17.1%	30,437	26,528	14.7%
Finance & insurance and other	<u>7,142</u>	<u>7,050</u>	<u>1.3%</u>	<u>13,711</u>	<u>12,039</u>	<u>13.9%</u>
<b>Total</b>	<u>133,619</u>	<u>125,377</u>	<u>6.6%</u>	<u>259,523</u>	<u>223,993</u>	<u>15.9%</u>
New vehicles sold	1,971	1,865	5.7%	3,949	3,335	18.4%
Used vehicles sold	<u>1,592</u>	<u>1,438</u>	<u>10.7%</u>	<u>2,883</u>	<u>2,683</u>	<u>7.5%</u>
<b>Total</b>	<u>3,563</u>	<u>3,303</u>	<u>7.9%</u>	<u>6,832</u>	<u>6,018</u>	<u>13.5%</u>

### *Same Store Analysis*

Same store revenue increased by 6.6% and 15.9% respectively in the three-month and six-month periods ended June 30, 2007 when compared to the same period in 2006. New vehicle revenues increased by \$2.3 million or 3.2% for the three-months ended June 30, 2007 over the same period in the prior year due in part to an increase in new vehicle sales of 106 units consisting of an increase of 10 retail units and 96 low margin fleet unit sales. Offsetting this increase in new vehicle revenues for the three-month period ended June 30, 2007 was a decrease in the average selling price per new vehicle retailed (“PNVR”) of \$866 over the same period in the prior year largely as a result of a change in vehicle sales mix between vehicle types in both retail and fleet sales. New vehicle revenues increased by \$24.0 million or 19.9% for the six-months ended June 30, 2007 over the same period in the prior year due to an increase in new vehicle sales of 614 units consisting of an increase of 317 retail units and 297 low margin fleet unit sales. Also contributing to the increase in new vehicle revenues for the six-month period ended June 30, 2007 was an increase in the average selling price PNVR of \$446 over the same period in the prior year largely as a result of both a change in vehicle sales mix between vehicle types in both retail and fleet sales and manufacturer pricing.

Used vehicle revenues increased by \$3.6 million or 10.3% and \$6.0 million or 9.2% respectively in the three-month and six-month periods ended June 30, 2007 over the comparable periods in the prior year. For the three-month period ended June 30, 2007, the increase was due to a combination of an increase in the number of used vehicles sold of 154 and a decrease in the average selling price per used vehicle retailed of \$91. For the six-month period ended June 30, 2007, the increase was due to both an increase in the number of vehicles sold of 200 and an increase in the average selling price per used vehicle of \$395.

The increase in parts, service and collision repair revenue of \$2.3 million or 17.1% in the three-month period ended June 30, 2007 compared to the same period in the prior year was primarily a result of a combination of a 16.6% increase in the average revenue per service and collision repair order completed and an increase of 0.4% in the number of service and collision repair orders completed for the three-month period ended June 30, 2007. The increase in parts, service and collision repair revenue of \$3.9 million or 14.7% in the six-month period ended June 30, 2007 compared to the same period in the prior year was primarily a result of a combination of a 19.3% increase in the average revenue per service and collision repair order completed and a decrease of 3.8% in the number of service and collision repair orders completed for the six-month period ended June 30, 2007.

Finance and insurance and other revenue increased by 1.3% and 13.9% respectively in the three-month and six-month periods ended June 30, 2007 over the same period in the prior year. For the three-month period ended June 30, 2007, the increase was due to both an increase in the number of units sold of 164 and a decrease in the average revenue per unit of \$85. For the six-month period ended June 30, 2007, the increase was due to both an increase in the number of units sold of 517 and an increase in the average revenue per unit of \$90.

### ***Gross profit***

During the three-month and six-month periods ended June 30, 2007 the gross profit increased by 25.7% to \$36.8 million and 27.6% to \$68.1 million respectively when compared to the same periods in 2006. Approximately 64% and 55% of these increases in the three-month and six-month periods ended June 30, 2007 respectively were the result of the four new dealerships that were opened or acquired during 2005, the three dealerships that were acquired in 2006, and two dealerships that were opened or acquired in 2007.

The following table summarizes the results for the three-month and six-month periods ended June 30, 2007 on a same store basis by revenue source for the nine dealerships that were owned and operated for all of 2006 and 2005 and compares these results to the results of these stores for the same period in 2006.

### Same Store Gross Profit and Gross Profit Percentage

	For the Three Months Ended						For the Six Months Ended					
	Gross Profit			Gross Profit %			Gross Profit			Gross Profit %		
	June 30, 2007	June 30, 2006	% Change	June 30, 2007	June 30, 2006	% Change	June 30, 2007	June 30, 2006	% Change	June 30, 2007	June 30, 2006	% Change
<b>(In thousands of dollars except % change and gross profit %)</b>												
<b>Revenue Source</b>												
New vehicles	5,164	4,483	15.2%	7.2%	6.4%	0.8%	9,883	7,993	23.6%	6.8%	6.6%	0.2%
Used vehicles	3,446	2,859	20.5%	8.9%	8.1%	0.8%	6,030	5,216	15.6%	8.5%	8.1%	0.4%
Parts, service & collision repair	7,639	6,231	22.6%	49.2%	47.0%	2.2%	14,474	12,148	19.1%	47.6%	45.8%	1.8%
Finance & insurance and other	<u>6,779</u>	<u>6,728</u>	<u>0.8%</u>	<u>94.9%</u>	<u>95.4%</u>	<u>(0.5)%</u>	<u>13,115</u>	<u>11,516</u>	<u>13.9%</u>	<u>95.7%</u>	<u>95.7%</u>	<u>0.0%</u>
<b>Total</b>	<u>23,028</u>	<u>20,301</u>	<u>13.4%</u>	<u>17.2%</u>	<u>16.2%</u>	<u>1.0%</u>	<u>43,502</u>	<u>36,873</u>	<u>18.0%</u>	<u>16.8%</u>	<u>16.5%</u>	<u>0.3%</u>

#### *Same Store Analysis*

Same store gross profit increased by 13.4% and 18.0% in the three-month and six-month periods ended June 30, 2007 when compared to the same period in the prior year. New vehicle gross profit increased by \$0.7 million or 15.2% in the three-month period ended June 30, 2007 when compared to the same period in the prior year as a result of the previously discussed increase in new vehicle sales of 106 units largely as a result of improved operating performance in a stronger than anticipated Canadian new vehicle market. New vehicle gross profit increased by \$1.9 million or 23.6% in the six-month period ended June 30, 2007 when compared to the same period in the prior year as a result of the previously discussed increase in new vehicle sales of 614 units.

Used vehicle gross profit increased by \$0.6 million or 20.5% in the three-month period ended June 30, 2007 over the same period in the prior year. The increase was due to both an increase in the number of units sold of 154 and an increase in the average gross per used vehicle retailed of \$176. Used vehicle gross profit increased by \$0.8 million or 15.6% in the six-month period ended June 30, 2007 over the same period in the prior year. The increase was due to a combination of an increase in the number of units sold of 200 and an increase in the average gross per used vehicle retailed of \$148.

The increase in parts, service and collision repair gross profit of \$1.4 million or 22.6% in the three-month period ended June 30, 2007 was the result of a combination of an increase in the average gross profit earned per service and collision repair order completed as a result of the previously discussed 16.6% increase in average revenue earned per service and repair order completed and an increase in the number of service and collision repair orders completed for the three-month period ended June 30, 2007. The increase in parts, service and collision repair gross profit of \$2.3 million or 19.1% in the six-month period ended June 30, 2007 was the result of a combination of an increase in the average gross profit earned per service and collision repair order as a result of the previously discussed 23.4% increase in average revenue earned per service and repair order completed and an decrease in the number of service and collision repair orders completed for the six-month period ended June 30, 2007.

Finance and insurance and other gross profit increased by 0.8% and 13.9% in three-month and six-month periods ended June 30, 2007 primarily as a result of increases in units sold of 5.3% and 9.4% respectively.

### ***Selling, general and administrative expenses***

During the three-month and six-month periods ended June 30, 2007, SG&A expenses increased by 28.2% to \$27.5 million and 28.0% to \$51.2 million respectively over the same periods in the prior year due to the three dealerships that were opened or acquired in 2006 and two dealerships opened or acquired in 2007. During the three-month and six-month periods ended June 30, 2007, SG&A as a percentage of gross profit increased from 73.4% to 74.8% and from 74.9% to 75.2% respectively. SG&A as a percentage of gross profit increased primarily due to a planned increase in salary and recruitment costs at head office, unit-based compensation, and various public company costs that were not incurred in the prior year. The increase in SG&A was partially offset by the increase in the gross profit as a result of the items noted above.

### ***Amortization expense***

During the three-month period ended June 30, 2007, amortization was \$770 while it was \$786 for the prior period in 2006. The decrease is due primarily to the decrease in the amortization of leasehold improvements, which are amortized over the remaining lease term that in some cases was less than two years from May 11, 2006.

### ***Floorplan interest expense***

During the three-month and six-month periods ended June 30, 2007, floorplan interest expense increased by 12.1% to \$2,414 and 16.9% to \$4,483 over the same periods in 2006. The increase in interest expense was caused by an increase in the overall number of dealerships over the periods, an increase in average prime lending rate interest rates for the three-month and six-month periods ended June 30, 2007 when compared to the same periods in 2006 offset by a general inventory reduction of approximately \$13.1 million.

Manufacturers provide non-refundable credits on the floorplan interest to offset the dealership's cost of inventory that, on average, effectively provide the dealerships with interest-free floorplan financing for the first 45 to 60 days of ownership. During the three-month period ended June 30, 2007, the net floorplan credits were \$1,343. GAAP requires the floorplan credits to be accounted for as a reduction in the cost of new vehicle inventory and subsequently a reduction in the cost of sales as vehicles are sold.

### **Sensitivity**

Our financial performance is dependent in part upon new vehicle sales. Based on our historical financial data, management estimates that an increase or decrease of one new retail vehicle sold (and the associated finance and insurance income on the sale) would result in a corresponding increase or decrease in our estimated cash available for distribution of approximately \$1,500 per vehicle. This analysis does not take into account any operating strategies which we may employ in response to changing trends in vehicle sales.

### **Acquisitions**

On October 31, 2006, the Fund expanded its presence in Western Canada by acquiring the net operating assets of Victoria Hyundai located in Victoria, British Columbia. The dealership's sales facility and real estate are leased from a related party. Victoria Hyundai sold 464 new vehicles and 410 used vehicles in its last fiscal year ended June 30, 2006. On April 27, 2007, we announced that the renovation of this dealership was substantially completed. The new renovated dealership facilities expand the dealership from approximately 6,000 sq. ft. to 18,296 sq. ft., and offers an incremental six service bays, and a larger new car show room amongst other enhancements.

We continue to actively pursue the acquisition of additional franchised automotive dealerships in Canada that meet our investment criteria. We are currently engaged in discussions with select manufacturers' regarding obtaining approval for public ownership of franchises that they operate.

### **Open Points**

The Fund announced on May 3, 2007, that it entered into a Letter of Intent with Mitsubishi Motor Sales of Canada Inc. which awards to the Fund a Mitsubishi Open Point dealership in Grande Prairie, Alberta. The new dealership is owned by the Fund and carries on business under the name of "Grande Prairie Mitsubishi". The dealership operates out of temporary premises pending completion of a new facility which shall be designed to Mitsubishi Motor Sales of Canada Inc. image design standards and shall provide for a 4 car showroom, and 5 service bays. The temporary facility has one service bay.

The Fund has entered into letters of intent to open one new franchised automobile dealership in Western Canada with each of Hyundai Auto Canada (“Hyundai”) and DaimlerChrysler Canada Inc. (“DaimlerChrysler”). In the case of the Hyundai Open Point, to be located in Burnaby, British Columbia, the closing of the land purchase and sale agreement has been delayed pending vendor’s site preparation and clean up, the completion of which is a condition to close. Regarding the DaimlerChrysler Open Point, to be located in Calgary, Alberta, we have not yet secured land acceptable to ourselves and the manufacturer, the search for which is continuing. Once the location has been approved, in the case of DaimlerChrysler, and the appropriate development permit has been obtained in both cases, it will take approximately nine months to complete construction of each facility. We are working with both Hyundai and DaimlerChrysler, respectively, and intend to open each Open Point as soon as the land has been secured and premises built, the date of which is not certain in the case of the DaimlerChrysler Open Point, and, in our best estimate, third quarter 2008 in the case of the Hyundai Open Point. The achievement of the opening of these Open Points is subject to various risks as described in the “Risk Factors” below. Some of these risks are beyond management’s control.

On February 7, 2007 the Fund granted consents to permit Patrick Priestner to open a new Toyota automobile dealership in exchange for an annual fee. Mr. Priestner is the majority shareholder of CAG and is the Chief Executive Officer of the Fund. The Fund’s action follows its previously announced strategic intent to enhance its relationships with a wider range of manufacturers in order to develop its long-term growth prospects. The new dealership, “Sherwood Park Toyota”, consists of a 55,000-square foot showroom, sales and repair facility building containing 22 service bays located on six acres of land in a suburb of Edmonton. Although discussions between Toyota Canada and Mr. Priestner began prior to the Fund’s Initial Public Offering in May 2006, consents are required under the terms of the non-competition agreements entered into between the Fund and CAG and its shareholders at the time of the Fund’s IPO. The Fund intends to work towards obtaining the approval of Toyota Canada Inc. to permit Sherwood Park Toyota to be owned by the Fund under arrangements approved by the automobile manufacturer. There can be no assurance that the Fund will be granted such permission.

#### **Dealerships Managed by the Fund**

On February 7, 2007, the Fund entered into a credit agreement with CAG to finance the acquisition of a Nissan dealership by CAG and entered into a management agreement to provide it with management services. The Nissan dealership is owned and operated by a subsidiary of CAG which owns 46% of the Fund on a fully diluted basis. The Fund obtained the funds to finance the acquisition of the Nissan dealership through its existing Revolving Term Facility. In connection with this arrangement, the Fund has granted consents to CAG and its subsidiary under the terms of the non-competition agreements entered into at the time of the Fund’s IPO.

The dealership named “Grande Prairie Nissan”, in Grande Prairie, Alberta, was established in 1969, and sold 388 new and 196 used vehicles in 2006. The dealership will be relocated to a new location in Grande Prairie that has been approved by Nissan Canada and construction is planned to commence during the summer of 2007. The Fund’s arrangement with CAG marks an expansion of the Fund’s business structure. In addition to owning franchised automobile dealerships, the Fund will earn fees from managing and financing the acquisition of franchised automobile dealerships offered by select manufacturers where there is not an arrangement in place with the manufacturer that would allow the franchised dealership to be owned directly by the Fund.

The Fund’s strategic intent is to continue to seek to expand the range of automobile brands it sells as automobile manufacturers become more familiar with the Fund’s management, business model and unique publicly traded status. The structure may vary among dealerships and manufacturers in order to accommodate the needs of the manufacturer, the dealership, and the Fund. These relationships are intended to provide the Fund with the financial benefits associated with an expanded network of dealerships while accommodating the requirements of the various automobile manufacturers. The Fund and CAG intend to work together to obtain the approvals of the various automobile manufacturers to permit these dealerships to be owned by the Fund under arrangements approved by the automobile manufacturer. There can be no assurance that the Fund will be granted such permission.

This new arrangement gives rise to additional risks inherent in its structure which include: (i) the contractual nature of the relationships compared with the direct ownership of the dealerships; (ii) the dependency upon CAG and its principal shareholder, Patrick Priestner, as the owner and principal operator of these dealerships; and (iii) conflicts of interest that may arise between the objectives of the Fund and CAG and their respective owners and management.

As a result of the Fund’s financing of the purchase and the related agreements, the Fund has determined that the Nissan Dealership is a variable interest entity and it is the primary beneficiary as defined by CICA Accounting Guideline 15. Accordingly, the Fund will account for the entry into these agreements as a business combination and consolidate the results of the Nissan Dealership subsequent to February 7, 2007. The Fund is in the process of finalizing its measurement and valuation of the net assets of the

Nissan Dealership, including the identification of goodwill and intangible assets. Thus determination of the final purchase price and its allocation is subject to the completion of this process.

On July 13, 2007, the Fund announced that it intends to enter into a credit agreement with CAG to finance the opening of a Nissan Dealership Open Point by CAG and enter into a management agreement to provide it with management services. The Nissan Dealership Open Point will be located in Prince George, British Columbia on new premises to be built on land which has been secured and will carry on business under the name Northland Nissan to be owned and operated by a subsidiary of CAG which owns 46% of the Fund on a fully diluted basis. In connection with this arrangement, the Fund has received Board approval to grant consents to CAG and its subsidiary under the terms of the non-competition agreements entered into at the time of the Fund's IPO.

The Fund is in the process of finalizing the structure and related agreements with CAG to assess whether Northland Nissan will be a variable interest entity requiring the Fund to consolidate its results subsequent to July 13, 2007.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Cash Flow from Operating Activities**

Cash flow from operating activities of the Fund for the period from April 1, 2007 to June 30, 2007 was \$2.368 million. The Fund generates sufficient cash flow from operations to fund capital expenditures, distributions, working capital requirements and to service its debt obligations.

### **Distributable Cash and Cash Distributions**

The Fund's policy is to make stable monthly distributions to its Unitholders based on its estimate of distributable cash for the year. The Fund has a policy to pay cash distributions on or about the 15th of each month to Unitholders of record on the last business day of the previous month. As we calculate the Fund's distributable cash, we take into consideration our debt management strategy and productive maintenance and growth capital strategy.

From the inception of the Fund, the Fund has generated \$15.3 million of cash in excess of distributions declared. During the three-month period ended June 30, 2007, distributions declared exceeded distributable cash by \$3.5 million. Distributable cash from April 1, 2007 to June 30, 2007 varies significantly from the results of operations measured by EBITDA of approximately \$6.7 million for the same period due primarily to the net change in non-cash operating working capital balances of approximately \$4.3 million. Management currently anticipates that earnings from operations will generate sufficient cash flow to fund future distributions.

### **Credit Facilities**

Our Credit Facilities with Chrysler Financial Corporation ("CFC") provide for a Revolving Floorplan Facility of up to \$183.1 million to finance our inventories and a Revolving Term Facility of up to \$50 million to assist in the financing of our working capital and the acquisition of franchised automobile dealerships.

Amounts drawn on the Revolving Term Facility to assist in the financing of our working capital will be primarily for used vehicles, parts inventory and general corporate purposes, including financing the costs incurred in equipping our Open Points, or in purchasing new equipment for our existing dealerships. Amounts drawn on the Revolving Term Facility to assist in acquisitions will be available to finance acquisitions of franchised automobile dealerships. We expect to repay the amounts drawn on the Revolving Term Facility to finance acquisitions through the issuance of Units, subject to market conditions. These facilities are available on a revolving basis. \$11 million of the \$50 million Revolving Term Facility has been drawn on as at June 30, 2007 in connection with the acquisition of Victoria Hyundai, financing the acquisition of Grande Prairie Nissan and to meet working capital requirements. The Fund has not drawn on the Revolving Term Facility to finance the start-up costs associated with Grande Prairie Mitsubishi which has instead been financed with cash flows from operations.

The Revolving Term Facility has a term of three years from May 11, 2006 with annual one year extensions at the discretion of CFC. Advances under this portion of the Credit Facilities are repayable without any pre-payment penalties or bonus (subject to normal breakage costs) and will bear interest at a floating rate plus an applicable spread.

Both the Revolving Floorplan Facility and the Revolving Term Facility require maintenance of certain financial covenants and are collateralized by a general security agreement consisting of a first security interest on all present and future property. The Credit

Facilities may in certain circumstances restrict the ability of the Fund to pay distributions if the payment would result in a default under the Credit Facilities. At June 30, 2007, the Fund was in compliance with these covenants.

### Interest Rate Sensitivity

The Fund's Revolving Floorplan Facility and Revolving Term Facility bear interest at floating rates, thus exposing the Fund to interest rate fluctuations. At June 30, 2007 the increase or decrease in net earnings for each one percent change in interest rates on floating rate debt amounted to approximately \$1,454.

### Credit Risk

Concentration of cash and cash equivalents exists due to the significant amount of cash held with CFC. Concentration of credit risk with respect to contracts-in-transit and accounts receivable is limited primarily to automobile manufacturers and financial institutions. Credit risk arising from receivables from commercial customers is not significant due to the large number of customers comprising our customer base.

### Capital Expenditures

Our capital expenditures consist primarily of leasehold improvements, the purchase of furniture and fixtures, service vehicles, computer hardware and computer software. Management expects that our annual capital expenditures will increase in the future, as a function of increases in the number of locations requiring maintenance capital expenditures, the cost of opening new locations and increased spending on information systems. Our future growth is dependent on our ability to acquire and integrate additional dealerships and to successfully operate existing dealerships. Management expects that our cash flow generated from operations, together with working capital availability under our Revolving Term Facility, is sufficient to fund our debt service, working capital requirements and capital spending.

In 2007 the Fund is continuing its upgrade of existing dealership management software supplied by ADP and converting our locations supplied by Reynolds and Reynolds to ADP. This will be another key enabler in supporting efforts to standardize processes and share best practices across all dealerships. Costs related to the Open Points will be treated as growth capital when incurred (see Open Points above).

### Contractual Obligations

The table below sets forth, as at June 30, 2007, the material contractual obligations of the Fund, due in the years indicated, which relate to various premises and equipment operating leases.

(In thousands of dollars)	<u>Operating Leases</u>	<u>Long-term Debt</u>	<u>Total</u>
	\$	\$	\$
Less than one year	4,501	198	4,699
One to three years	7,683	11,438	19,121
Four to five years	5,432	-	5,432
Thereafter	1,200	-	1,200
	<u>18,816</u>	<u>11,636</u>	<u>30,452</u>

## Financial Position

The following table shows selected unaudited balances of the Fund at June 30, 2007, unaudited balances of the Fund at March 31, 2007, unaudited balances of the Fund at September 30, 2006 and June 30, 2006, and the audited balances of the Fund for December 31, 2006.

	The Fund				
	June 30, 2007	March 31, 2007	December 31, 2006	September 30, 2006	June 30, 2006
<b>Balance Sheet Data</b>					
Cash and cash equivalents	21,077	24,268	20,880	20,265	20,271
Accounts receivable	35,980	31,200	27,742	30,562	25,875
Inventories	132,814	117,034	112,680	101,252	145,888
Total assets	369,678	351,732	338,532	325,017	364,939
Revolving floorplan facility	133,731	118,974	113,357	103,297	146,283
Total long term liabilities	30,795	11,674	5,775	294	105

### *Net Working Capital*

The automobile manufacturers represented by the Fund require the Fund to maintain an aggregate minimum net working capital of approximately \$27.8 million. At June 30, 2007, net working capital was approximately \$31.5 million.

### **Off Balance Sheet Arrangements**

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

### **Related Party Transactions**

Note 11 to the unaudited Interim Financial Statements of the Fund summarizes the transactions between the Fund and its related parties. These transactions are management and non-competition fees received and rents paid to companies with common ownership, management and directors. The total management and non-competition fees received from CAG for the period from April 1, 2007 to June 30, 2007 was \$90. We lease eleven of our existing eighteen locations from related parties to the Fund. The total rent paid by us to the related parties for the period from April 1, 2007 to June 30, 2007 was \$925. We have received advice from a national real estate appraisal company that the market rents at each of our facilities leased from related parties of the Fund are at fair market value rates when the leases were entered into.

### **Changes in Accounting Policies and Initial Adoption**

Effective January 1, 2007, the Fund adopted three new accounting standards related to financial instruments that were issued by the Canadian Institute of Chartered Accountants ("CICA") in 2005. These accounting policy changes were adopted on a prospective basis with no restatement of prior period financial statements. The new standards and accounting policy changes are as follows:

a) Financial Instruments – Recognition and Measurement (CICA Handbook Section 3855)

In accordance with this new standard, the Fund now classifies all financial instruments as either held-to-maturity, available-for-sale, held for trading, loans and receivables or other liabilities. Financial assets held to maturity, loans and receivables and financial liabilities other than those held for trading, are measured at amortized cost. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in other comprehensive income. Instruments classified as held for trading are measured at fair value with unrealized gains and losses recognized on the Interim Consolidated Statement of Operations, Comprehensive Income and Accumulated Deficit.

The Fund has made the following classifications:

- Cash and cash equivalents and restricted cash are classified as financial assets held for trading and are measured at fair value. Gains and losses related to periodical revaluation are recorded in net earnings;

- Accounts receivable are classified as loans and receivables and are initially measured at fair value and subsequent period revaluations are recorded at amortized cost; and,
- Accounts payable and accrued liabilities, revolving floorplan facility distributions payable, long-term debt, and obligation under capital lease are classified as other liabilities and are initially measured at fair value and subsequent periodical revaluations are recorded at amortized cost.

The estimated fair value of accounts receivable, accounts payable and revolving floorplan facility approximate carrying value due to the relatively short-term nature of the instruments and/or floating interest rates on the instruments. The estimated fair value of the long-term debt approximates the carrying value because interest rates are floating.

Consequently, as at January 1, 2007 and June 30, 2007, the impact on the consolidated balance sheet of measuring the financial assets and liabilities was nil.

The Fund selected January 1, 2003 as its transition date for embedded derivatives. An embedded derivative is a component of a financial instrument or other contract of which the characteristics are similar to a derivative. This had no impact on the consolidated financial statements.

b) **Comprehensive Income (CICA Handbook Section 1530)**

Comprehensive income is the change in unitholders' equity during a period from transactions and other events and circumstances from non-owner sources. In accordance with this new standard, the Fund now reports a consolidated statement of comprehensive income and a new category, accumulated other comprehensive income, has been added to the unitholders' equity section of the consolidated balance sheet. The components of this new category will include unrealized gains and losses on financial assets classified as available-for-sale and the effective portion of cash flow hedges, if any. There were no such components to be recognized in comprehensive income for the three month period ended June 30, 2007. As the Fund has no items of other comprehensive income, net earnings for the period is equivalent to comprehensive income.

c) **Hedges (CICA Handbook Section 3865)**

The new standard specifies the criteria under which hedge accounting can be applied and how hedge accounting can be executed. The Fund does not have any hedging items.

d) **Accounting changes (CICA Handbook Section 1506)**

The new standard allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information, requires changes in accounting policy to be applied retroactively unless doing so is impracticable, requires prior period errors to be corrected retroactively and calls for enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements. The impact that the adoption of Section 1506 will have on the Fund's results of operations and financial condition will depend on the nature of future accounting changes. The adoption of Section 1506 effective January 1, 2007 had no impact on these unaudited interim consolidated financial statements.

## **Financial Instruments**

The Fund's financial instruments include cash and cash equivalents, accounts receivable, due from vendors, accounts payable and accrued liabilities, revolving floorplan facility, distributions payable, long-term debt and obligation under capital lease. The fair value of these instruments are considered to approximate their carrying value due to their short-term maturities, variable rates of interest or ability of prompt liquidation, as noted in the Changes in Accounting Policy and Initial Adoption above. These financial instruments are subject to credit risk and interest rate risk, as described in those audited consolidated financial statements.

## **Critical Accounting Policies and Estimates**

We prepare our consolidated financial statements in conformity with GAAP, which requires management to make estimates, judgments and assumptions that management believes are reasonable based upon the information available. These estimates,

judgments and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates on historical experience and other assumptions which it believes to be reasonable under the circumstances. Management also evaluates its estimates on an ongoing basis.

Our significant accounting policies are described in Note 2 (“Significant Accounting Policies”) of the December 31, 2006 audited consolidated financial statements of the Fund. The policies which management believes are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

### ***Revenue Recognition***

#### *Vehicles, parts, service and collision repair*

Revenue from the sale of new and used vehicles is recognized upon delivery, passage of title, signing of the sales contract and approval of financing or receipt of payment. Revenue from the sale of parts, service and collision repair is recognized upon delivery of parts to the customer or at the time vehicle service or repair work is completed. Manufacturer vehicle incentives and rebates are recognized as a component of new vehicle cost of sales when earned, generally at the time the related vehicles are sold. Dealer trades are recognized on a net basis upon delivery. Net revenue associated with dealer trades is nominal.

#### *Finance and insurance*

The Fund arranges financing for customers through various financial institutions and receives a commission from the lender based on the difference between the interest rate charged to the customer and the interest rate set by the financing institution, or a flat fee. This revenue is included in vehicles revenue on the statement of operations. The Fund also receives commissions for facilitating the sale of third party insurance products to customers, including credit and life insurance policies and extended service contracts. These commissions are recorded as revenue at the time the customer enters into the contract and the Fund is entitled to the commission. The Fund is not the obligor under any of these contracts. In the case of finance contracts, a customer may prepay or fail to pay their contract, thereby terminating the contract. Customers may also terminate extended service contracts and other insurance products, which are fully paid at purchase, and become eligible for refunds of unused premiums. In these circumstances, a portion of the commissions the Fund receives may be charged back to the Fund based on the terms of the contracts. The revenue the Fund records relating to commissions is net of an estimate of the amount of chargeback’s the Fund will be required to pay. This estimate is based upon historical chargeback experience arising from similar contracts, including the impact of refinance and default rates on retail finance contracts and cancellation rates on extended service contracts and other insurance products.

#### *Lease revenue*

Lease revenue is recognized on a straight-line basis over the term of the related lease agreement as amounts become due.

### ***Inventory Valuation***

Inventory is valued at the lower of cost and net realizable value. The value of our inventory is dependent upon our ability to plan and manage our inventory so as to avoid miscalculation in brand or model popularity. Any such miscalculation could adversely affect the value of our inventory. Our planning procedures and our supply chain structure are designed to minimize inventory write downs.

### ***Finance and Insurance Commission Reserve***

As discussed above we may be required to pay back a portion of the commissions earned from the sale of third party finance and insurance products in the event of early contract termination by customers. A reserve for future repayments is established at the time the sale is made. Our process for establishing the reserve carefully considers our historical repayment percentages and the timing of such repayments.

### ***Income Taxes***

In accordance with CICA Emerging Issues Committee bulletin EIC-111 (Determination of Substantively Enacted Tax Rates under CICA Handbook Section 3465) and the guidance in EIC-D67 (Future Income Tax Liabilities and Income Trusts and other Specified Investment Flow-Throughs), during the second quarter of 2007 the Fund is required to recognize future income tax assets

or liabilities. The corresponding change to the future income tax expense is based on the temporary timing differences between the book and tax basis of assets and liabilities expected to reverse after the tax is imposed. The adoption of these new standards resulted in a future income tax liability of \$19.1 million in the second quarter of 2007 and a corresponding future income tax expense of the same amount in the statement of operations.

The Fund currently has unused tax shield of approximately \$66 million which can be utilized in the future to reduce the Fund's taxable income. This tax shield arises as a result of deferred financing costs related to the IPO and differences in the accounting and tax values of capital assets, goodwill and intangible assets. The Fund incurred approximately \$8.6 million of deferred financing charges related to the IPO which are deductible for Canadian income tax purposes at a rate of \$1.7 million per year over a five year period commencing in 2006. As of June 30, 2007, the Fund had tax pools of approximately \$22.6 million relating to intangibles and \$27.4 million relating to goodwill which are both deductible for Canadian income tax purposes at a rate of 7% per year on a declining balance basis.

AutoCanada is evaluating its alternatives as to the best structure for its unitholders including consideration of a corporate structure. In Alberta where the Fund is registered, a corporation is subject to a lower overall tax rate than the 31.5% tax that will apply to income trusts after 2010. We will consider other options that may emerge based on further information from the federal government with respect to the legislation and the related transitional rules when this information becomes available. Management believes that similar to American public companies which own and operate franchised automotive dealerships, AutoCanada continues to be a long-term value investment in the automotive industry in Canada and does not rely on the tax efficiency of a flow-through trust model to sustain our business. Our business model and growth prospects provide a solid foundation for future distributions and our ability to generate value for our unitholders.

#### **Disclosure Controls & Procedures**

In fiscal 2006, an evaluation was carried out for the effectiveness of our disclosure controls and procedures as defined in Multilateral Instrument 52-109. Based on that evaluation, we concluded that the design and operation of these disclosure controls and procedures are effective.

#### **Internal Controls Over Financial Reporting**

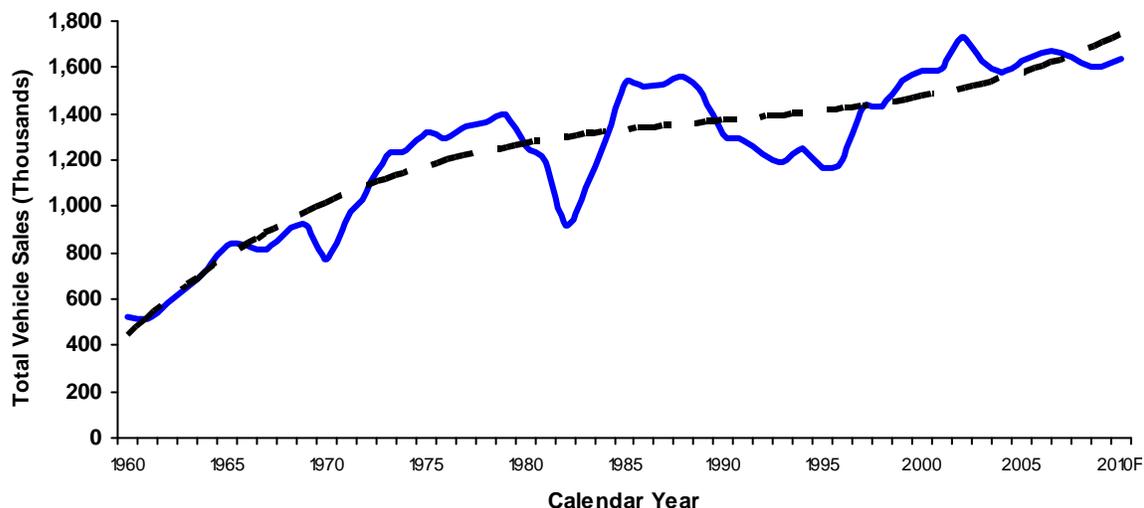
Management is responsible for designing such internal controls over financial reporting, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. No changes were made in the Fund's internal control over financial reporting during the period ended June 30, 2007, that have materially affected, or are reasonably likely to materially affect, the Fund's internal control over financial reporting. The Fund's financial reporting procedures and practices have enabled the certification of the Fund's interim filings in compliance with Multilateral Instrument 52-109 "Certification of Disclosure in Issuers' Annual and Interim Filings". Management has designed such internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements and other annual and interim filings in accordance with Canadian Generally Accepted Accounting Principles.

#### **CEO and CFO Certifications**

The Fund files certifications, signed by the CEO and CFO, with the Canadian Securities Administrators upon filing of the Fund's annual financial statements and MD&A. In those filings, the CEO and CFO certify, as required by Multilateral Instrument 52-109, the appropriateness of the financial disclosures, the effectiveness of the Fund's disclosure controls and procedures, and the design of internal controls over financial reporting to provide reasonable assurance as to its reliability and the preparation of financial statements for external purposes in accordance with GAAP. The Fund's CEO and CFO also certify the appropriateness of the financial disclosures in its interim filings with Securities Regulators, and that they have caused disclosure controls and procedures to be designed. The Audit Committee reviewed this MD&A, and the interim consolidated financial statements, and the Board of Directors and Trustees approved these documents prior to their release.

## Outlook

Canadian vehicle sales have been strong thus far in 2007 and are predicted to continue robust growth as illustrated in the following chart illustrating actual total Canadian vehicle sales (solid line) and the predicted trend line for the same period (dashed line):



Source: DesRosiers Automotive Consultants Inc.

We intend to continue to grow our cash flow through continued growth in same store gross profit and operating results, acquisitions, the planned opening of Open Points and the addition of franchised automobile dealerships managed by the Fund. Management intends to increase same store sales growth and realize further operating efficiencies and synergies by continuing to implement standardized operating policies. We have identified potential acquisitions that would be accretive to our existing operations and complement our growth model and strategies in 2007. We will also continue to seek opportunities to add additional franchised automobile dealerships under management similar to Grande Prairie Nissan in order to grow the Fund's cash flow and follow its previously announced strategic intent to develop relationships with a wider range of manufacturers in order to enhance its long-term growth prospects. We plan to take advantage of Open Points if and when they are offered by manufacturers and when suitable land can be acquired. The achievement of this outlook is subject to various risks as described in the "Risk Factors" below. Some of these risks are beyond management's control.

As a result of the strong Canadian dollar there is currently a significant difference between the prices of some similar new and used vehicles in Canada and the United States. There are barriers to entry with respect to importing these vehicles for resale into Canada which may include the transferability of new vehicle warranties, modifications required to meet Canadian safety standards, and transportation costs. We continue to monitor this trend to determine what, if any, adjustment in our strategies might be warranted.

On October 31, 2006, the Department of Finance Canada announced proposed legislation in connection with the taxation of income trusts and other flow-through entities (the "Plan"). Included in the Plan are proposed changes to the taxation of income trusts. Specifically, certain distributions of an income trust's income will be subject to tax at corporate income tax rates. Those distributions will, like the dividends that corporations pay, not be deductible by an income trust. The unitholders in an income trust will be taxed as though the distributions were dividends and taxable unitholders will be eligible for the dividend tax credit. Unitholders that hold their units in tax deferred accounts such as pension plans or registered pension plans or non-residents unitholders will not be eligible for the dividend tax credit. The entities that will be subject to these proposed new rules will be fully defined in the legislation to implement these measures. As a practical matter however, it can be assumed that the rules will apply to any publicly-traded "income trust" (or publicly-traded partnership), other than one that only holds passive real estate investments. These changes will generally take effect beginning with the 2007 taxation year for income trusts that begin to be publicly-traded after October 2006, but will only apply beginning with the taxation year ended December 31, 2011 for those income trusts that are already publicly-traded.

On December 15, 2006, the Department of Finance Canada released guidance for income trusts and other flow-through entities that qualify for the four-year transitional relief. The guidance establishes objective tests with respect to how much an income trust is

permitted to grow without jeopardizing its transitional relief. In general, the Fund will be permitted to issue new equity over the next four years equal to its market capitalization as of the end of trading on October 31, 2006 (subject to certain annual limits). Market capitalization, for these purposes, is to be measured in terms of the value of the Fund's issued and outstanding publicly traded units. Those safe harbour limits are 40% for the period from November 1, 2006 to December 31, 2007, and 20% each for calendar 2008, 2009 and 2010. Moreover, these limits are cumulative, so that any unused limit for a period carries over into the subsequent period. If required to fund its growth strategy the Fund could issue new Units for proceeds of approximately \$50 million in 2007 and approximately \$123 million for the period 2007 to 2010 and remain within the safe harbour guidelines. If these limits are exceeded, the Fund may lose its transitional relief and thereby become immediately subject to the proposed rules. Management currently believes that the provisions of the Plan are not a material constraint on the Fund's growth prospects.

As a result of new tax legislation, substantively enacted on June 12, 2007, the Fund recognized a non-cash future income tax expense in the quarter ended June 30, 2007. Current income tax will not be recognized until the new tax becomes effective on January 1, 2011 at which point the earnings of the Fund will be subject to a 31.5% tax. Until that time the new legislated tax does not impact the cash earnings of the business.

On November 12, 2006, DaimlerChrysler amended their Multi Dealer Group policy specific to the Fund allowing the Fund to acquire additional DCCI dealerships to a maximum 8% (previously 5%) of DaimlerChrysler Canadian annual sales. This gives the Fund the potential to acquire an estimated seven additional dealerships that could sell an additional 6,000 new vehicles per year at an average of approximately 800 new vehicles per dealership.

#### **Additional information**

Additional information relating to the Fund, including all public filings, is available on SEDAR ([www.sedar.com](http://www.sedar.com)).

#### **RISK FACTORS**

As at June 30, 2007, the inability to locate land acceptable to manufacturers on which to build Open Point dealerships and currency fluctuations which create significant differences between similar new and used vehicles in Canada and the United States have been identified as additional risks in the Fund's activities. There are no other material changes in the Fund's risks or risk management activities since the time of the initial public offering other than those discussed in "Dealerships Managed by the Fund" which are reiterated below. The Fund's results of operations, business prospects, financial condition, cash distributions to Unitholders and the trading price of the Fund's units are subject to a number of risks. These risk factors include: the retail automotive industry, which includes risks relating to: overall consumer demand; substantial competition in vehicle sales and services; dependence upon vehicle sales; mix of new vehicles; interest rates; automobile manufacturer incentive programs; seasonality; and import product restrictions and foreign trade; our business, which includes risks relating to: the loss of key personnel and limited management and personnel resources; unfavorable conditions in key geographic markets; governmental regulations and environmental regulation compliance costs; and insurance coverage; our acquisition strategy, which includes risks relating to: automobile manufacturers' restrictions on acquisitions; integration of acquisitions; financing constraints; and competition with other franchised automobile dealerships; our dependence on automobile manufacturers, which includes risks relating to: our automobile dealership franchise agreements; restrictions on ownership thresholds and the sale of our business; requirements to maintain minimum working capital; approval of Open Points; dealerships managed by the Fund which includes risk relating to: the contractual nature of the relationships compared with the direct ownership of the dealerships; the dependency upon CAG and its principal shareholder, Patrick Priestner, as the owner and principal operator of these dealerships; and conflicts of interest that may arise between the objectives of the Fund and CAG and their respective owners and management; and adverse conditions affecting one or more automobile manufacturers. Risks relating to our structure include: dependence upon the Partnership to fund cash distributions; the fact that cash distributions are not guaranteed and will fluctuate with business performance; the fact that our distributions are discretionary; the nature of the Units; limited liability of Unitholders; unpredictability and volatility of Unit prices; attributes of securities distributed on redemption of Units or termination of the Fund; dilution; leverage and restrictive covenants; future sales of Units by the Fund; income tax matters including changes to income tax law; limitations on future growth and cash flow; restrictions on the ownership of Units by non-residents of Canada; indemnities provided by CAG and the Principal Shareholders; and the fact that Unitholders are not afforded certain statutory rights.

For a discussion of these risks and other risks associated with an investment in Fund Units, see "Risk Factors" detailed in the Fund's final prospectus dated May 3, 2006 and the Fund's Annual Information Form dated March 22, 2007 available at [www.sedar.com](http://www.sedar.com).