CAPSTONE
INFRASTRUCTURE

CAPSTONE INFRASTRUCTURE CORPORATION

Financial Report for the Quarter Ended June 30, 2011

FINANCIAL HIGHLIGHTS

PERFORMANCE MEASURES

	Three months ended		Six months ended	
Earnings Measures ($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Revenue	37,028	35,497	83,943	79,649
Net income (loss)	(32,779)	(2,239)	8,553	25,394
Basic earnings per share	(0.531)	(0.048)	0.140	0.544

	Three months ended		Six months ended	
Cash Flow Measures ($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Cash flows from operating activities	(8,353)	7,364	5,764	21,237
Adjusted EBITDA (1)	(6,570)	9,220	11,299	29,121
Funds from operations (“FFO”) (1)	(10,893)	4,565	3,861	21,710
Adjusted funds from operations (“AFFO”) (1)	(13,595)	3,042	(450)	18,148
Payout ratio	nmf (2)	253.0%	nmf (2)	84.8%

(1) These performance measures are not defined by International Financial Reporting Standards (“IFRS”). Please see page 5 for a definition of each measure.
(2) The payout ratio for 2011 is not meaningful due to the internalization costs which result in a negative payout ratio

Capital Structure ($000s)	**Jun 30, 2011**	**Dec 31, 2010**
CPC–Cardinal credit facility	85,000	85,000
Erie Shores project debt	105,436	107,063
Convertible debentures – face value	42,766	53,221
Amherstburg Solar Park project debt	96,200	31,000
Levelization liability	24,584	23,714
Class B exchangeable units – market value	25,410	26,710
Preferred shares – market value	72,570	-
Common shares – market value	459,048	463,217

INVESTOR INFORMATION

Quick Facts	
Common shares outstanding	58,701,763
Preferred shares outstanding	3,000,000
Convertible debentures outstanding	42,766
Class B exchangeable units	3,249,390
Securities symbols and exchange	Toronto Stock Exchange: CSE, CSE.PR.A, CSE.DB.A
Index inclusion	S&P TSX Clean Technology Index
Ownership	Approximately 18,000 common shareholders

QUARTERLY TRADING INFORMATION

	High	Low	Closing	Average Daily Trading Volume
Common share price	$8.29	$7.60	$7.82	126,407
Preferred share price	$24.75	$24.00	$24.19	13,150
Debenture price	$117.40	$110.00	$112.90	837

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LEGAL NOTICE

This quarterly financial report is not an offer or invitation for subscription or purchase of or a recommendation of securities. It does not take into account the investment objectives, financial situation and particular needs of the investor. Before making an investment in Capstone Infrastructure Corporation (the "Corporation" or "Capstone"), the investor or prospective investor should consider whether such investment is appropriate to their particular needs, objectives and financial circumstances and consult an investment advisor if necessary.

CAUTION REGARDING FORWARD-LOOKING STATEMENTS

Certain of the statements contained in this Quarterly Financial Report are forward-looking and reflect management's expectations regarding the Corporation's future growth, results of operations, performance and business based on information currently available to the Corporation. Forward-looking statements are provided for the purpose of presenting information about management's current expectations and plans relating to the future and readers are cautioned that such statements may not be appropriate for other purposes. These statements use forward-looking words, such as "anticipate", "continue", "could", "expect", "may", "will", "estimate", "believe" or other similar words. These statements are subject to significant known and unknown risks and uncertainties that may cause actual results or events to differ materially from those expressed or implied by such statements and, accordingly, should not be read as guarantees of future performance or results. The forward-looking statements in this Quarterly Financial Report are based on information currently available and what the Corporation currently believes are reasonable assumptions, including the material assumptions for each of the Corporation's assets set out in its fiscal 2010 Annual Report under the heading "Asset Performance" and other filings made by the Corporation with the Canadian securities regulatory authorities (such documents are available on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval ("SEDAR") at www.sedar.com). Other material factors or assumptions that were applied in formulating the forward-looking statements contained herein include the assumption that the business and economic conditions affecting the Corporation's operations will continue substantially in their current state, including, with respect to industry conditions, general levels of economic activity, regulations, weather, taxes and interest rates, that there will be no unplanned material changes to the Corporation's facilities, equipment or contractual arrangements.

Although the Corporation believes that it has a reasonable basis for the expectations reflected in these forward-looking statements, actual results may differ from those suggested by the forward-looking statements for various reasons, including risks related to: power infrastructure (operational performance; power purchase agreements; fuel costs and supply; contract performance; development risk; technology risk; default under credit agreements; land tenure and related rights; regulatory regime and permits; environmental, health and safety; climate change and the environment; and force majeure) and the Corporation (tax-related risks; variability and payment of dividends, which are not guaranteed; geographic concentration and non-diversification; insurance; environmental, health and safety regime; availability of financing; shareholder dilution; and the unpredictability and volatility of the common share price of the Corporation). There are also a number of risks related to the Corporation's investment in Värmevärden, the district heating business in Sweden, including: fuel costs and availability; industrial and residential contracts; geographic concentration; regulatory environment; environmental, health and safety; reliance on key personnel; labour relations; assumption of liabilities; minority interest; and foreign exchange. There is also a risk that Värmevärden may not achieve expected results.

For a more comprehensive description of these and other possible risks, please see the Corporation's Annual Information Form dated March 24, 2011 for the year ended December 31, 2010 and other filings made by the Corporation with the Canadian securities regulatory authorities. These filings are available on SEDAR. The assumptions, risks and uncertainties described above are not exhaustive and other events and risk factors could cause actual results to differ materially from the results and events discussed in the forward-looking statements. These forward-looking statements reflect current expectations of the Corporation as at the date of this Quarterly Financial Report and speak only as at the date of this Quarterly Financial Report. Except as may be required by applicable law, the Corporation does not undertake any obligation to publicly update or revise any forward-looking statements.

LETTER TO SHAREHOLDERS

I am pleased to report on Capstone Infrastructure Corporation's (Capstone Infrastructure) second quarter results and recent activities, and to provide an update on our priorities and outlook for the balance of the year.

Operationally, our portfolio performed strongly in the second quarter of the year, with higher power production at the hydro power facilities and higher electricity rates at the Cardinal gas cogeneration facility. These drivers were partially offset by slightly lower production from Erie Shores Wind Farm and decreased production at Cardinal and the Whitecourt biomass facility due to planned seven-day maintenance outages completed in April and May, respectively. Combined, these factors resulted in a 4.3% increase in revenue from the same quarter in 2010. For the year-to-date period, total revenue increased by $4.3 million, or 5.4%, over the first six months of 2010. The main drivers of our quarterly and year-to-date financial performance are summarized below.

A key highlight of the quarter was the completion of the Amherstburg Solar Park, which achieved commercial operations under its Renewable Energy Standard Offer Program (RESOP) contract with the Ontario Power Authority (OPA) on June 30, 2011. This facility represents an important milestone for Capstone Infrastructure as our first development project and our first solar power facility. We are proud of the quality of the Amherstburg Solar Park and the contribution it will make to renewable energy in Ontario, generating enough green electricity annually to power approximately 4,000 homes. We expect the return on our investment to be consistent with the 10 – 14% post-tax, levered range we typically target for contracted infrastructure assets. We held an official dedication ceremony at the facility on July 21, 2011.

In June, we also strengthened our capacity for growth by raising $75 million in gross proceeds ($72.4 million in net proceeds) with the issuance of 3,000,000 cumulative preferred shares with a five-year rate reset. The net proceeds were partially used to fund our final equity payment for the Amherstburg Solar Park with the balance earmarked for future acquisitions and general corporate purposes.

Also during the quarter, Derek Brown stepped down as Chairman of the Board of Directors, a position he had held since 2004. We are delighted that he will continue to serve on the board with a focus on providing counsel on capital markets matters. Mr. Brown is succeeded in the chairman's seat by Jim Sardo, who has served as a director of the Corporation since November 2009. On behalf of the management team, I would like to thank Mr. Brown for his sage counsel over the years and welcome Mr. Sardo to his new role.

FINANCIAL HIGHLIGHTS

While our portfolio remains operationally sound, our financial results in the second quarter and year-to-date periods primarily reflected the impact of one-time costs related to the internalization of management, which amounted to $18.6 million and $19.3 million in the second quarter and first six months of the year, respectively. This financial report presents earnings and cash flow measures both including and excluding these one-time costs. Over the long term, we expect the internalization to result in lower costs compared with the former structure, particularly as we continue to grow over time.

Also during the quarter, we received our first distribution from Värmevärden, the district heating business in Sweden. The distribution amounted to $1.7 million and was received in the form of interest income, contributing favourably to Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) and Adjusted Funds from Operations (AFFO). AFFO reduces funds from operations for maintenance capital expenditures and the repayment of principal.

Total costs and expenses in the quarter increased by 55.0% over the same quarter in 2010 and were 31.1% higher than in the first six months of last year. As described on pages 8 and 9, the quarterly increase was primarily due to costs related to the internalization of management and higher gas transportation costs at Cardinal with increased business development expenses also contributing to the year-to-date variance.

Excluding internalization costs, Adjusted EBITDA and AFFO increased by 23.3% and 39.7%, respectively, over the second quarter last year, reflecting higher revenue from the power infrastructure businesses and an increase in interest income, primarily from Värmevärden. For the year-to-date period, Adjusted EBITDA increased by 3.0%, reflecting the impact of increased operating and administrative expenses and the absence of distributions from Leisureworld, which was sold in March 2010. For the first six months of the year, AFFO increased by 0.5% over the same period in 2010. Excluding internalization costs, AFFO per share in the quarter increased by 12.5% while AFFO per share for the year-to-date period decreased by 17.9% due to an increase in the number of common shares outstanding in 2011 compared with one year ago.

As outlined on page 16 of this report, our financial position remains strong. As at June 30, 2011, we had cash and cash equivalents of $109.4 million, including the net proceeds from the preferred share issuance. With amounts available under our credit facility, we have access to more than $100 million in capital with which to pursue growth opportunities. In addition, our debt to capitalization ratio at quarter end was 39.3%, which is conservative relative to the low risk profile of our businesses.

OUTLOOK

Operationally, our outlook for the balance of 2011 is positive. Our expectations for each business are described on pages 23 through 28. While we expect our operations to run smoothly, 2011 will nevertheless be a transitional year. Excluding the impact of the internalization costs, we expect Adjusted EBITDA and FFO from our portfolio to be higher than in 2010. This outlook assumes:

- Continuing stable performance from Cardinal and Whitecourt;
- The partial year cash flow from Amherstburg Solar Park and Värmevärden;
- That normal wind patterns and water flows will continue in the balance of the year; and
- That the TransCanada Pipelines Limited (TCPL) toll increase that went into effect on March 1, 2011 will continue at the current level for the remainder of 2011.

Including the one-time impact of the internalization costs, we currently expect fiscal 2011 Adjusted EBITDA to be approximately $40 million compared with $55.0 million in fiscal 2010. Excluding the impact of the internalization costs, Adjusted EBITDA is expected to be approximately $60 million in fiscal 2011. We expect our 2011 payout ratio, excluding the internalization costs, to be in the range of 120% compared with previous guidance of 110 – 120%, reflecting the impact of the preferred share issuance on June 30, 2011.

For 2012, we currently expect Adjusted EBITDA to be approximately $80 million, reflecting the full-year contribution from the Amherstburg Solar Park and Värmevärden and assuming a return to 2010 TCPL rates. We currently expect to achieve a payout ratio in 2012 of approximately 85% to 90%. As we execute our growth strategy, which could include development projects or businesses with a strong growth profile, our payout ratio may fluctuate in any given year.

Based on our current portfolio and outlook and barring any significant unexpected events, we expect our dividend policy of $0.66 per share on an annualized basis to be sustainable through 2014.

Our vision is to be Canada's pre-eminent infrastructure company, making growth a major focus for our team in 2011. Over the long term, we intend to diversify our portfolio across core infrastructure categories, including electricity generation and distribution businesses, water or wastewater facilities, roads, hospitals and schools, among others, including investments through public-private partnerships (P3s). We are continuing to assess a range of opportunities in Canada, the United States and abroad.

Adding new businesses to our portfolio will also help to mitigate the impact of Cardinal's power purchase agreement (PPA) expiry in 2014. Securing a new PPA for Cardinal, which currently operates as a base load facility, is a top priority. We have been working for nearly two years to build stakeholder support for a new contract and are optimistic about Cardinal's future prospects as a peaking facility. Most recently, in June, we provided technical, operating and economic data about Cardinal to the OPA. At the end of July, we were notified by the OPA that it will engage in negotiations with Cardinal. We are delighted to be moving the re-contracting process forward.

In closing, Capstone is committed to executing on its strategy and mission to deliver a superior total return to shareholders. More information about our portfolio, activities and future events is available on our new website at www.capstoneinfrastructure.com.

We greatly appreciate your continuing support.

Sincerely,

Michael Bernstein
President and Chief Executive Officer
August 12, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

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INTRODUCTION

Management's discussion and analysis ("MD&A") summarizes the Corporation's consolidated operating results for the quarter and six months ended June 30, 2011 and consolidated cash flows for the six months ended June 30, 2011 and the Corporation's financial position as at that date. This MD&A should be read in conjunction with the accompanying unaudited interim consolidated financial statements of the Corporation and notes thereto as at and for the quarter and six months ended June 30, 2011. Additional information about the Corporation can also be found in its Annual Information Form ("AIF") dated March 24, 2011 and in the most recent annual report of Macquarie Power and Infrastructure Corporation ("MPIC"), the previous name of the Corporation, for the year ended December 31, 2010 and other public filings of the Corporation, all of which are available on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com. The information contained in this MD&A reflects all material events up to August 12, 2011, the date on which this MD&A was approved by the Corporation's Board of Directors.

The 2011 and 2010 financial information contained herein is prepared in accordance with International Financial Reporting Standards ("IFRS"). On January 1, 2011, Capstone adopted IFRS and converted from Canadian generally accepted accounting principles ("GAAP"). The significant impact of the conversion to IFRS on the interim consolidated financial statements is discussed on page 5 of this MD&A.

All amounts are in Canadian thousands of dollars unless otherwise indicated.

CHANGES IN THE BUSINESS

Corporate Conversion

Following changes in Canadian tax rules for specified investment flow-through ("SIFT") entities, during 2010 Macquarie Power & Infrastructure Income Fund ("MPT" or the "Fund") completed a Plan of Arrangement (the "Arrangement") under the *Business Corporations Act* (British Columbia) to convert from a mutual fund trust structure into MPIC, a corporation (the "Conversion"). On completion of the Arrangement, effective January 1, 2011, MPIC became the owner, directly or indirectly, of the businesses owned by the Fund.

Internalization of Management

On April 15, 2011, MPIC terminated all management and administrative agreements with Macquarie Power Management Ltd. ("MPML" or "the Manager"), a subsidiary of Macquarie Group Limited ("MGL"), thereby internalizing its management. On internalization, the Corporation retained its current leadership team, which has deep expertise and broad relationships in the infrastructure sector. Additionally, MPIC was renamed Capstone Infrastructure

Corporation ("Capstone" or the "Corporation"). With the new corporate name, Capstone's Toronto Stock Exchange symbols were changed to CSE for the common shares and CSE.DB.A for the convertible debentures.

Capstone and its subsidiaries made payments to a subsidiary of MGL as consideration for terminating all management and administration agreements. MGL's subsidiary immediately used $7,000 of the $14,000 it received to subscribe for Capstone common shares, which MGL's subsidiary will hold for at least one year. MGL has provided a director to serve on Capstone's Board of Directors for a minimum of 12 months and Capstone will continue to have access to global growth opportunities available through the Macquarie Infrastructure and Real Assets division. Furthermore, MGL is providing transitional services to Capstone at no cost for a period to December 15, 2011, including the provision of premises, information technology support and tax and accounting services.

Preferred Shares

On June 30, 2011, Capstone completed an offering of 3,000,000 cumulative preferred shares with a five-year rate reset, at a price of 25 dollars per share for gross proceeds of $75,000 (net proceeds of $72,350). The preferred shares are publicly listed for trading on the Toronto Stock Exchange under the symbol CSE.PR.A.

NON-GAAP PERFORMANCE MEASURE DEFINITIONS

While the accompanying unaudited interim consolidated financial statements have been prepared in accordance with IFRS, this MD&A also contains figures that are performance measures not defined by IFRS. These non-GAAP performance measures do not have any standardized meaning prescribed by IFRS and are, therefore, unlikely to be comparable to similar measures presented by other issuers. The Corporation believes that these indicators are important since they provide additional information about the Corporation's performance and cash generating capabilities and facilitate comparison of results over different periods. The non-GAAP measures used in this MD&A are defined below.

Earnings before Interest, Taxes, Depreciation and Amortization ("EBITDA")

Standardized EBITDA follows the customary definition of net income (loss) adjusted for interest expense, income tax expense (recovery), depreciation and amortization. Standardized EBITDA is provided to illustrate how Adjusted EBITDA reconciles to net income (loss) on the interim consolidated statements of income.

Adjusted EBITDA

The Corporation uses Adjusted EBITDA to measure the performance of its assets prior to the impact of financing costs, taxes and charges for depreciation and amortization. Adjusted EBITDA is calculated as revenue less operating expenses and administrative expenses plus interest and dividends/distributions received from equity accounted investments. Adjusted EBITDA is reconciled to net income (loss) by adjusting standardized EBITDA for unrealized gains and losses on derivatives, unrealized loss on Class B exchangeable units, unrealized loss on the conversion option for the convertible debentures maturing on December 31, 2016, foreign exchange gains and losses, equity accounted income and dividends/distributions from equity accounted investments.

Funds from Operations ("FFO")

The Corporation uses FFO to measure the performance of its controlled and non-controlled assets net of financing costs and income taxes paid. The Corporation defines FFO as Adjusted EBITDA less interest paid plus principal received from loans receivable on equity accounted investments, less income taxes paid.

Adjusted Funds from Operations ("AFFO")

The Corporation uses AFFO as a measure of cash generated during the period for distribution to shareholders. The Corporation defines AFFO as FFO less maintenance capital expenditures and scheduled repayment of principal on debt.

Payout Ratio

Payout ratio measures the proportion of cash generated from operations that is paid as dividends. The payout ratio is calculated as dividends declared divided by AFFO.

INTERNATIONAL FINANCIAL REPORTING STANDARDS

On January 1, 2011, Capstone implemented IFRS as its financial reporting framework with a transition date of January 1, 2010. The transition required the Corporation to restate its 2010 financial results, which were previously prepared in accordance with Canadian GAAP. While many of the accounting principles and standards comprising IFRS are similar to Canadian GAAP, certain standards result in financial reporting differences that render financial results under Canadian GAAP and IFRS not comparable.

The Corporation's disclosure in its quarterly report for the three months ended March 31, 2011 described the financial reporting differences made during the conversion process in further detail. No additional financial reporting differences were identified for adjustment on transition during the second quarter.

As previously reported, Capstone converted from a mutual fund trust to a corporation on January 1, 2011. As a result, certain differences between Canadian GAAP and IFRS only impact financial results prior to January 1, 2011, while other IFRS differences impact financial reporting periods before and after January 1, 2011.

IFRS Adjustments Impacting both Historical and Prospective Financial Reporting

The adoption of IFRS has an impact on Capstone's historical and prospective financial reporting for capital assets and business combination transaction costs.

For capital assets, under IFRS major maintenance and inspections that are periodically undertaken at each facility may not be expensed as incurred. Instead, these costs must be capitalized and depreciated until the facility's next major maintenance cycle.

For business combination transaction costs, under IFRS, only transaction costs related to debt or equity issuance or acquisitions of equity accounted investments are eligible to be capitalized. All other transaction costs arising for a business combination must be expensed as incurred as opposed to being capitalized to the purchase price of the business combination as allowed under Canadian GAAP.

IFRS Adjustments Impacting only Historical Financial Reporting

Under IFRS, Capstone has additional financial reporting differences relative to Canadian GAAP that are only applicable to prior to January 1, 2011, when the Corporation operated as a trust. These differences relate to the Class B exchangeable units, the convertible debentures and deferred income taxes.

IFRS requires that the Class B exchangeable units of MPT LTC Holding LP, a subsidiary of Capstone, be classified as a financial liability and measured at fair value during the period that Capstone operated as a trust. The change in the fair value of the units and the distributions paid to the unitholders were charged to net income (loss)as a financing cost, consistent with the classification of the units as debt. Following conversion to a corporation on January 1, 2011, the Class B exchangeable units were reclassified under IFRS to the consolidated equity of the Corporation based on the carrying value of the units at December 31, 2010.

For the convertible debentures, IFRS requires Capstone to reclassify the conversion option from equity under Canadian GAAP to a liability for 2010. This classification is due to the debentures being convertible in 2010 into trust units, which are deemed to have a limited life, and therefore the debentures need to be measured as held for trading and accounted for at fair value with changes reported in the consolidated statements of income. On January 1, 2011, the conversion option was transferred to equity on the basis that the Corporation's shares are permanent in nature. The value of the conversion option on January 1, 2011 was equal to the carrying value on December 31, 2010, which is the same as fair value, which is adjusted for deferred income tax consequences being offset to shareholders' equity. Prospectively, the carrying value of the conversion option will remain unchanged aside from any future conversions.

For deferred income taxes, IFRS requires that a trust use the "undistributed" income tax rate in the determination of income tax amounts for financial reporting. This requires a trust to use the applicable income tax rate assuming that no distributions were made to offset taxable income. As a result, a trust is required to use the highest marginal personal income tax rate of 46% in the calculation of deferred income taxes. For Capstone, the impact is a non-cash increase to deferred income taxes in the January 1, 2010 opening consolidated statement of financial position to reflect the rate differential between the highest marginal personal tax rate of 46% and the SIFT tax rate of 25%.

The impact of the above adjustments on Capstone's 2010 net income (loss), retained earnings and non-GAAP measures is summarized in the following tables.

Adjustments to Net Income

($000s)	Year Ended Dec 31, 2010	For the Three Months Ended Mar 31, 2010	Jun 30, 2010	Sep 30, 2010	Dec 31, 2010
Net income (loss) – Canadian GAAP	11,569	21,012	(6,016)	(9,400)	5,973
Major maintenance and componentization	(1,792)	(264)	(588)	(708)	(232)
Capitalized transaction costs	2,142	(15)	2,822	(84)	(581)
Class B exchangeable units	(9,001)	(4,110)	309	(1,674)	(3,526)
Equity portion of convertible debentures	(3,459)	(1,897)	160	2,591	(4,313)
Deferred income taxes	16,442	12,907	1,074	2,430	31
Net income (loss) – IFRS	15,901	27,633	(2,239)	(6,845)	(2,648)

Adjustments to Non-GAAP Measures

($000s)	Year Ended Dec 31, 2010	For the Three Months Ended Mar 31, 2010	Jun 30, 2010	Sep 30, 2010	Dec 31, 2010
Adjusted EBITDA – Canadian GAAP	55,039	19,017	10,438	10,204	15,380
Accretion of asset retirement obligation	179	44	44	46	45
Capitalized transaction costs	(2,092)	(15)	(1,412)	(84)	(581)
Major maintenance and componentization	2,692	855	150	-	1,687
Adjusted EBITDA – IFRS	55,818	19,901	9,220	10,166	16,531
FFO – Canadian GAAP	40,037	16,261	5,791	7,336	10,649
Accretion of asset retirement obligation	179	44	44	46	45
Capitalized transaction costs	(2,092)	(15)	(1,412)	(84)	(581)
Major maintenance and componentization	2,692	855	150	-	1,687
FFO – IFRS	40,816	17,145	4,573	7,298	11,800
AFFO – Canadian GAAP	35,602	15,076	4,411	5,865	10,250
Accretion of asset retirement obligation	179	44	44	46	45
Capitalized transaction costs	(2,092)	(15)	(1,412)	(84)	(581)
AFFO – IFRS	33,689	15,105	3,043	5,827	9,714

Adjustments to Retained Earnings

($000s)	Jan 1, 2010	Mar 31, 2010	Jun 30, 2010	Sep 30, 2010	Dec 31, 2010
Retained earnings – Canadian GAAP	(214,073)	(201,297)	(215,548)	(233,184)	(235,979)
Major maintenance and componentization	167	(97)	(685)	(1,393)	(1,625)
Capitalized transaction costs	(3,075)	(3,090)	(268)	(352)	(933)
Class B exchangeable units	15,647	12,073	12,916	11,779	8,790
Equity portion of convertible debentures	(4,386)	(6,283)	(6,124)	(3,533)	(7,845)
Deferred income taxes	(51,033)	(38,126)	(37,049)	(34,622)	(34,591)
Retained earnings – IFRS	(256,753)	(236,820)	(246,758)	(261,305)	(272,183)

RESULTS OF OPERATIONS

Overview

For both the quarter and the six months ended June 30, 2011, Capstone's Adjusted EBITDA, FFO and AFFO were higher than in the prior comparable periods, excluding costs to internalize management. Growth in these measures over 2010 primarily reflected revenue growth from the power infrastructure businesses in excess of expense growth as well as new interest income from Värmevärden, the district heating business.

Revenue

	Three months ended		Six months ended	
($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Electricity sales	35,540	34,043	82,124	77,836
Steam sales	281	275	590	569
Gas sales	1,207	1,179	1,229	1,244
	37,028	35,497	83,943	79,649

Total revenue for the second quarter was $1,531, or 4.3%, higher than in 2010 and $4,294, or 5.4%, higher on a year-to-date basis. Second quarter growth was attributable to the strong performance of the hydro power facilities and Cardinal. Erie Shores also contributed favourably to the year-to-date results.

Electricity sales at the hydro power facilities were $1,276, or 37.1%, higher in the second quarter and $1,305, or 19.4%, higher in the first six months of the year. The increase was attributable to higher electricity production due to favourable hydrology arising from exceptional snow accumulation over the winter as well as below average production in the same period in 2010.

Electricity sales for Cardinal increased by $660, or 3.0%, during the second quarter for a year-to-date increase of $2,106, or 4.0%. The primary contributor to higher electricity sales was a 4.6% increase in the direct customer rate.

Erie Shores' electricity sales were $141, or 2.7%, lower in the second quarter of 2011, but $863, or 7.7%, higher for the six months ended June 30, 2011. The variances were attributable to favourable wind conditions in the first quarter of 2011.

In total, Capstone's assets produced 440,710 megawatt hours ("MWh") of electricity in the second quarter and 938,926 MWh in the first six months of 2011, compared with 437,254 MWh and 927,210 MWh, respectively, for the comparable periods of 2010.

Cardinal also produces steam that is sold to Canada Starch Operating Company Inc. ("Casco") for use in its manufacturing processes. Steam sales in the second quarter were comparable to 2010 and slightly higher on a year-to-date basis due to higher demand for steam from Casco during the first quarter.

Natural gas not used by Cardinal to produce electricity is sold through a mitigation arrangement with Cardinal's gas supplier. Gas sales were consistent with the prior comparable periods.

Costs and Expenses

	Three months ended		Six months ended	
($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Operating expenses	23,876	23,033	48,036	46,369
Administrative expenses	21,615	3,453	26,934	6,672
Depreciation on capital assets	5,946	6,027	11,895	12,324
Amortization on intangible assets	1,962	1,944	3,905	3,882
	53,399	34,457	90,770	69,247

Overall, costs and expenses for the second quarter of 2011 were $18,942, or 55.0%, higher and $21,523, or 31.1%, higher for the six months ended June 30, 2011. The increase was primarily attributable to $18,611 of internalization costs, which included termination of the MGL management agreements, certain one-time payments to staff and professional fees. Excluding these costs, total expenses were $331, or 1.0%, higher for the second quarter, and $2,277, or 3.3%, higher for the six months ended June 30, 2011.

Operating expenses

	Three months ended		Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Fuel expenses	18,658	16,541	37,939	34,639
Maintenance costs	1,146	3,332	2,095	4,582
Labour costs	2,167	1,933	4,179	3,798
Other operating expenses	1,905	1,227	3,823	3,350
	23,876	23,033	48,036	46,369

Fuel expenses, which represented 78.1% and 71.8% of total operating expenses in the second quarters of 2011 and 2010, respectively, were almost entirely attributable to Cardinal. During the second quarter, fuel expenses increased by $2,117, or 12.8%, representing a $3,300, or 9.5%, increase in the year-to-date period. Higher fuel prices and a higher TransCanada Pipelines Limited ("TCPL") gas transportation toll were the sources of the increase. Effective March 1, 2011, the transportation toll increased to $2.24 dollars per gigajoule ("GJ") from the previous rate of $1.64 dollars per GJ.

Maintenance costs during the second quarter were $2,186, or 65.6%, lower and $2,487, or 54.3%, lower for the six-month period. This variance was due to fewer repairs and maintenance requirements during the first and second quarters of 2011 as well as savings from the internalization of operations and maintenance ("O&M") at Erie Shores in July 2010.

Labour costs were $234, or 12.1%, higher in the second quarter of 2011 and $381, or 10.0%, higher during the first six months of 2011. Higher labour costs primarily reflected annual salary and wage increases and the addition of employees at Erie Shores in July 2010 for the internalization of O&M as described above.

Other operating expenses were $678, or 55.3%, higher in the second quarter and $473, or 14.1%, higher in the first six months of 2011. Other operating expenses include insurance, property taxes, materials and utilities. Higher costs in the second quarter of 2011 were due to higher water rights expenses on the hydro power facilities based on higher production as well as wastewater transportation costs for Whitecourt.

Administrative expenses

	Three months ended		Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Manager fees	284	444	2,084	2,677
Internalization expenses	18,611	548	19,246	548
Business development	508	1,343	1,817	1,516
Other administrative expenses	2,212	1,118	3,787	1,931
	21,615	3,453	26,934	6,672

Manager fees during the second quarter of 2011 were $160 lower than in the second quarter of 2010 and $593 lower for the six months ended June 30, 2011. The decrease was due to the termination of management contracts with MGL on April 15, 2011, following which Capstone no longer pays management and administrative fees, cost reimbursement or incentive fees to MGL as described under Related Party Transaction on page 30 of the MD&A in combination with the March 2010 divestment of Leisureworld.

Internalization expenses represent costs to terminate the management arrangements with MGL. During the second quarter of 2011, this included $14,117 to terminate the management agreements, $4,036 in one-time payments to staff and $458 in professional fees.

Business development expenses during the second quarter of 2011 were $835, or 62.2%, lower than in 2010, but $301, or 19.9%, higher in the first six months of 2011. Lower expenses during the second quarter of 2011 were attributable to the stage of various business development projects, which required less external assistance.

Other administrative expenses during the second quarter were $1,094, or 97.9%, higher than in 2010 and $1,856, or 96.1%, higher for the six months ended June 30, 2011. Other administrative expenses include corporate salaries, legal, audit, investor relations costs and other professional fees. The increase in the second quarter was primarily attributable to corporate salary expenses which were not incurred prior to internalization.

Other Income and Expenses

	Three months ended		Six months ended	
($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**June 30, 2010**
Interest income	1,893	209	2,326	382
Interest expense	(5,004)	(5,315)	(10,111)	(10,579)
Equity accounted (loss) income	(3,884)	(317)	(6,285)	3,151
Unrealized loss on derivatives	(4,489)	(5,516)	(2,610)	(9,561)
Unrealized (gain) loss on Class B exchangeable unit liability	-	845	-	(2,729)
Amherstburg gain on acquisition	-	4,234	-	4,234
Unrealized (gain) loss on convertible debentures	-	160	-	(1,737)
Foreign exchange loss	(627)	(9)	(633)	(4)
	(12,111)	(5,709)	(17,313)	(16,843)

Interest income

Capstone earns interest income on its cash resources and on its loans receivable with Värmevärden and Chapais Énergie, Société en commandite ("CHESEC"), the owner of the Chapais facility.

Interest income for the second quarter was $1,684, or 805.7%, higher than in 2010 and $1,944, or 508.9%, higher for the six months ended June 30, 2011. The increase was almost entirely attributable to $1,692 of interest on the loan to Värmevärden. Interest of $140 was earned on the CHESEC debt during the second quarter, reflecting a $22 reduction from 2010 due to principal repayments, resulting in a year-to-date decrease of $44.

Interest expense

During the second quarter of 2011, interest expense was $311, or 5.9%, lower and $468, or 4.4%, lower in the first six months of 2011. The decrease was primarily due to $534 of distributions on the Class B exchangeable units, which are treated as interest under IFRS in 2010 when Capstone operated as a mutual fund trust. In addition, interest on the convertible debentures was $289 lower during the second quarter of 2011 and $529 lower in the year-to-date period. In the first quarter of 2010, unamortized transaction costs on the debentures maturing in 2010 were charged to interest expense following their redemption. Interest expense on the 2016 convertible debentures was lower in the first six months of 2011 due to $14,734 of bonds converting to equity.

These two items were partially offset by $586 of fees for the letter of credit to support Capstone's equity commitment to Amherstburg as well as amortization of deferred financing expenses on the project debt in the first six months of 2011.

Equity accounted income

Equity income arises from Capstone's share of income on its interests in infrastructure businesses where Capstone has significant influence but not control, which includes Värmevärden, Chapais and, in 2010, Leisureworld.

For Värmevärden, Capstone reported a $3,884 loss during the second quarter and a $6,298 loss for the first six months of 2011. The successful disposition of Capstone's indirect investment in Leisureworld in March 2010 also contributed to the decrease in equity accounted income. Capstone reported $3,151 of equity accounted income from Leisureworld during the first six months of 2010.

For Capstone's equity interest in Chapais Électrique Limitée ("CHEL"), no income has been recorded on the investment since its acquisition in 2007. Capstone does not expect to earn any future equity accounted income from this investment.

Unrealized gain (loss) on derivatives

Capstone enters into derivative contracts to mitigate the economic impact of the fluctuations in foreign exchange rates, interest rates and the price of natural gas. Capstone has also separately valued embedded derivatives within its gas purchase agreement. Capstone does not use hedge accounting for any of its derivative financial instruments, which are recorded at their fair value on the consolidated statements of financial position with changes in fair value between reporting periods reported as unrealized gains (losses) in the interim consolidated statements of income.

The unrealized gain (loss) on derivatives on the interim consolidated statements of income is composed of:

	Three months ended		Six months ended	
($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Interest rate swap contracts				
Unrealized (loss) gain on derivative assets	(430)	1,474	216	1,493
Unrealized (loss) gain on derivative liabilities	(2,089)	(4,804)	(435)	(4,476)
	(2,519)	(3,330)	(219)	(2,983)
Gas swap contracts				
Unrealized (loss) gain on derivative asset	(821)	(1,159)	(709)	226
Foreign currency option contracts				
Unrealized gain on derivative asset	151	-	151	-
	(3,189)	(4,489)	(777)	(2,757)
Embedded derivative contracts				
Unrealized (loss) gain on embedded derivative asset	(1,238)	766	(1,683)	(4,602)
Unrealized loss on embedded derivative liability	(62)	(1,793)	(150)	(2,202)
	(1,300)	(1,027)	(1,833)	(6,804)
Total unrealized loss on derivatives	(4,489)	(5,516)	(2,610)	(9,561)

The net unrealized loss of $4,489 and $2,610 on derivatives during the second quarter and first six months of 2011, respectively, was primarily due to the interest rate swaps, which had net unrealized losses of $2,519 and $219 respectively and the embedded derivatives, which had net unrealized losses of $1,300 and $1,833 respectively.

The Amherstburg interest rate swap, which was entered into on June 23, 2010, contributed $1,984 to the loss during the quarter. The decrease in the fair value of the interest rate swaps was primarily due to a decrease in the long-term interest rates. Additionally, decreases in natural gas spot and forward prices, which are determined at a regional gas interconnection, storage and trading hub in southwest Ontario (the Union Gas Dawn facility), caused the net embedded derivative to incur a loss of $1,300 during the quarter, accumulating to $1,833 in the year-to-date six-month period.

Income Taxes

During the first six months of 2011, Capstone recorded an income tax recovery of $32,693, of which $32,701 was attributable to deferred income taxes and $8 was attributable to current taxes. The recovery included a $34,809 reduction in the deferred income tax liability following conversion from a mutual fund trust to a corporation on January 1, 2011, which caused the income tax rate applied to timing differences to decrease from 46% to 25%. See page 22 of this MD&A for further details. The deferred income tax recovery was offset primarily by timing differences between depreciation and capital cost allowance.

In the first six months of 2010, the income tax recovery included a $10,722 reduction in the deferred income tax liability attributable to the sale of Capstone's investment in Leisureworld. The remaining deferred income tax recovery was attributable to fluctuations in the fair value adjustments in financial instruments and timing differences between depreciation and capital cost allowance.

Adjusted EBITDA

In addition to the preceding analysis for the components of net income, Capstone's management evaluates financial performance through various non-GAAP measures defined on page 5 of this report. Adjusted EBITDA measures earnings from Capstone's assets excluding any non-cash items. The derivation of Adjusted EBITDA from net income, as reported in the interim consolidated statements of income, is shown in the table below:

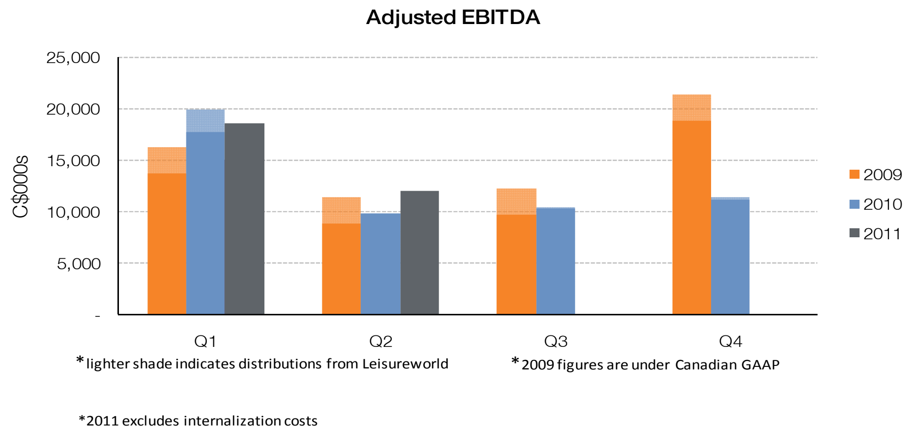
	Three months ended		Six months ended	
($000s)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Net income (loss)	(32,779)	(2,239)	8,553	25,394
Depreciation and amortization	7,908	7,971	15,800	16,206
Interest expense	5,004	5,315	10,111	10,579
Income tax expense (recovery)	4,297	(2,430)	(32,693)	(31,835)
Standardized EBITDA	(15,570)	8,617	1,771	20,344
Equity accounted (income) loss	3,884	317	6,285	(3,151)
Unrealized (gains) or loss on derivatives financial instruments	4,489	5,516	2,610	9,561
Unrealized loss on Class B exchangeable unit liability	-	(845)	-	2,729
Unrealized loss on convertible debentures - conversion option	-	(160)	-	1,737
Amherstburg gain on acquisition	-	(4,234)	-	(4,234)
Foreign exchange (gains) or loss	627	9	633	4
Distributions from equity accounted investments	-	-	-	2,131
Adjusted EBITDA	(6,570)	9,220	11,299	29,121
Internalization expenses	18,611	548	19,246	548
Adjusted EBITDA before internalization costs	12,041	9,768	30,545	29,669

Adjusted EBITDA for the second quarter was $15,790, or 171.2%, lower than in second quarter of 2010. For the first six months of 2011, Adjusted EBITDA was $17,822, or 61.2%, lower than in the first six months of 2010. In both cases, the decrease was primarily attributable to $18,611 of internalization costs incurred in the second quarter. Excluding internalization costs, second quarter Adjusted EBITDA was $2,273, or 23.3%, higher and year-to-date Adjusted EBITDA was $876, or 3.0%, higher than in the prior comparative periods.

The increase in second quarter Adjusted EBITDA before internalization costs was attributable to a $1,531 increase in revenue from the power assets and a $1,684 increase in interest income primarily from the Värmevärden investment. These drivers were partially offset by a $394 increase in operating and other administrative expenses.

The increase in the six-month Adjusted EBITDA before internalization costs was attributable to a $4,294 increase in revenue from the power assets and a $1,944 increase in interest income. These increases were partially offset by a $2,683 increase in operating and administrative expenses and a $2,131 decline in distributions from equity accounted investments due to the sale of Leisureworld in March 2010.

The chart illustrates the Adjusted EBITDA trend starting in 2009 with and without the distributions from Leisureworld and excluding the internalization costs. With these adjustments, Capstone's Adjusted EBITDA improved consistently on a year-over-year basis with the exception of the fourth quarter of 2010 when corporate conversion and related reorganization costs of $1,187 increased administrative expenses and caused Adjusted EBITDA to fall below the prior comparative period. In the second quarter of 2011, excluding internalization costs, Adjusted EBITDA was higher than both the 2010 and 2009 comparative periods even when the Leisureworld distributions are included.



Funds from Operations and Adjusted Funds from Operations

Capstone uses the non-GAAP measures of FFO and AFFO to evaluate cash generated from Capstone's assets. FFO is calculated by increasing Adjusted EBITDA for principal receipts on loans receivable and reducing for interest paid on debt and any income taxes paid. Adjusted FFO reduces FFO for maintenance capital expenditures and the scheduled repayment of debt principal. The calculation of FFO and AFFO are shown below:

	Three months ended		Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Adjusted EBITDA before internalization costs	12,041	9,768	30,545	29,669
Receipts from Chapais loan receivable	218	196	430	386
Interest paid (1)	(4,533)	(4,843)	(7,860)	(7,789)
Income taxes paid	(8)	(8)	(8)	(8)
Funds from operations (FFO) before internalization costs	7,718	5,113	23,107	22,258
Maintenance capital expenditures	(1,883)	(749)	(2,684)	(2,026)
Repayment of debt principal	(819)	(774)	(1,627)	(1,536)
Adjusted funds from operations (AFFO) before internalization costs	5,016	3,590	18,796	18,696
Internalization expenses	(18,611)	(548)	(19,246)	(548)
Adjusted funds from operations (AFFO)	(13,595)	3,042	(450)	18,148
Before internalization costs				
AFFO per share (1)	0.081	0.072	0.308	0.375
Dividends declared per share	0.165	0.165	0.330	0.330
Payout ratio	203.7%	214.4%	107.6%	82.4%
After internalization costs				
AFFO per share (1)	(0.220)	0.061 (1)	(0.007)	0.364 (1)
Dividends declared per share	0.165	0.165	0.330	0.330
Payout ratio	nmf (2)	253.0% (1)	nmf (2)	84.8% (1)

(1) For comparability, the calculation of FFO and AFFO in 2010 treats Class B exchangeable units as equity. As a result, interest paid in 2010 has been reduced and the weighted average number of shares has been increased.
(2) The payout ratio for 2011 is not meaningful due to the internalization costs which result in a negative payout ratio.

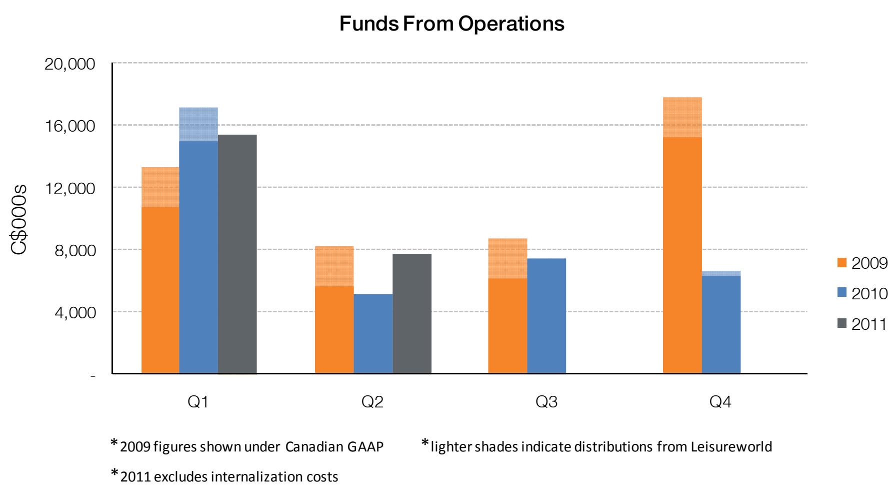
FFO before internalization costs was $2,605, or 50.9%, higher than in the second quarter of 2010 and $849, or 3.8%, higher in the first six months of the year. In both cases, the increase was primarily due to the factors that increased Adjusted EBITDA in 2011 as discussed previously.

AFFO before internalization costs was $1,426, or 39.7%, higher than in the second quarter of 2010 and $100, or 0.5%, higher in the first six months of the year. The improvement in AFFO for the second quarter was consistent with the increase in FFO. Additionally, Capstone incurred lower maintenance capital expenditures in the first quarter of 2011 compared with 2010.

Excluding internalization costs, AFFO per share increased by $0.009 in the second quarter of 2011 and decreased by $0.067 during the first six months of the year. The decline in AFFO per share was attributable to an increase in the number of shares outstanding from a year ago. The payout ratio for the second quarter was 203.7% compared with 214.4% for 2010. For the first six months of 2011, the payout ratio increased to 107.6% from 82.4% in 2010.

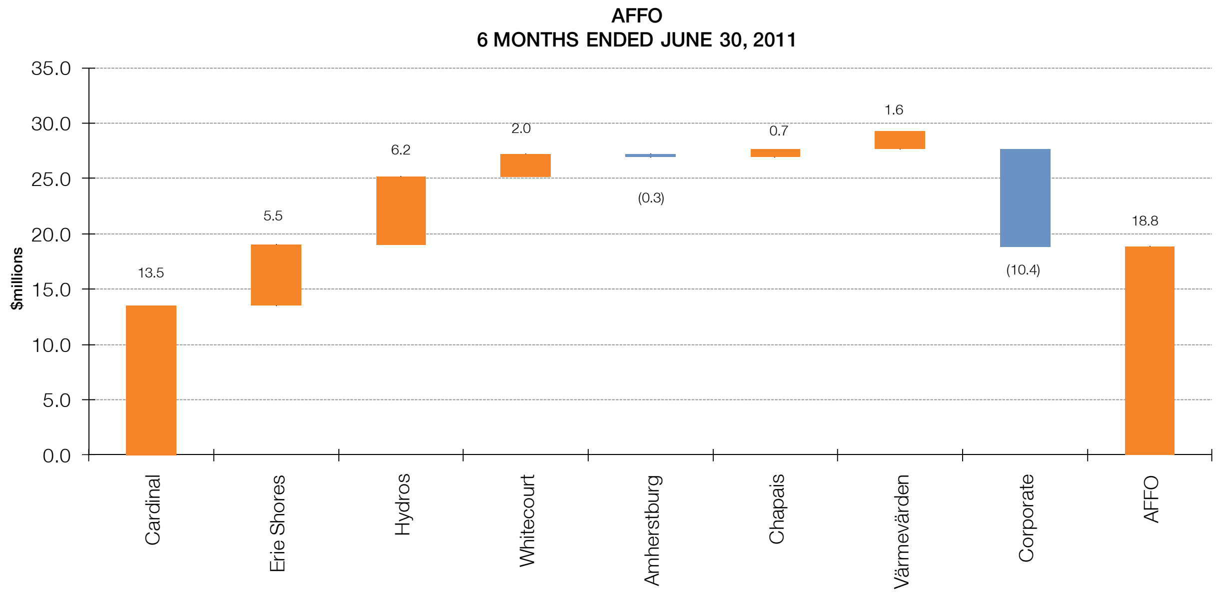
Including internalization costs, AFFO per share was $0.281 lower in the second quarter of 2011 and $0.371 lower for the first six months of the year. The major factors contributing to the decline were internalization costs as well as an increase in the number of shares outstanding in 2011 compared with 2010 following the issuance of shares in December 2010 and the conversion of convertible debentures into equity.

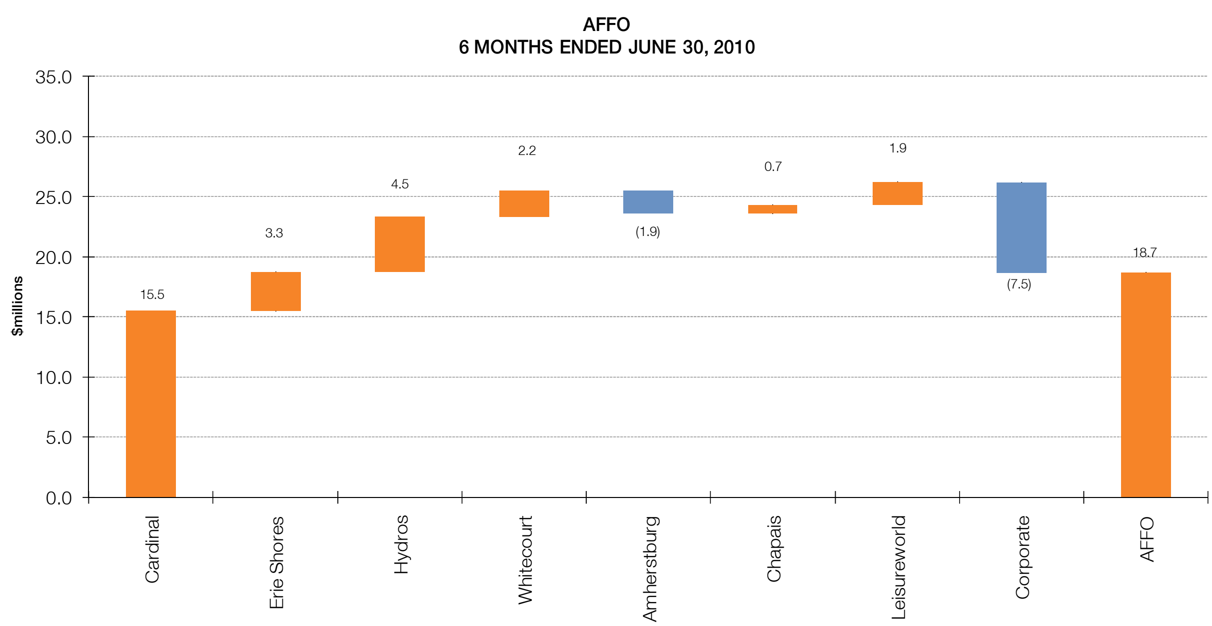
The following chart illustrates the year-over-year trend in FFO starting from 2009 with and without the Leisureworld distributions and excluding the internalization costs. Excluding these items, the chart shows an increasing FFO trend starting with the exception of the fourth quarter of 2010, when FFO declined due to corporate conversion and reorganization costs. The first and second quarters of 2011 were higher than the prior year amounts excluding the Leisureworld distributions.



The following charts illustrate the composition of AFFO for the second quarter of 2011 and 2010 as well as for the first six months of 2011 and 2010, excluding internalization expenses. For the second quarter, AFFO was higher on a year-over-year basis, reflecting improved water flow at the hydro power facilities, improved wind at Erie Shores, interest income from the Värmevärden investment and the absence of acquisition costs in 2011 at the Amherstburg facility. Offsetting these improvements were lower earnings at Cardinal due to fuel costs and higher corporate administrative costs.

Similarly, for the six months ended June 30, 2011, on a year-over-year basis, AFFO for Erie Shores, the hydro power facilities and Amherstburg improved as noted above. Offsetting these improvements were lower AFFO at Cardinal and at head office.


AFFO
6 MONTHS ENDED JUNE 30, 2011
$millions
35.0
30.0
25.0
20.0
15.0
10.0
5.0
0.0
13.5
5.5
6.2
2.0
(0.3)
0.7
1.6
(10.4)
18.8
Cardinal
Erie Shores
Hydros
Whitecourt
Amherstburg
Chapais
Värmevärden
Corporate
AFFO


AFFO
6 MONTHS ENDED JUNE 30, 2010
$millions
35.0
30.0
25.0
20.0
15.0
10.0
5.0
0.0
15.5
3.3
4.5
2.2
(1.9)
0.7
1.9
(7.5)
18.7
Cardinal
Erie Shores
Hydros
Whitecourt
Amherstburg
Chapais
Leisureworld
Corporate
AFFO

FINANCIAL POSITION REVIEW

Overview

As at June 30, 2011, Capstone had unrestricted cash and cash equivalents of $109,355 and a working capital deficit of $23,941, excluding the loans payable from current liabilities. The cash balance, along with available credit, provides Capstone with adequate resources for committed and future acquisitions as well as with a reserve for ongoing capital expenditures and other financial obligations.

Capstone's debt to capitalization ratio (as defined on page 18) increased to 39.3% from 37.9% as at December 31, 2010. The increase was attributable to a 4.9% decline in the share price since December 31, 2010 as well as a $65,200 increase in the Amherstburg project debt. This was partially offset by the increase in shareholders' equity for the preferred shares issued on June 30, 2011. As at June 30, 2011, Capstone operated within all of its debt covenants. Management believes Capstone is well capitalized for current operations and future business development opportunities.

Liquidity

Working capital

($000s)	Jun 30, 2011	Dec 31, 2010
Cash and cash equivalents	109,355	131,440
Restricted cash	6,148	7,575
Accounts receivable	20,521	21,696
Other assets	3,136	3,552
Current portion of loans receivable	933	884
Current portion of derivative contract assets	1,251	1,918
Current assets	141,344	167,065
Accounts payable and other liabilities	68,360	28,896
Current portion of derivative contract liabilities	3,079	2,505
Loans payable	58,098	49,200
Current portion of finance lease obligation	124	120
Current portion of long-term debt	93,722	44,838
Current liabilities	223,383	125,559
Working capital	(82,039)	41,506

The working capital deficit of $82,039 included $85,000 for the CPC-Cardinal credit facility and $58,098 for the loans payable. For the CPC-Cardinal facility, which matures on June 29, 2012, management is considering financing options available. The loans payable relate to the $54,666 arising from the Leisureworld disposition and a $3,432 loan payable to Värmevärden arising from the return of excess capital invested at the time of acquisition. Both loans are to be settled by non-cash distributions during 2011. In addition, accounts payable and other liabilities increased by $39,464 since December 31, 2010, due to accrued construction costs incurred for Amherstburg.

Cash and cash equivalents

Capstone's cash and cash equivalents and restricted cash were as follows:

($000s)	Jun 30, 2011	Dec 31, 2010
Cash and cash equivalents	109,355	131,440
Restricted cash	6,148	7,575
Total cash	115,503	139,015

Cash and cash equivalents decreased $22,085 from December 31, 2010 due to the $109,796 acquisition of Värmevärden on March 31, 2011 which was partially offset by $72,350 of net proceeds from the issue of preferred shares on June 30, 2011. Capstone continues to invest its excess cash in short-term, high quality money market instruments.

Restricted cash included $5,648 for the debt service reserve required under the Erie Shores project debt agreement ($2,304 was restricted at December 31, 2010) and $500 funds in deposit. The $4,000 cash backed letter of credit related to the construction of Amherstburg was cancelled during the quarter.

Cash flow

During the first six months of 2011, Capstone's cash and cash equivalents balance decreased by $22,085 compared with an increase of $12,643 in the same period in 2010. The details of the decrease are described in the consolidated statement of cash flows and are summarized as follows:

($000s)	Jun 30, 2011	Jun 30, 2010
Operating activities	5,764	21,237
Investing activities	(158,485)	(6,631)
Financing activities (excluding dividends to shareholders)	150,868	15,059
Dividends to shareholders	(20,232)	(17,022)
Change in cash and cash equivalents	(22,085)	12,643

Cash from operating activities reflects cash received from revenues less expenses as well as adjustments for non-cash items, including changes in working capital. During 2011, cash flow from operating activities decreased primarily due to internalization costs included in administrative expenses in 2011.

Cash from investing activities reflects income from and monies invested by Capstone in business acquisitions or capital assets. During 2011, Capstone invested $109,796 in the acquisition of Värmevärden and $49,070 in capital assets for the ongoing construction of Amherstburg. In 2010, Capstone received $2,131 in distributions from Leisureworld due to the divestment in March 2010.

Cash from financing activities includes proceeds received from the issuance of debt and equity less repayment of debt and dividends to shareholders of Capstone. During the 2011, cash from financing activities excluding dividends to shareholders, increased by $142,774, due primarily to net proceeds of $72,350 from a preferred share offering on June 30, 2011 and an additional $7,000 from equity issued to MGL as part of internalization. Capstone also received $65,200 under the construction facility for Amherstburg.

Capital Structure

Capstone manages its capital structure as shareholders' equity and long-term debt, both the current and non-current portion, and measures its capitalization ratio based on the fair values of long-term debt and shareholders' equity. The following table shows Capstone's capitalization ratio using fair values compared to the ratio calculated using the carrying values reported in Capstone's interim consolidated financial statements:

	Jun 30, 2011		Dec 31, 2010	
($000s)	Fair Value	Carrying Value	Fair Value	Carrying Value
CPC-Cardinal credit facility	85,000	85,000	85,000	85,000
Erie Shores project debt	105,950	105,436	106,197	107,063
Amherstburg Solar Park project debt	96,200	96,200	31,000	31,000
Convertible debentures (1)	48,272	39,706	61,311	48,875
Levelization liability	24,584	24,584	23,714	23,714
Deferred financing costs	-	(5,466)	-	(5,556)
Total long-term debt	360,006	345,460	307,222	290,096
Shareholders' equity (1) and (2)	557,028	379,995	463,217	264,095
Class B unit liability (2) and (3)	-	-	26,710	26,710
Convertible debentures – conversion option (1)	-	-	12,640	12,640
	557,028	379,995	502,567	303,445
Total capitalization	917,034	725,455	809,789	593,541
Debt to capitalization	39.3%	47.6%	37.9%	48.9%

(1) The fair value of Capstone's convertible debentures as at June 30, 2011 was based on a market price of $112.9 (December 31, 2010 - $115.2) and debentures outstanding of $42,766 (December 31, 2010 - $53,221) aggregate principal amount. The carrying value of the equity portion as at June 30, 2011 of Capstone's convertible debentures of $9,288 (December 31, 2010 - $12,640) was excluded from total debt and included as part of shareholders' equity.

(2) The fair value of shareholders' equity reflected the Corporation's market capitalization as at June 30, 2011 based on a share price of $7.82 (December 31, 2010 - $8.22) and shares outstanding of 61,951,153 (December 31, 2010 - 56,352,461 shares). Shares outstanding include Class B exchangeable units of MPT LTC Holding LP, a subsidiary of Capstone, of which there were 3,249,390 outstanding at December 31, 2010, which were classified as a liability on the interim consolidated statements of financial position. Fair value of the preferred shares issued on June 30, 2011 is based on a share price of $24.19 and total shares outstanding of 3,000,000.

(3) The Class B exchangeable unit liability is treated as part of equity in the comparative figures based on its characteristics and for consistency between periods.

CPC-Cardinal credit facility

The composition of the CPC-Cardinal credit facility is as follows:

	Jun 30, 2011		Dec 31, 2010	
($000s)	Term Facility	Revolving Facility	Term Facility	Revolving Facility
Commitment	138,125	40,625	141,875	40,625
Drawn	(85,000)	-	(85,000)	-
Letters of credit (1)	-	(2,533)	-	(40,625)
Guarantees (2)	(5,000)	-	(10,000)	-
Remaining credit	48,125	38,092	46,875	-

(1) Three letters of credit totalling $2,533 for Erie Shores have been authorized under the revolving credit facility. The $38,092 letter of credit for the Amherstburg project was released upon funding of Capstone's equity contribution to the project.

(2) Effective April 1, 2011, with the refinancing of Tranche C of Erie Shores' debt, guarantee was reduced to $5,000.

Advances under the credit facility are made in the form of a series of bankers' acceptances ("BAs") and prime rate loans. Interest paid on BAs is based on the then current BA rate plus an applicable margin ("stamping fee") based on the ratio of consolidated total debt to consolidated EBITDA. Collateral for the facility is provided by first ranking security interest covering the assets of CPC, Cardinal and certain direct subsidiaries, collectively the "restricted group". The restricted group is subject to and is in compliance with certain non-financial and financial covenants, including limits on the consolidated total debt to consolidated EBITDA ratio and interest coverage ratio.

Erie Shores project debt

As at June 30, 2011, Erie Shores had a loan of $105,436 in non-recourse project financing consisting of a $61,003 fully amortizing loan (“Tranche A”) maturing April 1, 2026, a $4,433 fully amortizing loan (“Tranche B”) maturing April 1, 2016, and a $40,000 fully amortizing loan (“Tranche C”) maturing April 1, 2026.

This project debt was borrowed by Erie Shores and is secured by the assets of Erie Shores. CPC has provided an unsecured guarantee in the amount of $5,000 to Erie Shores’ lenders in respect of the Tranche C loan.

Amherstburg Solar Park

Under the terms of the credit agreement, there is a project construction facility and a term facility. During the project development, Capstone made draws under the construction facility to finance work as it was completed on the project. All interest accruing on the construction facility during development has been capitalized to the outstanding balance of the debt.

In July 2011, upon completion of construction, the outstanding balance of the construction facility was converted into a term facility, which requires regular principal and interest payments amortized over 17 years, with a five year maturity. The effective interest rate of the debt is 7.32%. Amherstburg has entered into a swap to convert its floating interest rate obligations under the credit agreement to a fixed rate. The financing and the swap were arranged by Amherstburg and are secured only by the assets of Amherstburg.

Convertible debentures

In December 2009 and January 2010, Capstone issued $57,500 of 6.50% convertible unsecured subordinated debentures with a maturity date of December 31, 2016. Interest on the convertible debentures is payable semi-annually in arrears on June 30 and December 31. The convertible debentures are convertible into common shares of Capstone at the option of the holder at a conversion price of $7.00 per share.

During the quarter and six months ended June 30, 2011, Capstone issued 86,281 and 1,493,556 common shares, respectively, following conversion requests from various convertible debenture holders. Accordingly, the liability portion and equity portion of the convertible debentures were reduced by $609 and $128, respectively, for the quarter ($9,534 and $2,266, respectively, for the six-month period). As at June 30, 2011, $42,766 of face value was outstanding.

Levelization liability

As at June 30, 2011, Capstone had a levelization liability of $24,584 (December 31, 2010 - $23,714) relating to payments received from the Ontario Electricity Financial Corporation (“OEFC”) in excess of the base rate as set out under the Power Purchase Agreement (“PPA”) for the Wawatay hydro power facility. In accordance with the PPA, the OEFC is required to make monthly guaranteed payments as well as variable payments based on actual electricity production. To the extent these payments exceed the revenue recorded in a given month, Capstone records an increase in the levelization liability. To the extent these payments are less than the revenue recognized, Capstone records a reduction in the levelization liability. Interest on the levelization liability is accrued at a prescribed variable rate, which currently approximates 6.94% per annum.

Shareholders’ equity

Shareholders’ equity is the core of Capstone’s capital structure and is composed of the following:

($000s)	Jun 30, 2011	Dec 31, 2010
Shareholders’ capital	554,976	536, 278
Preferred shares	73,016	-
Class B exchangeable units	26,710	-
Equity portion of convertible debentures	9,288	-
Accumulated other comprehensive income	(133)	-
Retained earnings (deficit)	(283,862)	(272,183)
Total shareholders’ equity	379,995	264,095

Capstone is authorized to issue an unlimited number of common shares as well as a number of preferred shares equal to 50% of the outstanding common shares. The change in shareholders’ capital was as follows:

	Six months ended Jun 30, 2011		Twelve months ended Dec 31, 2010	
($000s and 000s of shares)	Shares	Amount	Units	Amount
Opening balance	56,352	536,278	46,665	466,662
Shares issued (1) and (2)	856	6,898	9,079	65,249
Conversion of convertible debentures (3)	1,494	11,800	611	4,390
Units redeemed	-	-	(3)	(23)
Ending balance	58,702	554,976	56,352	536,278

(1) On December 22, 2010, Capstone completed a private placement of 9,079,250 shares at a price of $7.60 per share for gross proceeds of approximately $69,000 before issue costs of $3,751. The net proceeds will be used by Capstone for acquisitions and for general purposes. During 2011, $102 of the private placement transaction costs were included in share capital.
(2) On April 15, 2011 the Corporation issued 856 common shares subscribed to by MGL as part of the management internalization at $8.18 dollars per share for gross proceeds of approximately $7,000.
(3) $11,800 (2010 - $4,390) of the convertible debentures were converted into shares of Capstone, which is net of transaction costs incurred to issue the convertible debentures.

On June 30, 2011, Capstone issued 3,000,000 cumulative 5-year reset preferred shares at a price of 25 dollars per share for gross proceeds of $75,000 before issue costs of $2,650. The net proceeds will be used by Capstone for acquisitions and for general purposes.

As discussed on page 7 of this MD&A, the Class B exchangeable units were classified as debt prior to the corporate conversion in accordance with IFRS. Capstone has 3,249,390 Class B exchangeable units outstanding that were issued by a subsidiary entity at the time Leisureworld was acquired. The Class B exchangeable units are eligible to receive distributions under the same terms and conditions as shares of Capstone. Each Class B exchangeable unit may be converted at the option of the unitholders into one share of Capstone any time up to October 18, 2020.

The equity portion of the convertible debentures pertains to the convertible debentures. Retained earnings (deficit) reflects Capstone's net income (loss) since Capstone was formed less aggregate dividends paid to shareholders and aggregate distributions paid to Class B exchangeable unitholders.

Derivative Financial Instruments

The fair value of these contracts, as reported on Capstone's interim consolidated statements of financial position was:

($000s)	Jun 30, 2011	Dec 31, 2010
Derivative contract assets		
Foreign currency contracts	861	-
Gas swap contracts	1,209	1,918
Interest rate swap contracts	1,508	1,292
Embedded derivatives	3,606	5,287
	7,184	8,497
Current portion of derivative contract assets	(1,251)	(1,918)
	5,933	6,579
Derivative contract liabilities		
Interest rate swap contracts	8,839	8,402
Embedded derivatives	9,054	8,904
	17,893	17,306
Current portion of derivative contract liabilities	(3,079)	(2,505)
	14,814	14,801

Foreign currency contracts

Capstone has purchased options to sell a total of 90,500 Swedish Kroner (SEK) over the next five years. These option contracts effectively allow Capstone to convert a portion of the interest received on the shareholder loans with Värmevärden from SEK to Canadian dollars at a fixed exchange rate of 6.5165.

Gas swap contracts

Cardinal has a natural gas swap contract for the seven-month period from April to October in 2011. The contract requires Cardinal to make payments to the counterparties based on 62,402 MMBtu (December 31, 2010 - 436,814 MMBtu) of gas at the then market rate of natural gas in exchange for receiving payments based on 62,402 MMBtu (December 31, 2010 - 436,814 MMBtu) of gas at a fixed price per MMBtu.

Interest rate swap contracts

For the CPC-Cardinal credit facility, Capstone holds five interest rate swap contracts, all of which mature in June 2012, to mitigate interest rate risk on a notional amount of $85,000, representing the total amount drawn under the credit facility. Under each contract, Capstone pays a fixed rate in return for a floating rate equal to the then current three-month BA rate. These interest rate swaps effectively convert Capstone's floating rate obligations to a fixed rate as shown in the table below:

Maturity Date	Notional Amount ($000s)	Swap Fixed Rate	Stamping Fee[(1)]	Effective Fixed Rate
June 29, 2012	11,700	3.12%	3.00%	6.12%
June 29, 2012	5,300	3.13%	3.00%	6.13%
June 29, 2012	18,000	3.13%	3.00%	6.13%
June 29, 2012	10,000	2.28%	3.00%	5.28%
June 29, 2012	40,000	2.14%	3.00%	5.14%
	85,000	2.56%	3.00%	5.56%

(1) The stamping fee represents the margin that was paid on advances from the CPC-Cardinal credit facility in the most recent quarter.

CPC also has a forward interest rate swap contract on a notional amount of $20,000 which was put in place to mitigate some of the refinancing risk associated with the Erie Shores project debt. Under the contract, CPC will pay a fixed rate of 5.63% for a period of five years following the maturity of the Erie Shores project debt from December 1, 2011 to December 1, 2016. In return, CPC will be paid a floating rate equal to the then current three-month BA rate.

On June 23, 2010, upon the acquisition of Amherstburg, Capstone entered into an interest rate swap contract to mitigate the interest rate risk on the project debt. The notional amount of the interest rate swap, initially zero, increased as the construction facility was used to finance the development of the project until June 30, 2011, at which time the notional amount reached $96,200 (December 31, 2010 - $35,803).

Capstone has exposure to market risk, credit risk and liquidity risk from its use of financial instruments. Refer to Note 9 (Risk Management) in the consolidated financial statements for the year ended December 31, 2010 for further detail.

Loans payable

In March 2010, Capstone divested its interest in Leisureworld, held by Macquarie Long Term Care L.P. ("MLTCLP"), of which Capstone holds an approximate 45% interest. Capstone received its proportionate share of the initial net cash proceeds from MLTCLP in the form of a loan payable for $49,200, which increased by $5,466 on March 23, 2011 when the final holdback conditions were satisfied. The loan is non-interest bearing and payable on demand and had principal outstanding of $54,666 as at June 30, 2011 (December 31, 2010 - $49,200). Management expects the loan to be settled by way of a non-cash distribution from MLTCLP.

On June 22, 2011, a loan payable between Värmevärden and Capstone was entered into for the return of surplus capital invested at the time of acquisition. The loan is non-interest bearing and payable on demand and had $3,432 of principal outstanding (22,500 SEK) as at June 30, 2011. Management expects the loan to be settled by a non-cash cancellation of existing share capital during 2011.

Deferred income taxes

Deferred income tax assets and liabilities are recognized on Capstone's consolidated statement of financial position based on temporary differences between the accounting and tax bases of existing assets and liabilities. Capstone had the following deferred income tax balances:

($000s)	Jun 30, 2011	Dec 31, 2010
Deferred income tax assets	15,884	24,211
Deferred income tax liabilities	(64,643)	(105,251)
	(48,759)	(81,040)

The reduction in the deferred income tax asset and liability balances was primarily attributable to moving from the undistributed income tax rate of 46% prior to conversion to a corporation to the general corporate rate of 25% to determine the balances in 2011.

During 2010, $1,910 of deferred income tax liability was recognized on the acquisition of Amherstburg from SunPower Corporation ("SunPower") through the purchase equation and $831 was related to the 46% undistributed income tax rate adjustment, which was released from the deferred income tax liability on January 1, 2011 upon conversion to a corporation.

Capstone also has unrecognized amounts related to net-capital and non-capital loss carry-forwards, which total $124,566 and $17,012, respectively.

Contractual Obligations

Capstone enters into contractual commitments in the normal course of business. These contracts include leases, purchase obligations, electricity supply contracts, gas purchase contracts, wood waste agreements, operations and management agreements and guarantees. There have been no material changes in the specified contractual obligations outside the normal course of operations during the first six months of 2011 that have not been previously disclosed in the annual MD&A for the year ended December 31, 2010, AIF filed March 24, 2011 or interim financial statements for the quarter ended March 31, 2011. Additionally, there have been no other significant changes to the specified contractual obligations that are outside the ordinary course of business and Capstone is not engaged in any off-balance sheet financing transactions.

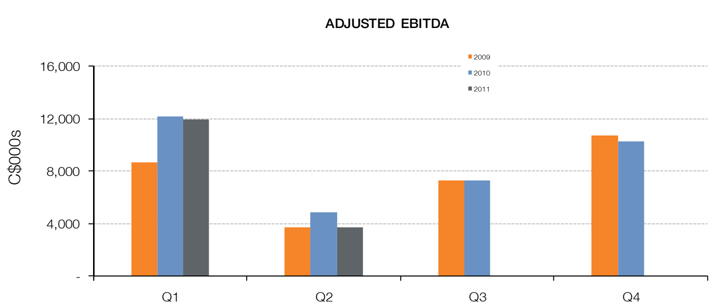
ASSET PERFORMANCE

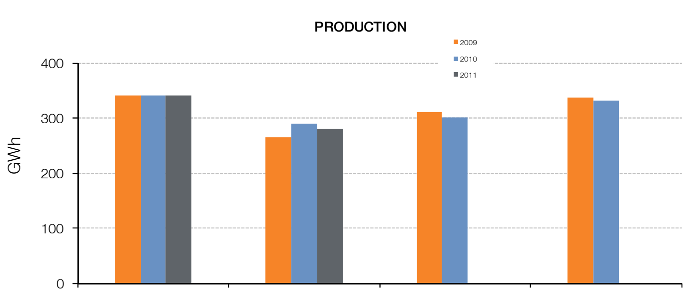
Gas Cogeneration Power: Cardinal

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Revenue	24,009	23,315	57,086	54,974
Operating and administrative expenses (1)	20,336	18,437	41,558	37,929
Adjusted EBITDA (1)	3,678	4,885	15,605	17,055
FFO (1)	3,402	4,637	15,067	16,564
Electricity production (MWh)	280,977	288,947	621,981	629,655
Steam production (KLbs)	176,789	174,317	371,349	360,221
Fuel consumption (MMBtu)	2,422,942	2,482,424	5,271,849	5,297,267
Capacity factors	87.8%	90.3%	92.9%	94.1%
Availability	92.3%	93.6%	96.1%	96.7%

(1) Operating and administrative expenses and Non-GAAP measures exclude internalization costs.





Performance review

During the second quarter, Cardinal's revenue increased by $694, or 3.0%, over the second quarter of 2010 and increased by $2,112, or 3.8%, in the first six months of the year. Higher revenue reflected higher electricity rates through the DCR adjustment as electricity production, capacity and availability were slightly lower than the prior year.

Higher revenue was offset by a $1,899, or 10.3%, increase in expenses during the second quarter and a $3,629, or 9.6%, increase in the first six months of the year due to higher fuel consumption and transportation costs than in the prior year. TCPL and Transportation costs increased from $1.64 per GJ in 2010 to $2.24 GJ effective March 1, 2011.

During the second quarter of 2011, Cardinal completed its seven-day annual maintenance outage on time and within budget.

Adjusted EBITDA and FFO decreased by 24.7% and 26.6%, respectively, for the second quarter. For the first six months of 2011, Adjusted EBITDA and FFO decreased by 8.5% and 9.0%, respectively.

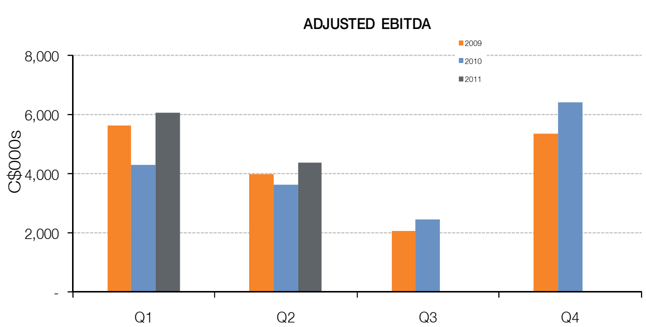
Outlook

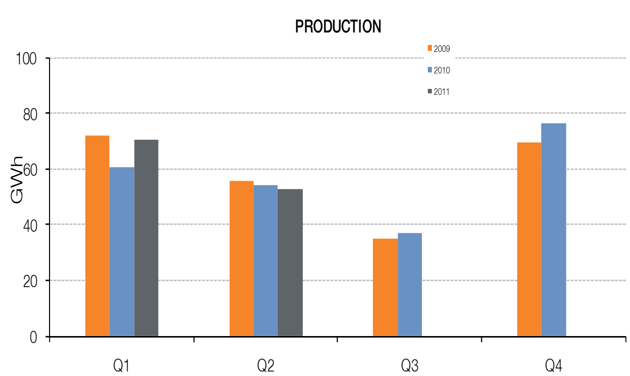
Revenue in 2011 is expected to be higher than in 2010 due to projected escalation in the DCR. The increase in revenue will be partially offset by planned maintenance activities and by higher TCPL gas transportation rates. Higher gas transportation rates are expected to result in approximately $5.5 million to $6 million in increased operating costs. As a result, Cardinal's Adjusted EBITDA and FFO are expected to be lower in 2011 than in 2010. Management continues to implement its strategy to secure a new contract for Cardinal to replace its current PPA that expires in 2014.

Wind Power: Erie Shores Wind Farm

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Revenue	5,119	5,260	12,004	11,141
Operating and administrative expenses	727	1,631	1,527	3,218
Adjusted EBITDA	4,394	3,629	10,479	7,923
FFO	2,910	2,110	7,371	4,874
Electricity production (MWh)	52,557	54,081	123,167	114,599
Capacity factors	24.4%	25.0%	28.6%	26.6%
Availability	92.3%	97.6%	95.4%	97.8%





Performance review

During the first six months of 2011, revenue increased by $863, or 7.7%, over the same period in 2010. The increase in revenue resulted from higher wind speeds combined with strong availability during the first quarter of 2011. Revenue for the second quarter of 2011 was consistent with the second quarter of 2010.

Operating and administrative expenses declined $904, or 55.4%, from the second quarter of 2010 when O&M services were internalized. The remaining variance was attributable to a greater number of repairs in 2010.

These factors resulted in a $765, or 21.1%, increase in Adjusted EBITDA over the second quarter of 2010 and a $800, or 37.9%, increase in FFO. For the first six months of the year, Adjusted EBITDA was $2,556, or 32.3%, higher while FFO was $2,497, or 51.2%, higher.

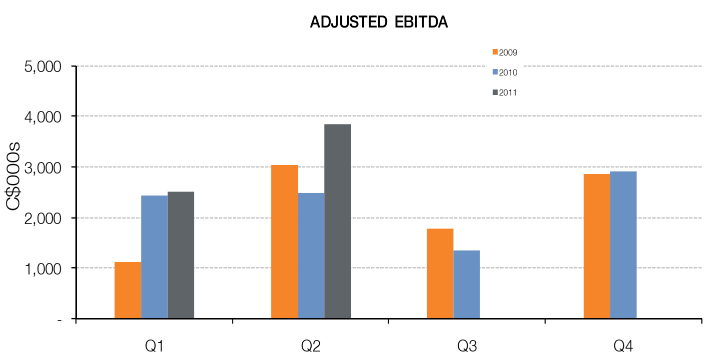
Outlook

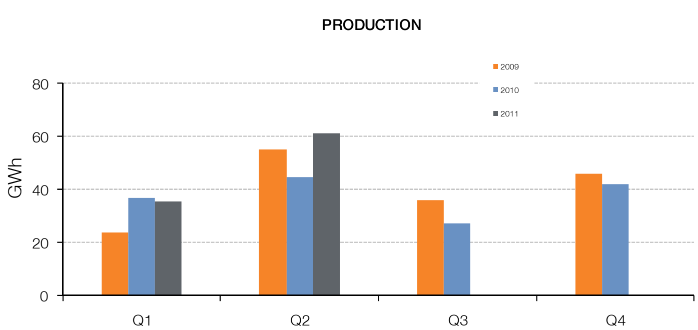
Erie Shores is anticipated to benefit from more typical wind conditions through the remainder of 2011, yielding higher production and corresponding higher revenue than in 2010. Capstone's annual long-term production target for the facility is approximately 248,000 MWh. Erie Shores is also expected to incur lower operating costs in 2011 following the O&M internalization in 2010. Due to these factors, Adjusted EBITDA and FFO are expected to be higher in 2011 than in 2010.

Hydro Power: Four Facilities

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Revenue	4,713	3,437	8,015	6,710
Operating and administrative expenses	864	952	1,669	1,802
Adjusted EBITDA	3,849	2,485	6,346	4,908
FFO	3,849	2,485	6,346	4,908
Electricity production (MWh)	61,389	44,700	96,786	81,516
Capacity factors	78.6%	57.6%	62.4%	52.7%
Availability	99.5%	99.2%	99.2%	98.3%





Performance review

During the second quarter of 2011, revenue for the four hydro power facilities was $1,276, or 37.1%, higher than in 2010 and $1,305, or 19.4% higher for the six months of 2011. Higher revenue was the result of substantially higher electricity production in 2011 based on strong water flows from the snow accumulation over the winter and poor conditions in 2010.

Operating and administrative expenses were $88, or 9.2%, lower during the second quarter and $133, or 7.4%, lower for the first six months of 2011. The decrease was primarily attributable to lower repairs and maintenance in 2011.

The impact on both Adjusted EBITDA and FFO was an increase of $1,364, or 54.9% over 2010 for the second quarter and an increase of $1,438, or 29.3%, for the first six months of 2011.

Outlook

The hydro power facilities are expected to exceed their long-term average annual production of approximately 166,000 MWh based on substantially improved hydrological conditions for Ontario and British Columbia in 2011. Higher revenue will also reflect the price escalators in certain of the facilities' PPAs. Operating costs are expected to be lower than in 2010. As a result, Adjusted EBITDA and FFO from the hydro power facilities are expected to be higher in 2011 than in 2010.

Biomass Power: Whitecourt

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Revenue	3,187	3,485	6,838	6,824
Operating and administrative expenses	2,160	2,386	4,083	4,104
Adjusted EBITDA	1,027	1,099	2,755	2,720
FFO	1,023	1,093	2,747	2,708
Electricity production (MWh)	45,863	49,526	97,067	101,440
Fuel consumption (GMT) [1]	68,794	74,422	145,600	148,940
Capacity factor	90.7%	93.2%	94.9%	96.0%
Availability	92.2%	93.3%	96.1%	96.3%

[1] Green metric tonnes

Performance review

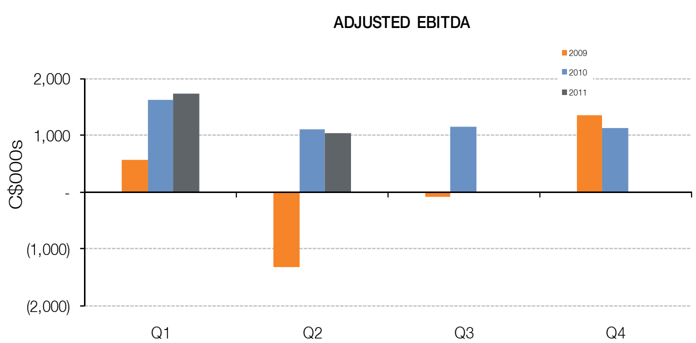
During the second quarter of 2011, Whitecourt's revenue was $298, or 8.6%, lower than in 2010 and $14, or 0.2% higher for the first six months of the year. The decrease resulted from lower electricity production partially offset by higher power rates. Whitecourt completed a seven-day maintenance outage in May.

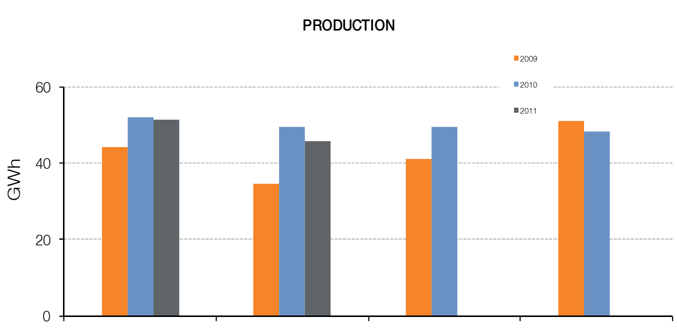
Operating and administrative expenses in the second quarter were $226, or 9.5%, lower than in 2010 and $21, or 0.5%, lower for the first six months of 2011 due to lower maintenance costs in 2011.

The net impact on Adjusted EBITDA and FFO was a decrease of 6.6% and 6.4%, respectively, for the second quarter of 2011. For the first six months of 2011, Adjusted EBITDA and FFO were 1.3% and 1.4% higher.

Outlook

Revenue in 2011 is expected to be consistent with 2010, primarily reflecting planned outages for maintenance and merchant power prices for the remainder of 2011. Adjusted EBITDA and FFO from this facility are expected to be slightly higher than in 2010. Whitecourt is anticipated to have a continuing stable and adequate supply of wood waste fuel in 2011.





Solar Power: Amherstburg Solar Park

Performance review

Work on the solar park progressed according to plan during the second quarter of 2011. Amherstburg successfully achieved commercial operations on June 30, 2011 after incurring final construction costs of $41,380 during the second quarter.

Outlook

Amherstburg is expected to produce up to approximately 37,600 MWh of electricity annually. In 2011, Capstone will benefit from the contribution of six months of Adjusted EBITDA and FFO from this facility.

Biomass Power: Chapais

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Interest income on loans receivable	140	162	286	330
Electricity production (MWh) [1]	60,148	55,082	121,417	115,303
Fuel consumption (GMT)	113,854	99,753	234,069	220,836
Capacity factor	99.3%	90.1%	97.3%	94.8%
Availability	97.1%	89.2%	98.5%	93.2%

[1] Total amount of electricity produced by the Chapais facility, in which Capstone holds a minority equity and debt interest.

Performance review

The Chapais facility's second quarter performance measures were ahead of the same period of 2010 for electricity production, availability, capacity and fuel consumption. Capstone continued to receive scheduled principal and interest income payments from the Tranche A portion of the outstanding debt of CHESEC. The fuel costs for the facility remain high and therefore the facility is only able to pay interest and principal on Tranche A of the outstanding debt. Capstone does not expect to earn income on its minority preferred equity investment.

Utilities Infrastructure: Värmevärden

Performance highlights

	Three months ended		Six months ended	
($000s unless otherwise noted)	**Jun 30, 2011**	**Jun 30, 2010**	**Jun 30, 2011**	**Jun 30, 2010**
Interest income on loans receivable	1,692	-	1,692	-
Heat and steam production (MWh) (1)	246,500	-	246,500	-
Fuel consumption (MWh)	300,600	-	300,600	-
Efficiency	82.0%	-	82.0%	-

(1) Total amount of heat and steam produced by Värmevärden, in which Capstone holds a minority equity interest.

Performance review

On March 31, 2011, Capstone completed its acquisition of a 33.3% interest in a district heating business in Sweden operating as Värmevärden. The year-to-date results included in Capstone's equity accounted income are made up of the losses from Värmevärden during the second quarter along with the transaction costs incurred by Värmevärden to complete the acquisition. Värmevärden experiences lower production during the summer months due to the seasonal nature of customer demand for heating.

Outlook

The fourth quarter is typically the strongest period for this business due to the increased need for heating in the winter months. In 2011, Capstone is expected to benefit from six months of Adjusted EBITDA and FFO contribution from this investment.

Social Infrastructure: Leisureworld

During the first six months of 2011, Capstone received a cash payment of $5,466 from MLTCLP following expiry of the holdback established when Leisureworld was sold in March 2010. Capstone continues to use equity accounting for its residual interest in MLTCLP until such time as the wind-up of the remaining activities of MLTCLP is completed.

SEASONALITY

Capstone's operating results may fluctuate due to seasonal factors that affect quarterly production of the individual facilities. The factors contributing to these results include scheduled major maintenance, seasonal electricity and heat demands and environmental factors such as water flows, wind speeds, temperature and humidity. For further information on asset specific seasonality considerations see the Corporation's most recent annual report for the year ended December 31, 2010 as no material changes have occurred to the nature of Capstone's operating assets, aside from our recent investment in Värmevärden, which is described further below.

In summary, the above factors result in the portfolio generating the highest average long-term electricity production during the first and fourth quarter as shown in the following table for the power generating facilities:

Project Name	Type	Electricity Purchaser	PPA Expiry	Net Installed Capacity (MW)	Q2 2011	Average long-term production (MWh) (1)			
						Q1	Q2	Q3	Q4
Cardinal	Gas	OEFC	2014	156	280,977	343,013	281,953	304,372	332,678
Erie Shores	Wind	OPA	2026	99 (2)	52,557	74,727	53,480	34,677	77,407
Whitecourt	Biomass	TransAlta	2014	25	45,863	49,882	44,964	49,624	49,302
Sechelt	Hydro	BC Hydro	2017	16	30,647	20,308	30,560	12,411	22,044
Wawatay	Hydro	OEFC	2042	14	22,899	4,847	18,995	9,613	14,464
Hluey Lakes	Hydro	BC Hydro	2020	3	1,352	2,192	1,348	1,189	2,055
Dryden (3)	Hydro	OEFC	2020	3	6,491	4,895	5,238	5,495	4,692
Chapais (4)	Biomass	Hydro Quebec	2015	28	60,148	60,340	52,998	58,193	49,570
Total				344	500,934	560,204	489,536	475,574	552,212

(1) Average long-term production is from March 2005 to June 2011, except for Erie Shores, which is from June 2006.
(2) One 1.5 MW turbine is owned by a landowner.
(3) The Dryden facility is composed of three facilities, built in 1922 (Wainwright), 1928 (Eagle) and 1938 (McKenzie). These facilities were refurbished in 1986.
(4) Capstone's investment in the Chapais facility consists of a 31.3% interest in one of two classes of preferred shares, a 24.8% interest in Tranche A and B debt and a 50% interest in Tranche C debt.

During the quarter, total power generated was 2.3% higher than the long-term average. With the exception of Wawatay, Dryden and Chapais, each facility performed within 2.5% of its second quarter average long-term production.

Wawatay and Dryden were 20.6% and 23.9%, respectively, above their second quarter long-term average production as a result of a later than normal spring runoff. Chapais was 13.5% above its second quarter production due to less down time than incurred in the historical average for the second quarter.

For Amherstburg, which generates power based on sunlight, longer sunnier days result in more electricity production. As a result, Capstone anticipates the power production during the second and third quarter each year to approximate 65% of the annual production.

For the Värmevärden investment, which generates heat for consumption in buildings, demand is higher in the colder months of the year. As a result, Värmevärden's contribution to Capstone's net income (loss) is expected to be more favourable in the first and fourth quarters of the year. The first and fourth quarters are expected to account for approximately 65% of the energy sold during the year.

Capstone maintains cash reserves in order to offset seasonality and other factors that may impact electricity and heat production. Management expects that Capstone's cash reserves and free cash flow will be sufficient to maintain monthly dividends to shareholders.

SUMMARY OF QUARTERLY RESULTS

The following table provides a historical summary for the previous eight quarters of Capstone's financial performance, which illustrates the effect of seasonality on Capstone's performance.

($000s, except for per share amounts)	2011		2010				2009 (Cdn GAAP)	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Revenue	37,028	46,915	44,265	34,598	35,497	44,152	42,795	32,731
Net income (loss)	(32,779)	41,332	(2,648)	(6,845)	(2,239)	27,633	11,501	(587)
Cash flows from operating activities	(8,353)	14,117	1,626	6,149	7,364	13,873	9,504	5,972
Adjusted EBITDA	(6,570)	17,869	16,531	10,166	9,221	19,901	21,360	12,232
FFO	(10,893)	14,754	11,800	7,298	4,565	17,145	17,797	8,756
AFFO	(13,595)	13,145	9,714	5,828	3,042	15,106	16,127	7,725
Dividends declared to shareholders	10,217	10,015	8,232	7,700	7,699	7,700	13,103	13,103
Earnings Per Share - Basic	(0.531)	0.685	(0.055)(1)	(0.147)(1)	(0.048)(1)	0.592(1)	0.230	(0.012)
Earnings Per Share - Diluted	(0.531)	0.625(2)	(0.055)	(0.163)(2)	(0.048)	0.547(2)	0.230	(0.012)
Cash flows from operating activities per share	(0.135)	0.231	0.021	0.145	0.158	0.297	0.190	0.120
AFFO per share 3	(0.220)	0.215	0.183	0.117	0.061	0.303	0.346	0.166
Dividends declared per share	0.165	0.165	0.165	0.165	0.165	0.165	0.262	0.262

(1) Class B exchangeable units were not included in the weighted average shares outstanding, as they were classified as debt during this period under IFRS.
(2) Convertible debentures were dilutive during the period.
(3) Included in the AFFO per share are the Class B exchangeable units to allow the non-GAAP measures to be comparative.

Dividends reflect Capstone's annualized $0.66 per share policy, which was revised effective January 1, 2010 from $1.05 per share.

RELATED PARTY TRANSACTIONS

On April 15, 2011, Capstone and MGL terminated the management and administration agreements that established the related party relationship with MGL and its subsidiaries. As such, after April 15, 2011, all transactions with MGL and its subsidiaries are considered to be at arm's length.

The Corporation has various related party transactions, which range from being common routine transactions in the ordinary course of business to non-routine as described below.

Transactions with MGL

From the prior quarter ended March 31, 2011 to April 15, 2011, Capstone had related party transactions with respect to services provided by MPML, including fees for certain administration and support functions carried out by the Manager under certain management and administrative agreements that totalled $14,620 during the quarter ended and $16,420 during the six-months ended June 30, 2011 ($2,677 - June 30, 2010). Costs of $14,336 related to the internalization have been included in these figures, which is further disclosed on page 30 of this MD&A.

Compensation of Key Management

Aside from amounts paid as part of the management internalization the disclosure of compensation of key management has remained consistent with the previous quarter ended and can be found in note 16 (b) to the interim financial statements for the period ended June 30, 2011.

Prior to April 15, 2011, the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") of Capstone and other employees were employed by the Manager. Accordingly, employee compensation disclosure only includes executive compensation since the internalization of management.

In the quarter, Capstone established a restricted share unit ("RSU") plan and performance share unit ("PSU") plan to compensate senior management of the Corporation. The RSUs and PSUs are expensed over the respective vesting period and the corresponding liability is adjusted in each reporting period for the fair value of the obligation based on the cash award that would be required as calculated from the fair value of the granted RSUs and PSUs. As at June 30, 2011, the value of the obligation included in the interim consolidated statement on financial position was $13.8.

RISKS AND UNCERTAINTIES

Capstone is subject to a number of risks and uncertainties that could have an adverse impact on our businesses, operating results and financial condition, which could negatively affect our ability to pay dividends to shareholders. Please refer to the "Risk Factors" section of the AIF filed March 24, 2011 for the year ended December 31, 2010 as updated in subsequently filed Quarterly Financial Reports and other filings made by the Corporation with the Canadian securities regulatory authorities. These filings are available on SEDAR at www.sedar.com.

Management believes that there have been no material changes in the business environment or risks faced by the Corporation during the quarter that have not been previously disclosed in the AIF or most recent annual report for the year ended December 31, 2010.

Climate Change and the Environment

Capstone monitors developments with respect to climate change and the environment with the assistance of external legal council. No material changes have occurred since the Corporation's prior disclosure in its most recent annual report for the year ended December 31, 2010, except as described below:

In July 2011, Québec published a draft regulation to facilitate the implementation of its cap-and-trade system under the Western Climate Initiative. The regulation, which will apply to industrial facilities emitting 25,000 or more tonnes of carbon dioxide equivalent per year, will be adopted following a 60 day consultation period. Québec has indicated that its cap-and-trade system will come into force on January 1, 2013. This regulation is not expected to have a material effect on our existing operations.

ACCOUNTING POLICIES AND INTERNAL CONTROL

Significant Changes in Accounting Standards

The notes to the unaudited interim consolidated financial statements as at and for the three-month period ended March 31, 2011 contain a summary of the critical accounting policies used in preparation of the unaudited interim consolidated financial statements. On January 1, 2011, Capstone transitioned to IFRS. New significant accounting policies are disclosed in the financial statements as at June 30, 2011.

Future Accounting Changes

The Corporation's disclosure in its quarterly report for the three-month period ended March 31, 2011 has described the relevant future accounting standards expected to materially impact on Capstone future reporting, additionally significant developments to IFRS that have occurred during the second quarter are as follows:

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 10, Consolidated Financial Statements (IFRS 10), IFRS 12, Disclosure of Interests in Other Entities (IFRS 12), IAS 27, Separate Financial Statements (IAS 27), IFRS 13, Fair Value Measurement (IFRS 13) and amended IAS 28, Investments in Associates and Joint Ventures (IAS 28). Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

Accounting Estimates

The interim consolidated financial statements are prepared in accordance with IFRS, which require the use of estimates and judgment in reporting assets, liabilities, revenues, expenses and contingencies.

The following accounting estimates included in the preparation of the interim consolidated financial statements are based on significant estimates and judgments, which are summarized as follows:

Area of significant estimate	Assumptions
• Derivative financial instruments	Interest rate, natural gas price, and direct costumer rate.
• Purchase price allocations	Initial fair value of net assets
• Depreciation on capital assets	Estimated useful lives and residual value
• Amortization on intangible assets	Estimated useful lives
• Asset retirement obligations	Expected settlement date and amount and discount rate
• Income taxes	Timing of reversal of temporary differences
• Impairment assessments	Estimated future cash flows and discount rate

Management's estimates are based on historical experience, current trends and various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from those estimates.

Internal Controls

Capstone's CEO and CFO are required by the various provincial securities regulators to certify annually that they have designed, or caused to be designed, Capstone's disclosure controls and procedures, as defined in the Canadian Securities Administrators' Multilateral Instrument 52-109 ("MI 52-109"), and that they have evaluated the effectiveness of these controls and procedures in the applicable period. Disclosure controls are those controls and other procedures that are designed to provide reasonable assurance that the relevant information that Capstone is required to disclose is recorded, processed and reported within the timeframes specified by such securities regulators.

Capstone's management, under the supervision of and with the participation of the CEO and CFO, has designed internal controls over financial reporting, as defined in MI 52-109. The purpose of internal controls over financial reporting is to provide reasonable assurance regarding the reliability of Capstone's financial reporting, in accordance with GAAP, focusing in particular on controls over information contained in the audited annual and unaudited interim consolidated financial statements. The internal controls are not expected to prevent and detect all misstatements due to error or fraud.

Capstone updated its internal controls and testing for changes in its operations during the three-month period ended June 30, 2011, including the construction of Amherstburg and acquisition of Värmevärden, as well as its internal controls over financial reporting specifically with respect to the transition to IFRS.

The CEO and CFO have concluded that Capstone's disclosure controls and procedures were effective as at June 30, 2011 to ensure that information required to be disclosed in reports that Capstone files or submits under Canadian securities legislation is recorded, processed, summarized and reported within applicable time periods.

There were no changes made in Capstone's internal controls over financial reporting during the quarter ended June 30, 2011 that have materially affected, or are reasonably likely to materially affect, Capstone's internal controls over financial reporting.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

($000s)	Notes	Jun 30, 2011	Dec 31, 2010
Current assets			
Cash and cash equivalents	7	109,355	131,440
Restricted cash	7	6,148	7,575
Accounts receivable		20,521	21,696
Other assets		3,136	3,552
Current portion of loans receivable		933	884
Current portion of derivative contract assets	8	1,251	1,918
		141,344	167,065
Non-current assets			
Loans receivable	9	88,912	5,221
Derivative contract assets	8	5,933	6,579
Equity accounted investments	9	73,997	54,789
Capital assets	10	483,652	408,623
Intangible assets	11	132,933	137,646
Deferred income tax assets		15,884	24,211
Total assets		942,655	804,134
Current liabilities			
Accounts payable and other liabilities		68,360	28,896
Current portion of derivative contract liabilities	8	3,079	2,505
Loans payable	9	58,098	49,200
Current portion of finance lease obligations		124	120
Current portion of long-term debt	13	93,722	44,838
		223,383	125,559
Long-term liabilities			
Derivative contract liabilities	8	14,814	14,801
Deferred income tax liabilities		64,643	105,251
Electricity supply and gas purchase contracts	11	5,716	6,524
Finance lease obligations		65	129
Long-term debt	13	251,738	284,608
Liability for asset retirement obligation		2,301	3,167
Total liabilities		562,660	540,039
Shareholders' equity (1)	14	379,995	264,095
Total liabilities and shareholders' equity (1)		942,655	804,134
Commitments and contingencies	19		

(1) 2010 is unitholders' equity
See accompanying notes to consolidated financial statements

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

($000s)	Notes	Share capital	Preferred shares	Class B Units	Convertible debentures	Accumulated Other Comprehensive Income	Retained Earnings	Total
Balance, January 1, 2010		466,662	-	-	-	190	(256,753)	210,099
Units redeemed	14a	(23)	-	-	-	-	-	(23)
Equity share of other comprehensive income (loss) of Leisureworld		-	-	-	-	(190)	-	(190)
Net income during the period		-	-	-	-	-	25,394	25,394
Distributions declared	14d	-	-	-	-	-	(15,399)	(15,399)
Balance, June 30, 2010		466,639	-	-	-	-	(246,758)	219,881
Units issued	14a	65,249	-	-	-	-	-	65,249
Conversions of debentures, net of costs	13d	4,390	-	-	-	-	-	4,390
Net loss during the period		-	-	-	-	-	(9,493)	(9,493)
Distributions declared	14d	-	-	-	-	-	(15,932)	(15,932)
Balance, Dec. 31, 2010		536,278	-	-	-	-	(272,183)	264,095
Shares issued	14a	6,898	73,016	-	-	-	-	79,914
Reclassification of class B exchangeable units	5a	-	-	26,710	-	-	-	26,710
Reclassification of convertible debentures – conversion option	13d	-	-	-	11,554	-	-	11,554
Debenture conversions, net of costs	13d	11,800	-	-	(2,266)	-	-	9,534
Equity share of other comprehensive income (loss) of Värmevärden	9a	-	-	-	-	(133)	-	(133)
Net income for the period		-	-	-	-	-	8,553	8,553
Dividends declared	14d	-	-	-	-	-	(20,232)	(20,232)
Balance, June 30, 2011		554,976	73,016	26,710	9,288	(133)	(283,862)	379,995

See accompanying notes to these consolidated financial statements

CONSOLIDATED STATEMENTS OF INCOME

($000s, except per share amounts)	Notes	Three months ended Jun 30, 2011	Three months ended Jun 30, 2010	Six months ended Jun 30, 2011	Six months ended Jun 30, 2010
Revenue		37,028	35,497	83,943	79,649
Costs and expenses					
Operating expenses		23,876	23,033	48,036	46,369
Administrative expenses		21,615	3,453	26,934	6,672
Depreciation of capital assets	10	5,946	6,027	11,895	12,324
Amortization of intangible assets	11	1,962	1,944	3,905	3,882
		53,399	34,457	90,770	69,247
		(16,371)	1,040	(6,827)	10,402
Other income and expenses					
Interest income		1,893	209	2,326	382
Interest expense		(5,004)	(5,315)	(10,111)	(10,579)
Equity accounted income (loss)	9	(3,884)	(317)	(6,285)	3,151
Amherstburg gain on acquisition		-	4,234	-	4,234
Unrealized loss on derivative financial instruments		(4,489)	(5,516)	(2,610)	(9,561)
Unrealized (gain) loss on Class B exchangeable unit liability		-	845	-	(2,729)
Unrealized (gain) loss on convertible debentures - conversion option		-	160	-	(1,737)
Foreign exchange loss		(627)	(9)	(633)	(4)
Loss before income taxes		(28,482)	(4,669)	(24,140)	(6,441)
Income tax recovery (expense)	12				
Current		(8)	(8)	(8)	(8)
Deferred		(4,289)	2,438	32,701	31,843
Total income tax recovery		(4,297)	2,430	32,693	31,835
Net income (loss)		(32,779)	(2,239)	8,553	25,394
Earnings per share [1]					
Basic		(0.531)	(0.048)	0.140	0.544
Diluted		(0.531)	(0.048)	0.140	0.513
Basic weighted average number of shares including Class B exchangeable units outstanding (2010 – excluding Class B exchangeable units)		61,759	46,663	61,058	46,664
Diluted weighted average number of shares		61,759	46,663	61,058	54,878

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

($000s)	Notes	Three months ended Jun 30, 2011	Three months ended Jun 30, 2010	Six months ended Jun 30, 2011	Six months ended Jun 30, 2010
Net income (loss)		(32,779)	(2,239)	8,553	25,394
Equity share of other comprehensive loss of equity accounted investments		(133)	-	(133)	(190)
Total comprehensive income (loss)		(32,912)	(2,239)	8,420	25,204

[1] 2010 is earnings per unit
See accompanying notes to these consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

		Six months ended	
($000s)	Notes	Jun 30, 2011	Jun 30, 2010
Operating activities:			
Net income		8,553	25,394
Depreciation and amortization		15,800	16,206
Equity accounted (income) loss		6,285	(3,151)
Unrealized loss on derivative investments		2,610	9,561
Deferred income tax recovery		(32,701)	(31,843)
Amortization of deferred financing costs		1,345	991
Non-cash financing costs		919	797
Amherstburg gain on acquisition		-	(4,234)
Loss on disposal of capital assets		90	-
Unrealized loss on Class B exchangeable unit liability		-	2,729
Unrealized loss on convertible debentures			1,737
Change in non-cash working capital	17	2,863	3,050
Total cash flows from operating activities		5,764	21,237
Investing activities:			
Loan to equity accounted investments	9	(84,170)	-
Investment in capital assets	10	(49,070)	(2,027)
Investment in equity accounted investments	9	(25,626)	-
Purchase of foreign exchange options		(710)	-
Receipt of loans receivable		430	386
Change in restricted cash		661	(6,304)
Transaction costs		-	(817)
Distributions received from equity accounted investments		-	2,131
Total cash flows from (used in) investing activities		(158,485)	(6,631)
Financing activities:			
Proceeds from long-term debt		65,200	-
Proceeds from loans payable		8,898	-
Proceeds from issuance of common and preferred shares, net of costs		79,248	49,200
Financing fees paid on debt issuance		(839)	(1,710)
Repayment of long-term debt and finance lease obligations		(1,639)	(990)
Dividends paid		(20,232)	(17,022)
Repayment of convertible debentures		-	(31,418)
Redemption of units		-	(23)
Total cash flows from (used in) financing activities		130,636	(1,963)
Increase/(decrease) in cash and cash equivalents		(22,085)	12,643
Cash and cash equivalents, beginning of period		131,440	53,121
Cash and cash equivalents, end of period		109,355	65,764
Supplemental information:			
Interest paid		7,860	7,789
Taxes paid		8	8

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. CORPORATE INFORMATION

Capstone is incorporated and domiciled in Canada and principally located at 181 Bay Street, Suite 3100, Toronto, Ontario, M5J 2T3. The mission of Capstone Infrastructure Corporation (formerly Macquarie Power and Infrastructure Corporation and Macquarie Power & Infrastructure Income Fund (the "Fund")) and its subsidiaries (together the "Corporation" or "Capstone") is to build and responsibly manage a high quality portfolio of infrastructure businesses in Canada and internationally in order to deliver a superior total return to our investors through stable dividends and capital appreciation. Capstone's portfolio includes investments in gas cogeneration, wind, hydro, biomass and solar power generating facilities, representing approximately 370 MW of installed capacity, and a 33.3% interest in a district heating business in Sweden that was acquired on March 31, 2011.

On January 1, 2011, Capstone converted into a corporation following a plan of arrangement whereby each unit of the Fund was automatically exchanged for one common share of the Corporation.

All amounts are in Canadian thousands of dollars or thousands of share amounts unless otherwise indicated.

2. BASIS OF PREPARATION AND ADOPTION OF IFRS

The Corporation prepares its financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in The Canadian Institute of Chartered Accountants Handbook ("CICA Handbook"). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards ("IFRS"), and to require publicly accountable enterprises to apply IFRS for years beginning on or after January 1, 2011. Consequently, the Corporation has commenced using IFRS in these consolidated financial statements. The term Canadian GAAP is used in these consolidated financial statements to refer to the GAAP applied prior to the adoption of IFRS.

Statement of Compliance

The condensed consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including International Accounting Standard ("IAS") 34 Interim Financial Reporting ("IAS 34") and IFRS 1 – First-time Adoption of IFRS ("IFRS 1") in initial application of IFRS as described in note 5 to these interim consolidated financial statements. Subject to certain transition elections disclosed in note 5, the Corporation has consistently applied the same accounting policies in its opening IFRS statement of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 5 discloses the impact of the transition to IFRS on the Corporation's reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Corporation's consolidated financial statements for the year ended December 31, 2010.

The policies applied in these interim condensed consolidated financial statements are based on IFRS issued and in effect as at August 12, 2011, the date that the Board of Directors approved the financial statements. Any subsequent changes to IFRS that are given effect in the Corporation's annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these interim consolidated financial statements, including transitional adjustments recognized on change-over to IFRS.

3. SEASONALITY

The seasonality of wind speed, density of water flows and pricing provisions within the power purchase agreements ("PPA") with the Ontario Electricity Financial Corporation ("OEFC") may result in fluctuations in revenue and net income (loss) during the period. The Corporation maintains reserve accounts and free cash in order to offset the seasonality and other factors that may impact electricity production.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These unaudited interim condensed consolidated financial statements should be read in conjunction with the audited Canadian GAAP consolidated financial statements for the year ended December 31, 2010, and Capstone's interim financial statements for the quarter ended March 31, 2011, which are prepared in accordance with IFRS applicable to interim financial statements and disclose Capstone's significant accounting policies. Except as disclosed below there have been no material changes to Capstone's accounting policies:

Long-term incentive plan

In the second quarter of 2011, Capstone implemented a long-term incentive plan ("LTIP") as described in Note 15 (b). The Corporation accounts for its grants under this plan in accordance with IFRS 2 Share-Based Payments. Compensation expense is measured at the grant date at fair value and recognized over the service period, based on the vesting period applicable and is adjusted for any changes in market value of the Corporation's share price.

Preferred shares

The Corporation classifies its preferred shares as equity for reporting purposes given that the preference shares may be convertible into a fixed number of the Corporation's own equity instruments and there is no settlement required at a future date. Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity.

Future Accounting Changes

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 10, Consolidated Financial Statements (IFRS 10), IFRS 12, Disclosure of Interests in Other Entities (IFRS 12), IAS 27, Separate Financial Statements (IAS 27), IFRS 13, Fair Value Measurement (IFRS 13) and amended IAS 28, Investments in Associates and Joint Ventures (IAS 28). Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

5. TRANSITION TO IFRS

The effect of the Corporation's transition to IFRS, described in note 2, is summarized in this note as follows.

(A) Reconciliation of Shareholders' Equity and Comprehensive Income as Previously Reported under Canadian GAAP to IFRS

Shareholders' Equity ($000s)	Notes	Dec 31, 2010	Jun 30, 2010
As reported under Canadian GAAP		340,594	292,054
IFRS adjustments			
Major maintenance and componentization	i	(1,626)	(686)
Capitalized transaction costs	ii	(933)	(268)
Class B exchangeable units	iii	(26,710)	(22,583)
Equity portion of convertible debentures	iv	(12,640)	(11,587)
Deferred income tax – rate adjustment	v	(34,809)	(37,395)
Deferred income tax – other adjustments	vi	219	346
As reported under IFRS		264,095	219,881

Comprehensive Income ($000s)	Notes	Dec 31, 2010	Three months ended Jun 30, 2010	Six months ended Jun 30, 2010
Net income (loss)- under Canadian GAAP		11,569	(6,016)	14,996
IFRS adjustments				
Major maintenance and componentization	i	(1,792)	(588)	(852)
Capitalized transaction costs	ii	2,142	2,822	2,807
Class B exchangeable units	iii	(9,001)	309	(3,801)
Equity portion of convertible debentures	iv	(3,459)	160	(1,737)
Deferred income tax – rate adjustment	v	16,591	1,073	14,004
Deferred income tax – other adjustment	vi	(149)	1	(23)
Net income (loss)- under IFRS		15,901	(2,239)	25,394
Other comprehensive loss – under Canadian GAAP and IFRS		(190)	-	(190)
Comprehensive income - under IFRS		15,711	(2,239)	25,204

Explanatory notes

i. Major maintenance and componentization

IFRS requires an entity to separately track components of capital assets that have shorter useful lives than the whole category of assets. Under Canadian GAAP, Capstone historically expensed major maintenance and inspection costs as they were incurred. Under IFRS, these costs must be capitalized and amortized separately over the period until the next major maintenance.

The effect of this change is a $1,626 decrease in shareholders' equity as at December 31, 2010 (June 30, 2010 – $686 decrease) and a $1,792 decrease in net income (loss) before tax for the year ended December 31, 2010 ($588 and $852 decrease, respectively, for the three and six months ended June 30, 2010).

ii. Capitalized transaction costs

Under IFRS, transaction costs for a business combination must be expensed as incurred. Only certain transaction costs directly related to the issuance of debt or equity are eligible to be capitalized. While business combinations before 2010 are exempt from restatement under the IFRS 1 elections, the June 2010 acquisition of the Amherstburg Solar Park, along with other deferred business development costs have been restated to exclude the transaction costs from the purchase price.

The effect of these changes is a $933 decrease in shareholders' equity as at December 31, 2010 (June 30, 2010 - $268 decrease) and an increase in net income (loss) before tax for the year ended December 31, 2010 of $2,142 ($2,822 and $2,807 increase, respectively, for the three and six months ended June 30, 2010).

Additionally in accordance with IFRS 3R, the acquisition of the Amherstburg Solar Park from SunPower has been capitalized, resulting in a gain at the time of acquisition in June 2010. The effect of this change was a $6,144 increase in intangibles ($4,234, net of the increase related to the deferred tax liability), $1,910 increase in the deferred tax liability and a $4,234 increase in net income. The Corporation released $831 of deferred tax liability for the six months ended June 30, 2010, to reflect the use of the general corporate rate as described further in note 5(a)(v).

iii. Class B exchangeable units

Until the end of 2010, the Corporation was organized as a mutual fund trust. Under this structure, IFRS requires that the Class B exchangeable units be treated as a liability and recorded at fair value with distributions to unitholders treated as interest expense and movements in the fair value reported on the consolidated statement of income. Under Canadian GAAP, the Class B exchangeable units were treated as equity, recorded at historical cost, with the distributions being recorded in equity.

On January 1, 2011, the Trust completed its plan of arrangement and became a corporation. Under IFRS, this change required reclassification of the Class B exchangeable units as equity. This requirement is based on the Class B exchangeable units feature to convert into the share capital and their terms allow them to participate on an equal basis with the corporate shareholders in all financial respects in the earnings of the corporation. The value of the Class B exchangeable units on January 1, 2011 is equal to their carrying value on December 31, 2010 which is the same as their fair value on December 31, 2010. The carrying value of the Class B exchangeable units remain unchanged while they are classified as equity and all future distributions will be recorded in equity.

Additionally, $2,144 of distributions to unitholders were treated as interest expense for the year ended December 31, 2010. ($536 and $1,072, respectively, for the three and six months ended June 30, 2010).

The effect of these changes is a $26,710 decrease in shareholders' equity as at December 31, 2010 (June 30, 2010 - $22,583 decrease) and a $9,001 decrease in net income (loss) before tax for the year ended December 31, 2010 (increase of $309 and decrease of $3,801, respectively, for the three and six months ended June 30, 2010).

iv. Equity portion of convertible debentures

The convertible debentures give the holders the right to convert into shares of the Corporation (prior to January 1, 2011 into trust units of the Fund). In accordance with IAS 32 and IAS 39 the instrument is to be separated into its financial component parts on inception, similar to Canadian GAAP.

Under IFRS, the Corporation is required to account for the conversion option as a liability prior to converting to a corporation, as the debentures were convertible into trust units, which have a limited life, and therefore the instrument must be measured as held for trading and accounted for at fair value with the change recorded in the consolidated statement of income. In 2011 the conversion option is transferred to equity as it is convertible to shares of a corporation. The value of the conversion option on January 1, 2011 is equal to its carrying value on December 31, 2010 which is the same as its fair value of $12,640 on December 31, 2010. As there was a change from a trust to a corporate structure, a deferred tax liability of $1,086 was recorded and offset to shareholders' equity. The carrying value of the conversion option will remain unchanged, aside from conversions.

The effect of these changes is a $12,640 decrease in shareholders' equity as at December 31, 2010 (June 30, 2010 - $11,587 decrease) and a $3,459 decrease in net income (loss) before tax for the year ended December 31, 2010 ($160 increase and $1,737 decrease, respectively, for the three and six months ended June 30, 2010).

v. Deferred income taxes – rate adjustment

Prior to January 1, 2011, Capstone qualified as a mutual fund trust for income tax purposes. As a mutual fund trust, Capstone was entitled to deduct distributions to unitholders from taxable income for the determination of taxes payable. As Capstone distributed all of its taxable income, minimal current income taxes were payable.

Under IFRS, mutual fund trusts are required to use the “undistributed” rate in the determination of income tax amounts for financial reporting. Consequently a mutual fund trust must use the applicable income tax rate assuming that no distributions are made to offset taxable income. As a result, mutual fund trusts are required to use the highest marginal personal income tax rate of 46% in the calculation of future income taxes. Capstone has applied this rate to the 2010 comparative financial statements.

The impact to Capstone is a $51,401 increase in deferred income tax liability in the January 1, 2010 opening IFRS consolidated statement of financial position to reflect the rate differential between the highest marginal personal income tax rate of 46% and the SIFT income tax rate of 25%. Under IFRS, this calculation will be applied to timing differences arising in 2010. On December 31, 2010, a $34,809 increase to the deferred income tax liability was recorded (June 30, 2010 - $37,395 increase).

In 2011, the calculation of deferred income taxes has been affected by Capstone’s conversion to a corporation on January 1, 2011. Under IFRS, the deferred income tax calculation will be based on the appropriate corporate tax rate. The impact to Capstone was a reversal of the rate change adjustment described above, resulting in a one-time deferred income tax recovery, which was a $36,990 increase in Capstone’s 2011 first quarter net income.

vi. Deferred income taxes – other adjustments

Deferred income tax assets and liabilities have been adjusted to give effect to IFRS adjustments as follows:

($000s)	Notes	Dec 31, 2010	Jun 30, 2010
Major maintenance	i	274	401
Capitalized transaction costs	ii	(55)	(55)
Total		219	346

The adjustments increased (decreased) deferred income tax expense recognized in both the consolidated statements of income and consolidated statements of comprehensive income as follows:

($000s)	Notes	Dec 31, 2010	Three months ended Jun 30, 2010	Six months ended Jun 30, 2010
Major maintenance	i	(149)	1	(23)

vii. Accretion of asset retirement obligations

Under Canadian GAAP, accretion was being included as part of operating and maintenance expenses while under IFRS it is required to be classified as a financing expense. Accretion expense of $179 for the year ended December 31, 2010 ($44 and $88 for the three and six months ended June 30, 2010 respectively) has been reclassified as a finance cost with other interest expense. This change does not affect net income (loss) for the year ended December 31, 2010 or the three and six months ended June 30, 2010.

(B) Presentation of Cash Flows

The presentation of the consolidated statement of cash flows under IFRS differs from the presentation of the consolidated statement of cash flows under Canadian GAAP. The changes made to the consolidated statements of financial position and comprehensive income resulted in reclassifications of various amounts on the consolidated statements of cash flows. The consolidated statements of cash flows were adjusted as follows:

	Six months ended Jun 30, 2010			
($000s)	Transaction costs	Major maintenance and componentization	Class B exchangeable units	Total
Operating activities	1,427	(1,005)	1,072	1,495
Investing activities	(1,427)	1,005	-	(423)
Financing activities		-	(1,072)	(1,072)
	-	-	-	-

6. ACQUISITIONS

On March 31, 2011, the Corporation acquired a 33.3% indirect interest in a portfolio of district heating operations from subsidiaries of Fortum Corporation (collectively, “Fortum”) located in Sweden, which is named Värmevärden, for approximately $108,954 (or 710,000 Swedish Krona (“SEK”)). The remaining 66.7% interest in Värmevärden was acquired by Macquarie European Infrastructure Fund II (“MEIF II”), a private unlisted infrastructure fund managed by a subsidiary of MGL.

The fair value of the investment in Värmevärden as at the date of acquisition is preliminary and may be adjusted as a result of obtaining additional valuation and legal clarifications along with closing adjustments. Transaction costs of $2,414 (or 15,667 SEK) were expensed in the consolidated statement of income as part of the equity accounted income of Värmevärden, as the entity paid the amounts to acquire the collective assets from Fortum.

During the second quarter, Värmevärden loaned a Capstone subsidiary $3,432 (22,500 SEK) as disclosed in note 9. The loan is intended to be settled with Capstone’s investment in share capital of Värmevärden during 2011.

7. CASH AND CASH EQUIVALENTS AND RESTRICTED CASH

($000s)	Jun 30, 2011	Dec 31, 2010
Cash backed letter of credit	-	4,011
Funds in deposit	500	500
Cash in escrow related to legacy obligations	-	760
Debt service reserve	5,648	2,304
Restricted cash	6,148	7,575
Unrestricted cash and cash equivalents	109,355	131,440
	115,503	139,015

The debt service reserve represents segregated cash under the terms of the project debt agreement for Erie Shores Wind Farm LP (“Erie Shores”). Under the agreement, as of April 1, 2011, Erie Shores is required to hold restricted cash equal to the principal and interest payments for the next six months of the term facilities. See note 13 for further detail.

8. DERIVATIVE FINANCIAL INSTRUMENTS

The Corporation uses gas and interest rate swap contracts to hedge the risk of gas price and interest rate volatility as well as foreign currency options to hedge currency volatility. Capstone has also separately valued embedded derivatives at their fair value on the statement of financial position and recognizes the change in fair value in the consolidated statements of income.

The fair values of the Corporation's derivative financial instruments are as follows:

($000s)	Jun 30, 2011	Dec 31, 2010
Current derivative contract assets		
Gas swap contracts	1,209	1,918
Foreign currency contracts	42	-
	1,251	1,918
Non-current derivative contract assets		
Gas swap contracts	-	-
Foreign currency contracts	819	-
Interest rate swap contracts	1,508	1,292
Embedded derivatives	3,606	5,287
	5,933	6,579
	7,184	8,497
Current derivative contract liabilities		
Interest rate swap contracts	3,079	2,505
Non-current derivative contract liabilities		
Interest rate swap contracts	5,760	5,897
Embedded derivatives	9,054	8,904
	14,814	14,801
	17,893	17,306

9. EQUITY ACCOUNTED INVESTMENTS

(A) Equity Accounted Investments

	Jun 30, 2011		Dec 31, 2010	
($000s)	Ownership %	Carrying value	Ownership %	Carrying value
MLTCLP	45.0%	54,562	45.0%	54,789
Värmevärden	33.3%	19,435	Nil	-
Chapais	31.3%	-	31.3%	-
	N/A	73,997	N/A	54,789

Capstone has loans receivable of $88,912, of which $4,742 is receivable from Chapais and $84,170 is receivable from Värmevärden (December 31, 2010 - $5,221 was due from Chapais).

The $84,170 (551,808 SEK) loan receivable from Värmevärden matures in 10 years. Interest accrues at 7.965% per annum and is due semi-annually on June 30 and December 31. Repayments of principal will be in SEK and may be made in part or in full, on such date or dates as agreed between Värmevärden, Capstone and MEIF II from time to time. The loan receivable is denominated in SEK and accordingly is re-measured at each reporting date. The change is recorded in the consolidated statement of income as part of unrealized foreign exchange. A one per cent increase or decrease in the SEK to Canadian exchange rate has an approximately $841 decrease or increase on net income.

The change in the Corporation's equity accounted investments for the six-month period ended June 30, 2011 and the year ended December 31, 2010 are as follows:

($000s)	Jun 30, 2011	Dec 31, 2010
Opening balance	54,789	54,186
Equity accounted income (loss)	(6,285)	3,332
Equity share of other comprehensive gain (loss)	(133)	(190)
Dividends / distributions received	-	(2,541)
Other	-	2
Acquisitions	25,626	-
Ending balance	73,997	54,789
Loans payable	(58,098)	(49,200)
Net investment	15,899	5,589

The loans payable of $58,098, include principal outstanding of $54,666 with MLTCLP and $3,432 (22,500 SEK) with Värmevärden as at June 30, 2011 (December 31, 2010 - $49,200 was due to MLTCLP). Both loans payable are non-interest bearing and payable on demand.

(B) Summarized Information for Equity Accounted Investments

The Corporation has summarized the information of its equity accounted investments at their gross values as follows:

	Jun 30, 2011		Dec 31, 2010	
($000s)	Assets	Liabilities	Assets	Liabilities
MLTCLP	121,782	-	121,754	-
Värmevärden	413,037	346,047	-	-
Chapais	29,395	47,388	27,888	48,612

	Three months ended Jun 30, 2011			Three months ended Jun 30, 2010		
($000s)	Revenue	Income	Capstone's Income	Revenue	Income	Capstone's Income
MLTCLP	-	-	-	-	(705)	(317)
Värmevärden	22,276	(11,647)	(3,884)	-	-	-
Chapais	3,390	(616)	-	3,499	(674)	-
	25,666	(12,263)	(3,884)	3,499	(1,379)	(317)

	Six months ended Jun 30, 2011			Six months ended Jun 30, 2010		
($000s)	Revenue	Income	Capstone's Income	Revenue	Income	Capstone's Income
MLTCLP	-	29,833	13	-	7,002	3,151
Värmevärden	22,276	(18,917)	(6,298)	-	-	-
Chapais	13,121	3,900	-	12,894	3,579	-
	35,397	14,816	(6,285)	12,894	10,581	3,151

10. CAPITAL ASSETS

($000s)	Jan 1, 2011	Additions	Disposals	Transfers	Jun 30, 2011
Cost					
Land	235	-	-	-	235
Equipment and vehicles	4,375	88	(46)	-	4,417
Property and plant	469,665	1,635	(197)	119,826	590,929
Construction in progress	34,535	85,291	-	(119,826)	-
	508,810	87,014	(243)	-	595,581
Accumulated depreciation					
Equipment and vehicles	(3,000)	(171)	45	-	(3,126)
Property and plant	(97,187)	(11,724)	108	-	(108,803)
Net carrying value	408,623	75,119	(90)	-	483,652

Included in equipment and vehicles are assets under finance leases having a net carrying value of $93 for the quarter ended ($161 - for the year ended December 31, 2010).

As Amherstburg is available for use, the construction in progress assets were transferred to property, plant and equipment and are amortized over their useful lives. Of the additions, $49,333 was accrued at quarter end ($10,427 for the year ended 2010).

Total additions were $87,014, made up of $49,070 of cash additions during 2011 and non-cash adjustments. ($35,852 for the year ended December 31, 2010) Non-cash adjustments include $49,333 Amherstburg accruals for 2011 less $10,427 related to 2010 Amherstburg accruals paid during 2011 and minus the asset retirement obligation adjustment of $962 during the six months ended June 30, 2011.

11. INTANGIBLES

($000s)	Jan 1, 2011	Additions	Disposals	Impairment	Jun 30, 2011
Assets					
Computer software	56	-	-	-	56
Electricity supply and gas purchase contract	108,048	-	-	-	108,048
Water rights	73,018	-	-	-	73,018
Amortization	(43,476)	(4,713)	-	-	(48,189)
	137,646	(4,713)	-	-	132,933
Provisions					
Electricity supply and gas purchase contracts	12,257	-	-	-	12,257
Utilization	(5,733)	(808)	-	-	(6,541)
	6,524	(808)	-	-	5,716

12. INCOME TAXES

Following the change in the tax status of the Corporation, the deferred income tax assets and liabilities have been recalculated. The adjustments are included in the statement of income for the period, except for the adjustments related to the convertible debentures which were recorded as part of equity on conversion to a corporation. As a result, equity decreased by $1,086 and a deferred income tax recovery of $34,808 was recognized.

The Corporation became a taxable corporation on January 1, 2011, pursuant to the reorganization of the Fund. The reconciliation of the income tax expense for the quarter and six-month period ended June 30, 2010 is not comparable to the current quarter since the majority of its earnings prior to 2011 were not subject to income taxes under the Fund's structure. As a result, the comparative figures are not disclosed.

The reconciliation of the difference between the income tax expense using the statutory tax rate and the effective tax rate is as follows:

($000s)	Six months ended Jun 30, 2011
Loss before income taxes	(24,140)
Statutory income tax rate	27.8%
Income tax expense based on statutory income tax rate	(6,711)
Permanent Differences	1,922
Loss of tax attributes as a result of SIFT reorganization	4,140
Unrecognized non-capital losses accrued within CIC	3,526
Change in tax status	(34,808)
Other	(762)
Total income tax recovery	(32,693)
Effective income tax rate	135.4%

13. LONG-TERM DEBT

(A) Components of Long-term Debt

($000s)	Maturity	Interest Rates	Jun 30, 2011	Dec 31, 2010
CPC – Cardinal credit facility	June 29, 2012	4.34%	85,000	85,000
Erie Shores project debt – Tranche A	April 1, 2026	5.96%	61,003	62,248
Erie Shores project debt – Tranche B	April 1, 2016	5.28%	4,433	4,815
Erie Shores project debt – Tranche C	April 1, 2026	6.15%	40,000	40,000
Amherstburg Solar Park project debt	June 30, 2016	7.32%	96,200	31,000
Convertible debentures	December 31, 2016	6.50%	39,706	48,875
Convertible debentures – conversion option	December 31, 2016		-	12,640
Class B exchangeable units	n/a		-	26,710
Levelization liability	June 30, 2032	6.94%	24,584	23,714
			350,926	335,002
Less: Deferred financing costs			(5,466)	(5,556)
			345,460	329,446
Current portion of long-term debt				
Erie Shores project debt			5,079	43,302
Amherstburg Solar Park project debt			3,643	1,536
CPC – Cardinal debt			85,000	-
			93,722	44,838
Long-term debt			251,738	284,608

(B) Erie Shores Wind Farm

On April 1, 2011, Capstone completed the refinancing of Tranche C of Erie Shores' non-recourse, project financing loan. Under the refinancing, the Erie Shores' Tranche C loan was replaced with a fully amortizing term loan in the amount of $40,000, with a fixed rate of interest at 6.145% which matures on April 1, 2026. Transaction costs of $889 have been capitalized.

Under the agreement, the next six months of principal and interest payments must be funded in a debt service reserve account. As a result, $5,648 has been recorded as restricted cash on the consolidated statement of financial position. Additionally, CPC has an unsecured guarantee of $5,000.

(C) Amherstburg Solar Park

Under the terms of the credit agreement, there is a project construction facility and a term facility. During the project development, Amherstburg made draws under the construction facility to finance work as it was completed on the project.

In July 2011, upon completion of construction, the outstanding balance of the construction facility was converted into a term facility, which requires regular principal and interest payments, amortized over 17 years, with a five-year maturity. The effective interest rate of the debt is 7.32%. Amherstburg has entered into a swap to convert its floating interest rate obligations under the credit agreement to a fixed rate. The financing and the swap were arranged by Amherstburg and are secured only by the assets of Amherstburg.

(D) Convertible Debentures

The carrying values of the liability and the equity components of the debentures are as follows:

($000s)	Jun 30, 2011	Dec 31, 2010
Liability component	48,875	51,749
Conversion to shares, net of costs (1)	(9,532)	(3,721)
Amortization and accretion	363	847
	39,706	48,875
Deferred financing costs	(2,518)	(2,518)
	37,188	46,357
Convertible debentures – conversion option	-	12,640
	37,188	58,997
Equity component (2)	11,554	-
Conversion to shares (1), net of costs	(2,266)	-
	9,288	-
Total carrying value	46,476	58,997

(1) $11,800 of carrying value was converted to shares of the Corporation (note 14) ($4,390 - 2010), which is net of transaction costs incurred in connection with the issuance the convertible debentures.

(2) The carrying value of the convertible debentures – conversion option was re-measured to the fair value at January 1, 2010 and December 31, 2010. On January 1, 2011, the amount is classified as equity and no longer re-measured to fair value.

(E) Long-term Debt Covenants

As at June 30, 2011, the Corporation and its subsidiaries were in compliance with all financial and non-financial long-term debt covenants.

Collateral for the CPC-Cardinal credit facility is provided by a first ranking priority security interest covering the assets of CPC, Cardinal and certain direct subsidiaries, collectively the "restricted group". As at June 30, 2011, the carrying value of the assets of the restricted group exceeded total amounts drawn on the facility.

The Erie Shores project debt is secured only by the assets of Erie Shores, with no recourse to the Corporation's other assets. As at June 30, 2011, the carrying value of the assets of Erie Shores exceeded the total amount of project debt outstanding.

14. SHAREHOLDERS' EQUITY

Effective January 1, 2011, the Fund converted from a mutual fund trust to a corporation whereby each unit of Macquarie Power & Infrastructure Income Fund was automatically exchanged for one common share of the Corporation.

(A) Shares

Capstone is authorized to issue an unlimited number of common shares.

	Three months ended Jun 30, 2011		Six months ended Jun 30, 2011		Twelve months ended Dec 31, 2010	
($000s and 000s shares)	Shares	Carrying Value	Units	Carrying Value	Units	Carrying Value
Opening balance	57,759	547,237	56,352	536,278	46,665	466,662
Shares issued (1) and (2)	856	7,000	856	6,898	9,079	65,249
Conversion of convertible debentures, net of cost (3)	87	739	1,494	11,800	611	4,390
Units redeemed	-	-	-	-	(3)	(23)
Ending balance	58,702	554,976	58,702	554,976	56,352	536,278

(1) On December 22, 2010 the Corporation closed a private placement financing (the "Offering") of 9,079,250 units at a price of $7.60 dollars per unit for gross proceeds of approximately $69,000 before issue costs of $3,751. The net proceeds of the Offering were used by the Corporation for acquisitions and for general purposes. During 2011, $102 of the private placement transaction costs were included in share capital.

(2) On April 15, 2011 the Corporation issued 856 common shares subscribed to by MGL as part of the management internalization at $8.18 dollars per share for gross proceeds of approximately $7,000.

(3) $11,800 of the convertible debentures were converted to shares of the Corporation (note 13 (d)) ($4,390 - 2010), which is net of original issuance transaction costs.

(B) Class B Exchangeable Units

LTC Holding LP had 3,249,390 Class B exchangeable units outstanding as at June 30, 2011 and December 31, 2010. Each unit is exchangeable into one share of the Corporation. The Class B exchangeable units are eligible to receive distributions under the same terms and conditions as shares of the Corporation.

The holders of the Class B exchangeable units are not permitted to acquire any additional shares of the Corporation (other than pursuant to the exchange of the Class B exchangeable units or pursuant to a distribution reinvestment plan) without the consent of the Corporation until October 18, 2020. Each Class B exchangeable unit will convert into a share of the Corporation on October 18, 2020 unless converted earlier at the option of the Class B exchangeable unitholders. The Class B exchangeable unitholders are not permitted to sell more than 5% of their aggregate outstanding shares in any four-month period and are not eligible to vote with any shares they receive on exchange of their Class B exchangeable units until they together hold 1% or less of the aggregate outstanding shares.

(C) Preferred Shares

Capstone is authorized to issue preferred shares equal to 50% of the outstanding common shares. As at June 30, 2011, there were 3,000 series A preferred shares outstanding.

The series A preferred shares have a 5% cumulative dividend which resets on each 5-year anniversary. The shares are non-voting and redeemable at the Corporation's discretion. Subsequent to the initial 5-year fixed rate period, the issuer will determine the annual dividend for the next 5-year period based on the 5-year Government of Canada Bond Yield plus 2.71%. After June 30, 2016, the series A preferred shares are convertible on a one to one basis to series B cumulative, floating rate first preferred shares at the holders option. The series B preferred shares are redeemable at the Corporation's discretion after June 20, 2021 and every 5 years thereafter at 25 dollars per share plus accrued and unpaid dividends.

(D) Dividends

Dividends to shareholders are paid monthly in arrears on the 15th day of each month or the next business day. For the quarter and six months ended June 30, 2011, dividends totaled $10,217 and $20,232, respectively (for the year ended December 31, 2010 - distributions of $31,331 to unitholders and $2,144 to holders of the Class B exchangeable units).

Dividends on the series A preferred shares are payable quarterly.

In 2010, the distributions to the Class B exchangeable unitholders were included in interest expense in the statements of income as described in note 5(a)(iii).

The Board of Directors of the Corporation reviews the level of dividends paid to shareholders on a quarterly basis.

15. Share based Compensation

(A) Deferred Share Units

Effective January 1, 2011, fixed grants equivalent to 3,750 dollars are made on the first day of each quarter to eligible directors and converted to Deferred Share Units (“DSUs”) at the five day volume weighted average price (“VWAP”) on the grant date. These grants vest immediately upon the last trading day of each quarter. In addition, directors may elect to receive their quarterly trustee fees in the form of DSUs, with the same vesting as the fixed grants. Dividend equivalents are granted as of each record date for dividends on shares in accordance with Capstone’s dividend policy on common shares. DSUs do not have an exercise price and can only be settled in cash at the time a director ceases to be a board member.

The volume weighted average fair value per DSU granted during the quarter ended June 30, 2011 was 7.99 dollars. As at June 30 the carrying value of the DSUs, based on a market price of 7.82 dollars, was $29.9 and is included in accounts payable and other liabilities in the consolidated statement of financial position. The resulting DSU expense for the second quarter was $15.1 and is recorded as compensation expense in the consolidated statement of income.

	Three months ended Jun 30, 2011		Six months ended Jun 30, 2011	
($000s, except unit amounts)	**Number of units**	**Fair Value**	**Number of units**	**Fair Value**
Outstanding at beginning of period	1,865	14.8	-	-
Fixed quarterly grants during the period	1,880	14.9	3,720	30.1
Dividend equivalents	78	0.6	103	0.8
	3,823	30.3	3,823	30.9
Unrealized gain (loss) on revaluation	-	(0.4)	-	(1.0)
	3,823	29.9	3,823	29.9

(B) Long-Term Incentive Plan

On June 17, 2011, 67,056 Restricted Stock Units (“RSUs”) and 67,056 Performance Share Units (“PSUs”) were granted at the five day VWAP to the senior management of the Corporation. These grants cliff vest on December 31, 2013. Dividend equivalents are granted as of each record date for dividends on shares in accordance with Capstone’s dividend policy on common shares. RSUs and PSUs do not have an exercise price and can be settled in shares or cash at the Board’s discretion. Additionally, the valuation also takes into consideration that the amount of the PSUs is subject to Capstone’s total return relative to a peer group.

The VWAP per RSU and PSU granted on June 17, 2011 was 7.87 dollars. As at June 30, the carrying value of the RSUs and PSUs, based on a market price of 7.82 dollars, was $13.8 and is included in accounts payable and other liabilities in the consolidated statement of financial position. The RSU and PSU compensation expense of $13.8 is recorded as compensation expense in the consolidated statement of income for the second quarter.

($000s, except unit amounts)	Three months ended Jun 30, 2011 Notional number of units	Three months ended Jun 30, 2011 Fair Value	Six months ended Jun 30, 2011 Notional number of units	Six months ended Jun 30, 2011 Fair Value
Grants during the period	134,112	1,062	134,112	1,062
Dividend equivalents	-	-	-	-
	134,112	1,062	134,112	1,062
Unrealized loss on revaluation	-	(14)	-	(14)
	134,112	1,048	134,112	1,048

16. RELATED PARTY TRANSACTIONS

During the quarter, Capstone mutually terminated the management and administration agreements that established the related party relationship with MGL and its subsidiaries. As such, after April 15, 2011 all transactions with MGL and its subsidiaries are not considered to be related.

All related party transactions were carried out under normal arm's length commercial terms.

(A) Transactions with MGL

Included in the table below are the related party transactions with MPML:

	Three months ended		Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Management fees (1)	13,412	330	13,821	784
Administrative fees (2)	1,021	29	1,053	58
Cost reimbursement	187	1,039	1,546	1,835
Incentive fees	-	(954)	-	-
	14,620	444	16,420	2,677

(1) Includes $13,101 paid to MGL to terminate the management and administration agreements and $220 as reimbursement for staff vacation pay.
(2) Includes $1,016 paid to MGL to terminate the administrative agreement.

In addition to the above amounts, in March 2011, due diligence and legal fees of $1,313 (8,334 SEK) were paid to a subsidiary of MGL with respect to the acquisition of Värmevärden in Sweden. This cost has been expensed in the consolidated statement of income as at June 30, 2011 as part of equity accounted income as it was incurred by the equity accounted investee.

In March 2011, $646 became payable to MEIF II for the reimbursement of due diligence costs with respect to the acquisition of Värmevärden in Sweden. These costs have been accrued in accounts payable and other liabilities and capitalized to equity accounted investments as at June 30, 2011.

In March 2011, a financial advisory fee of $500 was payable to a subsidiary of MGL with respect to the refinancing of Tranche C of the Erie Shores project debt. These costs have been accrued in accounts payable and other liabilities and capitalized to the long-term debt as at June 30, 2011.

On April 15, 2011, upon the internalization of management, Capstone and its subsidiaries paid MGL $14,117 as consideration for terminating all management and administration agreements and $220 as reimbursement for vacation payments to staff who joined Capstone. MGL immediately used $7,000 of the money it received to subscribe for Capstone common shares.

(B) Compensation of Key Management

Key management includes the Corporation's directors, Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Compensation awarded to key management consisted of salaries, directors fees and short-term employee benefits, which include fees paid to directors. Eligible directors and senior management of the Corporation also receive forms of stock-based compensation as described in note 15.

The following table summarizes key management compensation:

	Three months ended		Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010	Jun 30, 2011	Jun 30, 2010
Salaries, directors fees and short-term employee benefits	2,292	197	2,409	311
Share based compensation	23	-	38	-
	2,315	197	2,447	311

Prior to April 15, 2011, the CEO and CFO of Capstone and other employees were employed by the Manager. Accordingly, no employee compensation prior to April 15, 2011 was included directly in these consolidated financial statements.

17. SEGMENTED INFORMATION

The Corporation has two reportable segments (the Social segment pertains to comparative information when Capstone held an interest in Leisureworld) based on how management has organized the business to assess performance and for operating and capital allocation. Each reportable segment has similar economic characteristics based on the nature of the products or services, type of customers, method of distributing their products or services and regulatory environment. Management evaluates the performance of these segments primarily on revenue and operating cash flows.

	Geographical location	
Infrastructure segments consist of:	2011	2010
Power The Corporation's investments in gas cogeneration, wind, hydro, biomass power and solar power assets.	Canada	Canada
Utilities The district heating business (Värmevärden), in which the Corporation acquired a 33.3% indirect interest on March 31, 2011.	Sweden	n/a
Social For the Corporation's 45% indirect interest in Leisureworld until it was sold in March 2010 as reported in the comparative figures.	n/a	Canada

	Three months ended Jun 30, 2011				Three months ended Jun 30, 2010			
($000s)	Power	Utilities	Corporate	Total	Power	Social	Corporate	Total
Revenue	37,028	-	-	37,028	35,497	-	-	35,497
Depreciation of capital assets	5,946	-	-	5,946	6,027	-	-	6,027
Amortization of intangible assets	1,959	-	3	1,962	1,939	-	5	1,944
Interest income	181	1,692	20	1,893	162	-	47	209
Interest expense	(4,122)	-	(882)	(5,004)	(4,137)	-	(1,178)	(5,315)
Income tax recovery	-	-	(4,297)	(4,297)	117	-	2,313	2,430
Net income (loss)	(6,374)	(2,919)	(23,486)	(32,779)	(7,062)	(337)	5,160	(2,239)
Additions to capital assets	42,374	-	-	42,374	751	-	-	751

	As at Jun 30, 2011				As at Dec 31, 2010			
($000s)	Power	Utilities	Corporate	Total	Power	Social	Corporate	Total
Total assets	718,772	95,730	128,153	942,655	597,790	-	206,345	804,135

	Six months ended Jun 30, 2011				Six months ended Jun 30, 2010			
($000s)	Power	Utilities	Corporate	Total	Power	Social	Corporate	Total
Revenue	83,943	-	-	83,943	79,649	-	-	79,649
Depreciation of capital assets	11,895	-	-	11,895	12,324	-	-	12,324
Amortization of intangible assets	3,896	-	9	3,905	3,872	-	10	3,882
Interest income	402	1,692	232	2,326	330	-	52	382
Interest expense	(8,266)	-	(1,845)	(10,111)	(8,194)	-	(2,385)	(10,579)
Income tax recovery	-	-	32,693	32,693	117	-	31,718	31,835
Net income (loss)	5,286	(5,333)	8,600	8,553	(3,032)	2,902	25,524	25,394
Additions to capital assets	87,014	-	-	87,014	2,028	-	-	2,028

18. NON-CASH WORKING CAPITAL

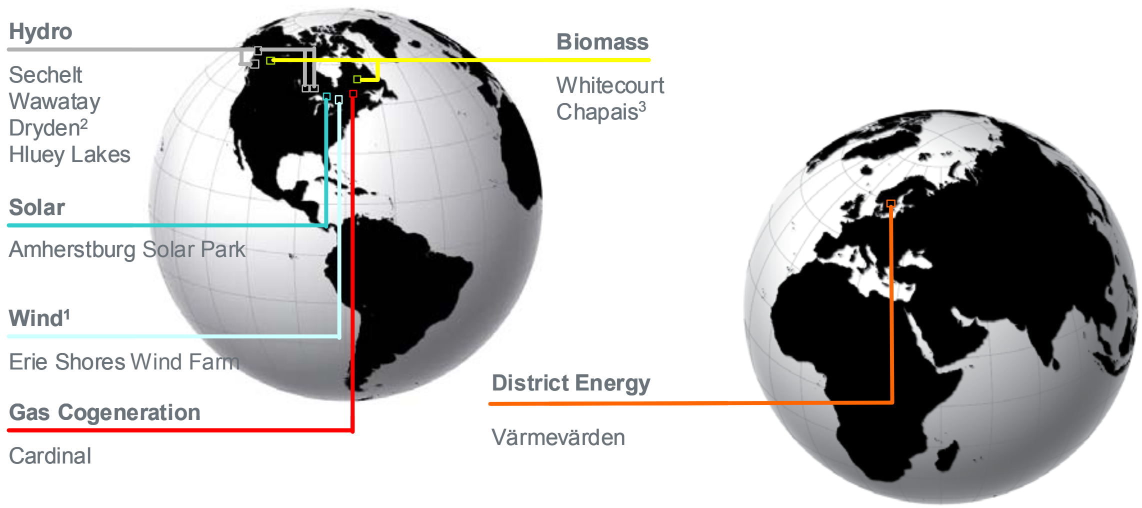
The changes in non-cash working capital is composed of the following:

	Six months ended	
($000s)	Jun 30, 2011	Jun 30, 2010
Accounts receivable	1,175	3,491
Other assets	430	3,034
Accounts payable and other liabilities	1,258	(3,475)
	2,863	3,050

19. COMMITMENTS AND CONTINGENCIES

The Corporation, either directly or indirectly through its subsidiaries, has entered into various contracts and commitments as disclosed in the annual consolidated financial statements for the year ended December 31, 2010. No material developments arose during the six-month period ended June 30, 2011.

PORTFOLIO

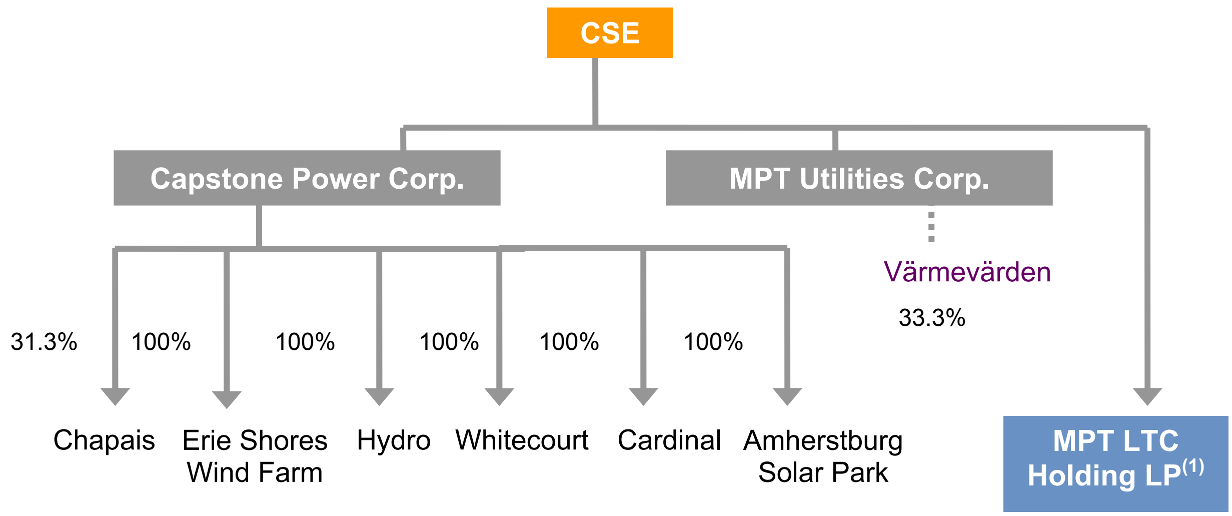


Asset	Year Built	Interest	Net Capacity (MW)	PPA Counterparty	PPA Expiry	Fuel Supply Counterparty	Fuel Supply Expiry
Cardinal	1994	100%	156	OEFC	2014	Husky	2015
Erie Shores(1)	2006	100%	99	OPA	2026	n/a	n/a
Whitecourt	1994	100%	25	TransAlta	2014	Millar Western	2016
Sechelt	1997	100%	16	BC Hydro	2017	n/a	n/a
Wawatay	1992	100%	14	OEFC	2042	n/a	n/a
Hluey Lakes	2000	100%	3	BC Hydro	2020	n/a	n/a
Dryden(2)	Various	100%	3	OEFC	2020	n/a	n/a
Amherstburg Solar Park	2011	100%	20	OPA	2031	n/a	n/a
Chapais(3)	1995	31.3%	28	Hydro-Québec	2015	Barrette/Chantiers/ Société en commandite Scierie Opitciwan	2015

Asset	Year Built	Interest	Heat Production Capacity (MWth)	Counterparties	Supply Points	Kilometres of Underground Pipes	2010 Heat Sales (terawatt hours)
Värmevärden	11 businesses and various facilities with an average age of 20 years	33.3%	786	Mix of industrial and retail customers, with industrial counterparties representing 25% of revenue	4,000	317	1.4

(1) One 1.5 MW turbine is owned by a landowner.
(2) The Dryden facility is composed of three facilities, built in 1922 (Wainwright), 1928 (Eagle) and 1938 (McKenzie). These facilities were refurbished in 1986.
(3) CSE's investment in Chapais consists of a 31.3% interest in one of two classes of preferred shares, a 24.8% interest in Tranche A and B debt, and a 50% interest in Tranche C debt.

ORGANIZATIONAL STRUCTURE



(1) MPT LTC Holding LP is the issuer of 3,249,390 Class B exchangeable units, which have economic rights equivalent to CSE common shares.

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