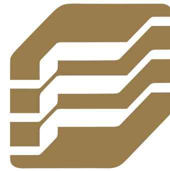
A BRIGHT FUTURE



EQUITABLE GROUP INC.

ANNUAL REPORT 2009

ON A FOUNDATION OF STRENGTH...

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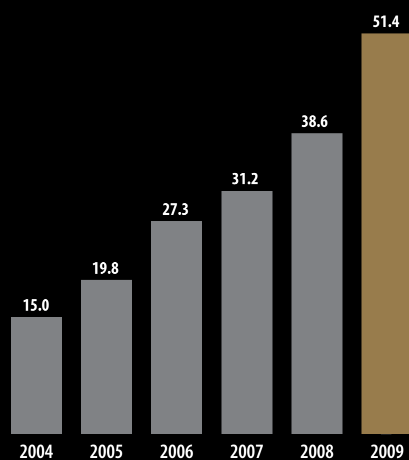
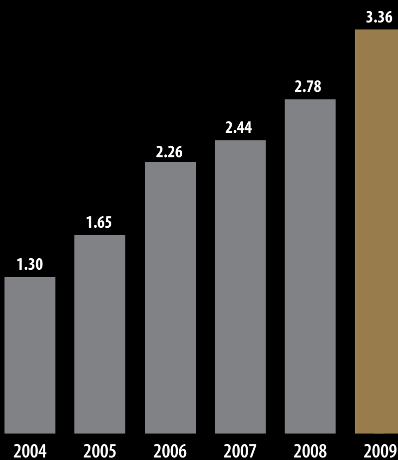
About Equitable Group Inc.

Equitable Group Inc. is a niche mortgage lender. Our core business is first charge mortgage financing, which we offer through our wholly owned subsidiary, The Equitable Trust Company. Founded in 1970, Equitable Trust is a federally incorporated trust company. Our Company serves single family, small and large commercial borrowers and their mortgage advisors. It also serves the investing public as a provider of Guaranteed Investment Certificates. Equitable provides GICs across all Canadian provinces and territories. We actively originate mortgages in Alberta, Manitoba, Ontario and Quebec. Equitable Group's common and preferred shares are traded on the Toronto Stock Exchange under the symbols ETC and ETC.PR.A. Visit the Company on line at www.equitablegroupinc.com or www.equitabletrust.com.

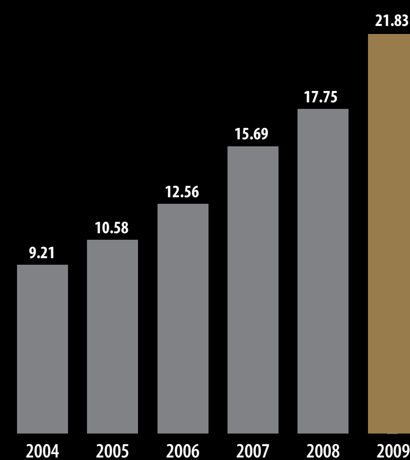
Net income ($ millions)



Earnings per share – diluted ($)



Book value per share ($)



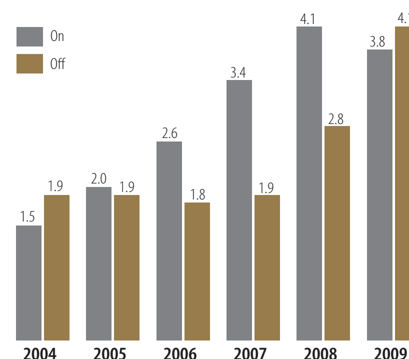
For our Shareholders

Building a bright future means...

Growing our lending business in the areas where we have the best opportunity to earn attractive and sustainable returns.

Through our three core lending businesses, Single Family Lending Services, Commercial Mortgage – Broker Services and Commercial Lending Services, Equitable has the market presence, competitive strength and capabilities to profitably add new mortgage assets to our portfolio while limiting our exposure to risk. Going forward, we are focused on long-term growth and on identifying and investing in the development of mortgage products and selected geographic markets that will enhance shareholder value.

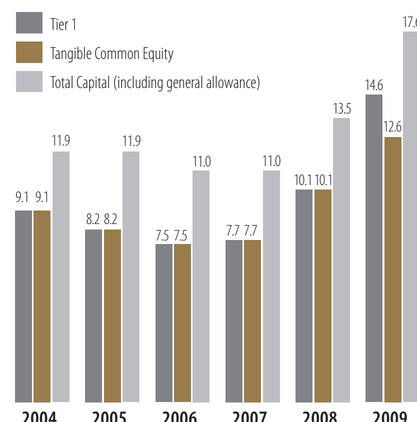
***Total on and off-balance sheet assets** ($ billions)*



Funding growth by leveraging our strong capital position.

Through earnings retention and the successful completion of a non-dilutive preferred share offering in 2009, Equitable completed the year with the strongest capital ratio in our history. Our tangible common equity ("TCE") ratio at year end was also strong, both on an absolute basis and in comparison to the ratios of Canada's largest banks. As a result, we are well positioned to take advantage of opportunity for mortgage asset growth in a favourable competitive environment – and in a recovering economy.

***Capital ratios** [(1)] (%)*

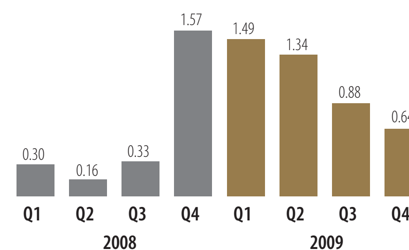


[(1)] Capital ratios for 2007 – 2009 are calculated under Basel II.

Protecting shareholder value and the integrity of our institution through focused monitoring and mitigation of business risks.

Lending institutions are exposed to a variety of risks. We seek to mitigate each one, including the key challenge – credit risk. To do this, we adjust our mortgage products, terms and credit criteria according to both market conditions and our risk-weighted return requirements. We place a strong emphasis on security evaluation and analysis of the risks in each transaction. We limit the loan to value ratios on uninsured mortgages at origination. This approach, along with effective mortgage administration and collection processes, has provided us with strong credit metrics – even during the recent economic recession – and limited our exposure to loss.

***Mortgages in arrears 90 days or more** [(1)]*
(% of total mortgage principal outstanding)

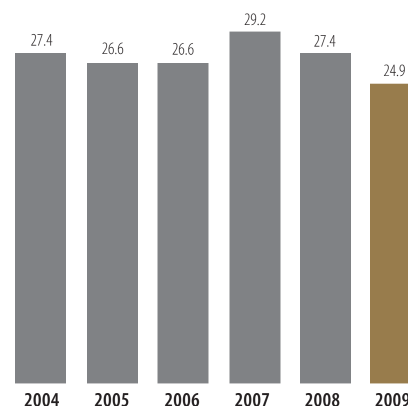


[(1)] Excludes CMHC-insured mortgages which are less than 365 days in arrears.

Continuously improving our operating efficiencies for the benefit of shareholders, customers and business partners.

Equitable operates successfully as both a niche lender and nationally regulated deposit taking member of the Canada Deposit Insurance Corporation ("CDIC") without a branch network. By maintaining valued relationships with mortgage brokers who originate mortgages and deposit agents who originate deposits, effectively managing costs and improving efficiencies, we have achieved low overheads, one of the best productivity ratios in the Canadian financial services industry and a reputation for effective service.

Productivity ratio – taxable equivalent basis[1] (%)

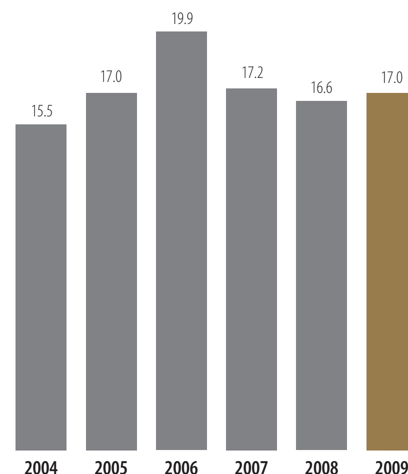


[1] Productivity ratios for 2004 – 2006 have been restated to conform to the presentation in the following years.

Optimizing return on equity ("ROE") adjusted for risk.

Each Equitable mortgage is expected to deliver a return that meets established ROE thresholds. To make this happen, we assess our pricing on a mortgage-by-mortgage basis. We have delivered average annual growth in net income of 33.0% and an average ROE of 17.2% since we became a public company in 2004 – despite significant volatility in credit, capital and real estate markets over the past two years.

Return on equity[1] (%)



[1] Return on equity is calculated based on net income available to common shareholders divided by the weighted average common equity outstanding during the year.

For our Customers & Business Partners
Building a bright future means...

Providing superior service.

Stated simply, today's markets demand more from everyone, particularly those who provide professional advice. We understand this reality and seek to provide superior service to our business partners – mortgage brokers, national mortgage banking organizations and deposit agents – so they can provide superior service to their customers. Superior service means many things, but most especially clear communications, delivered in a responsive manner. As a nimble organization, we pride ourselves on responding to opportunity quickly with decisions, rates and terms. The competitive nature of mortgage and GIC markets means we won't win every deal but by demonstrating that service is in our lifeblood, and empowering our team to serve, we intend to make Equitable Trust the first choice provider in our chosen markets.

Improving our processes.

We know how to close a deal quickly, but most of all, we know the importance of time – to our customers and business partners. For that reason, we strive to deliver quick turnaround, we monitor our level of service, use benchmarking to track performance and efficiency, and continue to enhance what we do and how we do it.

Using technology smartly.

Equitable will never lose sight of the fact that ours is a people business where personal attention to detail, including security evaluation and risk assessment, have long been cornerstones of our success. We also believe that the effective use of technology helps us to better serve our customers and business partners. In general, we look for technology opportunities that enrich rather than replace personal interaction.

Developing our products.

When it comes to mortgages and deposits, we understand that one size does not fit all and that product features are important. For this reason, we have developed a number of different solutions for our markets. As a member of the CDIC, we provide both long-term and Cashable GICs available for Tax Free Savings Account ("TFSA") or non-registered purchases. And within our mortgage lending business, we offer a variety of fixed and floating rate products to meet the specific needs of customers with different borrowing requirements.

Empowering our resources.

Unquestionably, it's a challenge to grow while also delivering superior service, ensuring that we are prudent in our lending practices and compliant with the regulations and standards set for us as a federally regulated trust company. To meet this challenge, we keep pace with the pressures of growth by managing our resources carefully, recruiting the best talent, creating appropriate incentives and empowering our employees. In a business that relies on judgment rather than formulas, and personal touch rather than execution by rote, we are proud of the experience, knowledge and ideas that our team brings to work every day.

Taking a team approach.

Equitable is not a large financial institution measured on the basis of employment. Our team numbers 145, but what we lack in size, we more than make up for in skill, capabilities, determination and a coordinated, team-based approach for achieving success across our business. Our team engages in a wide range of activities including securitization of single and multi-family insured mortgages, origination of conventional mortgages of all types from single family through to large commercial, mortgage servicing and deposit raising – while meeting all of the regulatory and reporting requirements of a regulated financial institution – in a highly efficient manner. We've used our size to our advantage by engineering each of the business lines and operational areas to work in partnership in pursuing an over-arching goal: to offer the best mortgage and investment solutions to Canadians in our chosen markets. Everyone talks about service: we deliver and we've been doing so for 40 years.

Hearing the whole story.

Through open conversation with borrowers, we seek to uncover and understand each customer's unique circumstance, unlike lenders that rely strictly on automated underwriting systems. This enables us to make much more informed credit decisions and to see beyond numbers to the character and potential of our customers. While credit scores play their part, we are different in an otherwise compartmentalized industry because through personal inquiry, Equitable teams see and hear what others often miss. This allows us to lend with confidence, offering customized and personalized service to entrepreneurs and new Canadians who are often overlooked and under-served by large, impersonal financial institutions.

Knowing our markets.

To us, the starting point for good mortgage lending decisions is an intimate understanding of real estate markets. We don't just take a macro view, we immerse ourselves in our niches, right down to the neighbourhoods in which our borrowers live. As a result, we research employment trends, labour markets, new housing starts, migration and immigration statistics before entering new markets. We make a point of getting to know appraised values and valuation trends and initiate lending activity in a cautious manner. But once we know the market, our market intimacy pays dividends because it gives us the insight to better serve customers and their advisors with efficient and informed decision making.

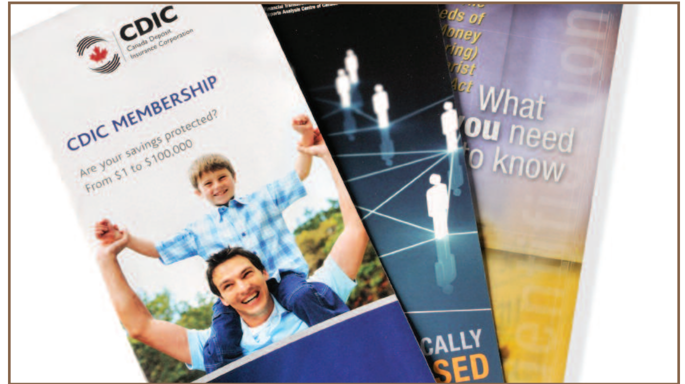
Equitable in Profile

Single Family Lending Services

Our Single Family Lending Services line of business offers excellent investment return potential and has proven credit evaluation and collection capabilities. Competitively, it enjoys broad relationships with an extensive network of licensed mortgage brokers and agents in our selected territories, has a highly responsive customer service ethic and delivers solutions to an attractive, under-served niche. Single family customers include business-for-self Canadians, new immigrants and investors who have the financial resources to achieve real estate ownership but don't meet the traditional credit criteria of the major banks. For new single family purchases or re-financings, we provide open and fixed-term mortgages with terms of up to five years on a variety of properties including homes and rental units. At year end 2009, Single Family Lending Services accounted for $836.5 million or 30.2% of our total mortgage principal outstanding and remained on track to be our fastest-growing line of business.

Commercial Mortgage – Broker Services

Through this proven line of business, we specialize in mortgage lending to qualified entrepreneurs, business operators and real estate investors who seek to buy mixed-use (storefront), retail office, multi-residential, commercial and industrial properties. Commercial Mortgage – Broker Services ("Broker Services") has a long history of success built on its extensive network of mortgage broker relationships, disciplined underwriting process, deep understanding of customer needs and clear niche market focus. Borrowers who use our solutions are often new Canadians who have strong business credentials in their native countries. Broker Services has originated mortgages with value that is in the $100,000 to $2.5 million range. As with single family mortgages, our rigorous lending process is coupled with consideration of the applicant beyond numerical measures. At year end 2009, this business represented $670.8 million or 24.2% of mortgage principal outstanding.



Commercial Lending Services

Commercial Lending Services funds large, sophisticated transactions that are secured by mortgages originated by commercial broker specialists. These commercial mortgages are chosen to provide low risk and good return characteristics. With many years of extensive experience, a market-oriented strategy and disciplined underwriting practices, Commercial Lending Services has successfully participated in lending on a variety of commercial property types – including multi-family residential apartment buildings – with mortgages ranging from $500,000 to more than $25 million. Like all of our lending businesses, Commercial Lending Services employs a strategy to optimize ROE adjusted for risk. At year end 2009, this line of business represented $1.3 billion or 45.6% of mortgage principal outstanding.

Deposit Services

Through The Equitable Trust Company, we are a federally regulated deposit taking institution and member of the CDIC. As such, we are licensed to issue Guaranteed Investment Certificates ("GICs") in every province and territory in Canada. The taking of GIC deposits is central to funding our business. To build additional relationships with independent deposit agents, investment dealers, financial planners and other intermediaries who recommend our products, we maintain a dedicated Deposit Services operation and provide short, long-term (up to five years) and Cashable GICs for investors wishing to save securely for the future. At year end 2009, total deposit principal outstanding was $3.3 billion.

Message to Shareholders

Austin Beutel
Chairman of the Board

Andrew Moor
President and
Chief Executive Officer

Fellow Owners:

In 2009, Equitable Group took significant and deliberate steps to build on the foundation we've created for a bright future, while also delivering record earnings in a recessionary economic climate. As a result, we enter the new decade with a great opportunity for value creation.

The most visible sign of corporate development was in our capital structure. On every key metric, Equitable displayed strength and progress. Our total capital ratio including general allowance was 17.6% at year end and our Tier 1 capital ratio was 14.6% – both well above the levels achieved in any previous period in our 40-year history. Our tangible common equity ratio of 12.6% was also well above that of Canada's major chartered banks.

We built this position by retaining earnings, shifting our business to lower risk-weighted assets and completing a non-dilutive preferred share equity offering which qualified for Tier 1 regulatory capital for our wholly-owned subsidiary Equitable Trust.

Consequently, we have the capacity to substantially grow our mortgage assets and the strength necessary to protect the integrity of our institution from volatility that often accompanies early stage economic recoveries.

2009 Performance

Equitable delivered outstanding results in 2009.

- Net income increased year over year by 33.2% to $51.4 million – a new record;
- Diluted earnings per share grew 20.9% to $3.36 – also a new record;
- Return on equity was 17.0%, ahead of the 2008 return of 16.6%;
- Productivity ratio, a measure of the efficiency of our business, improved to 24.9%; thereby, maintaining Equitable's status as a low-cost leader in our industry;
- Book value per share reached $21.83, up 23.0% from $17.75 a year ago.

The quality of our mortgage book was also preserved through disciplined underwriting decisions and diligent collection. While higher than they have been in the past five years, net realized loan losses of $6.5 million were low relative to the size of our institution and small considering the impact of the recession on employment levels and personal bankruptcies in Canada.

Based on Equitable's performance in 2009, results achieved since we became a public issuer in 2004, and since our founding in 1970, we can confidently conclude that Equitable can perform in good times as well as bad. The most recent example is the 2008/2009 time period of performing in bad times and it reflects well on both the Equitable team and the success of our strategies. In particular, our mortgage pricing strategies, which were implemented to reduce our exposure to the monetary easing of the past two years, served us well and resulted in a steady expansion of net interest margin in each quarter of 2009.

Service and Value: The Foundation for Our Future

Now that credit markets have been largely restored and economic recession is giving way to signs of recovery, we are focused on building our business.

Our plan for continued success is based on two imperatives: superior service for our customers and business partners and superior value creation for our shareholders.

For the increasing number of mortgage brokers, deposit agents and customers we do business with, our goal is to offer responsive solutions. This means taking advantage of our size and market knowledge to make decisions more efficiently than our competitors – recognizing that time is money for our business partners and their customers. Our responsive service ethic is being augmented by investments in automation and new product development. Overall,

we want our customers and their advisors to select Equitable first in our chosen markets.

Underlying these efforts is a firm understanding within our culture that we can only be successful, as a financial institution, by serving the needs of the marketplace. Over the past five years, we believe Equitable has done this, as evidenced by 22.5% average annual growth in our GIC deposits and 20.8% average annual growth in total mortgage assets.

For shareholders, we seek to build on our strengths to drive value. These strengths include:

- a solid presence and growing reputation in real estate markets chosen for their potential and made more attractive over the past two years due to diminished competition;
- extensive relationships with mortgage agents/brokers and deposit agents;
- ample liquidity and capital;
- an effective and low-cost, non-branch business model;
- proven credit risk management capabilities that are sensitive to, and calibrated for, our niches and economic conditions.

Responsible Growth and Improvement

In 2010 and beyond, we intend to capitalize on our stronger foundation to grow our mortgage book in a diversified, low-risk manner and with a continued emphasis on single family mortgage asset accumulation – balanced by originating attractive assets in our commercial businesses.

Our Single Family Lending Services business receives funding priority not only because of its strong capabilities but because it offers:

- excellent return potential in an environment of diminished competition;
- the advantage of requiring lower levels of economic capital relative to commercial mortgages, which is important as we strive to maintain financial strength.

To achieve responsible growth, we will maintain our sound credit risk management practices as we originate new assets. In response to improved market conditions, we stepped up the pace of our sales efforts late in 2009 and were rewarded with sizeable increases in production for Single Family Lending Services as well as our other business lines. We believe that there are quality growth opportunities available in the markets we serve.

In 2010, we will also continue to shape the various components of our commercial mortgage portfolio as we have been doing over the past two years to enhance returns and improve the credit risk profile.

The year past saw significant growth in our CMHC-insured securitization business, which ended the year with $4.1 billion of assets. We anticipate that market dynamics will be less favourable for this business in 2010 than was the case in 2009. However, we do expect to continue to securitize insured mortgages that generate recurring income.

Our enterprise risk management approach is designed to protect both the integrity of the institution and shareholder value. We intend to manage risk carefully as we grow.

The Year Ahead

Credit and economic conditions in Canada have shown clear signs of recovery since the middle of 2009. Demand for residential real estate has been surprisingly strong driven, in large part, by exceptionally low interest rates. With recovery comes the inevitable prospect of higher interest rates. We actively monitor the local real estate markets we lend in and adjust our credit policies to try to ensure that we are not lending imprudently against unsustainable values. Our current view is that, while house prices have likely risen faster than justified by economic fundamentals, the risk of a significant and sudden downward adjustment to house prices remains low. We are vigilant to the possibility that a house price bubble could develop and are managing our lending activities to ensure that this would not impact the integrity of Equitable.

A Great Opportunity

In closing, we believe we have a great opportunity to create value, but also a clear and well-accepted duty to ensure we build responsibly and in a low-risk manner. We are confident in the strength of our foundation and we will act in a way that preserves this strength. Directors and Officers collectively own 16.3% of Equitable's common shares, meaning our interests and those of all shareholders are aligned in the singular objective of delivering value.

Our sincere thanks go to the employees and Board of Directors of Equitable for your investment of time, energy and expertise. Most especially, we thank our shareholders, customers and business partners for participating in the Equitable success story. We are committed to making a bright future for all.

Yours sincerely,

Austin Beutel
Chairman of the Board

Andrew Moor
President and Chief Executive Officer

Management Q&A

The Canadian economy appears to be recovering and this raises the prospect of interest rate increases later in 2010. How is this affecting your thinking with regard to originations?

Most economists believe that interest rates will increase through 2010 and Equitable is managing its business in a manner that manages risks in this environment. Increases in interest rates are reflective of an improving economy and for many of our customers this will improve the stability of income to service mortgage debt even with higher interest rates. As we originate new mortgages, we encourage appropriate mortgage products that will reduce our customers' risk exposure to rising interest rates.

In terms of risk management, have you adjusted your underwriting criteria based on the potential for improving markets?

Equitable continuously adjusts its underwriting criteria to adjust to market conditions. In the latter part of 2008, we adjusted our underwriting criteria to reflect our view that there was an elevated risk of real estate prices softening in the face of a severe recession. Since that time Equitable has adjusted its underwriting to more normal criteria that have served the institution well over the years. We actively monitor the markets we serve and will make further adjustments as we see risks and opportunities emerge.

What is Equitable doing to attract single family business given the increased focus placed on originating this business in 2010?

We are focused on service and being the lender of choice for brokers operating in our market segments. To support this mission, we have expanded our underwriting staff and streamlined internal processes. This service focus has enabled us to attract new relationships and expand others and this has resulted in increased originations and will continue to do so in the future. In addition, we have recruited top talent in sales management to deepen existing broker relationships and to forge new partnerships within our broker network. Overall, we are focused on providing service at every touch point.

Equitable Trust's capital ratios were significantly stronger at year end 2009. How does this impact Equitable's business for 2010?

Our position gives us a very strong foundation to pursue growth but not at the expense of our strength. Our approach will be to achieve the dual goal of building high quality assets, including single family mortgages that consume less regulatory capital than other forms of mortgage lending, as a means of earning attractive investment returns while keeping our total capital ratio, Tier 1 ratio and tangible common equity at robust levels to enable solid growth beyond 2010.

What's your plan with respect to managing capital?

Equitable's strategic plan is to fund growth primarily through the retention of earnings and through the issuance of non-dilutive forms of capital. The Company's view is that shareholders will be best served by adopting rigorous processes for the allocation of capital to the assets and projects that produce the highest returns adjusted for risk. Strong returns on capital strengthen the foundations of our business and give Equitable the capital strength to grow assets and earnings faster. During 2009, the Company was successful in raising non-dilutive Tier 1 capital and Tier 2 sub-debt that augmented the growth in our capital base through the retention of earnings. We expect to raise these non-dilutive forms of capital as necessary and as part of our overall capital plan.

Do you plan to expand business from a product and geographic perspective?

Equitable is a growth company. We believe that our products and services occupy well-defined niches within the Canadian mortgage market that are not well served by traditional financial institutions. In our core market of Ontario, we believe there is substantial opportunity for growth in all areas of our business. Over the last few years, we have expanded successfully into Alberta and Manitoba and have built solid foundations for further growth in these markets. In 2010, we expect to further expand our geographic footprint in other parts of Canada. The latest example includes our recent opening of an office focused on commercial mortgage lending in Montreal. Future expansion might include secured lending on asset types other than real estate. While we are ambitious to expand our business, we will not compromise our passion to provide outstanding service to our customers or our determination to manage risk in pursuit of growth.

What impact will the January 1, 2011 adoption of International Financial Reporting Standards ("IFRS") have on Equitable's business in the foreseeable future?

Disclosure of the impact of the adoption of IFRS is found in the MD&A, beginning on page 36 of this Annual Report. The most significant impact of this change in accounting standards for Equitable is related to the accounting treatment of the securitization of CMHC-insured mortgages. Under IFRS, mortgages securitized under these programs will now be shown on the balance sheet and earnings will be recognized as spread income over the life of the mortgage. This is a significant change to the treatment under prevailing Canadian GAAP which removes these mortgages from our balance sheet at the time of securitization and recognizes most of the profit at that time. Equitable expects to continue to actively participate in the Canada Mortgage Bond (CMB) program under IFRS as this funding mechanism provides a reliable and low-cost source of funding for mortgages. The transition from Canadian GAAP to IFRS is complicated and will have significant impacts on both the financial statements of the Company, as well as the regulatory capital position and ratios of Equitable Trust. Management believes that it is well organized to make the transition to IFRS and that the adoption of this new accounting standard does not warrant a fundamental change in the Company's business activities.

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

For the three months and year ended December 31, 2009

Management's Discussion and Analysis ("MD&A") is provided in order to enable readers to assess the financial position and the results of operations of Equitable Group Inc. ("Equitable" or the "Company") for the three months ("quarter") and year ended December 31, 2009. This MD&A should be read in conjunction with the Company's unaudited interim consolidated financial statements for the fourth quarter (see Tables 17, 18 and 19 on pages 33, 34 and 35 of this report) and the audited consolidated financial statements for the year ended December 31, 2009, and accompanying notes. The consolidated financial statements have been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). This report, and the information provided herein, is dated as at February 24, 2010. Additional information about the Company, including its Annual Information Form, is available on the Company's website at www.equitablegroupinc.com and on SEDAR at www.sedar.com.

The material below contains forward-looking statements. Please see "Cautionary Note Regarding Forward-Looking Statements."

Business Profile and Objectives

The Company is a niche mortgage lender that provides loans secured by first mortgages and mortgages insured by the Canada Mortgage and Housing Corporation ("CMHC"), through its wholly-owned subsidiary, The Equitable Trust Company ("Equitable Trust"), which was founded in 1970. Equitable Trust is a federally-regulated financial institution whose activities are supervised by the Office of the Superintendent of Financial Institutions Canada ("OSFI"). The primary sources of the Company's revenues are interest income as well as commitment, renewal and discharge fees derived from its mortgage financing business. In addition, the Company earns income from the securitization of insured mortgages administered by CMHC through the Government of Canada's National Housing Act Mortgage Backed Securities ("MBS") and Canada Mortgage Bond ("CMB") Programs, which comprises income in the form of gains earned at the time of securitization as well as recurring income from its continuing residual interest in the cash flows that are earned by the securitized mortgages. The Company also earns interest and dividend income from investments. The Company operates without a branch network, choosing instead to achieve lower overheads by using independent mortgage brokers to originate mortgages and independent deposit agents to originate deposits. This business model and the Company's strong competitive position have established it as a leader in its mortgage lending niches and have contributed to excellent long-term financial results.

Equitable Trust's ability to fund its mortgage business by attracting depositors as a regulated Canada Deposit Insurance Corporation ("CDIC") member is also a core strength of enduring enterprise value. This ability has allowed Equitable to build a diversified mortgage portfolio secured by residential and commercial real estate. The Board and management are focused on long-term growth, identifying and investing in the development of mortgage products and those selected geographic markets that will deliver superior returns on capital, thereby enhancing shareholder value.

Given this focus and its assessment of the current economic environment, management has established the following key corporate objectives for 2010:

- Grow the lending businesses in which the Company has the best opportunity to earn attractive and sustainable returns.
- Optimize return on equity ("ROE") adjusted for risk, with a view to enhancing the value of its diversified mortgage portfolio and maintaining prudent credit risk practices.
- Protect shareholder value through focused monitoring and mitigation of the Company's business risks, including the use of prudent credit risk practices, the disciplined management of arrears and the maintenance of optimal levels of regulatory capital and liquidity.
- Fund growth by leveraging the Company's strong capital position, which is primarily supported through the retention of earnings.
- Continuous improvement of processes and operating efficiencies, recognizing that the provision of superior service to its business partners and customers is critical to its growth objectives.

Lending Businesses

The Company has three core lending businesses, which align well with its competitive strengths, competencies and profitability objectives:

- Single Family Lending Services ("Single Family"): This business benefits from Equitable Trust's well-established relationships with a large independent broker network, its focus on customer service, as well as Equitable's experience in utilizing a disciplined approach to credit evaluation and collections.
- Commercial Mortgage – Broker Services ("Broker Services"): This line of business funds mortgages on a variety of property types, including mixed-use, apartment buildings, commercial and industrial properties sourced from independent mortgage brokers. Broker Services

specializes in assisting experienced entrepreneurs, business operators and real estate investors. Its broad mortgage broker relationships and strong underwriting capabilities are among its key strengths.

- Commercial Lending Services: This business funds larger, more sophisticated transactions that are secured by mortgages originated through commercial broker specialists. These commercial mortgages provide low risk and good return characteristics for Equitable.

Operating Efficiency and ROE

Equitable evaluates each mortgage and assesses its pricing based on the respective contribution that the mortgage can make to ROE, such that each mortgage is expected to deliver a return on investment that meets established requirements. While attractive pricing can be garnered on a variety of loan types, single family residential mortgages typically generate a higher ROE than commercial mortgages because they require less regulatory capital, even though they involve higher processing costs.

Management believes that shareholders are best served by focusing on lending opportunities that optimize ROE. The Company is also committed to using automation and other means to improve operating efficiencies and reduce costs where possible.

2009 Highlights

During 2009, the Company achieved its highest earnings ever and posted strong results that were in line with its financial and strategic goals for the year, despite the protracted and severe turbulence from which Canadian and international capital and credit markets are struggling to recover. Consistent with its 2009 objectives and on the basis of improving market conditions in the latter half of the year, the Company grew its Single Family business faster than its other mortgage businesses and continued to reshape various aspects of its commercial mortgage portfolio in order to enhance its interest rate and credit risk profile. At the same time, owing to retention of earnings and the recent $50 million preferred share transaction, Equitable Trust held the strongest capital ratio and liquidity positions since the Company was publicly listed, with a total capital ratio of 17.6% (including general allowance), as well as a Tier 1 regulatory capital ratio and tangible common equity ratio (see explanation in the Non-GAAP Financial Measures section of this MD&A) at December 31, 2009 of 14.6% and 12.6%, respectively.

Earnings Performance

In 2009, Equitable produced strong earnings that reflected growth in its net interest margin. Equitable also securitized and sold CMHC-insured mortgages valued at $1.4 billion. As a result, Equitable established another new annual earnings record:

- net income increased 33.2% over 2008 to $51.4 million;
- diluted earnings per share increased 20.9% over 2008 to $3.36 per share; and
- ROE for 2009 increased to 17.0% compared to 16.6% in 2008.

In the fourth quarter of 2009, the Company's results were impacted by a one-time benefit that lowered its income taxes, primarily as a result of reductions in future income tax rates that were enacted during the quarter by the province of Ontario. These newly enacted rates lowered the Company's future tax provision by $1.5 million or $0.10 per share.

Demonstrating the efficiency of the Company's approach to business, the 2009 productivity ratio on a taxable equivalent basis ("TEB" – see explanation of TEB in the "Non-GAAP Financial Measures" section of this MD&A) was 24.9% – an improvement over the 27.4% ratio achieved in 2008.

Credit Quality

The quality of the Company's mortgage portfolio at year end continued to reflect the effectiveness and prudence of its underwriting. The Company does not lend against uninsured mortgages at high loan-to-value ratios, thereby limiting its exposure to loss. Management continually monitors credit risk exposure in order to ensure that underwriting policies are prudent and reflective of current and expected economic conditions. Mortgages in arrears 90 days or more were 0.64% of total mortgage principal outstanding at December 31, 2009 compared to 1.57% a year earlier. The quarter-over-quarter consecutive improvement in this ratio throughout the year is the result of effective mortgage administration and collections practices and reflects a relative improvement in real estate market conditions within Equitable's lending regions over the course of the year. Nonetheless, management took the prudent step at the end of the third quarter to deem a $19.2 million residential construction mortgage as being impaired, placing a $1.0 million specific allowance against this mortgage in that quarter and a further $1.0 million allowance in the fourth quarter. The provisions taken reflect the increased credit risk that is associated with this mortgage and the respective borrower. Notwithstanding the increased risk, the interest payments related to this mortgage were up-to-date

at December 31, 2009. Inclusion of this mortgage in net impaired mortgages was the primary reason that the impaired mortgages were 1.20% of total mortgage principal at the end of 2009, only slightly lower than the 1.21% reported at the end of 2008. Similarly, the provision for this mortgage resulted in an increased allowance for credit losses as a percentage of total mortgage principal of 0.53% at December 31, 2009 compared to 0.48% reported at December 31, 2008. Net realized loan losses of $6.5 million incurred during 2009 primarily relate to the successful completion of loan workout activities disclosed in the Company's 2008 Annual Report.

2010 Business Outlook

Management is confident in the strength of the Company's business model based on 2009 and long-term financial performance, solid operational progress in executing against its plan and the current strength of demand for mortgage financing in Equitable's product and market niches. Management has been focused on identifying and originating quality lending opportunities and continues to find these in Canadian real estate markets. Equitable continues to monitor the economic and credit market landscape, which, while volatile in the recent past, has shown signs of continual improvement since the second quarter of 2009.

Given improving real estate markets and the increasing comfort that management has with credit conditions, Equitable Trust has increased its sales efforts, within the context of ongoing lending and risk management discipline. In the latter part of 2009 and early in 2010, these increased sales efforts have resulted in increased single family residential origination volumes, which is a trend that management expects to continue. In line with the focus that the Company has placed on safeguarding the future health of the mortgage portfolio, management continues to be confident that its underwriting processes will ensure improving returns that do not demand the taking of excessive risk. While management continues to be concerned that there is some potential for further volatility in real estate markets, the levels of defaults and losses that the Company experienced during 2009 have been manageable. Although the Company has had to manage higher delinquency levels during 2009 than those experienced historically, the relatively healthier real estate markets that have been experienced have allowed it to sell properties and work out problem loans in an expeditious and effective manner. Management believes that its levels of arrears and defaults will continue to be manageable in 2010.

As anticipated in prior quarters, the Company's net interest margin has continued to improve. Relative to years past, Equitable faces fewer competitors in its core mortgage markets and this is expected to provide a continuing opportunity to improve interest rate spreads on the Company's mortgage portfolio. The Bank of Canada has recently announced that, conditional on its outlook for inflation, it continues to expect that its benchmark interest rate will remain at its current level until the end of the second quarter of 2010. As such, the Company does not anticipate reductions in the prime rate of interest ("Prime Rate") from its current very low level. Indeed, any increases in this benchmark interest rate that may occur in the latter half of 2010 may temporarily expand the Company's net interest margin ("NIM") as a result of the fact that floating rate mortgage yields tend to increase immediately, while corresponding increases in the pricing of Guaranteed Investment Certificate ("GIC") deposits lag behind and take effect only as new deposits are raised. Generally, recent market dynamics have resulted in an easing of overall deposit costs and an improvement in interest spreads. During 2009, management implemented significantly improved pricing for its new and renewing commercial mortgages and added interest rate floors to variable rate mortgage business that was originated or renewed. Furthermore, the Company's portfolio of customer deposits comprised of cashable GICs that have matured or are maturing in the near future have or will be replaced with less expensive funding. These factors will continue to support the Company's currently strong NIM position, though significant improvements are not expected beyond this position in the next few quarters.

Equity securities held by the Company are comprised of preferred shares, which are classified as available for sale assets for financial instrument accounting purposes. This portfolio increased by $53.2 million during 2009, primarily as a result of $33.2 million in purchases, net of sales and redemptions, and $20.0 million in decreased unrealized losses related to market value deficiencies reported at December 31, 2008. This improvement in market value continues to support management's view that, while economic volatility in Canadian stock markets and resultant unrealized losses have affected these high-quality investments, there is no permanent impairment in this portfolio.

The GIC market continues to provide ample funding for Equitable Trust's business. However, management believes that the maintenance of higher than normal levels of liquidity on its balance sheet is a prudent measure, intended to insulate the Company's business and ensure it is well-positioned to manage any unexpected and unforeseen events that may impact its liquidity during periods of uncertainty in Canadian and international capital markets. The cost associated with maintaining excess liquidity has a negative impact on NIM.

The Company's fee income and earnings are expected to perform commensurate with real estate market stabilization and health. As an approved seller under the CMB Program, Equitable Trust has been able to transact securitization activities at interest rate spreads that continue to be above historic norms. While it believes that it will originate strong insured mortgage volumes that it will be able to securitize through this program, Equitable expects to transact 2010 securitization activities at lower volumes and lower spreads than those experienced in 2009.

While the majority of the Company's earnings and cash flows are generated from the interest it earns on the mortgage portfolio held on its balance sheet, the Company also benefits from the recurring cash flows it receives from its $4.1 billion securitized mortgage portfolio – a portfolio that has grown by just under $1.3 billion since the fourth quarter of 2008 and that management intends to continue to grow during the next few quarters.

On September 1, 2009, the Company issued 2.0 million non-cumulative 5-year rate reset Series 1 perpetual preferred shares at an issue price of $25.00 per share to initially yield 7.25% per annum, for gross proceeds of $50.0 million. This was a ground-breaking transaction for Equitable, which it expects will allow it to continue to access a form of Tier 1 regulatory capital that was previously unavailable to financial institutions of its size. The gross proceeds of this offering were intended for use for general corporate purposes, in support of growth in the Company's mortgage business operations and future redemption of Equitable Trust's subordinated debt obligations. Concurrent with the issuance of the preferred shares, Equitable Trust redeemed $2.5 million of its Series 5 Debentures ("Series 5").

During December 2009, the Company issued a total of $23.2 million of Series 8 Debentures ("Series 8"), a new class of subordinated debt, at an initial interest cost of 6.50% – approximately 376 basis points over the then current 5-year Government of Canada benchmark yield. The gross proceeds of the offering of the Series 8 were used by the Company to purchase subordinated debt of Equitable Trust, which qualifies as Tier 2B regulatory capital and will, in turn, be used for general corporate purposes. The Series 8 will pay fixed interest semi-annually for the first five years of its 10-year term, and then bear a floating interest rate that is calculated at the 90-day Banker's Acceptance Rate plus 480 basis points thereafter. Concurrent with the Series 8 issuance, Equitable Trust redeemed all $30.8 million of its remaining Series 5 subordinated debentures, which bore a weighted average interest cost to Equitable Trust of 7.43%. The Company also repaid $13.3 million of its term credit facilities with a Canadian chartered bank. The issuance of the new Series 8 provided Equitable the ability to extend the average term of its subordinated debt at lower average interest costs, on advantageous terms and with better structure. Subject to regulatory approval, the Company may provide the holders of certain of its other outstanding subordinated debentures the option of re-investing in a new debenture or having their existing debenture redeemed. Irrespective of potential redemptions that may cause some marginal decline in the Company's total capital ratio, the Company's capital position will remain robust and will be able to support meaningful growth in Equitable's mortgage portfolio.

Given its strong balance sheet, quality mortgage portfolio and focused risk management philosophy, Equitable remains well-positioned, with a high level of financial health, including prudent levels of capital and liquidity, to capitalize on future business opportunities.

The purpose of this outlook is to give the reader an indication of factors that may affect Equitable's performance in the near-term. Readers should be aware that information contained in this section may not be appropriate for any other purpose. See "Cautionary Note Regarding Forward-Looking Statements."

Dividends

On February 24, 2010, the Company's Board of Directors declared a quarterly dividend in the amount of $0.10 per common share, payable on April 5, 2010, to common shareholders of record at the close of business on March 15, 2010.

Also, on February 24, 2010, the Company's Board of Directors declared a quarterly dividend in the amount of $0.453125 per preferred share, payable on March 31, 2010, to preferred shareholders of record at the close of business on March 15, 2010 (see Note 14 to the consolidated financial statements).

Table 1: Selected financial information

($ THOUSANDS, EXCEPT SHARE, PER SHARE AND EMPLOYEE AMOUNTS)	2009	2008	2007[1]	Change from 2008	
OPERATIONS					
Net income	**51,438**	38,611	31,171	12,827	33.2%
EPS – basic	**$ 3.37**	$ 2.79	$ 2.47	$ 0.58	20.8%
EPS – diluted	**$ 3.36**	$ 2.78	$ 2.44	$ 0.58	20.9%
Net interest income	**73,169**	64,343	61,579	8,826	13.7%
Total revenue	**207,824**	226,766	185,933	(18,942)	(8.4%)
Return on equity[2]	**17.0%**	16.6%	17.2%		
Return on average assets	**1.3%**	1.0%	1.0%		
Mortgage origination[3]	**2,272,537**	2,330,593	1,903,581	(58,056)	(2.5%)
Productivity ratio – TEB[4]	**24.9%**	27.4%	29.2%		
Number of employees at year end	**145**	135	124		
BALANCE SHEET AND OFF-BALANCE SHEET					
Total assets	**3,846,074**	4,087,551	3,409,626	(241,477)	(5.9%)
Mortgages receivable	**2,763,020**	3,023,015	2,874,241	(259,995)	(8.6%)
Shareholders' equity	**373,861**	264,146	203,170	109,715	41.5%
Mortgage backed security assets under administration	**4,093,180**	2,825,063	1,888,250	1,268,117	44.9%
COMMON SHARES					
Number of common shares outstanding at year end	**14,903,846**	14,882,710	12,952,710		
Dividends per common share	**$ 0.40**	$ 0.40	$ 0.40	$ –	– %
Book value per common share	**$ 21.83**	$ 17.75	$ 15.69	$ 4.08	23.0%
Common share price – close	**$ 21.25**	$ 11.75	$ 28.75	$ 9.50	80.9%
Market capitalization	**316,707**	174,872	372,390	141,835	81.1%
EQUITABLE TRUST CAPITAL RATIOS					
Tangible common equity ratio[5][6]	**12.6%**	10.1%	7.7%		
Tier 1 capital ratio[6]	**14.6%**	10.1%	7.7%		
Total capital ratio (including general allowance)[6]	**17.6%**	13.5%	11.0%		
CREDIT QUALITY					
Realized loan losses – net of recoveries	**6,516**	36	21		
Mortgages in arrears 90 days or more as a % of total mortgages[7]	**0.64%**	1.57%	0.30%		
Net impaired mortgages as a % of total mortgages[8]	**1.20%**	1.21%	0.30%		

[1] 2007 results include a $3.4 million after tax write-down of the Company's preferred shares included in its investment portfolio. Excluding the impairment write-down, net income would have been $34.5 million, basic and diluted earnings per share would have been $2.74 and $2.71, respectively, return on equity would have been 18.9%, return on average assets would have been 1.1% and productivity ratio – TEB would have been 27.2% – see the "Non-GAAP Financial Measures" section of this MD&A.

[2] Return on equity is calculated based on net income available to common shareholders divided by the weighted average common equity outstanding during the year.

[3] Does not include $546,846 for the year ended December 31, 2009 (2008 - $777,393, 2007 - $824,656) of advances related to mortgages held for sale warehouse facilities. See Table 8 - Mortgages held for sale.

[4] Decreases in this ratio reflect improved efficiencies.

[5] The tangible common equity ratio is defined as shareholder's equity plus any qualifying other non-controlling interest in subsidiaries less preferred shares issued and outstanding, any goodwill, other intangible assets and certain components of accumulated other comprehensive income, as a percentage of risk-adjusted assets less other intangible assets. This ratio is a non-GAAP financial measure that is used as a key indicator of capital strength.

[6] 2007 capital ratios are calculated under Basel II.

[7] Mortgages in arrears 90 days or more do not include CMHC-insured mortgages that are less than 365 days in arrears.

[8] Net impaired mortgages do not include CMHC-insured mortgages that are less than 365 days in arrears and reflect gross mortgage principal of impaired mortgages less specific allowance.

Financial Review – Earnings

Net Income

Net income increased 33.2% year-over-year to $51.4 million in 2009 from $38.6 million in the prior year.

Diluted earnings per share were $3.36, compared to $2.78 in 2008, an increase of 20.9%. These increases are primarily due to increased net interest income as well as fees and other income earned in 2009. The drivers of this growth are discussed below.

Net Interest Income

Net interest income is the main driver of profitability for the Company. It is measured on a TEB so that income from equity securities may be compared on a pre-tax basis to ordinary interest income. Table 2 illustrates the Company's net interest margin in 2009 compared to 2008 on a TEB.

Table 2: Net interest income

($ THOUSANDS)	2009 Average balance	2009 Revenue/ expense	2009 Average rate[(1)(2)(3)]	2008 Average balance	2008 Revenue/ expense	2008 Average rate[(1)(2)(3)]
Interest revenues derived from:						
Assets:						
Mortgages	**$ 2,880,584**	**$ 162,991**	**5.7%**	$ 2,934,665	$ 186,519	6.4%
Liquidity investments[(2)]	**799,500**	**12,078**	**1.8%**	574,172	19,226	3.3%
Equity securities – TEB[(2)]	**123,368**	**8,419**	**7.3%**	126,270	9,789	7.3%
Total interest earning assets – TEB	**$ 3,803,452**	**$ 183,488**	**4.8%**	$ 3,635,107	$ 215,534	5.9%
Total assets – TEB	**$ 3,966,813**	**$ 183,488**	**4.6%**	$ 3,748,589	$ 215,534	5.7%
Interest expenses related to:						
Liabilities and shareholders' equity:						
Customer deposits	**$ 3,433,864**	**$ 101,471**	**3.0%**	$ 3,319,612	$ 142,238	4.3%
Bank term loans[(3)]	**36,048**	**3,188**	**7.4%**	44,595	3,025	6.8%
Subordinated debentures[(3)]	**34,820**	**2,310**	**7.3%**	31,969	2,348	7.3%
Total interest bearing liabilities	**$ 3,504,732**	**$ 106,969**	**3.1%**	$ 3,396,176	$ 147,611	4.3%
Total liabilities and shareholders' equity	**$ 3,966,813**	**$ 106,969**	**2.7%**	$ 3,748,589	$ 147,611	3.9%
Net interest income – TEB		**$ 76,519**			$ 67,923	
Net interest margin – TEB			**1.9%**			1.8%
Less: Taxable equivalent adjustment		**(3,350)**			(3,580)	
Net interest income		**$ 73,169**			$ 64,343	

(1) Average rate is a simple average calculated with reference to opening and closing period balances.
(2) Average rates for liquidity investments and equity securities are calculated based on the average of the month-end balances outstanding during the year.
(3) Average rate for bank term loans and subordinated debentures is calculated based on weighted average balances outstanding during the year.

Total interest revenues, using the TEB approach, decreased 14.9% to $183.5 million in 2009, compared to $215.5 million in the prior year. Mortgage interest income decreased $23.5 million or 12.6% for the year ended December 31, 2009 over the prior year, primarily due to decreases in the Prime Rate and the resultant reduction in yields that the Company earned on variable rate mortgage assets, as well as its more recently originated fixed rate mortgages. Mortgage interest income also declined commensurate with the level of contraction in the Company's mortgage portfolio. Decreases in government and bank benchmark rates also resulted in reduced interest income being earned by the Company on its liquidity investments, which was approximately $7.1 million less in 2009 than that in the prior year. Income derived from equity securities on a TEB decreased $1.4 million to $8.4 million for the year ended December 31, 2009 compared to the prior year.

Average interest rates paid on average customer deposit balances outstanding during 2009 decreased to 3.0% compared to 4.3% in 2008. During 2009, overall interest expense on customer deposits decreased $40.8 million or 28.7% over 2008, despite a 3.4% increase in average customer deposits outstanding during the year compared to 2008. This was primarily the result of lower prevailing GIC rates in the market. The market for customer deposits provides ample funding for the Company's mortgage lending operations. Late in 2008, increased competitive demand for GIC deposits resulted in short-term deposits being raised at tighter spreads to Prime Rate than have historically prevailed in the market, with a corresponding compression in interest rate spread on floating rate mortgages. However, during 2009, competitive demand for GIC deposits moderated to more normal levels.

Net interest income – TEB increased $8.6 million or 12.7% to $76.5 million for the year ended December 31, 2009 compared to $67.9 million earned during 2008. During the first quarter and early in the second quarter of 2009, the Company experienced consecutive total decreases of 125 basis points in the Prime Rate. Generally, interest on the Company's floating rate mortgages is immediately affected by any change in the Prime Rate while the effect on liabilities is delayed. Since customer deposits are in the form of GICs, the Company's Cashable GICs are the only liabilities that might be immediately affected by an increase in interest rates through early redemption and reinvestment by GIC holders. Therefore, an increase in the Prime Rate usually leads to temporary improvements in net interest margin while a decrease has the opposite effect. Despite the effects of these earlier decreases in the Prime Rate, the Company was able to increase net interest margin over consecutive quarters by significantly improving pricing for new and renewing mortgages. The Company also continued its initiative of implementing interest rate floors to the variable rate mortgage business that renewed or was originated. Improved pricing and implementation of floors favorably impacted the Company's net interest margin during the latter half of 2009. The Company also benefitted from lower GIC rates that prevailed in the latter half of 2009, as deposits that were locked in for longer terms or were cashable in nature matured and were replaced with less expensive money. The Company's net interest margin increased to an average 1.9% in 2009, compared to 1.8% in 2008. Improvement in net interest margin was noted throughout the year, progressing from an average 1.6% in the first quarter with consecutive increases of approximately 30 basis points per quarter, to an average of 2.4% in the fourth quarter of 2009.

From time to time, the Company enters into interest rate swaps in order to hedge interest rates on term GICs used to fund floating rate mortgages. Interest rate swaps of $10.0 million were outstanding at December 31, 2009. The GICs to which these swaps relate were designated as held for trading financial instruments and carried at fair value. Any change in their value is included in interest expense and all transaction costs related to raising these GICs are expensed at the time of designation.

Other Income

Other income includes ancillary fees related to the origination and administration of the mortgage portfolio, as well as gains on the securitization and sale of mortgages and the related excess interest spread, net of servicing fees, earned on mortgages securitized through the CMHC MBS and CMB Programs. Sundry income, gains or losses on investments and other non-mortgage related fees are also included in other income. Other income increased by $12.9 million or 86.9% to $27.7 million in 2009, compared to $14.8 million in 2008. This was primarily the result of an increase of $11.1 million in total income from loan securitization activities, as well as a $1.4 million increase in fees and other income.

The increase in total income from loan securitizations was directly related to the fact that, during 2009, the Company securitized and sold $1.4 billion of CMHC-insured mortgages compared to $1.3 billion in 2008. Gross margins on the securitization of CMHC-insured mortgages increased to an average of 131 basis points during 2009 (118 basis points in the fourth quarter of 2009) from 80 basis points during 2008 (125 basis points in the fourth quarter of 2008). Since the second quarter of 2008, Equitable Trust has been able to benefit from credit market dynamics that have allowed it to securitize single family and multi-family residential mortgages at spreads and volumes that have been higher than historical norms. The primary components of securitization income are excess interest spread, net of servicing fees and gains on sale of mortgages.

Table 3: Other income

($ THOUSANDS)	2009	2008	Change from 2008	
Loan securitizations – gains on securitization activities	**$ 20,221**	$ 10,076	$ 10,145	100.7%
Loan securitizations – excess interest spread, net of servicing fees	**4,169**	3,199	970	30.3%
Total income from loan securitizations	**24,390**	13,275	11,115	83.7%
Fees and other income	**3,246**	1,832	1,414	77.2%
Net gain (loss) on investments	**50**	(295)	345	116.9%
Total	**$ 27,686**	$ 14,812	$ 12,874	86.9%

Non-interest Expenses

The largest component of non-interest expenses relates to compensation and benefits. The year-over-year increase of $3.2 million or 14.2% in 2009 compared to 2008 reflected a $2.1 million increase in payroll costs as well as an increase in general and administrative costs of $1.1 million. Included in compensation and benefits expense during 2009 and 2008 was a charge for stock-based compensation expense in the amount of $0.8 million related to grants of options. The accounting effect of charges for stock-based compensation expense result in corresponding increases to contributed surplus.

The Company's productivity ratio – TEB was 24.9% in 2009 compared to 27.4% in 2008. This ratio is a non-GAAP financial measure derived by dividing non-interest expenses by the sum of net interest income – TEB and other income. While a lower productivity ratio is generally associated with a more efficient cost structure, the Company's productivity index can also be affected by increases and declines in funding volumes and the Company's need to maintain human resource staffing levels commensurate with volume expectations. Management believes this ratio will increase over time as a result of growth in single family mortgage originations, since origination and servicing of these mortgages are more costly per dollar of underlying mortgage; however, the offset is an expected improvement in risk-adjusted returns on equity.

Table 4: Non-interest expenses and productivity ratio

($ THOUSANDS)	2009	2008	Change from 2008	
Compensation and benefits	**$ 15,367**	$ 13,253	$ 2,114	16.0%
Licenses, regulatory fees and insurance	**1,917**	1,452	465	32.0%
Premises and equipment	**2,449**	2,385	64	2.7%
Marketing, travel and communications	**1,130**	1,223	(93)	(7.6%)
Mortgage servicing	**687**	1,121	(434)	(38.7%)
Legal, audit and related services	**550**	630	(80)	(12.7%)
Other	**3,807**	2,627	1,180	44.9%
Total	**$ 25,907**	$ 22,691	$ 3,216	14.2%
Productivity ratio – TEB	**24.9%**	27.4%		

Income Taxes

The Company's statutory income tax rate decreased to 32.4% from 33.3% in 2008. This decrease was caused by a reduction in Ontario corporate income tax rates that were enacted in the fourth quarter of 2009 as well as the Company's increased operations in Alberta, which has a lower income tax rate than the Company's Ontario operation. The Company's effective income tax rate in 2009 was 24.7% compared to 27.2% in 2008.

The effective tax rate was less than the statutory tax rate of 32.4% primarily as a result of tax-exempt dividend income earned from its equity securities portfolio. Income taxes are allocated between current and future taxes. Future taxes result from timing differences between the Company's financial statement income and net income for tax purposes. Future taxes are established at the rates expected to be in effect at the date of the reversal of the timing differences. The net decrease in future income tax expense of $5.2 million from the prior year was primarily due to future taxes payable relating to loan securitizations as well as future rate reductions.

Financial Review – Balance Sheet

Mortgage Portfolio

Equitable's mortgage portfolio is diversified across both residential and commercial real estate asset categories and consists of first charge and CMHC-insured mortgages. Mortgage principal decreased $260.7 million or 8.6% during 2009 to $2.8 billion at year end. This reduction resulted from management's explicit earlier intention to maintain a slower pace of commercial mortgage growth in order to improve capital ratios as well as overall investment returns on a risk-weighted basis, as well as a more conservative credit approach in its single family and mixed-use businesses. In addition to being affected by the natural amortization and payout of mortgages, the decline in the size of this portfolio should be put in the context of the 2009 growth of 44.9% or $1.3 billion in the Company's off-balance sheet portfolio of securitized CMHC-insured multi-unit residential and single family mortgages.

Table 5: Mortgages receivable – by property type

($ THOUSANDS)	2009	% of total	2008	% of total	2007	% of total
Single family dwelling[1]	**$ 1,010,266**	**36.5%**	$ 1,035,300	34.2%	$ 739,050	25.8%
Mixed-use property	**325,816**	**11.8%**	333,235	11.0%	287,643	10.0%
Multi-unit residential	**383,945**	**13.9%**	515,575	17.0%	660,071	23.0%
CMHC-insured multi-unit residential	**141,460**	**5.1%**	74,380	2.5%	178,971	6.2%
Commercial	**689,402**	**24.9%**	649,591	21.5%	652,783	22.8%
Mortgages held for sale	**104,728**	**3.8%**	297,952	9.8%	272,370	9.5%
Construction	**110,596**	**4.0%**	120,908	4.0%	77,395	2.7%
Total mortgage principal	**2,766,213**	**100.0%**	3,026,941	100.0%	2,868,283	100.0%
Deferred net mortgage commitment fees, net (discounts) premiums and sundry	**(13)**		(2,786)		368	
Mortgages receivable	**2,766,200**		3,024,155		2,868,651	
Accrued interest	**11,455**		13,411		14,515	
Allowance for credit losses	**(14,635)**		(14,551)		(8,925)	
Total mortgages receivable	**$ 2,763,020**		$ 3,023,015		$ 2,874,241	

[1] *Includes $56,777 (2008 - $176,436, 2007 - nil) of CMHC-insured and $37,869 (2008 - $12,267, 2007 - nil) of other insured single family dwelling mortgages.*

At December 31, 2009, single family dwelling mortgages represented the largest portion of the portfolio (see Table 5). CMHC-insured single family dwelling mortgages comprised 2.1% of the portfolio. Single family dwelling mortgages decreased by $25.0 million or 2.4% from December 31, 2008, consistent with the Company's more conservative approach to credit during the unstable credit, real estate and employment markets of the early part of 2009. However, management noted an increased pace of origination from the Company's Single Family line of business, starting with the fourth quarter of 2009.

The portfolio of mortgages on mixed-use properties decreased by $7.4 million or 2.2% from December 31, 2008. Mortgages on mixed-use properties are originated by Equitable's Commercial Mortgage – Broker Services team.

Multi-unit residential mortgages decreased by $131.6 million or 25.5% from December 31, 2008, primarily as a result of the Company's success in renewing a significant number of these as CMHC-insured mortgages during the year. The multi-unit residential portfolio includes apartment buildings and retirement residences.

CMHC-insured multi-unit residential mortgages comprised 5.1% of the portfolio compared to 2.5% a year ago, while the principal balance outstanding increased $67.1 million over the preceding year to $141.5 million. The principal balance outstanding is affected by the timing of securitization activities and the emphasis that the Company has placed on securitizing and selling this category of mortgages through the CMB Program. The majority of the securitization business conducted by the Company in 2009 related to CMHC-insured multi-unit residential mortgages.

Commercial mortgages increased $39.8 million or 6.1% from December 31, 2008.

At December 31, 2009, the Company's portfolio of mortgages held for sale was comprised of 25.5% residential and 74.5% commercial mortgages that are held within mortgage warehouse line of credit facilities that the Company has made available to third-party financial lending firms who require financing prior to pooling and eventually selling their mortgages to investors. Mortgages held for sale decreased 64.9% from 2008.

During 2009, construction mortgages decreased $10.3 million or 8.5% from the prior end-of-year level to comprise 4.0% of the portfolio at December 31, 2009.

Floating rate mortgages within the portfolio comprised $0.8 billion at December 31, 2009 and represented 29.9% of the portfolio. In order to limit the Company's interest rate exposure on floating rate mortgages during 2009, management implemented a policy of converting floating rate mortgages to fixed or putting interest rate floors on these mortgages as they renewed. As a result, fixed rate mortgages within the portfolio represented 70.1% of the portfolio at December 31, 2009, compared to 50.0% at December 31, 2008. Floating rate mortgages that had no floors amounted to 15.6% of the portfolio at December 31, 2009, compared to 39.4% at December 31, 2008. However, management does not expect to see further declines in variable rate exposure in coming quarters.

The majority of the Company's mortgages are sourced each year by a network of independent mortgage brokers and other mortgage originators. A mortgage brokerage arrangement exists with First National Financial LP ("FNFLP"), one of Canada's leading mortgage banking organizations, to source and administer CMHC-insured multi-unit residential and conventional mortgages, including a component of mortgages held for sale. FNFLP originated approximately $601.4 million of the Company's outstanding on-balance sheet mortgage principal at December 31, 2009. CMHC-insured mortgages are funded almost exclusively for securitization through CMHC Programs. When these mortgages are securitized and sold, the Company records a gain on sale and retains the rights and obligations with respect to servicing the mortgages.

At December 31, 2009, consistent with a year ago, 72.7% of the Company's mortgages were secured by properties located in Ontario. The Company's Alberta business continued to grow at a conservative pace in 2009 to 16.2% of the portfolio. Of the remaining portfolio, 5.1% are located in Quebec, 1.3% in Manitoba, 2.6% in British Columbia, with the remaining 2.0% in the rest of Canada.

Table 6: Mortgage principal outstanding – by lending business

($ THOUSANDS)	**2009**	**% of total**	2008	% of total
Single Family Lending Services	**$ 836,526**	**30.2%**	$ 818,290	27.0%
Commercial Mortgage – Broker Services	**670,767**	**24.2%**	673,648	22.3%
Commercial Lending Services	**1,258,920**	**45.6%**	1,535,003	50.7%
Total mortgage principal	**$ 2,766,213**	**100.0%**	$ 3,026,941	100.0%

In the context of the market turbulence experienced over the course of the last 24 months, management communicated its explicit earlier intention to maintain a slower pace in its Commercial Lending Services business and the commercial mortgage growth therein (in order to improve capital ratios as well as overall investment returns on a risk-weighted basis) and to take a more conservative credit approach in its single family and mixed-use businesses. However, during the latter half of 2009, Equitable Trust increased its sales efforts, within the context of ongoing lending and risk management discipline, commensurate with improving real estate markets and the increasing comfort that management has with credit conditions. These facts are evidenced in the funding results expressed in Table 7. The Company funded $2.3 billion of mortgages during 2009, on par with 2008. Consistent with the Company's corporate objectives, the Company funded $397.7 million through its Single Family Lending Services business during 2009, $167.2 of which was funded in the fourth quarter of the year. Through its Commercial Mortgage – Broker Services business, the Company funded $105.7 million in mortgages in 2009 compared to $165.1 million in 2008. During 2009, the Company continued to focus its Commercial Lending Services business on those niches that offer the best potential return, including CMHC-insured mortgages on multi-family apartment buildings. Commercial Lending Services originated a total of $1.8 billion of mortgages during the year, comprised of $1.6 billion of CMHC-insured mortgages, $26.7 million of construction loans, and $139.1 million of other conventional mortgages.

Table 7: Mortgage production – by lending business

	2009		2008			
($ THOUSANDS)	**Mortgage principal funded**	**% of total**	Mortgage principal funded	% of total	Change from 2008	
Single Family Lending Services	**$ 397,684**	**17.5%**	$ 609,887	26.1%	$ (212,203)	(34.8%)
Commercial Mortgage — Broker Services	**105,690**	**4.7%**	165,069	7.1%	(59,379)	(36.0%)
Commercial Lending Services:[(1)]						
CMHC-insured multi-unit residential	**1,603,357**	**70.5%**	1,253,345	53.8%	350,012	27.9%
Conventional mortgages	**165,806**	**7.3%**	302,292	13.0%	(136,486)	(45.2%)
Total	**$ 2,272,537**	**100.0%**	$ 2,330,593	100.0%	$ (58,056)	(2.5%)

[(1)] *Does not include $546,846 (2008 – $777,393) of advances related to mortgages held for sale warehouse facilities.*

Table 8: Mortgages held for sale

($ THOUSANDS)	**2009**	2008
Principal balance, beginning of year	**$ 297,952**	$ 272,370
Advances	**546,846**	777,393
Repayments and discharges	**(740,070)**	(751,811)
Principal balance, end of year	**$ 104,728**	$ 297,952
Net change in principal balance	**$ (193,224)**	$ 25,582

The timing of advances and discharges on mortgages held for sale in warehoused mortgage facilities can lead to variability in those balances. During 2009, $546.8 million of advances were made with respect to mortgages held for sale in those facilities. Much of these advances related to CMHC-insured single family warehoused mortgages, in which Equitable continues to see good activity. Despite ongoing disruption in the Commercial Mortgage Backed Securities market, exposure to commercial warehouse facilities was reduced by $82.4 million to $77.9 million at December 31, 2009 from $160.3 million a year earlier. The Company achieved these reductions and was also successful in restructuring and upwardly repricing certain of the facilities in this portfolio.

Credit Quality and Allowance for Credit Losses

Table 9: Mortgage credit quality

($ THOUSANDS)	2009	2008	2007	Change from 2008	
Credit quality measures:					
Gross impaired mortgage principal	**$ 37,562**	$ 39,631	$ 8,617	$ (2,069)	(5.2%)
Allowance for credit losses	**14,635**	14,551	8,925	84	0.6%
Allowance for credit losses as a % of total mortgage principal	**0.53%**	0.48%	0.31%		
Mortgage principal in arrears 90 days or more[(1)]	**17,832**	47,627	8,617	(29,795)	(62.6%)
Mortgage principal in arrears 90 days or more as a % of total mortgage principal[(1)]	**0.64%**	1.57%	0.30%		
Continuity of allowance for credit losses:					
Balance, beginning of year	**$ 14,551**	$ 8,925	$ 8,046		
Provision charged to statement of income	**6,600**	3,450	900		
Allowance for credit losses on acquired portfolio	**–**	2,212	–		
Recovery of prior losses	**108**	–	29		
Realized losses deducted from allowance	**(6,624)**	(36)	(50)		
Balance, end of year	**$ 14,635**	$ 14,551	$ 8,925		

[(1)] Mortgage principal in arrears 90 days or more does not include CMHC-insured mortgages that are less than 365 days in arrears.

Mortgage principal in arrears 90 days or more (excluding CMHC-insured mortgages that are less than 365 days in arrears) improved to 0.64% of total principal outstanding at December 31, 2009 from 1.57% at December 31, 2008. The quarter-over-quarter consecutive improvement in this ratio, which is the result of effective mortgage administration, default management and collections practices, also reflected a relative improvement in real estate market conditions within Equitable's lending regions over the course of the year. Mortgages that were in early stage delinquency, between 30 to 89 days past due, increased from 0.54% of total outstanding principal at December 31, 2008 to 0.68% at December 31, 2009, representing $18.7 million in principal. Management took the prudent step at the end of the third quarter to deem a $19.2 million residential construction mortgage as being impaired, placing a $1.0 million specific allowance against this mortgage in the third quarter and a further $1.0 million allowance in the fourth quarter. The provisions taken reflect the increased credit risk that is associated with this mortgage and the respective borrower. Notwithstanding the increased risk, the interest payments related to this mortgage were up-to-date at December 31, 2009. An independent third party has assessed these properties as having the ability to cover the interest payments from future asset sales and concluded that the outstanding loan balance is lower than certain current appraisals of the properties that secure the mortgage. Inclusion of this mortgage in net impaired mortgages was the primary reason that the impaired mortgages were 1.20% of total mortgage principal at the end of 2009, only slightly lower than the 1.21% reported at the end of 2008. Similarly, the provision for this mortgage resulted in an increased allowance for credit losses as a percentage of total mortgage principal of 0.53% at December 31, 2009 compared to 0.48% reported at December 31, 2008.

Net realized loan losses of $6.5 million incurred during 2009 primarily related to the successful completion of loan workout activities disclosed at the end of 2008. A total specific allowance for losses of $4.3 million was recorded as at December 31, 2009; 98.2% of this specific allowance related to mortgages that are secured by properties located in Ontario, while 1.3% relates to Alberta and 0.5% to Quebec. By way of comparison, 91.5% of the Company's gross impaired mortgages relate to Ontario, 7.1% to Alberta and 1.0% to Quebec. For further information, see Note 7 to the consolidated financial statements.

The Company is actively managing its arrears portfolio and has had to foreclose on certain properties and cause certain properties to either sell or discharge in order to ensure successful collection of the respective mortgage principal. During the year ended December 31, 2009, the Company recognized $0.4 in losses related to foreclosure – none of which were incurred during the fourth quarter of the year. Net fair value of real estate owned as a result of foreclosure was $2.5 million and related to nine remaining single family properties at December 31, 2009. Real estate owned is recorded as held for sale at its net realizable value. Real estate owned at December 31, 2009 has been appraised by third party consultants and the amounts recorded represent management's best estimate of the proceeds to be received on sale. Effective collections management and the improving health of real estate markets have allowed the Company to sell properties and work out problem loans in an expeditious and effective manner, without incurring unreasonable losses.

The quality of the Company's mortgage portfolio continued to reflect the effectiveness and prudence of its underwriting during 2009. The Company does not lend against uninsured mortgages at high loan-to-value ratios, thereby limiting its exposure to loss. As indicated above, given improving real estate markets, increasing interest spreads and the increasing comfort that management has with credit conditions, Equitable has increased its sales efforts. Management actively analyzes the profile of its originations in tandem with external market conditions, including employment conditions. Where management judges that the commensurate risk associated with a particular region or product is no longer acceptable, it adjusts its underwriting criteria to safeguard the future health of its portfolio. When appropriate, Equitable also responds to the changing marketplace with initiatives that result in improved mortgage originations and which continue to ensure a prudent credit risk profile for its portfolio. Management monitors the real estate markets in which it operates to assess the Company's credit risk exposure therein in order to re-evaluate its expectations and the potential need for an increase in general and specific credit loss provisions.

Liquidity Investments and Equity Securities

At December 31, 2009, assets held for the purpose of providing liquidity protection amounted to $763.6 million and consisted of $129.7 million of Government of Canada Bonds that were purchased under reverse repurchase agreements, $238.1 million of MBS, also guaranteed by the Government of Canada, and $395.8 million of cash held with major Canadian banks. Although the cost associated with maintaining excess liquidity compresses net interest margin, management continues to believe that the maintenance of higher than normal levels of liquidity on its balance sheet is a prudent measure, intended to insulate the Company's business from unexpected and unforeseen events that may impact liquidity during the current period of economic uncertainty in the Canadian and international capital markets.

Management closely monitors its liquidity position. Management believes that the liquid capital resources that the Company has at its disposal, together with its ability to raise GIC deposits, are sufficient to meet the requirements of its funding commitments, as well as ensure the collection of its receivables and the discharge of its liabilities and other obligations. Liquidity is used by the Company to manage its funding needs, which include the funding of $318.9 million in mortgage commitments issued by the Company that were outstanding at December 31, 2009 ($94.4 million at December 31, 2008). Given the indications of relative stability that have returned to capital markets in recent months, management has begun to slowly reduce the level of assets that are held for the purpose of providing liquidity protection. Nonetheless, the assets held to provide liquidity protection amounted to 19.9% of Equitable Trust's total assets at December 31, 2009, as compared to 20.1% at December 31, 2008. In addition to assets that are held for the purpose of providing liquidity protection, other liquid assets held by the Company include other deposits held with the Company's bank and the Company's investment in preferred shares.

Equity securities in which the Company invests are comprised of preferred shares that are held to yield tax-preferred dividend income, which are classified as available for sale assets for financial instrument accounting purposes. As such, unrealized changes in fair value on this portfolio are included in the Company's other comprehensive income. At December 31, 2009, equity securities were $53.2 million or 55.0% higher than at December 31, 2008. The increased balance from December 31, 2008 resulted from a combination of sales, redemptions, purchases and the change in unrealized losses in the market values of the preferred shares caused by volatility in Canadian stock markets. Total net unrealized losses related to the equity portfolio as at December 31, 2009 amounted to $9.0 million compared to $30.5 million at December 31, 2008, as a result of preferred share price increases that moderated previous declines in value. Tax-exempt dividend income from equity securities assists in lowering the Company's effective tax rate, which was 24.7% for the year ended December 31, 2009 compared to the Company's statutory income tax rate of 32.4%. Unrealized changes in fair value on this portfolio affect Equitable Trust's capital ratios.

Table 10: Liquid assets

($ THOUSANDS)	2009	2008	2007	Change from 2008	
Eligible deposits with regulated financial institutions[1]	**$ 395,784**	$ 23,466	$ 15,705	$ 372,318	1,586.6%
Government guaranteed debt instruments:					
Investments purchased under reverse repurchase agreements	**129,721**	698,276	232,120	(568,555)	(81.4%)
Debt securities issued by a Canadian Province or Government of Canada	**–**	24,996	38,851	(24,996)	(100.0%)
Debt securities guaranteed by Government of Canada	**238,061**	73,563	26,064	164,498	223.6%
Assets held for the purpose of providing liquidity protection	**763,566**	820,301	312,740	(56,735)	(6.9%)
Other deposits with regulated financial institutions	**51**	1,659	222	(1,608)	(96.9%)
Equity securities	**149,976**	96,758	155,782	53,218	55.0%
Total liquid assets	**$ 913,593**	$ 918,718	$ 468,744	$ (5,125)	(0.6%)
Total liquid assets as a % of total assets	**23.8%**	22.5%	13.7%		
Total assets held for the purpose of providing liquidity protection as a % of total Equitable Trust assets	**19.9%**	20.1%	9.2%		

[1] *Eligible deposits with regulated financial institutions represent deposits of Equitable Trust which are held with major Canadian banks and excludes $5.0 million (2008 – $8.4 million, 2007 – $5.0 million) of restricted cash held as collateral by a third party for the Company's interest rate swap transactions.*

Securitization Retained Interests

The Company periodically securitizes mortgages primarily to diversify funding sources and enhance liquidity positions. The Company securitizes CMHC-insured mortgages through the creation of MBS, and the ultimate sale of MBS through the CMB Program. Equitable either directly or indirectly retains the responsibility for the servicing of the underlying mortgages. See Note 1 of the consolidated financial statements for the accounting policy on securitization retained interests.

Securitization retained interests increased $45.4 million to $147.2 million at December 31, 2009 from $101.8 million at December 31, 2008. Total mortgages in the CMHC MBS program outstanding at December 31, 2009 were $4.1 billion, a $1.3 billion increase from $2.8 billion outstanding at December 31, 2008. Securitization retained interests represent the discounted future earnings to be received relating to the insured mortgages securitized through the CMHC MBS Program. Securitization retained interests are presented gross of the estimated future servicing liability included in other liabilities for securitizations entered into after July 1, 2001. For securitizations entered into prior to this date, the servicing liability and the future excess interest spread are reported on a net basis. For further information, see Note 5 to the consolidated financial statements, as well as and the "Critical Accounting Estimates" and "Off-Balance Sheet Arrangements and Derivative Financial Instruments" sections of this MD&A.

Deposit Liabilities

As a regulated CDIC member, Equitable Trust's ability to fund its mortgage businesses by attracting depositors and providing excellent service is critical to its business. Deposits, which are primarily in the form of GICs, provide a reliable and stable source of funding that can be properly matched against mortgage maturities. Customer deposits are used to fund most of the Company's liquidity needs, including asset acquisitions, and consist of GIC deposits sourced primarily through a national distribution network of independent deposit agents. This has historically been, and continues to be, a deep and liquid market.

Total deposit principal outstanding decreased $345.3 million or 9.5% to $3.3 billion at year end from $3.6 billion of the prior year. At year end, cashable GICs represented 21.1% of total deposits outstanding versus 22.9% in 2008. The Company's cashable GIC is a one-year product, cashable after its initial 30-day term at any time upon demand. Other GIC products consist of 30-day to five-year fixed term GICs. Equitable Trust is licensed to accept deposits in all Canadian jurisdictions.

Table 11: Deposits

($ THOUSANDS)	2009	2008	2007	Change from 2008	
Cashable GIC deposits	$ 688,782	$ 826,438	$ 710,194	$ (137,656)	(16.7%)
Fixed-term GIC deposits	2,582,186	2,789,869	2,330,040	(207,683)	(7.4%)
Accrued interest on deposits	71,798	85,363	72,507	(13,565)	(15.9%)
Deferred deposit agent commissions	(10,447)	(9,101)	(8,217)	(1,346)	14.8%
Total	$ 3,332,319	$ 3,692,569	$ 3,104,524	$ (360,250)	(9.8%)

Subordinated Debentures and Bank Term Loans

Subordinated debentures are subordinated to the rights of Equitable Trust's depositors and other creditors. Such debentures form an integral part of regulatory capital. Subordinated debentures are issued for a period of 10 years. The Company can elect to redeem these debentures during their term subject to the approval of OSFI. During the first nine months of 2009, $3.8 million of Series 5 subordinated debentures ("Series 5") held by the Company was redeemed in separate transactions. As part of these transactions the Company repaid $3.8 million of its bank term loans.

In December 2009, the Company issued $23.2 million in Series 8 subordinated debentures ("Series 8"), a new class of subordinated debt. Equitable Trust concurrently redeemed the remaining $30.8 million of its Series 5, $13.3 million of which was held by the Company. As part of this transaction, the Company repaid $13.3 million of its bank term loans. The gross proceeds of the offering of the Series 8 were used by the Company to purchase subordinated debentures of Equitable Trust, which qualify as Tier 2B regulatory capital and will, in turn, be used for general corporate purposes. The Series 8 will pay fixed interest semi-annually for the first five years of its 10-year term, and then bear a floating interest rate that is calculated at the 90-day Banker's Acceptance Rate plus 480 basis points thereafter.

The Company is in compliance with all of the covenants required by its bank loan facility.

Table 12: Subordinated debentures and bank term loans

($ THOUSANDS)		2009	2008	2007	Change from 2008	
Subordinated debentures						
Series 5	7.31% – 7.58%	$ –	$ 17,519	$ 17,519	$ (17,519)	(100.0%)
Series 6	7.27%	5,000	5,000	5,000	–	– %
Series 7	7.10%	9,450	9,450	9,450	–	– %
Series 8	6.50%	23,221	–	–	23,221	N/A
Total subordinated debentures		$ 37,671	$ 31,969	$ 31,969	$ 5,702	17.8%
Bank term loans						
	6.37%	$ –	$ 17,095	$ 17,095	$ (17,095)	(100.0%)
	6.82%	15,000	15,000	15,000	–	– %
	6.41%	12,500	12,500	12,500	–	– %
Total bank term loans		$ 27,500	$ 44,595	$ 44,595	$ (17,095)	(38.3%)
Total subordinated debentures and bank term loans		$ 65,171	$ 76,564	$ 76,564	$ (11,393)	(14.9%)

Other Assets, Future Income Taxes and Other Liabilities

Other assets decreased $18.3 million or 51.5% to $17.3 million from $35.6 million a year earlier. Other assets include fair value on derivative financial instruments, income taxes recoverable, real estate held for sale, capital assets consisting of leasehold improvements, office furniture and computer equipment and sundry receivables and prepaid expenses. During the year, items affecting this aggregate balance included a $7.4 million reduction in income taxes recoverable, much of which related to a reversal of unrealized losses in the Company's preferred share portfolio and a $14.5 million reduction in unrealized interest rate swap mark-to-market balances, offset by a $2.6 million increase in the value of other derivative financial instruments and a $2.5 million increase in real estate owned.

Other liabilities include the future servicing liability of securitized mortgages, realty taxes collected from borrowers, accounts payable and accrued liabilities, and the fair value of derivative financial instruments. Securitized mortgage servicing liability relates to the Company's estimate of the future cost of servicing the mortgages that have been previously securitized.

Future income taxes payable result from differences between the measurement of assets and liabilities for financial statement purposes versus measurement for tax purposes. A large portion of future taxes relates to the Company's securitization activities net of its general allowance for credit losses. On a year-over-year basis, future income taxes increased primarily as a result of future taxes that will be paid by the Company on the residual cash flows that will be received in future periods from its loan securitizations.

Table 13: Other assets, future income taxes and other liabilities

($ THOUSANDS)	**2009**	2008	2007	Change from 2008	
Other assets:					
Other receivables and prepaids	**$ 5,434**	$ 6,334	$ 3,586	$ (900)	(14.2%)
Income taxes recoverable	**4,187**	11,588	3,382	(7,401)	(63.9%)
Real estate owned	**2,518**	–	–	2,518	N/A
Derivative financial instruments – securitization activities	**2,358**	–	–	2,358	N/A
Capital assets	**2,211**	2,536	2,857	(325)	(12.8%)
Derivative financial instruments – interest rate swaps	**294**	14,836	539	(14,542)	(98.0%)
Derivative financial instruments – hedges	**264**	–	–	264	N/A
Mortgage commitments	**–**	296	63	(296)	(100.0%)
Total	**$ 17,266**	$ 35,590	$ 10,427	$ (18,324)	(51.5%)
Future income taxes and other liabilities:					
Securitized mortgage servicing liability	**$ 40,606**	$ 19,945	$ 5,953	$ 20,661	103.6%
Future income taxes	**19,999**	17,839	7,945	2,160	12.1%
Mortgagor realty taxes	**10,317**	9,048	6,616	1,269	14.0%
Accounts payable and accrued liabilities	**3,787**	3,505	2,858	282	8.0%
Mortgage commitments	**14**	–	–	14	N/A
Derivative financial instruments – securitization activities	**–**	3,527	1,996	(3,527)	(100.0%)
Derivative financial instruments – hedges	**–**	408	–	(408)	(100.0%)
Total	**$ 74,723**	$ 54,272	$ 25,368	$ 20,451	37.7%

Shareholders' Equity

Total shareholders' equity increased $109.7 million or 41.5% to $373.9 million at December 31, 2009 from $264.1 million at December 31, 2008.

In 2009, the Company issued 2.0 million non-cumulative 5-year rate reset Series 1 preferred shares at a price of $25.00 per share for gross proceeds of $50.0 million. The Company used the proceeds from the offering to acquire non-cumulative 5-year rate reset Series 1 preferred shares from Equitable Trust, which qualify as Tier 1 regulatory capital for Equitable Trust. The Series 1 preferred shares yield 7.25% annually, payable quarterly as and when declared by the Board of Directors for an initial period ending September 30, 2014. Thereafter, the dividend rate will reset every five years at a level of 4.53% over the then five-year Government of Canada bond yield.

Subject to regulatory approval, the Company may redeem all or part of the outstanding Series 1 shares, at its option, without the consent of the holder, by payment in cash of $25.00 per share with all declared and unpaid dividends on September 30, 2014 and on September 30 every five years thereafter.

Holders of Series 1 preferred shares, subject to certain conditions, have the option to convert their shares to non-cumulative floating rate Series 2 preferred shares on September 30, 2014 and on the fifth anniversary thereafter. Holders of the Series 2 preferred shares will be entitled to a floating quarterly dividend rate equal to the 90-day Canadian Treasury Bill Rate plus 4.53%, as and when declared by the Board.

In 2008, the Company issued 1.9 million common shares at a price of $21.50 per share for gross proceeds of $40.9 million. Included in this issuance were 1.7 million common shares issued by public offering and 0.2 million common shares issued under private placement to Emberwood Glen Enterprise Ltd., a wholly-owned subsidiary of Oakwest Corporation Limited, whose controlling shareholders are directors of the Company. The Company used the proceeds, after deducting certain underwriting, legal and other expenses, to invest $38.9 million in the equity of Equitable Trust, in order to augment its Tier 1 regulatory capital base and support its continued growth, as well as for general corporate purposes.

On March 4, 2009, the Company announced the introduction of a Dividend Reinvestment Plan ("DRIP"). Participation in the plan is optional and under the terms of the plan, cash dividends on common shares are used to purchase additional common shares at the volume weighted average trading price of the common shares on the Toronto Stock Exchange for the five trading days immediately preceding the dividend payment date. Common shares issued as a result of participation in the DRIP are issued from the Company's treasury. During the year ended December 31, 2009, 11,136 common shares were issued under the DRIP.

At December 31, 2009, the Company had 14,903,846 common shares issued and outstanding compared to 14,882,710 common shares issued and outstanding at December 31, 2008. During 2009, 172,000 options were granted and 10,000 stock options were exercised that contributed $0.2 million to common share capital. At December 31, 2009, there were 814,750 unexercised stock options, which are or will be exercisable, to purchase 814,750 common shares for maximum proceeds of $19.3 million.

The Company paid an annual dividend of $0.40 per common share in 2009, consistent with the dividend paid in 2008. At the date of this report, the Company has 14,909,743 common shares issued and outstanding.

The Company paid the initial dividend on the Series 1 preferred shares on December 31, 2009, which was $0.605822 per share.

Table 14: Shareholders' equity

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	2009	2008	2007	Change from 2008	
Shareholders' equity:					
Preferred shares	**$ 48,523**	$ –	$ –	$ 48,523	N/A
Common shares	**127,424**	126,993	87,062	431	0.3%
Contributed surplus	**3,267**	2,553	1,778	714	28.0%
Retained earnings	**193,635**	149,365	116,325	44,270	29.6%
Accumulated other comprehensive income (loss)	**1,012**	(14,765)	(1,995)	15,777	106.9%
Total shareholders' equity	**$ 373,861**	$ 264,146	$ 203,170	$ 109,715	41.5%
Dividends on common shares	**$ 5,956**	$ 5,571	5,081	$ 385	6.9%
Dividends per common share	**$ 0.40**	$ 0.40	$ 0.40	$ –	– %
Dividends on preferred shares	**$ 1,212**	$ –	–	$ 1,212	N/A
Dividends per preferred share	**$ 0.61**	$ –	–	$ 0.61	N/A

Capital Management

Equitable Trust manages its capital in accordance with guidelines established by OSFI, based on standards issued by the Bank for International Settlements, Basel Committee on Banking Supervision ("Basel II"). In order to determine prudent capital levels and govern the quality and quantity of capital necessary to maintain the business based on its inherent risks, Equitable Trust utilizes an Internal Capital Adequacy Assessment Process ("ICAAP").

The Company has been successful in shifting its business to lower risk-weighted assets and in retaining its earnings. Equitable Trust's total capital ratio (when general allowance is included in capital) increased by 410 basis points to 17.6% at December 31, 2009 from 13.5% at December 31, 2008. Equitable Trust's Tier 1 regulatory capital position was significantly stronger at December 31, 2009 at 14.6% compared to 10.1% at December 31, 2008. As at December 31, 2009, tangible common equity was 12.6% as compared to 10.1% one year earlier. Tangible common equity ratio (a non-GAAP measure) is defined as shareholder's equity plus any qualifying other non-controlling interest in subsidiaries less preferred shares issued and outstanding, any goodwill, other intangible assets and certain components of accumulated other comprehensive income, as a percentage of risk-adjusted assets less other intangible assets. Tangible common equity ratio is considered by management and many investors and investment analysts to be a key measure of capital strength. This ratio is particularly strong compared to that of the Canadian chartered banks, which themselves are regarded as well-capitalized by international standards.

Equitable Trust is positioned to maintain strong capital levels through the retention of earnings and the management of its risk-weighted asset mix. As the need arises, the Company also intends to investigate opportunities that will allow it to raise non-dilutive forms of additional capital.

Table 15: Capital measures (relating solely to Equitable Trust)

($ THOUSANDS)	**December 31, 2009**	December 31, 2008	January 1, 2008
Risk weighted assets:			
Credit risk	**$ 2,355,526**	$ 2,423,996	$ 2,510,966
Operational risk[1]	**154,352**	125,086	100,724
Total risk-weighted assets	**$ 2,509,878**	$ 2,549,082	$ 2,611,690
Tier 1 capital:			
Common shares	**$ 129,337**	$ 128,162	$ 87,621
Non-cumulative preferred shares	**50,000**	–	–
Contributed surplus	**2,852**	2,138	1,363
Retained earnings	**189,715**	146,901	114,645
Accumulated other comprehensive loss[2]	**(5,953)**	(20,330)	(2,982)
Total	**365,951**	256,871	200,647
Tier 2 capital:			
Subordinated debentures (Tier 2B)[3]	**65,171**	76,564	76,564
Total	**65,171**	76,564	76,564
Total regulatory capital	**$ 431,122**	$ 333,435	$ 277,211
Regulatory capital to risk-weighted assets:			
Tier 1 capital	**14.6%**	10.1%	7.7%
Tier 2 capital	**2.6%**	3.0%	2.9%
Total regulatory capital as a % of total risk-weighted assets	**17.2%**	13.1%	10.6%
Total capital calculated as defined under ICAAP:			
Total regulatory capital	**$ 431,122**	$ 333,434	$ 277,211
General allowance[4]	**10,339**	11,651	8,775
Total capital as defined under ICAAP	**$ 441,461**	$ 345,085	$ 285,986
Total capital ratio for ICAAP purposes	**17.6%**	13.5%	11.0%

(1) For operational risk, Equitable Trust uses the Basic Indicator Approach – calculated as 15% of the previous three-year average of net interest income and other income, excluding gain or loss on investments. The risk-weighted equivalent is determined by multiplying the capital requirement for operational risk by 12.5.

(2) As prescribed by OSFI, certain components of accumulated other comprehensive income are included in the determination of regulatory capital. Net unrealized fair value losses on available for sale equity securities are deducted in the determination of Tier 1 capital while net unrealized fair value gains on available for sale equity securities are included in Tier 2A capital.

(3) Tier 2B capital may be included in Tier 2 capital to a maximum of 50% of net Tier 1 capital.

(4) Equitable Trust includes its general allowance in capital when assessing its capital requirements under its ICAAP.

Summary of Quarterly Results

Table 16 summarizes the Company's performance over the last eight quarters. Equitable does not expect material seasonality in its earnings, but changes in short-term interest rates and volumes of mortgages securitized may cause some volatility in earnings from quarter to quarter as described elsewhere in this MD&A.

Table 16: Summary of quarterly results

($ THOUSANDS, EXCEPT BALANCE SHEET AND OFF-BALANCE SHEET ITEMS AND PER SHARE AMOUNTS)	2009				2008			
	Q4	**Q3**	**Q2**	**Q1**	Q4	Q3	Q2	Q1
OPERATIONS								
Net income	**15,572**	**12,045**	**11,877**	**11,944**	7,894	10,752	10,280	9,685
EPS – basic	**$ 0.96**	**$ 0.81**	**$ 0.80**	**$ 0.80**	$ 0.53	$ 0.74	$ 0.79	$ 0.75
EPS – diluted	**$ 0.96**	**$ 0.81**	**$ 0.80**	**$ 0.80**	$ 0.53	$ 0.74	$ 0.79	$ 0.74
Net interest income	**21,113**	**19,547**	**17,503**	**15,006**	14,862	16,398	15,473	17,610
Net interest margin – TEB	**2.4%**	**2.2%**	**1.9%**	**1.6%**	1.5%	1.7%	1.8%	2.2%
Total revenues	**50,891**	**50,748**	**50,758**	**55,427**	56,613	61,488	55,852	52,813
Return on equity – annualized	**17.9%**	**15.7%**	**16.5%**	**17.8%**	11.8%	16.7%	19.1%	18.8%
Return on average assets – annualized	**1.6%**	**1.3%**	**1.3%**	**1.2%**	0.8%	1.1%	1.2%	1.1%
Productivity ratio – TEB	**25.1%**	**25.7%**	**24.4%**	**24.3%**	32.7%	24.9%	26.8%	26.0%
Conventional mortgage production	**272,168**	**197,338**	**139,557**	**60,117**	174,059	355,907	350,106	197,176
CMHC-insured multi-unit residential production	**368,419**	**257,144**	**505,762**	**472,032**	260,209	450,881	439,611	102,644
Mortgages held for sale warehouse advances	**65,144**	**126,122**	**85,483**	**270,097**	356,776	170,105	180,054	70,458
BALANCE SHEET AND OFF-BALANCE SHEET ($ millions)								
Total assets	**3,846**	**3,688**	**3,719**	**3,889**	4,088	4,094	3,814	3,368
Mortgages receivable	**2,763**	**2,829**	**2,857**	**2,895**	3,023	3,036	2,916	2,811
Shareholders' equity	**374**	**359**	**297**	**281**	264	268	221	212
Book value per common share	**$ 21.83**	**$ 20.86**	**$ 19.94**	**$ 18.90**	$ 17.75	$ 17.98	$ 17.03	$ 16.35
Mortgage backed security assets under administration	**4,093**	**3,792**	**3,537**	**3,232**	2,825	2,629	2,285	1,970

Fourth Quarter Overview

During the three months ended December 31, 2009:

- net income was $15.6 million, an increase of 97.3% from the fourth quarter of 2008;
- diluted earnings per share were $0.96 compared to $0.81 in the immediately preceding quarter and $0.53 in the fourth quarter of 2008; and
- ROE was 17.9% compared to 11.8% in the fourth quarter of 2008.

In terms of the lines of business it operates, during the quarter:

- Single Family Lending Services production was $167.2 million, or 63.1% higher than the $102.5 million of the corresponding period of 2008;
- Commercial Mortgage – Broker Services production increased to $42.6 million compared to $16.8 million in the fourth quarter of 2008; and
- Commercial Lending Services production was $430.7 million, compared to $314.9 million in the fourth quarter of 2008. Of the 2009 fourth quarter production, $368.4 million related to CMHC-insured multi-unit residential mortgages that were originated for the purpose of being securitized and sold to government sponsored programs, compared to $260.2 million in the fourth quarter of 2008.

During the fourth quarter, the balance of average interest-earning assets was $3.6 billion, down 9.0% from $4.0 billion in the same period a year ago. As a result of this, as well as lower interest lending rates, mortgage interest income decreased 10.7% to $40.9 million compared to $45.9 million a year earlier. Nonetheless, net interest income increased $6.3 million or 42.1% from the same quarter a year ago, primarily due to reductions in funding costs, as well as the effect of implementing interest rate floors on variable rate mortgages and improved pricing on new and renewing mortgages in earlier quarters of 2009.

The Company held a larger proportion of its liquidity in the form of Government of Canada guaranteed debt securities in 2009, during a period that interest rates have significantly decreased, whereas its liquidity position was primarily held in the form of other short-term investments during significant periods of the prior year. Interest on Government guaranteed debt securities is reported as interest income – investments. Since the interest income related to other short-tem investments is reported under interest income – other, this income balance experienced a significant year-over-year reduction.

Other income increased $2.3 million or 68.8% during the fourth quarter of 2009, primarily as a result of a $1.7 million increase in securitization gains. During the quarter, the Company securitized and sold $344.9 of mortgages compared $281.0 in the corresponding quarter of 2008.

Non-interest expenses increased $0.8 million in the fourth quarter compared to the same quarter of 2008. As a component of non-interest expenses, compensation costs for the quarter increased $0.5 million or 14.1% reflecting higher staffing levels during the quarter compared to the corresponding period of 2008.

Income tax expense was affected by downward adjustments made during the quarter in relation to lower future tax rates that were enacted in Ontario as well an annual recalibration of the increased amount of business that the Company carried out in Alberta, which bears a lower tax rate than Ontario.

At December 31, 2009, book value per share was $21.83 compared to $17.75 at the close of the prior year.

Table 17: Unaudited interim consolidated statements of income – fourth quarters 2009 and 2008

($ THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)	For the three months ended December 31, 2009	December 31, 2008
Interest income:		
Mortgages	**$ 40,939**	$ 45,855
Investments	**3,701**	2,119
Other	**614**	5,300
	45,254	53,274
Interest expense:		
Customer deposits	**20,651**	35,243
Deposit agent commissions	**1,965**	1,825
Bank term loans	**972**	754
Subordinated debentures	**553**	590
	24,141	38,412
Net interest income	**21,113**	14,862
Provision for credit losses	**2,250**	1,550
Net interest income after provision for credit losses	**18,863**	13,312
Other income:		
Fees and other income	**706**	526
Net gain (loss) on investments	**14**	(453)
Gains on securitization activities and income from retained interests	**4,917**	3,266
	5,637	3,339
Net interest income and other income	**24,500**	16,651
Non-interest expenses:		
Compensation and benefits	**4,133**	3,622
Other	**2,888**	2,585
	7,021	6,207
Income before income taxes	**17,479**	10,444
Income taxes (recovery):		
Current	**1,327**	(1,271)
Future	**580**	3,821
	1,907	2,550
Net income	**15,572**	7,894
Dividends on preferred shares	**1,212**	–
Net income available to common shareholders	**$ 14,360**	$ 7,894
Earnings per share:		
Basic	**$ 0.96**	$ 0.53
Diluted	**$ 0.96**	$ 0.53
Weighted average number of common shares outstanding:		
Basic	**14,897,076**	14,882,710
Diluted	**14,969,290**	14,882,710

Table 18: Unaudited interim consolidated statements of comprehensive income – fourth quarters 2009 and 2008

	For the three months ended	
($ THOUSANDS)	**December 31, 2009**	December 31, 2008
Net income	**$ 15,572**	$ 7,894
Other comprehensive income (loss), net of tax:		
Available for sale investments:		
Net unrealized gains (losses) from change in fair value[1]	**2,397**	(9,929)
Reclassification of net gains to income[2]	**(970)**	(168)
Other comprehensive income (loss)	**1,427**	(10,097)
Comprehensive income (loss)	**$ 16,999**	$ (2,203)

[1] *Net of income tax expense of $1,149 (2008 – tax benefit of $4,955).*
[2] *Net of income tax benefit of $465 (2008 – tax benefit of $84).*

Table 19: Unaudited interim consolidated statements of cash flows – fourth quarters 2009 and 2008

($ THOUSANDS)	For the three months ended December 31, 2009	December 31, 2008
Cash provided by (used in):		
Operating activities:		
Net income	**$ 15,572**	$ 7,894
Non-cash items:		
Financial instruments - fair value adjustments	**(2,168)**	(4,616)
Securitization gains	**(4,131)**	(2,108)
Amortization of capital assets	**161**	215
Provision for credit losses	**2,250**	1,550
Net (gain) loss on investments	**(27)**	195
Future income taxes	**580**	4,519
Stock-based compensation	**161**	208
Amortization of premiums on investments, net	**255**	184
	12,653	8,041
Changes in operating assets and liabilities:		
Other assets	**(4,016)**	(2,768)
Other liabilities	**(1,642)**	3,829
	6,995	9,102
Financing activities:		
Increase (decrease) in customer deposits	**145,417**	(24,625)
Repayment of bank term loan	**(13,284)**	–
Issuance of subordinated debentures	**23,221**	–
Redemption of subordinated debentures	**(17,519)**	–
Dividends paid on preferred shares	**(1,212)**	–
Dividends paid on common shares	**(1,299)**	(1,488)
Preferred share issuance expenses	**(76)**	–
Issuance of common shares	**104**	(698)
	135,352	(26,811)
Investing activities:		
Purchase of investments	**(215,521)**	–
Proceeds on sale or redemption of investments	**199,781**	8,602
Purchase of investments purchased under reverse repurchase agreements	**(129,721)**	(698,276)
Proceeds on sale or redemption of investments purchased under reverse repurchase agreements	**126,230**	748,183
Change in restricted cash	**3,070**	(3,422)
Increase in mortgages receivable	**(713,019)**	(803,587)
Mortgage principal repayments	**368,031**	516,323
Proceeds from loan securitizations	**348,011**	282,998
Securitization retained interests	**7,892**	6,318
Purchase of capital assets	**(81)**	(294)
	(5,327)	56,845
Increase in cash and cash equivalents	**137,020**	39,136
Cash and cash equivalents, beginning of period	**258,815**	10,985
Cash and cash equivalents, end of period	**$ 395,835**	$ 50,121

Changes in Accounting Policies

The Company's significant accounting policies are essential to an understanding of its reported results of operations and financial position. A summary of the Company's significant accounting policies is presented in Note 1 to the consolidated financial statements.

Future Accounting Changes

International Financial Reporting Standards:

Canadian Public Companies are required to prepare their financial statements in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), for financial years beginning on or after January 1, 2011. Equitable will transition to IFRS on this date.

In order to meet the transition requirements, management has developed a project plan that is arranged according to the following phases:

- Impact assessment of IFRS
- Requirements gathering, detailed review of IFRS and adoption planning
- Results delivery (selection of IFRS policies)
- Training and communication
- Refinement or updating of policy selection choices (for IFRS changes that are instituted prior to 2011)

The major differences identified, as applicable to the Company, between IFRS and Canadian GAAP are as follows:

- Certain financial assets that previously qualified for derecognition on transfer are expected to be re-recognized under IFRS. This would result in an adjustment to retained earnings intended to unwind the previously reported impact of all securitization transactions since January 1, 2004, and retroactively re-recognize the assets that were previously considered to have been sold as amortizing assets that continue to reside on the Company's balance sheet, earning spread interest income over the course of their term.
- Changes are expected to the impairment methodology followed by the Company in order to meet the requirements of IFRS. More emphasis will be placed on objective evidence of loss events and historical loss events and the extrapolation thereof to the entire portfolio. The amount of the impairment allowance is not expected to differ materially.
- Additional disclosure is required on transition for the first IFRS compliant financial statements per IFRS 1 *"First Time Adoption of IFRS."* As a result, transition reconciliations will be prepared for both the March 31, 2011 and December 31, 2011 financial statements.
- Additional and enhanced disclosure as required by IFRS to enable users to further understand the transactions and circumstances that affect the Company during the reporting period.

Pursuant to the re-recognition of securitized assets, discussed above, an area of significant anticipated IFRS impact relates to the Company's past securitization activities. Under the current IFRS regime and a recent draft advisory that has been tabled for discussion with federally regulated entities by OSFI that deals with the regulatory implications of IFRS conversion on regulatory capital, the Company anticipates being required to include its CMB and MBS securitization activities entered into after December 31, 2009 within its regulatory assets-to-capital multiple ("ACM") limit. Prior to converting to IFRS, mortgage assets securitized through the CMB and MBS programs have been held off-balance sheet and have therefore not been included in this multiple. In March 2009, the IASB published an exposure draft to replace the requirements in International Accounting Standard ("IAS") 39 *Financial Instruments: Recognition and Measurement* and to improve the disclosure requirements in IFRS 7 *Financial Instruments: Disclosures* relating to the transfer of financial assets and liabilities. Several approaches to the issue of derecognition were proposed as part of this exposure draft. Recently, the IASB has issued commentary that it is tentatively pursuing the alternative approach proposed in the exposure draft and that it is their intention to further develop this approach in accounting for retained interests. Although this approach, as proposed, may impact whether certain of the Company's securitization activities will remain off-balance sheet and, as such, not impact Equitable Trust's ACM, there is no certainty related to the final outcome.

Equitable is on schedule with its IFRS transition plan, having completed the requirements gathering, detailed planning and results delivery phases of the project. Although accounting policy choices are based on current standards issued by the IASB, various standards that are applicable to Equitable may be amended through current projects being undertaken by the IASB. The Company is continuing its training and review efforts to ensure that any of the revisions applicable are identified in a timely manner to facilitate a smooth transition.

The table that follows is a status assessment of the Company's progress on its plan to transition to IFRS, as at December 31, 2009.

Table 20: Status of transition to IFRS at December 31, 2009

Key activity or milestone	Planned completion date	Status
Financial Statement Preparation		
Identification of differences in Canadian GAAP / IFRS accounting policies and IFRS policy selection:		
• Identify differences in Canadian GAAP / IFRS policies	Second quarter, 2009	• Complete
• Select ongoing IFRS accounting policies	Fourth quarter, 2009	• Complete
• Select IFRS 1 exemptions and exceptions (at transition)	Fourth quarter, 2009	• Complete
• Develop financial statement format	Second quarter, 2010	• Significant progress made, on schedule
• Quantify effects of transition to IFRS	First quarter, 2010	• Significant progress made, on schedule
Infrastructure		
IFRS expertise identification and development at levels of:		
• Accounting staff	Fourth quarter, 2009	• Training program complete, updates as required
• Senior Executives and Board (including audit committee)	Second quarter, 2010	• Training plan on schedule
Information Technology applications IFRS compliant:		
• Program upgrades / changes	Third quarter, 2009	• Impact assessment complete, areas identified
• One off calculations (IFRS 1)	Fourth quarter, 2009	• Infrastructure assessment complete
• Gathering data for disclosures	Fourth quarter, 2009	• Infrastructure assessment complete
Business Policy Assessment		
Financial covenants:		
• Identify impacts on financial covenants (including securitization)	First quarter, 2010	• Impact assessment complete, on schedule
• Complete any required renegotiations / changes	Second quarter, 2010	• Impact assessment complete, on schedule
Compensation arrangements:		
• Identify if arrangements are affected	First quarter, 2010	• Impact assessment to be completed
• Renegotiate arrangements if required	Third quarter, 2010	• Impact assessment to be completed
Capital adequacy:		
• Assess impact on capital plan	First quarter, 2010	• Significant progress made, on schedule
• Amend capital plan if required	Second quarter, 2010	• Significant progress made, on schedule
Control Environment		
Internal Control Over Financial Reporting:		
• For all accounting policy changes identified, assess Internal Control Over Financial Reporting design effectiveness	Third quarter, 2010	• Impact assessment to be completed
• Implement appropriate changes	Fourth quarter, 2010	• Impact assessment to be completed
Disclosure controls and procedures:		
• For all accounting policy changes identified, publish impact of conversion on key performance indicators in MD&A	Third quarter, 2010	• Impact assessment to be completed
• MD&A communications package verification	First quarter, 2011	• Impact assessment to be completed

Critical Accounting Estimates

The Company's critical accounting estimates primarily relate to the areas of credit risk, allowance for credit losses and valuation of securitization retained interests and other financial instruments. The policies and methodologies used to determine these estimates and their significance to the Company's financial condition have been outlined in this MD&A and in Note 1 to the consolidated financial statements.

The allowance for credit losses reflects management's best estimate of probable losses in the Company's mortgage portfolio as at the consolidated balance sheet date. In order to assess the likelihood of a loss, management takes into consideration a broad range of information, including economic factors, developments affecting particular property types and geographic areas, the age of a mortgage and specific issues with respect to individual borrowers. Changes in any of these factors may cause future assessment of credit risk to be significantly different from current assessments and could affect the level of allowance for credit losses being maintained by the Company. The Company's general allowance for credit losses of $10.3 million as at December 31, 2009 represented 0.37% of total mortgage principal outstanding.

The Company uses estimates in valuing retained interests in loan securitizations. This valuation and changes thereto affect the gain on sale of mortgages in a securitization and could affect the measurement of excess interest spread, net of servicing fees. Management uses its best estimates in determining the value of retained interests on each securitization, taking into account current interest rates, the terms of the mortgages being sold, the propensity for prepayment and the cost of the future mortgage servicing. On a quarterly basis, management reassesses its estimates to ensure that these estimates are still valid under the current economic environment. Management uses historical data to support any amendments to its estimation methodology and the carrying value of securitization retained interests. A sensitivity analysis of two adverse changes in the estimate used to value the Company's retained interests in loan securitizations is presented in Note 5 to the consolidated financial statements.

Off-Balance Sheet Arrangements and Derivative Financial Instruments

The Company hedges the interest rate risk on CMHC-insured multi-unit residential mortgages and mortgage commitments intended for securitization, as well as certain other mortgages designated as held for trading. In order to protect against rises in interest rates that can occur between the rate commitment date and the sale date, which can lead to a reduced value of the mortgage upon securitization, the Company enters into Government of Canada guaranteed debt security short sale and repurchase agreements. The hedges act to significantly reduce the likelihood that, as a result of interest rate movements, the proceeds on the sale of the mortgage (comprised of the fair value of the mortgage and the fair value of hedge) will vary from the fair value of the mortgage at the date of rate commitment.

The Company securitizes CMHC-insured residential mortgages through the creation of MBS. These MBS are sold through the CMHC MBS and CMB Programs or are otherwise retained on the Company's consolidated balance sheet. After securitization, the Company retains the rights to certain excess interest spreads and servicing obligations and records these on its consolidated balance sheet as securitization retained interests and servicing liabilities, respectively. The Company administers all securitized mortgages after sale and, upon maturity of the mortgage, will renew these mortgage loans whenever possible. At December 31, 2009, the outstanding securitized mortgage portfolio totaled $4.1 billion (2008 – $2.8 billion) with a securitization retained interest of $147.2 million (2008 – $101.8 million). The servicing liability was $40.6 million (2008 – $19.9 million) at December 31, 2009.

In order to participate in the CMB Program administered by Canada Housing Trust ("CHT"), the Company enters into certain arrangements with accredited counterparties that are intended to secure the cash flows payable to the CHT. The mismatch and reinvestment risk that exists between the amortizing MBS and the CMB is managed by the Company through the retention of replacement assets, in the form of MBS, on its consolidated balance sheet, and their periodic sale to CHT to replace the original MBS that has amortized. Approved counterparties are limited to chartered banks and other financial intermediaries.

With respect to market interest rate exposure on term GICs to fund floating rate mortgages, the Company uses interest rate swaps to manage its interest rate risk as required. The Company has not entered into any complex derivative contracts. For more information on hedges and interest rate swaps see Note 6 to the consolidated financial statements.

Contractual Obligations

Material contractual obligations of the Company at December 31, 2009 are outlined in Table 21.

Table 21: Contractual obligations

		Payments due by period			
($ THOUSANDS)	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
GIC principal and interest	$ 3,489,892	$ 2,036,110	$ 1,100,350	$ 353,432	$ –
Subordinated debentures principal and interest[1]	63,616	2,544	5,088	5,088	50,896
Bank term loans principal and interest	30,592	1,824	28,768	–	–
Operating leases[2]	3,383	575	1,092	1,144	572
Total contractual obligations	$ 3,587,483	$ 2,041,053	$ 1,135,298	$ 359,664	$ 51,468

[1] *Obligations do not include any pre-maturity redemptions relating to Equitable Trust's prior year's net income.*
[2] *Represents minimum lease payments for premises rental.*

In addition to these contractual obligations, the Company is responsible for ongoing servicing for mortgages securitized through the CMHC MBS Program. This obligation is discussed in "Off-Balance Sheet Arrangements and Derivative Financial Instruments" section of this MD&A and Note 5 to the consolidated financial statements for the year ended December 31, 2009. Details related to the Company's bank term loans can be found in Note 12 and details related to the Company's subordinated debentures can be found in Note 13 to the consolidated financial statements. There have been no material changes to contractual obligations that are outside the ordinary course of the Company's business.

Related Party Transactions

Certain of the Company's directors and officers have purchased GICs and subordinated debentures from the Company in the ordinary course of business, at market terms and conditions.

Risk Management

The Company, like other financial institutions, is exposed to the symptoms and effects of global economic conditions and other factors that could adversely affect its business, financial condition and operating results, which may also influence an investor to buy, sell or hold shares in the Company. Many of these risk factors are beyond the Company's direct control. Senior management is responsible for identifying risks and developing an appropriate risk management framework. The Board of Directors and the Committees of the Board play an active role in monitoring the Company's key risks and in determining the policies that are best suited to manage these risks.

The discussion below highlights certain key risks. For additional discussion of the risks that affect this business, please refer to pages 18 to 25 of the Company's Final Short Form Prospectus dated August 24, 2009, which is available on SEDAR at www.sedar.com. The Company cautions that the discussion of risks set out below is not exhaustive.

Credit Risk

Credit risk is defined as the possibility that Equitable will not receive the full value of amounts and recovery costs owed to it if counterparties fail to honor their obligations to the Company.

Equitable Trust's focus is on providing first mortgages on real estate. All mortgages are individually evaluated by underwriters using internal and external credit risk assessment tools and are assigned a risk rating, in accordance with the level of credit risk attributed to each loan. The underwriting approach places a strong emphasis on security evaluation and judgmental analysis of the risks in the transaction rather than being formulaic in nature. As a result, Equitable Trust can underwrite mortgages on favorable terms to borrowers who have good equity and debt service ratios in situations where conventional lenders may typically decline borrowers.

Key components of credit risk that are closely monitored and measured are credit concentration risk and the risk associated with economically-sensitive assets. By way of definition, credit concentration risk results if an unduly large proportion of the Company's lending business involves a single person, organization or group of related persons or organizations, a single geographic area, a single industry or a single category of investment. On a regular basis, management establishes credit limits for exposure to certain counterparties, industries or market segments, monitors these credit exposures, and prepares detailed analyses and reports assessing overall credit risk within the mortgage portfolio.

The Company also invests in preferred share securities to generate returns that meet an acceptable ROE hurdle threshold. These securities represent a potential source of liquidity to the Company. However, such investments expose the Company to credit risk if the issuer of the preferred shares cannot make dividend payments, or in the worst case scenario, if the issuer becomes insolvent.

Securities rated P-2 and higher comprised 61.9% of the preferred share equity securities portfolio at December 31, 2009, compared to 75.6% a year earlier. This year-over-year decrease related to the rating downgrade of a group of connected preferred securities and the net redemption in 2009 of $7.8 million of securities rated P-2 and higher.

Interest Rate Risk

Interest rate risk is defined as the possibility that changes in market interest rates will adversely affect the Company's financial condition. Interest rate risk may be affected if an unduly large proportion of the Company's assets or liabilities have unmatched terms, interest rates or other attributes.

The Company's primary method of managing interest rate risk involves the matching of asset and liability maturity profiles, closely monitoring interest rates and acting upon any mismatch in a timely manner to ensure that any sudden or prolonged change in interest rates does not significantly affect the Company's net interest income.

The Company uses simulated interest rate change sensitivity models to estimate the effects of various interest rate change scenarios on the economic value of shareholders' equity and on net interest income for the 12 months following the measurement date. Certain assumptions that are based on actual experience are built into the simulations, including assumptions related to the pre-maturity redemptions of cashable GICs and early payouts of mortgages.

Management's sensitivity modeling indicates that in the event of an immediate and sustained 1% interest rate increase, net interest income during the 12-month period following December 31, 2009 would increase by $3.9 million. Conversely, if interest rates were to decrease to a floor of 0% (and therefore not be allowed to go negative), net interest income would increase by $0.2 million.

The Company hedges the interest rate risk for all multi-unit residential mortgages that are to be securitized through the CMHC MBS Program. Hedging protects the Company from losses due to changes in interest rates during the relevant period.

The Company also holds replacement assets in the form of MBS in order to reduce the interest rate risk and replacement asset exposure inherent in its participation in the CMB Program.

The Company's earnings are affected by changes in interest rates. The estimate of sensitivity to interest rate changes is dependent on a number of assumptions that could result in a difference in actual outcomes in the event of an actual interest rate change.

Funding Risk

Funding or liquidity risk is defined as the possibility that the Company will be unable to generate or obtain sufficient cash or its equivalents in a timely manner, at a reasonable price, to meet its commitments as they come due. Funding risk may be affected if an unduly large proportion of the Company's deposit-taking business is concentrated in a single person, organization or group of related persons or a single geographic area.

Managing funding risk requires management to keep sufficient liquid assets on hand at all times to meet the mortgage funding needs, investment purchase commitments and GIC redemption and maturity obligations of Equitable Trust. Assets held for the purpose of providing liquidity protection consist of cash and cash equivalents and debt instruments guaranteed by governments that were held by Equitable Trust. These assets amounted to $763.6 million at December 31, 2009 and $820.3 million at December 31, 2008.

The Company adheres to a funding and liquidity risk management policy that provides guidelines relating to the required maintenance of a pool of high quality liquid assets, including asset eligibility, liquidity portfolio composition criteria, minimum liquidity ratios, the measurement and forecast of cash flows, liquidity stress testing and an approved contingency plan. The Company's liquidity position and adherence to the requirements of this policy are monitored daily by management, with quarterly reporting to the Investment Committee of the Board of Directors. As defined in the policy, the stress analysis model considers seven scenarios that incorporate institution-specific and financial market disruptions. In order to establish these scenarios, the Company assesses deposit benchmarks and makes assumptions related to the cash flow behavior of each type of asset and liability. For all scenarios that comprised Equitable's liquidity stress testing conducted during 2009, the Company held sufficient liquidity and funding capacity to meet all funding obligations over the one-year forecasting period.

The Company was in compliance with its liquidity policy at December 31, 2009 and at the date of this report.

Operational Risk

Operational risk is the possibility that a loss will result from inefficient, inadequate or failed internal processes, people or systems or from external events. As a minimum, operational risk takes into account the following:

- regulatory, legal and contractual obligations;
- fraud;
- employee practices and workplace safety;
- client, product and business practices;
- damage to physical assets;
- business disruptions and system failures; and
- execution, delivery and process management.

The Company maintains a control environment to manage these risks, recognizing that operational risks may arise in the normal course of business.

Changes to laws and regulations, including changes in their interpretation or application, could affect the Company, limiting the products or services it may provide and increasing the ability of competitors to compete with Equitable's products or services. Failure to comply with applicable laws and regulations could result in sanctions and financial penalties that could adversely impact earnings and damage the Company's reputation. Management undertakes reasonable and prudent measures designed to achieve compliance with governing laws and regulations including Equitable's legislative compliance management framework.

Control/Management Risk

Control/management risk is the possibility that the Company will experience control or management deficiencies due to limitations typically found in smaller institutions that may have insufficient resources and capacities to establish appropriate governance systems and controls.

Equitable's operations depend on the abilities, experience and efforts of management and other key employees. Should any of these persons be unable or unwilling to continue in their employment, this could potentially have a material adverse effect on the business, financial condition and results of the operations of the Company.

Strategic Risk

Strategic risk is defined as the possibility that the Company's ability to implement its strategy successfully over the next three-to-five years will be affected by changes in the business environment, technological limitations, adverse business decisions, unsuccessful implementation of decisions or lack of responsiveness to changes in the business environment.

The Company manages strategic risk through a comprehensive annual strategic planning process, which includes establishing Board-approved business growth strategies and quantifiable performance targets for each business unit over the forthcoming three-year period. Management of this risk includes regular monitoring of actual versus forecasted performance and reporting to senior management and to the Board of Directors.

Business Risk

Business risk is the possibility that an unfavorable development of business factors will lead to an operating result that varies from the expected result for the current year and beyond.

The residential and commercial first mortgage business is highly competitive and Equitable Trust's products compete with those offered by other trust companies, banks, insurance companies, and other financial institutions in the jurisdictions in which it operates, especially in Ontario and Alberta. Many of these companies are strongly capitalized and hold a larger percentage share of the Canadian residential and commercial mortgage business. There is always a risk that there will be new entrants in the market with more efficient systems and operations that could impact the Company's market share in its mortgage lending and deposit-taking activities.

The Company's business model does not use retail branches to originate GICs or mortgages. Through its deposit-taking activities, Equitable Trust relies on business conducted on behalf of investing clients by members of the Investment Industry Regulatory Organization of Canada and the Registered Deposit Brokers Association, formerly the Federation of Canadian Independent Deposit Brokers, to raise funds. Mortgage originations depend on a network of independent mortgage brokers, mortgage brokerage firms and other mortgage banking organizations. Under adverse circumstances, it may be difficult to attract new deposits from agents or mortgage business from brokers to sustain current operating requirements. The potential failure to sustain or increase current levels of deposits or mortgage originations from these sources could negatively affect the financial condition and operating results of the Company. A single mortgage broker, FNFLP, originated 22% of the Company's outstanding on-balance sheet mortgages at December 31, 2009. Management believes it has a strong relationship with FNFLP. If the Company were to lose a major mortgage broker or deposit agent, it would need to replace the product supplied by that broker or agent, either from existing or new brokers or retail agents, in order to meet corporate targets.

Reputational Risk

Reputational risk is the possibility that current and potential customers, counterparties, analysts, shareholders, investors, regulators or others will have an adverse opinion of the Company – irrespective of whether this is based on facts or merely public perception. This can result in potential losses to the Company arising from a decline in business volumes or increased funding costs. The Company has established a number of policies and procedures to manage this risk.

Responsibilities of Management and the Board of Directors

Management is responsible for the information disclosed in this MD&A and the accompanying consolidated financial statements. Equitable has in place appropriate information systems and procedures to ensure that information used internally by management and disclosed externally is materially complete and reliable. In addition, the Company's Audit Committee, on behalf of the Board of Directors, performs an oversight role with respect to all public financial disclosures made by the Company and has reviewed and approved this MD&A and the accompanying consolidated financial statements.

Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is accumulated and communicated to senior management, including the President and Chief Executive Officer on a timely basis, to enable appropriate decisions to be made regarding public disclosure. Management has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in the rules of the Canadian Securities Administrators) as of December 31, 2009. Based on that evaluation, management has concluded that these disclosure controls and procedures were effective.

Internal Control Over Financial Reporting

Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP. Management has evaluated the design and operational effectiveness of the Company's internal control over financial reporting as of December 31, 2009 to provide reasonable assurance regarding the reliability of financial reporting. This evaluation was conducted in accordance with the framework established by the Committee of Sponsoring Organizations of the Treadway Commission for Smaller Businesses, a recognized control model, and the requirements of National Instrument 52-109 of the Canadian Securities Administrators. Based on this evaluation, management has concluded that the design and operational effectiveness of internal control over financial reporting was effective as of December 31, 2009.

Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting that occurred during the fourth quarter of 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Non-Generally Accepted Accounting Principles ("GAAP") Financial Measures

Management uses a variety of financial measures to evaluate the Company's performance. In addition to GAAP prescribed measures, management uses certain non-GAAP measures that it believes provide useful information to investors regarding our financial condition and results of operations. Readers are cautioned that non-GAAP measures, such as the tangible common equity ratio do not have any standardized meaning prescribed by Canadian GAAP, and therefore, are unlikely to be comparable to similar measures presented by other companies. This ratio is a key measure of capital strength that is defined as shareholder's equity plus any qualifying other non-controlling interest in subsidiaries less preferred shares issued, any goodwill, other intangible assets and certain components of accumulated other comprehensive income, as a percentage of risk-adjusted assets less other intangible assets.

The presentation of financial information on a TEB is a common practice in the banking and trust company industries and does not have a standardized meaning within GAAP. Therefore, TEB calculations may not be comparable to similar measures presented by other companies. On a selective basis, the Company uses TEB in the discussion of revenues, interest margins and productivity ratios in this MD&A. The TEB methodology grosses up tax-exempt income, such as dividends from equity securities, by an amount which makes this income comparable on a pre-tax basis to regular taxable income such as mortgage interest. In 2009, the grossed-up amount was $3.4 million as compared to $3.6 million in 2008.

From time to time, the Company also utilizes non-GAAP financial measures to reflect circumstances where management separates and discloses non-recurring items from results that have otherwise been reported, in order to more accurately represent the underlying, recurring business performance. The Company believes that adjusted results can sometimes enhance comparability between reporting periods or provide the reader with a better understanding of how management views the Company's performance.

Cautionary Note Regarding Forward-Looking Statements

Statements made by the Company in the sections entitled "Business Profile and Objectives", "2010 Business Outlook", "Net Interest Income", "Non-Interest Expenses", "Mortgage Portfolio", "Credit Quality and Allowance for Credit Losses", "Liquidity Investments and Equity Securities", "Capital Management", "Future Accounting Changes" and "Risk Management" of this report, in other filings with Canadian securities regulators and in other communications include forward-looking statements within the meaning of applicable securities laws ("forward-looking statements"). These statements include, but are not limited to, statements about the Company's objectives, strategies and initiatives, financial result expectations and other statements made herein, whether with respect to the Company's businesses or the Canadian economy. Generally, forward-looking statements can be identified by the use of forward-looking terminology such as "plans", "expects" or "does not expect", "is expected", "budget", "scheduled", "planned", "estimates", "forecasts", "intends", "anticipates" or "does not anticipate", or "believes", or variations of such words and phrases which state that certain actions, events or results "may", "could", "would", "might" or "will be taken", "occur" or "be achieved". Forward-looking statements are subject to known and unknown risks, uncertainties and other factors that may cause the actual results, level of activity, closing of transactions, performance or achievements of the Company to be materially different from those expressed or implied by such forward-looking statements, including but not limited to risks related to capital markets and additional funding requirements, fluctuating interest rates and general economic conditions, legislative and regulatory developments, the nature of our customers and rates of default, and competition as well as those factors discussed under the heading "Risk Management" herein and in the Company's documents filed on SEDAR at www.sedar.com.

All material assumptions used in making forward-looking statements are based on management's knowledge of current business conditions and expectations of future business conditions and trends, including their knowledge of the current credit, interest rate and liquidity conditions affecting the Company and the Canadian economy. Although the Company believes the assumptions used to make such statements are reasonable at this time and has attempted to identify in its continuous disclosure documents important factors that could cause actual results to differ materially from those contained in forward-looking statements, there may be other factors that cause results not to be as anticipated, estimated or intended. Certain material assumptions are applied by the Company in making forward-looking statements, including without limitation, assumptions regarding its continued ability to fund its mortgage business at current levels, a continuation of the current level of economic uncertainty that affects real estate market conditions, continued acceptance of its products in the marketplace, as well as no material changes in its operating cost structure and the current tax regime. There can be no assurance that such statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. The Company does not undertake to update any forward-looking statements that are contained herein, except in accordance with applicable securities laws.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of Equitable Group Inc. (the "Company") are prepared by management, which is responsible for the integrity and fairness of the information presented. The information provided herein, in the opinion of management, has been prepared, within reasonable limits of materiality, using appropriate accounting policies that are in accordance with Canadian generally accepted accounting principles as well as the accounting requirements of the Office of the Superintendent of Financial Institutions Canada ("OSFI") as these apply to its subsidiary, The Equitable Trust Company ("Equitable Trust"). The consolidated financial statements reflect amounts which must, of necessity, be based on informed judgments and estimates of the expected effects of current events and transactions.

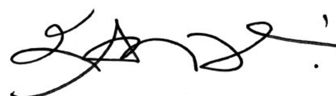
Management maintains a system of internal control to meet its responsibility for the integrity of the consolidated financial statements. Management also administers a program of ethical business conduct, which includes quality standards in hiring and training employees, written policies and a written corporate code of conduct.

The Board of Directors of the Company (the "Board") oversees management's responsibilities for the consolidated financial statements through the Audit Committee. The Audit Committee conducts a detailed review of the consolidated financial statements with management and internal and external auditors before recommending their approval to the Board.

The Company's subsidiary, Equitable Trust, is federally regulated under the Trust and Loan Companies Act (Canada) by OSFI. On a regular basis, OSFI conducts an examination to assess the operations of Equitable Trust and its compliance with statutory requirements and sound business practices.

KPMG LLP has been appointed as external auditors by the shareholders to examine the consolidated financial statements of the Company in accordance with Canadian generally accepted auditing standards. The external auditors have unrestricted access to and periodically meet with the Audit Committee, with and without management present, to discuss their audits and related matters.

Andrew Moor
President and Chief Executive Officer



John Ayanoglou
Chief Financial Officer

February 24, 2010

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Equitable Group Inc. as at December 31, 2009 and 2008 and the consolidated statements of income, changes in shareholders' equity, comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants, Licensed Public Accountants
Toronto, Canada

February 24, 2010

CONSOLIDATED BALANCE SHEETS

($ THOUSANDS)

As at December 31	2009	2008
Assets		
Cash and cash equivalents *(note 3)*	**$ 395,835**	$ 50,121
Restricted cash *(note 3)*	**5,000**	8,422
Investments purchased under reverse repurchase agreements *(note 4)*	**129,721**	698,276
Investments *(note 4)*	**388,037**	170,321
Securitization retained interests *(note 5)*	**147,195**	101,806
Mortgages receivable *(note 7)*	**2,763,020**	3,023,015
Other assets *(note 8)*	**17,266**	35,590
	$ 3,846,074	$ 4,087,551
Liabilities and Shareholders' Equity		
Liabilities:		
Customer deposits *(note 9)*	**$ 3,332,319**	$ 3,692,569
Future income taxes *(note 10)*	**19,999**	17,839
Other liabilities *(note 11)*	**54,724**	36,433
Bank term loans *(note 12)*	**27,500**	44,595
Subordinated debentures *(note 13)*	**37,671**	31,969
	3,472,213	3,823,405
Shareholders' equity *(notes 14 and 15)*:		
Preferred shares	**48,523**	–
Common shares	**127,424**	126,993
Contributed surplus	**3,267**	2,553
Retained earnings	**193,635**	149,365
Accumulated other comprehensive income (loss)	**1,012**	(14,765)
	373,861	264,146
Commitments and contingencies *(note 18)*		
	$ 3,846,074	$ 4,087,551

See accompanying notes to consolidated financial statements.

Austin Beutel
Chairman

Andrew Moor
President and Chief Executive Officer

CONSOLIDATED STATEMENTS OF INCOME

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)

Years ended December 31	2009	2008
Interest income:		
Mortgages	$ 162,991	$ 186,519
Investments	13,548	8,180
Other	3,599	17,255
	180,138	211,954
Interest expense:		
Customer deposits	94,322	133,770
Deposit agent commissions	7,149	8,468
Bank term loans	3,188	3,025
Subordinated debentures	2,310	2,348
	106,969	147,611
Net interest income	73,169	64,343
Provision for credit losses *(note 7)*	6,600	3,450
Net interest income after provision for credit losses	66,569	60,893
Other income:		
Fees and other income	3,246	1,832
Net gain (loss) on investments *(note 4)*	50	(295)
Gains on securitization activities and income from retained interests *(note 5)*	24,390	13,275
	27,686	14,812
Net interest income and other income	94,255	75,705
Non-interest expenses:		
Compensation and benefits	15,367	13,253
Other	10,540	9,438
	25,907	22,691
Income before income taxes	68,348	53,014
Income taxes *(note 10)*:		
Current	12,660	4,929
Future	4,250	9,474
	16,910	14,403
Net income	51,438	38,611
Dividends on preferred shares	1,212	–
Net income available to common shareholders	$ 50,226	$ 38,611
Earnings per share *(note 16)*:		
Basic	$ 3.37	$ 2.79
Diluted	$ 3.36	$ 2.78

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

($ THOUSANDS)

Years ended December 31	2009	2008
Preferred shares *(note 14)*:		
Balance, beginning of year	$ –	$ –
Gross proceeds of equity issue, Series 1	50,000	–
Issue expenses, net of tax recovery of $638 (2008 – nil)	(1,477)	–
Balance, end of year	48,523	–
Common shares *(note 14)*:		
Balance, beginning of year	126,993	87,062
Gross proceeds of equity issue	–	40,850
Issue expenses, net of tax recovery of nil (2008 – $698)	–	(1,510)
Proceeds from reinvestment of dividends	189	–
Proceeds from exercise of stock options	195	525
Transferred from contributed surplus relating to the exercise of stock options	47	66
Balance, end of year	127,424	126,993
Contributed surplus:		
Balance, beginning of year	2,553	1,778
Stock-based compensation *(note 15)*	761	841
Transferred to common shares relating to the exercise of stock options	(47)	(66)
Balance, end of year	3,267	2,553
Retained earnings:		
Balance, beginning of year	149,365	116,325
Net income	51,438	38,611
Dividends		
Preferred shares	(1,212)	–
Common shares	(5,956)	(5,571)
Balance, end of year	193,635	149,365
Accumulated other comprehensive income (loss):		
Balance, beginning of year	(14,765)	(1,995)
Other comprehensive income (loss)	15,777	(12,770)
Balance, end of year	1,012	(14,765)
Total retained earnings and accumulated other comprehensive income	194,647	134,600
Total shareholders' equity	$ 373,861	$ 264,146

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

($ THOUSANDS)

Years ended December 31	2009	2008
Net income	$ 51,438	$ 38,611
Other comprehensive income (loss), net of tax:		
Available for sale investments:		
Net unrealized gains (losses) from change in fair value[1]	19,324	(12,483)
Reclassification of net gains to income[2]	(3,547)	(287)
Other comprehensive income (loss)	15,777	(12,770)
Comprehensive income	$ 67,215	$ 25,841

[1] *Net of income tax expense of $9,262 (2008 – tax benefit of $6,229).*

[2] *Net of income tax benefit of $1,700 (2008 – tax benefit of $144).*

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

($ THOUSANDS)

Years ended December 31	2009	2008
Cash provided by (used in):		
Operating activities:		
Net income	$ 51,438	$ 38,611
Non-cash items:		
Financial instruments – fair value adjustments	2,572	(10,023)
Securitization gains	(20,221)	(10,076)
Amortization of capital assets	605	779
Provision for credit losses	6,600	3,450
Net (gain) loss on investments	(27)	39
Future income taxes	2,798	9,475
Stock-based compensation	761	841
Amortization of premiums on investments, net	803	1,344
	45,329	34,440
Changes in operating assets and liabilities:		
Other assets	5,783	(3,586)
Other liabilities	(6,312)	511
	44,800	31,365
Financing activities:		
(Decrease) increase in customer deposits	(355,328)	582,665
Repayment of bank term loan	(17,095)	–
Issuance of subordinated debentures	23,221	–
Redemption of subordinated debentures	(17,519)	–
Dividends paid on preferred shares	(1,212)	–
Dividends paid on common shares	(5,765)	(5,571)
Issuance of preferred shares	47,885	–
Issuance of common shares	195	39,167
	(325,618)	616,261
Investing activities:		
Purchase of investments	(239,098)	(5,000)
Proceeds on sale or redemption of investments	248,080	104,538
Purchase of investments purchased under reverse repurchase agreements	(941,681)	(2,133,537)
Proceeds on sale or redemption of investments purchased under reverse repurchase agreements	1,510,236	1,667,381
Change in restricted cash	3,422	(3,422)
Increase in mortgages receivable	(2,838,218)	(3,135,352)
Mortgage principal repayments	1,454,319	1,581,808
Proceeds from loan securitizations	1,402,222	1,291,679
Securitization retained interests	27,530	18,931
Purchase of capital assets	(280)	(458)
	626,532	(613,432)
Increase in cash and cash equivalents	345,714	34,194
Cash and cash equivalents, beginning of year	50,121	15,927
Cash and cash equivalents, end of year	$ 395,835	$ 50,121
Supplemental cash flow information:		
Interest paid	$ 102,811	$ 135,084
Income taxes paid	15,767	10,415

See accompanying notes to consolidated financial statements.

Equitable Group Inc. (the "Company") was formed on January 1, 2004 as the parent company of its wholly owned subsidiary, The Equitable Trust Company ("Equitable Trust"). Equitable Trust is federally regulated under the Trust and Loan Companies Act (Canada) by the Office of the Superintendent of Financial Institutions Canada ("OSFI"). The Company operates principally in one industry segment as a deposit-taking institution investing in mortgages.

1. Significant accounting policies:

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The following notes describe the Company's significant accounting policies:

(a) Basis of presentation:

The consolidated financial statements include the assets, liabilities and results of operations of the Company and its wholly owned subsidiary, Equitable Trust, after the elimination of intercompany transactions and balances.

(b) Cash and cash equivalents:

Cash and cash equivalents consist of deposits with regulated financial institutions and highly liquid short-term investments, including government guaranteed investments and other money market instruments, whose term to maturity at date of purchase is less than three months. Interest earned on cash and cash equivalents is included in interest income – other in the consolidated statements of income. These short-term investments are carried at cost plus accrued interest, which approximates fair value.

(c) Investments purchased under reverse repurchase agreements:

Investments purchased under reverse repurchase agreements represent a purchase of Government of Canada guaranteed debt securities by the Company effected with a simultaneous agreement to sell the assets back at a specified price on a specified future date, which is generally short term. The investment is held on the consolidated balance sheets and is recorded at its carrying value, which approximates its fair value due to the short-term nature of the transaction. The interest income related to these investments is recorded on an accrual basis and is included in interest income – other.

(d) Investments:

Investments have been designated as available for sale, are accounted for at settlement date and are reported on the consolidated balance sheets at fair value with unrealized gains and losses reported in other comprehensive income, net of income taxes.

Investments are purchased with the original intention to hold the securities to maturity or until market conditions render alternative investments more attractive. If impairment in value is other than temporary, any write-down to net realizable value is reported in the consolidated statements of income. Gains and losses realized on the sale, redemption or write-down of investments are recorded in other income in the consolidated statements of income. Interest income earned, amortization of premiums and discounts and dividends are included in interest income – investments in the consolidated statements of income. The fair values of investments are generally based on quoted market prices.

(e) Mortgages receivable and revenue recognition:

(i) Mortgages receivable designated as loans and receivables:

Mortgages receivable are recorded at amortized cost plus accrued interest, net of unamortized origination fees, unearned income, unamortized premiums or discounts and an allowance for credit losses. Net fees relating to mortgage origination are amortized to income on an effective yield basis over the term of the mortgages to which they relate, and are included in interest income – mortgages in the consolidated statements of income.

(ii) Mortgages held for securitization designated as held for trading:

Mortgages held for securitization designated as held for trading are carried at fair value with changes in fair value included in gains on securitization activities and income from retained interests in the consolidated statements of income. Net fees relating to

1. Significant accounting policies (continued):

mortgage origination are expensed as incurred and are included in gains on securitization activities and income from retained interests in the consolidated statements of income.

(iii) Other mortgages designated as held for trading:

Certain mortgages designated as held for trading are carried at fair value with changes in fair value included in interest income – mortgages in the consolidated statements of income.

Interest on mortgages receivable is recorded on the accrual basis. The Company classifies a mortgage receivable as impaired when, in the opinion of management, there is reasonable doubt as to the collectability, either in whole or in part, of principal or interest. Conventional mortgages where payment is contractually past due 90 days and mortgages guaranteed by the Government of Canada where payment is contractually past due 365 days are automatically placed on a non-accrual basis, unless management is reasonably assured as to the recoverability of principal and interest. Thereafter, interest income is recognized on a cash basis, but only after prior write-offs and provisions for losses have been recovered, provided there is no further doubt as to the collectability of principal.

When an impaired mortgage is identified, the carrying amount of the mortgage is reduced to its net realizable amount, measured on the basis of expected future cash flows, and discounted at the mortgage's effective interest rate. This impairment is reflected in the consolidated statements of income in the years in which the impairment is recognized. In subsequent periods, recoveries of amounts previously written off and any increase in the carrying value of the mortgage are credited to the allowance for credit losses on the consolidated balance sheets.

(f) Allowance for credit losses:

The allowance for credit losses consists of both specific and general allowances. Specific allowances relate to individual mortgages that, in the opinion of management, are necessary to reflect the estimated net realizable value of the particular mortgage as described in (e) above. General allowances are based on management's assessment of probable, unidentified losses in the portfolio at the consolidated balance sheet dates that have not been specifically identified as impaired. The allowance is determined based on management's identification and evaluation of problem accounts and includes an assessment of statistical and qualitative analyses of the performance of the portfolio, taking into account such factors as economic conditions, security and mortgage type, concentration risks and geographical exposure.

(g) Securitization retained interests:

For each securitization transaction, where the Company retains the servicing rights, an asset is recognized as securitization retained interests on the consolidated balance sheets. Securitization retained interests are investments classified as available for sale securities and are carried at fair value with changes in fair value reported in other comprehensive income, net of income taxes. When mortgages are sold in a securitization transaction under terms that transfer control to third parties, the transaction is recognized as a sale and the related mortgage assets are removed from the consolidated balance sheets. In the securitization transaction, certain interests are retained, including the right to receive the future excess interest spread and the mortgage servicing obligation. For securitizations entered into after July 1, 2001, the servicing liability is reported as a component of other liabilities. For securitizations entered into prior to this date, the servicing liability and the future excess interest spread are reported on a net basis. A gain or loss on the sale of the mortgages is recognized immediately in the consolidated statements of income. The amount of the gain or loss recognized depends in part on the previous carrying amount of the mortgages involved in the transfer, allocated between the assets sold and the retained interests based on their relative fair values at the date of transfer. To obtain fair values, the Company uses estimates based on the present value of future expected cash flows determined using management's best estimates of key assumptions, including prepayment rates and discount rates commensurate with the risks involved.

(h) Derivative financial instruments:

The Company uses derivative financial instruments primarily to manage exposure to interest rate risk. Derivative products that are primarily used are interest rate swaps and short sale and repurchase agreements of Government of Canada guaranteed debt securities. Interest rate swaps are used to adjust exposure to interest rate risk by modifying the maturity characteristics of existing assets and liabilities. Short sale and repurchase agreements are used to hedge interest rate exposure on mortgages held for securitization, on commitments for mortgages to be securitized and on certain other mortgages designated as held for trading.

1. Significant accounting policies (continued):

Derivative financial instruments are recorded on the consolidated balance sheets as held for trading financial instruments and are carried at fair value. Changes in fair value for derivatives related to securitization activities are included, as appropriate, in gains on securitization activities and income from retained interests. Changes in fair value for derivatives related to other mortgages designated as held for trading are included in interest income. Changes in fair value for derivatives related to interest rate swap activities are included in interest expense.

(i) Stock-based compensation:

The Company has a stock option plan for directors and eligible employees of Equitable Trust. Under this plan, options are periodically awarded to participants to purchase common shares at prices equal to the closing market price of the shares on the date prior to the date the options were granted. Prior to the initial public offering of the Company's shares on March 18, 2004, certain options were granted to purchase common shares at prices equal to the fair value of the shares, as determined under the plan. The Company uses the fair value-based method of accounting for stock options and recognizes compensation expense based on the fair value of the options on the date of the grant, which is determined using the Black-Scholes option pricing model. The fair value of the options is recognized over the vesting period of the options granted as compensation expense with a corresponding increase in contributed surplus. The contributed surplus balance is reduced as the options are exercised and the amount initially recorded for the options in contributed surplus is credited to capital stock. Compensation expense related to the stock-based compensation plan is included in the consolidated statements of income.

In addition to the stock option plan, the Company has a Deferred Share Unit ("DSU") Plan for directors. The obligation that results from the award of a DSU is recognized in income upon the grant of the unit and the corresponding amount is included in other liabilities in the consolidated balance sheets. The change in the obligation attributable to the change in stock price and dividends paid on common shares is recognized in compensation expense in the consolidated statements of income for the period in which the changes occur. The redemption value of each DSU is the volume-weighted average trading price of the common shares of the Company on the Toronto Stock Exchange ("TSX") for the five trading days prior to the date the individual ceases to be a director.

(j) Income taxes:

The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities represent the amount of tax applicable to temporary differences between the carrying amounts of the assets and liabilities and their values for tax purposes. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the years that include the date of enactment or substantive enactment.

(k) Capital assets:

Capital assets are carried at cost less accumulated amortization. Amortization is calculated using a reducing-balance method over the estimated useful lives of the assets at the following annual rates:

Furniture, fixtures and office equipment	20%
Computer hardware and software	30%

Leasehold improvements are amortized on a straight-line basis over the remaining term of the lease.

(l) Customer deposits:

Customer deposits are comprised of guaranteed investment certificates ("GICs") issued to depositors. Customer deposits, with the exception of those designated as held for trading, are recorded on the consolidated balance sheets at amortized cost using the effective interest method. Deferred deposit agent commissions are accounted for as a component of customer deposits with the amortization of these commissions – with the exception of commissions relating to customer deposits designated as held for trading, which are expensed as incurred – being calculated on an effective yield basis as a component of interest expense.

1. Significant accounting policies (continued):

(m) Bank term loans and subordinated debentures:

Bank term loans and subordinated debentures are recorded in the consolidated balance sheets at amortized cost using the effective interest method.

(n) Earnings per share:

Earnings per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the year. Diluted earnings per share reflects the potential dilution that could occur if additional common shares are assumed to be issued under securities or contracts that entitle their holders to obtain common shares in the future. The number of additional shares for inclusion in diluted earnings per share calculations is determined using the treasury stock method. Under this method, stock options which exercise price is less than the average market price of the Company's common shares are assumed to be exercised and the proceeds are used to repurchase common shares at the average market price for the year. The incremental number of common shares issued under stock options and repurchased from proceeds is included in the calculation of diluted earnings per share.

(o) Use of estimates:

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenue and expenses during the years. Certain estimates, including the allowance for credit losses, the fair values of financial instruments, accounting for securitizations and income taxes require management to make subjective or complex judgments. Accordingly, actual results could differ from those estimates.

(p) Changes in accounting policy:

Credit Risk and the Fair Value of Financial Assets and Financial Liabilities:

On January 20, 2009, the Emerging Issues Committee issued Abstract 173 (EIC 173), *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities.* The abstract requires an entity to take into account its own credit risk and the credit risk of the counterparty when determining the fair value of financial assets and financial liabilities, including derivative instruments. The new guidance did not have a material effect on its consolidated financial statements.

Fair Value and Liquidity Risk Disclosure – Amendments to: Financial Instruments – Disclosures:

In June 2009, the Accounting Standards Board ("AcSB") amended Section 3862, *Financial Instruments – Disclosures*, to enhance the disclosure requirements regarding fair value measurements and the liquidity risk, also referred to as funding risk in these financial statements, of financial instruments.

Section 3862 now requires that all financial instruments valued at fair value be categorized into one of three fair value hierarchy levels, ranging from those fair value measurements that are determined using quoted market prices in an active market to those fair value measurements that are based on inputs that are not based on observable market data. Refer to note 2 for the new disclosure.

The additional disclosures over liquidity risk require disclosure of maturity analysis for financial liabilities. Refer to note 17 for additional disclosure.

(q) Future accounting changes:

International Financial Reporting Standards ("IFRS"):

The AcSB requires that all publicly accountable enterprises adopt IFRS for years beginning on or after January 1, 2011. IFRS will replace Canadian GAAP and on January 1, 2011, these standards will apply to the Company. A description of the Company's implementation plan, progress and the expected impact on its financial reporting is included in the Company's Management's Discussion and Analysis for the three months and year ended December 31, 2009 on pages 36 and 37.

(r) Comparative figures:

Certain comparative figures have been reclassified to conform to the financial statement presentation adopted for 2009.

2. Financial instruments:

The Company's business activities result in a consolidated balance sheet that consists primarily of financial instruments and the majority of net income results from gains, losses, income and expenses related to the same.

Financial instrument assets include cash and cash equivalents, restricted cash, investments purchased under reverse repurchase agreements, investments, mortgages receivable, securitization retained interests and derivative financial instruments. Financial instrument liabilities include customer deposits, securitized mortgage servicing liability, derivative financial instruments, bank term loans and subordinated debentures.

Financial assets and liabilities are recognized in the consolidated balance sheets at fair value, cost or amortized cost according to the categories determined by the accounting framework for financial instruments.

(a) Risks associated with financial instruments:

The use of financial instruments exposes the Company to credit risk, interest rate risk and funding risk. The following is a discussion of the Company's risk exposures and how it manages those risks:

Credit risk management:

Credit risk is defined as the possibility that the Company will not receive the full value of amounts and recovery costs owed to it if counterparties fail to honour their obligations.

The Company's focus is on providing first mortgages on real estate. All mortgages are individually evaluated by underwriters using internal and external credit risk assessment tools and are assigned a risk rating, in accordance with the level of credit risk attributed to each loan. The underwriting approach places a strong emphasis on security evaluation and judgmental analysis of the risks in the transaction rather than being formulaic in nature. As a result, the Company can underwrite mortgages on favourable terms to borrowers who have good equity and debt service ratios in situations where conventional lenders may typically decline borrowers.

On a regular basis, management establishes credit limits for exposure to certain counterparties, industries or market segments. Management also monitors these credit exposures, and prepares detailed analyses and reports assessing overall credit risk within the mortgage portfolio. Key components of credit risk that are closely monitored and measured are credit concentration risk and the risk associated with economically-sensitive assets. By way of definition, credit concentration risk results if an unduly large proportion of the Company's lending business involves a single person, organization or group of related persons or organizations, a single geographic area, a single industry or a single category of investment.

The Company also invests in preferred share securities to generate returns that meet an acceptable hurdle threshold from a return on equity perspective. These securities represent a potential source of liquidity to the Company. However, such investments expose the Company to credit risk if the issuer of the preferred shares cannot make dividend payments, or in the worst case scenario, if the issuer becomes insolvent.

Securities rated P-2 and higher comprised 61.9% of the preferred share equity securities portfolio at December 31, 2009, compared to 75.6% a year earlier.

Interest rate risk management:

Interest rate risk is defined as the possibility that changes in market interest rates will adversely affect the Company's financial condition. Interest rate risk may be affected if an unduly large proportion of the Company's assets or liabilities have unmatched terms, interest rates or other attributes.

The Company's primary method of managing interest rate risk involves the matching of asset and liability maturity profiles, closely monitoring interest rates and acting upon any mismatch in a timely manner to ensure that any sudden or prolonged change in interest rates does not significantly affect the Company's net interest income.

The Company uses simulated interest rate change sensitivity models to estimate the effects of various interest rate change scenarios on the economic value of shareholders' equity and on net interest income for the 12 months following the measurement date. Certain assumptions that are based on actual experience are built into the simulations, including assumptions related to the pre-maturity redemptions of GICs and early payouts of mortgages. Estimates of Cashable GIC redemptions are also modeled.

2. Financial instruments (continued):

The Company hedges the interest rate risk for all multi-unit residential mortgages that are to be securitized through the Canada Mortgage and Housing Corporation ("CMHC") Mortgage Backed Securities ("MBS") and Canada Mortgage Bond ("CMB") Programs. Hedging protects the Company from losses due to changes in interest rates during the relevant period.

The Company also holds replacement assets in the form of MBS in order to reduce the interest rate risk and replacement asset exposure inherent in its participation in the CMB Program.

The Company's earnings are affected by changes in interest rates. The estimate of sensitivity to interest rate changes is dependent on a number of assumptions that could result in a difference in actual outcomes in the event of an actual interest rate change.

Funding risk management:

Funding risk (also referred to as liquidity risk) is defined as the possibility that the Company will be unable to generate or obtain sufficient cash or its equivalents in a timely manner, at a reasonable price, to meet its commitments as they fall due. Funding risk may be affected if an unduly large proportion of the Company's deposit-taking business involves a single person, organization or group of related persons or a single geographic area.

Managing funding risk requires management to keep sufficient liquid assets on hand at all times to meet the mortgage funding needs, investment purchase commitments and GIC redemption and maturity obligations of Equitable Trust. Assets held for the purpose of providing liquidity protection consist of cash and cash equivalents and debt instruments guaranteed by governments held by Equitable Trust. These assets amounted to $763.6 million at December 31, 2009 and $820.3 million at December 31, 2008.

The Company was in compliance with its liquidity policy at December 31, 2009. It is the Company's policy to maintain, at all times, regulatory liquid assets at levels equivalent to, or greater than 22.5% of GICs maturing in the next 100 days and all Cashable GICs ("100 Day Maturities"). At December 31, 2009, these maturities amounted to $991.2 million. The Company held regulatory liquid assets corresponding to 77.0% of its 100 Day Maturities as at December 31, 2009.

(b) Determination of fair value:

When a financial instrument is initially recognized, its fair value is the amount of consideration for which the financial instruments would be exchanged in an arm's-length transaction between knowledgeable parties who are under no compulsion to act.

Subsequent to initial recognition, for financial instruments measured at fair value where active market prices are available, bid prices are used for financial assets and ask prices for financial liabilities. For those financial instruments measured at fair value where an active market is not available, fair value estimates are determined using valuation methods which refer to observable market data and include discounted cash flow analysis and other commonly used valuation techniques.

Valuation methods and assumptions used to estimate fair values of financial instruments:

(i) Financial instruments whose carrying value approximates fair value:

The carrying value of certain financial assets and financial liabilities corresponds to a reasonable approximation of fair value. The Company considers that the carrying value of cash and cash equivalents, restricted cash, investments purchased under reverse repurchase agreements as well as certain other assets and liabilities, approximates fair value.

(ii) Available for sale and held for trading financial assets and liabilities:

These financial assets and financial liabilities are presented on the consolidated balance sheets at fair value. For financial instruments measured at fair value where active market prices are available, bid prices are used for financial assets and ask prices for financial liabilities. For those financial instruments measured at fair value where an active market is not available, fair value estimates are determined using valuation methods which refer to observable market data and include discounted cash flow analysis and other commonly used valuation techniques.

The fair value of securitization retained interests is determined with internal valuation models using market data inputs, where possible, by discounting expected future cash flows at a yield plus a spread for like term Government of Canada guaranteed debt securities.

2. Financial instruments (continued):

(iii) Mortgages receivable:

The estimated fair value of mortgages receivable is determined using a discounted cash flow calculation and the market interest rates offered for mortgages with similar terms and credit risks.

(iv) Customer deposits:

The estimated fair value of customer deposits is determined by discounting expected future contractual cash flows using observed market interest rates offered for deposits with similar terms.

(v) Bank term loans and subordinated debentures:

The estimated fair value of bank term loans and subordinated debentures are determined by discounting expected future contractual cash flows using market interest rates offered for similar terms.

The following table presents the carrying values for each category of financial assets and liabilities and their estimated fair values. The table does not include assets and liabilities that are not considered financial instruments.

2009	Financial instruments required to be classified as held for trading	Financial instruments designated as held for trading	Available for sale	Loans and receivables/ financial liabilities at cost or amortized cost	Carrying value	Fair value
Financial assets:						
Cash and cash equivalents	$ 395,835	$ –	$ –	$ –	$ 395,835	$ 395,835
Restricted cash	5,000	–	–	–	5,000	5,000
Investments purchased under						
reverse repurchase agreements	–	–	–	129,721	129,721	129,721
Investments	–	–	388,037	–	388,037	388,037
Securitization retained interests	–	–	147,195	–	147,195	147,195
Mortgages receivable[(1)]	–	141,449	–	2,621,571	2,763,020	2,796,545
Other assets:						
Fair value of derivative financial						
instruments – interest rate swaps	294	–	–	–	294	294
Fair value of derivative financial						
instruments – hedges	264	–	–	–	264	264
Fair value of derivative financial						
instruments – securitization activities	2,358	–	–	–	2,358	2,358
Other	–	–	–	3,503	3,503	3,503
Total financial assets	$ 403,751	$ 141,449	$ 535,232	$ 2,754,795	$ 3,835,227	$ 3,868,752
Financial liabilities:						
Customer deposits[(1)]	$ –	$ 10,238	$ –	$ 3,322,081	$ 3,332,319	$ 3,343,148
Other liabilities:						
Mortgage commitments	14	–	–	–	14	14
Other	–	–	–	54,243	54,243	54,243
Bank term loans	–	–	–	27,500	27,500	28,838
Subordinated debentures	–	–	–	37,671	37,671	37,610
Total financial liabilities	$ 14	$ 10,238	$ –	$ 3,441,495	$ 3,451,747	$ 3,463,853

[(1)] *Mortgages receivable are presented net of deferred loan origination fees and deferred commitment income. Customer deposits are presented net of deferred deposit agent commissions.*

2. Financial instruments (continued):

2008	Financial instruments required to be classified as held for trading	Financial instruments designated as held for trading	Available for sale	Loans and receivables/ financial liabilities at cost or amortized cost	Carrying value	Fair value
Financial assets:						
Cash and cash equivalents	$ 50,121	$ –	$ –	$ –	$ 50,121	$ 50,121
Restricted cash	8,422	–	–	–	8,422	8,422
Investments purchased under						
reverse repurchase agreements	–	–	–	698,276	698,276	698,276
Investments	–	–	170,321	–	170,321	170,321
Securitization retained interests	–	–	101,806	–	101,806	101,806
Mortgages receivable[(1)]	–	83,636	–	2,939,379	3,023,015	3,034,760
Other assets:						
Fair value of derivative financial						
instruments – interest rate swaps	14,836	–	–	–	14,836	14,836
Mortgage commitments	296	–	–	–	296	296
Other	–	–	–	5,266	5,266	5,266
Total financial assets	$ 73,675	$ 83,636	$ 272,127	$ 3,642,921	$ 4,072,359	$ 4,084,104
Financial liabilities:						
Customer deposits[(1)]	$ –	$ 620,042	$ –	$ 3,072,527	$ 3,692,569	$ 3,751,844
Other liabilities:						
Fair value of derivative financial						
instruments – hedges	408	–	–	–	408	408
Fair value of derivative financial						
instruments – securitization activities	3,527	–	–	–	3,527	3,527
Other	–	–	–	30,987	30,987	30,987
Bank term loans	–	–	–	44,595	44,595	47,222
Subordinated debentures	–	–	–	31,969	31,969	32,889
Total financial liabilities	$ 3,935	$ 620,042	$ –	$ 3,180,078	$ 3,804,055	$ 3,866,877

[(1)] Mortgages receivable are presented net of deferred loan origination fees and deferred commitment income. Customer deposits are presented net of deferred deposit agent commissions.

2. Financial instruments (continued):

(c) Fair value hierarchy:

Financial instruments recorded at fair value on the consolidated balance sheet are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 – valuation based on quoted prices (unadjusted) observed in active markets for identical assets and liabilities.

Level 2 – valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 – valuation techniques with significant unobservable market inputs.

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

The following table presents the financial instruments recorded at fair value in the consolidated balance sheet, classified using the fair value hierarchy:

2009	Level 1	Level 2	Level 3	Total financial assets/ financial liabilities at fair value
Financial assets:				
Cash and cash equivalents	$ 395,835	$ –	$ –	$ 395,835
Restricted cash	5,000	–	–	5,000
Investments	151,147	236,890	–	388,037
Securitization retained interests	–	147,195	–	147,195
Mortgages receivable	–	141,449	–	141,449
Other assets:				
Fair value of derivative financial instruments – interest rate swaps	–	294		294
Fair value of derivative financial instruments – hedges	264	–	–	264
Fair value of derivative financial instruments – securitization activities	2,358	–	–	2,358
Total financial assets	$ 554,604	$ 525,828	$ –	$ 1,080,432
Financial liabilities:				
Customer deposits	$ –	$ 10,238	$ –	$ 10,238
Other liabilities:				
Mortgage commitments	–	14	–	14
Total financial liabilities	$ –	$ 10,252	$ –	$ 10,252

3. Cash and cash equivalents and restricted cash:

	2009	2008
Deposits with regulated financial institutions	$ 395,835	$ 25,125
Short-term investments	–	24,996
	$ 395,835	$ 50,121

Restricted cash of $5,000 (2008 – $8,422) is held as collateral by a third party for the Company's interest rate swap transactions.

4. Investments:

The analysis of investments at carrying value, by type and maturity, is as follows:

	Maturities				2009	2008
	Within 1 year	Over 1 to 3 years	Over 3 to 5 years	Over 5 years	Total carrying value	Total carrying value
Debt securities issued or guaranteed by:						
Canada	$ 26,944	$ 27,515	$ 147,727	$ 35,875	$ 238,061	$ 73,563
Equity securities:						
Preferred shares	-	56,392	22,028	71,556[1]	149,976	96,758
	$ 26,944	$ 83,907	$ 169,755	$ 107,431	$ 388,037	$ 170,321

[1] *Includes investments with no specific maturity.*

The analysis of investments at fair value is as follows:

	2009				2008			
	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
Debt securities issued or guaranteed by:								
Canada	$ 230,212	$ 8,035	$ (186)	$ 238,061	$ 69,950	$ 3,613	$ –	$ 73,563
Equity securities:								
Preferred shares	158,958	2,588	(11,570)	149,976	127,235	12	(30,489)	96,758
	$ 389,170	$ 10,623	$ (11,756)	$ 388,037	$ 197,185	$ 3,625	$ (30,489)	$ 170,321

The Company held investments under reverse repurchase agreements at December 31, 2009 in the amount of $129,721 (2008 – $698,276). Investments purchased under reverse repurchase agreements represent a purchase of Government of Canada guaranteed debt securities by the Company effected with a simultaneous agreement to sell the assets back at a specified price on a specified future date, which is generally short-term.

5. Securitization retained interests:

(a) Retained interests:

The Company securitizes Government of Canada guaranteed residential mortgages through the creation of mortgage backed securities. These mortgage backed securities are sold through the CMHC MBS and CMB Programs or are otherwise retained on the Company's consolidated balance sheets. As at December 31, 2009, outstanding securitized mortgages totaled $4,093,180 (2008 – $2,825,063).

Under GAAP, the Company accounts for securitization transactions as sales when control over the mortgages has been surrendered and consideration, in addition to beneficial interests in the transferred mortgages, have been received in exchange. At the time of sale, a gain is recognized based on the Company's best estimate of the net present value of expected future cash flows, primarily the retained interests, net of an estimate for the cost of servicing obligations as the Company retained the responsibility for servicing the mortgages. The retained interests are recorded as part of securitization retained interests while the servicing liability is recorded as part of other liabilities (note 11). During the life of the securitization, the retained interests are amortized as cash is received. Similarly, the servicing liability previously recognized is also amortized to gains on securitization activities and income from retained interests in the consolidated statements of income.

Retained interests are accounted for at settlement date. The fair value of the retained interests is determined – with internal valuation models using market data inputs, where possible – by discounting the expected future cash flows at a yield plus a spread for like term Government of Canada guaranteed debt securities.

The following table provides quantitative information about the securitization activities during the year:

	2009	2008
Mortgages securitized and sold	**$ 1,400,939**	$ 1,295,955
Mortgages securitized and retained	**205,883**	74,364
Cash proceeds, net of accrued interest received on mortgages securitized and sold	**1,402,222**	1,291,679
Retained rights to future excess interest	**76,395**	66,504
Servicing liability recorded	**28,522**	16,718
Gains on mortgages securitized and sold	**18,320**	10,330
Gains (losses) on other securitization activities	**1,901**	(254)

The following table provides quantitative information about key assumptions in measuring the Company's retained interests at the date of securitization during the year:

	2009	2008
	Residential mortgages	Residential mortgages
Discount rate	**2.82%**	3.66%
Prepayment rate[1]	**1.33%**	0.69%
Excess spread	**1.11%**	1.21%

[1] *The prepayment rate assumption used for single-family residential mortgages is 20.00%. Multi-family residential mortgages have no prepayment rate assumption, as under the terms of the multi-family residential mortgages, prepayment penalties are sufficient to ensure that the Company will receive all of its investment upon the early discharge or prepayment of any mortgage.*

With respect to expected credit losses, the Company has assumed no credit losses for purposes of measuring its retained interests since all mortgages securitized are Government of Canada guaranteed.

5. Securitization retained interests (continued):

Other quantitative information related to securitization retained interests is as follows:

	2009	2008
Cash flows received on securitization retained interests, net of servicing fees paid	$ 23,837	$ 19,405
Securitization retained interests	147,195	101,806
Amortization of securitization retained interests	27,530	18,931
Securitized mortgage servicing liability *(note 11)*	40,606	19,945
Amortization of securitized mortgage servicing liability	7,862	2,725
Net unrealized fair value gain included in securitization retained interests	1,692	4,908

The components of income from gains on securitization activities and income from retained interests are as follows:

	2009	2008
Excess interest spread, net of servicing fees	$ 4,169	$ 3,199
Gains on securitization activities	20,221	10,076
	$ 24,390	$ 13,275

The following table presents the sensitivity of the fair value of retained interests to two adverse changes in the key assumption relating to the discount rate as at December 31, 2009. The following sensitivity analysis is hypothetical and should be used with caution:

	2009	2008
	Residential mortgages	Residential mortgages
Carrying value of retained interests	$ 147,195	$ 101,806
Discount rate	2.82%	2.28%
Impact on fair value of a 10% adverse change	(973)	(542)
Impact on fair value of a 20% adverse change	(1,932)	(1,078)

The valuation of the future excess interest spread includes a weighted average excess spread of 0.98% (2008 – 0.92%), and the key assumption of a weighted average discount rate of 2.82% (2008 – 2.28%). There are no expected credit losses as the mortgages are government guaranteed. Multi-family residential mortgages have no prepayment rate estimates, as under the terms of the multi-family residential mortgages, prepayment penalties are sufficient to ensure that the Company will receive all of its investment upon the early discharge of any mortgage. Single family residential mortgages have been valued with an estimated annual prepayment rate of 20.00%.

The Company estimates that the future excess interest spread and servicing liability will be received or paid as follows:

	Excess interest spread	Servicing liability
2010	$ 34,851	$ 9,074
2011	33,023	8,956
2012	30,657	8,728
2013	25,997	7,476
2014	10,334	3,012
Thereafter	12,333	3,360
	$ 147,195	$ 40,606

5. Securitization retained interests (continued):

(b) Mortgage commitments:

Mortgage commitments for government guaranteed mortgages to be securitized are designated as held for trading and are carried at fair value. Fair value is determined by reference to the change in the bid side of like term Government of Canada guaranteed debt securities plus a spread. Changes in fair value reflect changes in interest rates that have occurred since commitment to the mortgage interest rate. The fair value of mortgage commitments of ($14) (2008 – $296) is included in other liabilities (note 11) and other assets (note 8) for 2008.

6. Derivative financial instruments:

(a) Hedge instruments:

The Company's securitization activities are subject to interest rate risk, which represents the potential for changes in the value of assets and liabilities due to fluctuations in interest rates. The Company enters into hedging transactions to manage interest rate exposures on mortgages held for securitization and on commitments for mortgages to be securitized, typically for periods of up to 90 days, as well as on certain other mortgages designated as held for trading.

Hedge instruments outstanding at year end are short sale and repurchase agreements of Government of Canada guaranteed debt securities, where the counterparties are chartered banks, their subsidiaries or other financial intermediaries, and are as follows:

			2009			2008
Bond term (years)	**Notional amount**	**Fair value**	**Unrealized (gain) loss** [1]	Notional amount	Fair value	Unrealized (gain) loss [1]
1 to 5	**$ 62,100**	**$ 61,652**	**$ (533)**	$ 73,900	$ 77,884	$ 3,527
6 to 10	**103,745**	**102,732**	**(2,089)**	13,357	14,940	408
	$ 165,845	**$ 164,384**	**$ (2,622)**	$ 87,257	$ 92,824	$ 3,935

[1] Hedge instruments to manage interest rate exposures on mortgages held for securitization and on commitments for mortgages to be securitized are fair value hedges carried at fair value with changes in fair value included in gains on securitization activities and income from retained interests. Hedge instruments to manage interest rate exposures on certain other mortgages designated as held for trading are fair value hedges and are carried at fair value with changes in fair value included in interest income – mortgages. The fair values of the hedge instruments are determined by reference to the ask side of the related Government of Canada guaranteed debt securities at the reporting date. The unrealized gain is included in other assets (note 8) and the unrealized loss for 2008 is included in other liabilities (note 11).

(b) Interest rate swaps:

The Company enters into interest rate swaps to manage interest rate exposures on GICs used to fund floating rate mortgages. These hedging facilities are secured by investments in preferred shares and cash equivalents. The fair value of the GIC interest rate swap agreements are included in other assets (note 8) with the changes in fair value included in interest expense. Approved counterparties are limited to chartered banks and other financial intermediaries.

Interest rate swaps outstanding at year end are as follows:

		2009		2008
Swap term (years)	**Notional amount**	**Fair value**	Notional amount	Fair value
1 to 5	**$ 10,000**	**$ 294**	$ 615,000	$ 14,836

(c) Embedded derivatives:

The Company's equity securities contain embedded derivatives which are required to be bifurcated from the underlying investment and valued separately. These bifurcated derivatives do not currently have significant value and, therefore, are not reported separately.

7. Mortgages receivable:

(a) Mortgages receivable:

		Allowance for credit losses			
2009	**Gross amount**	**Specific**	**General**	**Total**	**Net amount**
Residential mortgages	**$ 1,783,664**	**$ 2,266**	**$ 8,181**	**$ 10,447**	**$ 1,773,217**
Other mortgages	**739,656**	**2,030**	**1,927**	**3,957**	**735,699**
Mortgages held for securitization or for sale	**242,880**	**–**	**231**	**231**	**242,649**
Accrued interest	**11,455**	**–**	**–**	**–**	**11,455**
	$ 2,777,655	**$ 4,296**	**$ 10,339**	**$ 14,635**	**$ 2,763,020**

		Allowance for credit losses			
2008	Gross amount	Specific	General	Total	Net amount
Residential mortgages	$ 1,978,004	$ 2,650	$ 8,728	$ 11,378	$ 1,966,626
Other mortgages	684,494	250	2,215	2,465	682,029
Mortgages held for securitization or for sale	361,657	–	708	708	360,949
Accrued interest	13,411	–	–	–	13,411
	$ 3,037,566	$ 2,900	$ 11,651	$ 14,551	$ 3,023,015

Included in mortgages held for securitization or for sale are Government of Canada insured multi-unit residential mortgages of $127,866 (2008 – $69,201) which have been designated as held for trading and are carried at fair value determined by reference to the change in the bid side of like term Government of Canada guaranteed debt securities plus a spread. Changes in fair value reflect changes in interest rates that have occurred since commitment to the mortgage interest rate. The fair value adjustment of Government of Canada guaranteed mortgages held for securitization is ($1,553) (2008 – $2,683). Mortgages held for sale include mortgages which are to be pooled and discharged subsequent to the consolidated balance sheet date at their investment cost. These mortgages are carried at amortized cost.

Included in other mortgages are certain mortgages designated as held for trading and are carried at fair value with changes in fair value included in interest income – mortgages. As at December 31, 2009, mortgage principal outstanding for these mortgages held for trading is $13,065 (2008 – $13,224) and the fair value adjustment is $518 (2008 – $1,211).

Real estate owned held for sale at December 31, 2009 amounted to $2,518 (2008 – nil) and are included in other assets (note 8).

Concentration of credit exposure may arise when a group of counterparties have similar economic characteristics or are located in the same geographical region. The ability of these counterparties to meet contractual obligations may be affected by changing economic or other conditions. The Company's mortgage portfolio consists of $2,012,289 (2008 – $2,110,896) of mortgages secured by properties located in the Province of Ontario and $447,599 (2008 – $583,182) of mortgages secured by properties located in the Province of Alberta. All mortgages are secured by real estate property in Canada.

(b) Impaired and past due mortgages:

The Company classifies a mortgage receivable as impaired when, in the opinion of management, there is reasonable doubt as to the collectability, either in whole or in part, of principal or interest. Conventional mortgages where payment is contractually past due 90 days and mortgages guaranteed by the Government of Canada where payment is contractually past due 365 days are automatically placed on a non-accrual basis, unless management is reasonably assured as to the recoverability of principal and interest.

7. Mortgages receivable (continued):

Outstanding impaired mortgages, net of allowance for credit losses are as follows:

			2009			2008
	Gross	Specific allowance	Net	Gross	Specific allowance	Net
Residential mortgages	$ 29,635	$ (2,266)	$ 27,369	$ 38,470	$ (2,650)	$ 35,820
Other mortgages	7,927	(2,030)	5,897	1,161	(250)	911
Mortgages held for securitization or for sale	–	–	–	–	–	–
	$ 37,562	$ (4,296)	$ 33,266	$ 39,631	$ (2,900)	$ 36,731

Outstanding mortgages that are past due but not classified as impaired are as follows:

				2009
	30 – 59 days	60 – 89 days	90+ days	Total
Residential mortgages	$ 7,467	$ 3,908	$ 5,450	$ 16,825
Other mortgages	7,300	–	531	7,831
Mortgages held for securitization or for sale	–	–	–	–
	$ 14,767	$ 3,908	$ 5,981	$ 24,656

				2008
	30 – 59 days	60 – 89 days	90+ days	Total
Residential mortgages	$ 11,881	$ 3,908	$ 8,113	$ 23,902
Other mortgages	632	–	–	632
Mortgages held for securitization or for sale	–	–	–	–
	$ 12,513	$ 3,908	$ 8,113	$ 24,534

(c) Allowance for credit losses:

			2009			2008
	Specific allowance	General allowance	Total	Specific allowance	General allowance	Total
Balance, beginning of year	$ 2,900	$ 11,651	$ 14,551	$ 150	$ 8,775	$ 8,925
Provision for credit losses	7,912	(1,312)	6,600	2,786	664	3,450
Allowance for credit losses on acquired portfolio	–	–	–	–	2,212	2,212
Realized losses	(6,624)	–	(6,624)	(36)	–	(36)
Recoveries	108	–	108	–	–	–
Balance, end of year	$ 4,296	$ 10,339	$ 14,635	$ 2,900	$ 11,651	$ 14,551

7. Mortgages receivable (continued):

(d) The following table presents information about the Company's reported and securitized mortgages:

2009	**Gross amount**	**Principal amount of mortgages 90 or more days past due**
Residential mortgages	**$ 5,876,844**	**$ 20,178**
Other mortgages	**739,656**	**2,361**
Mortgages held for securitization or for sale	**242,880**	**–**
Total mortgages reported and securitized	**6,859,380**	**22,539**
Less mortgages securitized	**4,093,180**	**4,112**
Mortgages reported prior to accrued interest	**$ 2,766,200**	**$ 18,427**

2008	Gross amount	Principal amount of mortgages 90 or more days past due
Residential mortgages	$ 4,803,067	$ 48,229
Other mortgages	684,494	1,161
Mortgages held for securitization or for sale	361,657	–
Total mortgages reported and securitized	5,849,218	49,390
Less mortgages securitized	2,825,063	1,763
Mortgages reported prior to accrued interest	$ 3,024,155	$ 47,627

8. Other assets:

	2009	2008
Income taxes recoverable	**$ 4,187**	$ 11,588
Real estate owned *(note 7)*	**2,518**	–
Derivative financial instruments – securitization activities *(note 6)*	**2,358**	–
Capital assets	**2,211**	2,536
Receivables relating to securitization activities	**2,075**	2,643
Prepaid expenses and other	**1,930**	1,070
Accrued interest and dividends on non-mortgage assets	**1,429**	2,621
Derivative financial instruments – interest rate swaps *(note 6)*	**294**	14,836
Derivative financial instruments – hedges *(note 6)*	**264**	–
Mortgage commitments *(note 5)*	**–**	296
	$ 17,266	$ 35,590

9. Customer deposits:

	2009	2008
Cashable GICs, payable on demand	**$ 688,782**	$ 826,438
GICs with fixed maturity dates	**2,582,186**	2,789,869
Accrued interest	**71,798**	85,363
Deferred deposit agent commissions	**(10,447)**	(9,101)
	$ 3,332,319	$ 3,692,569

9. Customer deposits (continued):

Included in GICs with fixed maturity dates are $10,000 (2008 – $614,882) of GICs designated as held for trading. These GICs are carried at fair value determined by discounting expected future contractual cash flows using observed market interest rates offered for deposits with similar terms. Changes in fair value reflect changes in interest rates which have occurred since the GICs were issued. The fair value adjustment of ($238) (2008 – ($5,160)) is included in interest expense.

The following table outlines the maturity profile of customer deposits:

					2009	2008
	Maturities					
	Payable on demand	Within 1 year	1 to 3 years	4 to 5 years	Total	Total
GICs	$ 688,782	$ 1,274,456	$ 985,816	$ 321,914	$ 3,270,968	$ 3,616,307

10. Income taxes:

The provision for income taxes shown in the consolidated statements of income differs from that obtained by applying statutory income tax rates to income before the provision for income taxes for the following reasons:

	2009	2008
Canadian statutory income tax rate	32.4%	33.3%
Increase (decrease) resulting from:		
Tax-exempt income	(2.9%)	(4.5%)
Future tax rate decreases	(4.2%)	(2.2%)
Non-deductible expenses and other	(0.6%)	0.6%
Effective income tax rate	24.7%	27.2%

The net future income tax liability is comprised of:

	2009	2008
Future income tax assets:		
Allowance for credit losses	$ 2,715	$ 3,438
Share issue expenses	1,080	960
Deferred mortgage fees	–	11
Other	1,360	–
	5,155	4,409
Future income tax liabilities:		
Deferred GIC commissions	3,020	2,892
Securitization retained interests	22,134	19,035
Other	–	321
	25,154	22,248
Net future income tax liability	$ 19,999	$ 17,839

11. Other liabilities:

	2009	2008
Securitized mortgage servicing liability *(note 5)*	**$ 40,606**	$ 19,945
Mortgagor realty taxes	**10,317**	9,048
Accounts payable and accrued liabilities	**3,787**	3,505
Mortgage commitments *(note 5)*	**14**	–
Derivative financial instruments – securitization activities *(note 6)*	**–**	3,527
Derivative financial instruments – hedges *(note 6)*	**–**	408
	$ 54,724	$ 36,433

12. Bank facilities:

(a) Operating credit facility:

The Company has a $35,000 credit facility in place with a major Canadian chartered bank. The facility is secured by the Company's investments in equity securities. There was no outstanding balance as December 31, 2009 (2008 – nil).

(b) Term loans:

The Company has non-revolving term loans totaling $27,500. Each loan is for a fixed term of five years with the balance of the loan, together with all accrued and unpaid interest, due on the fifth anniversary of the loan. The proceeds of the loans were used to purchase $15,000 of Series 6 and $12,500 of Series 7 subordinated debentures of the Company's subsidiary, Equitable Trust. The loans are repayable in full at the option of the Company at any time during their term. As collateral for the loans, the Company has provided a promissory note, a general security agreement, a pledge of all the issued and outstanding shares in the capital of Equitable Trust and an assignment of the subordinated debentures purchased from Equitable Trust using the proceeds of the loans. Interest is paid monthly. Under the terms of these loans, the Company is required to maintain a minimum tangible net worth ratio, an interest coverage ratio and a maximum assets-to-capital ratio. The Company is in compliance with the financial covenants required by the term loans.

2009

Interest rate	Date loan received	Maturity date	**Outstanding December 31, 2008**	**Issued during the year**	**Repaid during the year**	**Outstanding December 31, 2009**
6.37%	March 2005	March 2010	**$ 17,095**	**$ –**	**$ 17,095**	**$ –**
6.82%	April 2006	April 2011	**15,000**	**–**	**–**	**15,000**
6.41%	March 2007	March 2012	**12,500**	**–**	**–**	**12,500**
			$ 44,595	**$ –**	**$ 17,095**	**$ 27,500**

2008

Interest rate	Date loan received	Maturity date	Outstanding December 31, 2007	Issued during the year	Repaid during the year	Outstanding December 31, 2008
6.37%	March 2005	March 2010	$ 17,095	$ –	$ –	$ 17,095
6.82%	April 2006	April 2011	15,000	–	–	15,000
6.41%	March 2007	March 2012	12,500	–	–	12,500
			$ 44,595	$ –	$ –	$ 44,595

13. Subordinated debentures:

The Company has issued debentures which are unsecured obligations and are subordinated in right of payment to the claims of depositors and other liabilities of the Company. All subordinated debentures are redeemable at the Company's option. Any redemption of this debt, contractual or earlier, is subject to regulatory approval. Interest is paid quarterly on Series 5, 6 and 7 subordinated debentures. Interest on Series 8 subordinated debentures is paid at a fixed rate of 6.50% per annum, payable semi-annually for the first five years of its 10-year term. Thereafter, the Series 8 will bear a floating rate of interest to maturity at 90-day Banker's Acceptance Rate plus 480 basis points, payable quarterly.

2009

Debenture	Interest rate	Issue date	Maturity date	**Outstanding December 31, 2008**	**Issued during the year**	**Repaid during the year**	**Outstanding December 31, 2009**
Series 5	7.31% – 7.58%	2004 / 05	January 2015	**$ 17,519**	**$ –**	**$ 17,519**	**$ –**
Series 6	7.27%	2006	January 2016	**5,000**	**–**	**–**	**5,000**
Series 7	7.10%	2007	January 2017	**9,450**	**–**	**–**	**9,450**
Series 8	6.50%	2009	December 2019	**–**	**23,221**	**–**	**23,221**
				$ 31,969	**$ 23,221**	**$ 17,519**	**$ 37,671**

2008

Debenture	Interest rate	Issue date	Maturity date	Outstanding December 31, 2007	Issued during the year	Repaid during the year	Outstanding December 31, 2008
Series 5	7.31% – 7.58%	2004 / 05	January 2015	$ 17,519	$ –	$ –	$ 17,519
Series 6	7.27%	2006	January 2016	5,000	–	–	5,000
Series 7	7.10%	2007	January 2017	9,450	–	–	9,450
				$ 31,969	$ –	$ –	$ 31,969

14. Shareholders' equity:

(a) Capital stock:

Authorized:

Unlimited number of non-cumulative 5-year rate reset preferred shares, Series 1

Unlimited number of non-cumulative floating rate preferred shares, Series 2

Unlimited number of common shares

Issued and outstanding shares:

	2009			2008		
	Number of shares	**Amount**	**Dividends per share**	Number of shares	Amount	Dividends per share
Preferred shares, Series 1:						
Balance, beginning of year	**–**	**$ –**		–	$ –	
Equity issue	**2,000,000**	**48,523**		–	–	
Balance, end of year	**2,000,000**	**$ 48,523**	**$ 0.61**	–	$ –	$ –

14. Shareholders' equity (continued):

			2009			2008
	Number of shares	**Amount**	**Dividends per share**	Number of shares	Amount	Dividends per share
Common shares:						
Balance, beginning of year	**14,882,710**	**$ 126,993**		12,952,710	$ 87,062	
Equity issue	**–**	**–**		1,900,000	39,340	
Issued on reinvestment of dividends	**11,136**	**189**		–	–	
Issued on exercise of stock options	**10,000**	**195**		30,000	525	
Transferred from contributed surplus relating to the exercise of stock options	**–**	**47**		–	66	
Balance, end of year	**14,903,846**	**$ 127,424**	**$ 0.40**	14,882,710	$ 126,993	$ 0.40

(b) Preferred shares:

Issuance of preferred shares

On September 1, 2009, the Company issued 2,000,000 Series 1 Preferred Shares at a price of $25.00 per share for gross proceeds of $50,000, before issue expenses. Expenses of $1,477 related to the issuance have been recorded in capital stock, net of income taxes recovered of $638. The initial dividend was paid on December 31, 2009 and was $0.605822 per share.

Series 1 – 5 Year Rate Reset Preferred Shares

Holders of Series 1 Preferred Shares are entitled to receive fixed quarterly non-cumulative preferential cash dividends, as and when declared by the Board of Directors, which will be paid at a per annum rate of 7.25% per share for an initial period ending September 30, 2014. Thereafter, the dividend rate will reset every five years at a level of 4.53% over the then five-year Government of Canada bond yield. Series 1 Preferred Shares are redeemable in cash at the Company's option, subject to prior regulatory approval, on September 30, 2014 and September 30 every five years thereafter, in whole or in part, at a price of $25.00 per share plus all declared and unpaid dividends at the date fixed for redemption. Series 1 Preferred Shares are convertible at the holder's option, subject to certain conditions, to non-cumulative floating rate preferred shares, Series 2 (the "Series 2 Preferred Shares") on September 30, 2014 and on September 30 every five years thereafter.

Series 2 – Floating Rate Preferred Shares

Holders of the Series 2 Preferred Shares will be entitled to receive a floating rate quarterly non-cumulative preferential cash dividend equal to the 90-day Canadian Treasury Bill Rate plus 4.53%, as and when declared by the Board of Directors. Redeemable in cash at the Company's option, subject to prior regulatory approval, (i) on September 30, 2019 and September 30 every five years thereafter, in whole or in part, at a price of $25.00 per share plus all declared and unpaid dividends at the date fixed for redemption; or (ii) $25.50 plus all declared and unpaid dividends to the date fixed for redemption in the case of redemptions on any other date on or after September 30, 2014. Convertible at the holder's option, subject to certain conditions, to non-cumulative 5-year rate reset preferred shares, Series 1 (the "Series 1 Preferred Shares") on September 30, 2019 and on September 30 every five years thereafter.

14. Shareholders' equity (continued):

(c) Common shares:

Issuances of common shares

During 2009, 10,000 (2008 – 30,000) shares were issued as a result of the exercise of stock options for cash consideration of $195 (2008 – $525) and $47 (2008 – $66) was transferred from contributed surplus to common shares as a result of these exercises. In addition, 11,136 common shares were issued under the Dividend Reinvestment Plan.

In 2008, the Company issued 1,900,000 common shares, at a price of $21.50 per share for aggregate gross proceeds of $40,850 before issue expenses. Included in these issuances were 1,660,000 common shares which were issued by public offering and 240,000 common shares which were issued under private placement. Expenses of $1,510 related to the issuances have been recorded in capital stock, net of income taxes recovered of $698.

(d) Dividend reinvestment plan:

On March 4, 2009, the Company announced the introduction of a Dividend Reinvestment Plan. Participation in the plan is optional and under the terms of the plan, cash dividends on common shares are used to purchase additional common shares at the volume weighted average trading price of the common shares on the TSX for the five trading days immediately preceding the dividend payment date. At the option of the Company, the common shares may be issued from the Company's treasury or acquired from the open market at market price.

(e) Dividend restrictions:

The Company's subsidiary, Equitable Trust, is subject to minimum capital requirements, as prescribed by OSFI under the *Trust and Loan Companies Act (Canada)*. In addition, OSFI must be notified of any dividend declaration, and prescribes restrictions as to the amount of dividends which can be paid out in any fiscal year.

15. Stock-based compensation:

(a) Stock-based compensation plan:

Under the Company's stock option plan, options on common shares are periodically granted to eligible participants for terms of five or six years and vest over a four or five-year period. The maximum number of common shares available for issuance under the plan is 10% of the Company's issued and outstanding common shares. The outstanding options expire on various dates to December 2015. A summary of the Company's stock option activity and related information for the years ended December 31, 2009 and 2008 is as follows:

	2009		2008	
	Number of stock options	**Weighted average exercise price**	Number of stock options	Weighted average exercise price
Outstanding, beginning of year	**896,750**	**$ 22.99**	692,500	$ 26.14
Granted	**172,000**	**20.42**	284,750	15.52
Exercised	**(10,000)**	**19.52**	(30,000)	17.50
Forfeited/cancelled	**(244,000)**	**18.93**	(50,500)	27.22
Outstanding, end of year	**814,750**	**$ 23.71**	896,750	$ 22.99
Exercisable, end of year	**241,950**	**$ 27.05**	263,500	$ 23.47

15. Stock-based compensation (continued):

The following table summarizes information relating to stock options outstanding and exercisable at December 31, 2009:

	Options outstanding		Options exercisable
Exercise price	Number outstanding	Weighted average remaining contractual life (years)	Number exercisable
$ 24.10	29,000	0.9	23,000
$ 28.75	125,000	1.9	75,000
$ 34.49	150,000	2.2	60,000
$ 31.75	30,000	2.6	12,000
$ 28.79	25,000	2.9	10,000
$ 28.63	30,000	2.9	12,000
$ 24.10	27,500	3.2	5,500
$ 20.90	30,000	3.3	6,000
$ 21.63	25,000	3.4	5,000
$ 11.55	171,250	3.9	33,450
$ 10.00	3,000	4.2	–
$ 20.60	169,000	5.9	–

Under the fair value-based method of accounting for stock options, the Company has recorded compensation expense in the amount of $761 (2008 – $841) related to grants of options under the stock option plan. This amount has been credited to contributed surplus. The fair value of options granted during 2009 was estimated at the date of grant using the Black-Scholes valuation model, with the following assumptions: (i) risk-free rate of 3.7% (2008 – 2.8%); (ii) expected option life of 4.0 years (2008 – 4.0 years); (iii) expected volatility of 30.0% (2008 – 28.1%); and (iv) expected dividends of 1.9% (2008 – 2.8%). The weighted average fair value of each option granted during 2009 was $3.67 (2008 – $2.77).

(b) Deferred share unit plan:

On February 25, 2009, the Board of Directors approved a DSU Plan for Directors for implementation during the year ended December 31, 2009. Under the DSU Plan, notional units are allocated to a Director from time to time by the Board of Directors and the units vest at the time of the grant. When an individual ceases to be a Director (the "Separation Date"), the DSUs shall be redeemed for cash no later than the end of the first calendar year commencing after the Separation Date. The redemption value of each DSU redeemable by a Director is the volume-weighted average trading price of the common shares of the Company on the TSX for the five trading days prior to the Separation Date. In the event of any stock dividend, stock split, reverse stock split, consolidation, subdivision, reclassification or any other change in the capital of the Company affecting its common shares, the Company will make, with respect to the number of DSUs outstanding under the DSU Plan, any proportionate adjustment as it considers appropriate to reflect that change. A Director will be credited with additional DSUs whenever a cash dividend is declared by the Company. The DSU Plan will be administered by the Board or a committee thereof. For the year ending December 31, 2009, 8,046 DSUs had been granted by the Company. The Company has recorded compensation expense in the amount of $172 (2008 – nil) related to DSUs granted during the year.

16. Earnings per share:

Diluted earnings per share are calculated based on net income available to common shareholders divided by the weighted average number of common shares outstanding, taking into account the dilution effect of stock options using the treasury stock method.

	2009	2008
Earnings per common share – basic:		
Net income	$ 51,438	$ 38,611
Dividends on preferred shares	1,212	–
Net income available to common shareholders	$ 50,226	$ 38,611
Weighted average basic number of common shares outstanding	14,888,797	13,841,836
Earnings per common share – basic	$ 3.37	$ 2.79
Earnings per common share – diluted:		
Net income available to common shareholders	$ 50,226	$ 38,611
Weighted average basic number of common shares outstanding	14,888,797	13,841,836
Adjustment to weighted average number of common shares outstanding		
Stock options	40,104	30,724
Weighted average diluted number of common shares outstanding	14,928,901	13,872,560
Earnings per common share – diluted	$ 3.36	$ 2.78

For the year ended December 31, 2009, the calculation of the diluted earnings per share excluded 602,636 (2008 – 608,874) average options outstanding with a weighted average exercise price of $26.73 (2008 – $26.81) as the exercise price of these options was greater than the average price of the Company's common shares.

17. Capital management:

Equitable Trust manages its capital in accordance with guidelines established by OSFI, based on standards issued by the Bank for International Settlements, Basel Committee on Banking Supervision (Basel II). This guideline requires deposit-taking financial institutions to maintain a minimum ratio of capital to risk-weighted assets and off-balance sheet items of 8%, of which 4% must be Tier 1 capital ("Tier 1") and the remainder supplementary capital ("Tier 2"). However, OSFI has established that deposit-taking institutions need to maintain a minimum total capital ratio of 10%, with a Tier 1 ratio of not less than 7%. Equitable Trust's Tier 1 capital is comprised of common and preferred shareholder's equity while Tier 2 capital is comprised of subordinated debentures. In addition to Tier 1 and total capital ratios, Canadian deposit-taking institutions are required to ensure that their assets-to-capital multiple, which is calculated by dividing gross adjusted assets by total capital, does not exceed the maximum level prescribed by OSFI.

On September 1, 2009, Equitable Trust issued 2,000,000 non-cumulative preferred shares at a price of $25.00 per share for gross proceeds of $50,000. These preferred shares qualify as Tier 1 capital.

During the year, Equitable Trust redeemed $34,614 of Series 5 subordinated debentures, of which $17,095 was held by the Company. The Company used these funds to repay a portion of its term loan facility and in turn issued $23,221 in Series 8 subordinated debentures. The gross proceeds of this issuance were used by the Company to invest in Series 8 subordinated debentures issued by Equitable Trust.

Equitable Trust maintains capital management policies to govern the quality and quantity of capital utilized in its operations. The objective of these policies is to ensure that adequate capital requirements are met, while providing sufficient return to investors. During the year, Equitable Trust complied with all internal and external capital requirements.

17. Capital management (continued):

Regulatory capital (relating solely to Equitable Trust) is as follows:

	2009	2008
Tier 1 capital:		
Common shares	**$ 129,337**	$ 128,162
Non-cumulative preferred shares	**50,000**	–
Contributed surplus	**2,852**	2,138
Retained earnings	**189,715**	146,901
Accumulated other comprehensive loss[1]	**(5,953)**	(20,330)
Total	**365,951**	256,871
Tier 2 capital:		
Subordinated debentures (Tier 2B)[2]	**65,171**	76,564
Total	**65,171**	76,564
Total regulatory capital	**$ 431,122**	$ 333,435

(1) *As prescribed by OSFI, certain components of accumulated other comprehensive income are included in the determination of regulatory capital. Net unrealized fair value losses on available for sale equity securities are deducted in the determination of Tier 1 capital while net unrealized fair value gains on available for sale equity securities are included in Tier 2A capital.*

(2) *Tier 2B capital may be included in Tier 2 capital to a maximum of 50% of net Tier 1 capital.*

18. Commitments and contingencies:

(a) The following table summarizes the contractual maturities of the Company's financial liabilities as at December 31, 2009:

		Payments due by period			
	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
GIC principal and interest[1]	$ 3,489,892	$ 2,036,110	$ 1,100,350	$ 353,432	$ –
Subordinated debentures principal and interest[1]	63,616	2,544	5,088	5,088	50,896
Bank term loans principal and interest[1]	30,592	1,824	28,768	–	–
Other liabilities	54,257	22,725	17,684	10,488	3,360
Total contractual obligations	$ 3,638,357	$ 2,063,203	$ 1,151,890	$ 369,008	$ 54,256

(1) *The balances for the financial liabilities above will not agree with those in our consolidated balance sheet as this table incorporates all cash flows, on an undiscounted basis, including both principal and interest.*

18. Commitments and contingencies (continued):

(b) The Company is committed to annual payments under two non-cancellable operating leases for office premises through 2015. Annual payments are:

2010	$ 575
2011	552
2012	540
2013	572
2014	572
Thereafter	572
	$ 3,383

In addition to these minimum lease payments for premises rental, the Company will pay its share of common area maintenance and realty taxes over the term of the leases.

(c) The Company has commitments to fund a total of $318,919 (2008 – $94,361) of mortgages in the ordinary course of business at year end.

(d) In the normal course of operations, the Company enters into agreements that provide general obligations in connection with its loan securitization activities. The nature of these agreements prevents the Company from making a reasonable estimate of the maximum amount required to be paid. There are no expected credit losses as the mortgages are government guaranteed.

(e) The Company is subject to various claims and litigation arising from time to time in the ordinary course of business. Management has determined that the aggregate liability, if any, which may result from various outstanding legal proceedings would not be material and no provisions have been recorded in these consolidated financial statements.

19. Related party transactions:

Certain of the Company's directors and officers have purchased GIC deposits, and/or purchased subordinated debentures from the Company. These purchases were made in the ordinary course of business at terms comparable to those offered to unrelated parties. As at December 31, 2009, directors and officers held $1,701 (2008 – $652) of GIC deposits and $3,650 (2008 – $3,947) of subordinated debentures.

In 2008, the Company issued 1,900,000 common shares, at a price of $21.50 per share for aggregate gross proceeds of $40,850 before issue expenses. Included in the issuance were 1,660,000 common shares which were issued by public offering and 240,000 common shares which were issued under private placement to Emberwood Glen Enterprises Ltd., a wholly-owned subsidiary of Oakwest Corporation Limited, whose controlling shareholders are directors of the Company.

20. Interest rate sensitivity:

The following table shows the Company's position with regard to interest rate sensitivity of assets, liabilities and equity on the date of the earlier of contractual maturity or repricing date, as at December 31, 2009:

	Floating rate	0 – 3 months	4 – 12 months	1 – 5 years	Greater than 5 years	Non-interest sensitive	Total[(1)(2)(3)]
Assets:							
Cash and cash equivalents and restricted cash	$ 400,835	$ –	$ –	$ –	$ –	$ –	$ 400,835
Effective interest rate	0.51%	–	–	–	–	–	0.51%
Investments purchased under reverse repurchase agreements	–	129,721	–	–	–	–	129,721
Effective interest rate	–	0.23%	–	–	–	–	0.23%
Investments	–	48,858	34,872	301,656	9,072	(6,421)	388,037
Effective interest rate	–	4.35%	4.28%	3.47%	4.01%	–	3.73%
Securitization retained interests	–	8,763	25,615	99,536	12,215	1,066	147,195
Effective interest rate	–	3.48%	3.48%	3.42%	4.28%	–	3.48%
Mortgages receivable	821,444	217,930	665,817	1,017,970	25,660	14,199	2,763,020
Effective interest rate	4.32%	6.23%	5.73%	6.24%	5.94%	–	5.51%
Other assets	–	–	–	–	–	17,266	17,266
Total assets	$ 1,222,279	$ 405,272	$ 726,304	$ 1,419,162	$ 46,947	$ 26,110	$ 3,846,074
Liabilities:							
Customer deposits	$ 688,782	$ 294,176	$ 980,042	$ 1,307,730	$ –	$ 61,589	$ 3,332,319
Effective interest rate	0.72%	1.18%	2.17%	3.68%	–	–	2.34%
Other liabilities	–	–	–	–	–	74,723	74,723
Bank term loans	–	–	–	27,500	–	–	27,500
Effective interest rate	–	–	–	6.63%	–	–	6.63%
Subordinated debentures	–	–	–	23,221	14,450	–	37,671
Effective interest rate	–	–	–	6.50%	7.16%	–	6.75%
Shareholders' equity	–	–	–	48,523	–	325,338	373,861
Total liabilities and shareholders' equity	$ 688,782	$ 294,176	$ 980,042	$ 1,406,974	$ 14,450	$ 461,650	$ 3,846,074
Excess (deficiency) of assets over liabilities and shareholders' equity	$ 533,497	$ 111,096	$ (253,738)	$ 12,188	$ 32,497	$ (435,540)	$ –
Total assets – 2008	$ 1,513,756	$ 877,383	$ 295,808	$ 1,323,037	$ 12,648	$ 64,919	$ 4,087,551
Total liabilities and shareholders' equity – 2008	$ 826,438	$ 1,198,003	$ 542,094	$ 1,089,208	$ 31,969	$ 399,839	$ 4,087,551
Excess (deficiency) of assets over liabilities and shareholders' equity – 2008	$ 687,318	$ (320,620)	$ (246,286)	$ 233,829	$ (19,321)	$ (334,920)	$ –

[(1)] *Totals include interest sensitive interest rate hedges at the notional amount.*

[(2)] *Accrued interest is excluded in calculating interest sensitive assets and liabilities.*

[(3)] *Potential prepayments of fixed rate mortgages have not been estimated. Cashable GICs are included with floating rate liabilities as these are cashable by the depositor upon demand. Any prepayments of subordinated debentures, contractual or otherwise, have not been estimated as these would require pre-approval by OSFI.*

20. Interest rate sensitivity (continued):

At December 31, 2009, an immediate and sustained 1.0% decrease in interest rates that is not allowed to decrease beyond a floor of 0% (and is therefore not allowed to be negative) would positively impact net interest income by $0.2 million during the 12 months that follow. For the purpose of this sensitivity analysis, Cashable GICs are assumed to perform in the same manner as floating rate liabilities. Certain assumptions have been made with respect to prepayment of fixed rate mortgages. No prepayments of subordinated debentures and bank term loans, contractual or otherwise, have been assumed.

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an investment holding company

Eric Beutel
Vice-President, Oakwest Corporation Limited,
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Joseph Dickstein
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Eric Kirzner
Professor of Finance, Rotman School of Management,
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Andrew Moor
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Katherine Rethy
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President, KAR Development Corp.,
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Lionel Robins
President, PFDL Investments Limited,
an investment holding company

Morris Shohet
Principal, The Dorchester Corporation,
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Michael Shulman
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OFFICERS

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Chief Risk Officer of Equitable Trust

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Chief Compliance Officer and Secretary
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Vice-President, Financial Controls of Equitable Trust

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John Simoes
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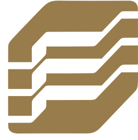
Stock Listings
TSX: ETC and ETC.PR.A

Annual Meeting of Shareholders
Monday, May 17, 2010, 10 a.m. EST
TSX Broadcast Centre
The Exchange Tower
130 King Street West
Toronto, Ontario, Canada

Dividend Reinvestment Plan
For information regarding Equitable Group's dividend reinvestment plan, please contact the Plan Agent at www.computershare.com or toll free at 1.800.564.6253. To obtain a copy of the Offering Circular, Enrollment Form and to review commonly asked questions, please visit the Company's website at www.equitablegroupinc.com under Investor Relations.



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