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EDITED TRANSCRIPT

EQB.TO - Q3 2021 Equitable Group Inc Earnings Call

EVENT DATE/TIME: NOVEMBER 03, 2021 / 12:30PM GMT

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PRESENTATION

Operator

Welcome to Equitable's Third Quarter Analyst Call and Webcast on Wednesday, November 3, 2021. It is now my pleasure to turn the call over to Richard Gill, Senior Director, Corporate Development and Investor Relations at Equitable. Please go ahead, sir.

Richard Gill;Senior Director, Corporate Development and Investor Relations

Thanks, ma'am. Your hosts today are Andrew Moor, President and Chief Executive Officer; Chadwick Westlake, Chief Financial Officer; and Ron Tratch, Chief Risk Officer. For those on the phone lines only, we encourage you to log on to our webcast as well as it includes our quarterly slide deck, including Slide 2, containing Equitable's caution regarding forward-looking statements. It's now my pleasure to turn the call over to Andrew.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Thank you, Richard, and good morning, everyone. I'm really pleased with the Bank's progress this year. Equitable is now larger, more diversified and more capable than ever. In every area across our single-family alternative, wealth accumulation, commercial loan and leasing businesses and EQ Bank. Our teams are challenging a status quo, working really hard to fulfill our purpose every day, and generating great success. Today, we're 3 quarters complete towards our high-growth ambition for 2021. I will offer more context of what our record commercial loan growth and outstanding performance at EQ Bank mean for the fourth quarter and offer an early look at 2022 guidance we normally reserve for February. Chadwick will then provide more details, and Ron is here to address questions on our credit outlook, which has continued to improve.

To start, I'll remind you that we raised 2021 growth targets in May based on our read of demand signals and clear sign that Canadians and increasing numbers are ready to embrace fintech -driven Challenger Bank services. This was the right call. Today, we are within striking distance of achieving our 2021 growth objectives. We have conviction that at the end of Q4, we will meet or exceed all of our stated targets on a full year basis. Pursuing these objectives, we've gained the trust of a significant number of new customers. And through engagement metrics, we know Canadians are relying on us more than ever to give them the enriching experience that we promised.

Looking at the trend beyond Q4, we foresee another great year ahead for Canada's Challenger Bank, reflecting the expected impact of continued strong growth in higher-margin conventional loans, plus an additional cost of funds tailwind with the benefit of our new covered bond program. Following our Q4 results next February, we will provide more detailed guidance. What we want to notably offer today includes perspective on ROE, our North Star, capital and key balance sheet categories that drive earnings. One of the most important categories of alternative single-family loan portfolio, which we expect to grow 12% to 15% next year. This guidance partly rests on the assumption that housing activity will return to a more

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normal cadence post pandemic. We like the prospect of greater stability that allows us to focus on the fundamentals of service excellence rather than making disruptive adjustments to our risk appetite. A return to the office for many workers and Caritas plan to worker to 420,000 permanent residents next year will help big city real estate, where the bank has a very strong franchise and a constructive view of risk. Once again, we forecast a significant expansion of wealth decumulation business. In 2022, we are targeting Reverse Mortgage asset growth of more than 150%, and CSV asset growth, up more than 100% on market share gains and mutual success with our business partners. Our ambitions are also high for a commercial bank lines, and we published 2022 targets, reach to our conventional and commercial loan categories. For EQ Bank, we will seek 20% to 30% deposit growth, a target that does not take into account the expected uplift from planned innovations and payments to arrive in 2022. To achieve our goal, we intend to give customers more products to use and more reasons to use them, which is good for them and good for the bank as it means keeping customer lifetime value well ahead of acquisition costs. Of note, as interest rates rise, we expect EQB or EQ to be an even more competitive source of funds for the Bank. As you know in the past calls, our EQ Bank is a huge part of our plan, but it is only one element of growing and diversifying our deposit book. Directionally, our 2022 outlook supports ROE of 15% or greater, consistent with our historical best-in-class returns.

Now, the third quarter results and further context our milestone achievement. Assets under management surpassed CAD 40 billion at September 30, 13% or CAD 4.7 billion higher than a year ago last year. As managers, we do think long term, and it pleases me to note that the bank's AUM is more than twice as large as it was at the end of 2015. As you saw on that earlier slide, our full year 2021 target for total loan growth is 8% to 12%. After 9 months, we're now at 14% with good contributions from both sides of the bank. What's important is that year-over-year loan growth of 17% in the commercial bank and 13% of the personal bank, very much favored wider spread conventional loans. Conventional loans are the earnings engine of this bank, so it's good to know that Q3 was our most productive quarter ever for conventional loan accumulation. For institutional is incredibly disciplined in risk management, you can draw an important conclusion We believe it is now entirely prudent to put more risk-weighted capital to work than a year ago because the economic recovery, including a recovery of all the jobs lost during the pandemic. I'm particularly pleased with the performance of our single-family alternative business, our largest generator of conventional loans. We achieved record originations of CAD 2 billion in Q3, more than 3 times higher than last year when we constrained asset growth to control risk exposure, and CAD 251 million higher than the previous quarterly record set in Q2 2021. Retention rates also improved towards pre pandemic levels. By working hard to reinforce our standard with mortgage broker partners and support their businesses, these results prove that we've regained momentum as the market leader, all while maintaining our traditional underwriting disciplines. For our personal bank, the other big news was a sharp increase in our wealth deccumulation book, where asset shot passed the CAD 200 million mark, led by a 229% year over growth in reverse mortgage balances. The reverse mortgage market is a sleeping giant. Before entering in 2018, we spent considerable time, studying the high-growth equity release markets in the UK and Australasia. And the reason that equitable had the opportunity to build a position on for growth but propelled by underlying demographic forces of an aging population. We also believed and continue to believe that innovation can benefit this market. Competitively, the presence of just one monoline lender in the entire Canadian market was also appealing. Let Linda was recently acquired by the Ontario Teachers' Pension Plan, what we understand was an attractive price-to-book value multiple for the sellers. Meanwhile, CSV ranges 127% growth year-over-year. With the third quarter addition of Foresters Financial, we now have arrangements with 8 leading partners to bring cash surrender bank lines of credit to their policyholders. We're working to expand the breadth and depth of our relationships.

On the commercial side, loan assets increased 17% to a record CAD 10.1 billion, with record quarterly commercial loan originations of CAD 1.3 billion, 14% ahead of last year. The strongest contributor was conventional-commercial, where production was up 53% year-over-year to CAD 786 million. In comparison to 2021 targets, each commercial line was on or ahead of plan. In the interest of time, I will single out 2. After experiencing elevated scheduled maturities in Q2, our commercial Finance group came back strong in Q3, with year-over-year loan growth of 21%, right in line with our annual objective. Within equipment leasing, portfolio growth of 25% year-over-year was well ahead of our target range for the year. The drive is the transportation and logistics sector of the economy. The credit metrics in this business are performing very well, and I'm delighted with the performance of this business since we bought it just over 2 and a half years ago. We also set out to build stronger channels to market for both our multiunit and Prime Single-Family Assured Mortgage businesses as a means of improving franchise value, and we're doing that, too. Our growth ambitions and our broader purpose of enriching people's lives are very much supported by the fantastic success of our digital platform and fintech-related operations. This year, we've added real substance to our claim on making EQ Bank the hub that Canadians to rely on for the most important financial transactions, and we're seeing the benefits. EQ Bank deposits grew 60% over 2020 to a record CAD 6.9 billion at September 30 against our full year 30% to 50% target. Growth continued through October as EQ Bank deposits surpassed CAD 7 billion and the number of customers increased to CAD 240,000. I'm proud of the fact that we reward all customers with good everyday rates and an even better experience. While this means that we don't chase hot money, it does say something really positive about our customer philosophy and the confidence we now have in the services we offer. In Q3, those services were well used. Digital transactions increased 99% on a year-to-date basis. Engagement like this

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means EQ Bank is becoming more important in the lives of our customers. One of those new services is the EQ Bank US Dollar Account. Launched in June to address the need of financially savvy customers who want real-time exchange rates with full-fee transparency, and easier, cheaper and faster money transfers and US dollars worldwide. It reached our annual deposit growth goal in the first quarter. With ongoing account growth and now have nearly CAD 150 million of deposits that has formed a source of growing non-interest FX revenue for the Bank. I know I'm repeating myself by saying how proud I am with the US dollar capability we've built, but I do urge you to use this solution to really experience what a state of the art digital bank is capable of delivering.

Our journey to enrich people's lives continues. In late September, we launched a new e-transfer service. Our original capability was built using our minimum viable product philosophy. We replaced this basic service with an innovative capability using the insights we gained by talking to customers. There has never been a better time to have a modern, flexible, cloud-based infrastructure. I'd say so, not only because it enables us to serve Canadians the way they wish to be served, but because the future will see the modernization of Canada's payments infrastructure, and the advent of open banking. The real-time rail, a major part of that modernization effort will arrive in the next couple of years in the former national payment system that will enable fast data-rich payments, giving Canadians the ability to move meaningful sums of money instantly and with certainty. We are readying ourselves in this bank in several ways. In the second half of 2022, we will introduce an EQ Bank payment card. True to our brand philosophy, we'll allow customers to use their cards to make e-commerce and in-store purchases, along with cash withdrawals, all with no fees, attractive rewards and a seamless or digital experience. The EQ card will add an important new level of convenience for customers and some (inaudible) status as a fully capable hub bank. The card will also add an interchange-based revenue stream for the bank. We recently entered a 6-year strategic arrangement with Mastercard as a formative step in our payments plan. That plan also envisions offering credit card services to fintechs and others by positioning equitable for what's known in the industry as a bin sponsorship. Thinking more broadly, as part of our payment strategy, we are committed to connecting directly to the real-time rail. This will allow us to enable real-time payments and become a service provider for fintech to connect into the RTR.

Another important milestone achieved in Q3 is that the Bank became carbon neutral in our Scope 1 and Scope 2 greenhouse gas emissions with details contained in the press release issued last night. Our emissions per dollar of revenue are far lower than branch-based banks. We'll share more details on our ESG strategy and a new report next year, and plan to set meaningful reduction targets that align with the bank's purpose. We think publicly expressing targets, whether for GHG or asset deposit growth gives all stakeholders a means to assess progress and holds to account. Stepping back, it's been just every year since Chadwick joined as part of our broad organizational redesign, and the realignment into personal and commercial banking divisions led by Mahima Poddar and Darren Lorimer respectively. We made those changes to ensure that our structure and leadership are suitable for institution is far bigger and more capable than the Equitable evolves. We also added more strength and depth in our management team with key hires and promotions in many areas of the bank. I'm glad to have the executive talent around decision-making and strategy development that is increasingly aligned -- well aligned with our long-term ambitions. We absolutely have the proven management talent to take care of Canada's Challenger Bank to the next level and detailed plans in place behind all of our 2022 targets. Most important, our team numbering over 1,000 Challengers is aligned and ready to take on new possibilities with the creativity and discipline that has been so critical to record-breaking performance this year. My thanks to all team members.

Chadwick, over to you.

Chadwick Westlake - *Equitable Group Inc. - Senior VP & CFO*

Thanks, Andrew, and good morning, everyone. As a footnote to Andrew's comments about leadership, we will also be sending out save-the-dates in coming weeks for an Investor Day that will land at the end of February or early March 2022. At which time, you will see our broader team in action and in person. Results for the third quarter and first 9 months are right on point as we close in on meeting our high-growth targets for 2021. As expected, we made significant investments in order to create future shareholder value, while delivering the ROE, CET1, book value in EPS growth that rewards our owners today. I'm pleased to say that among Canadian banks, Equitable's 2021 performance to date continues to stand out. Through Q3, risk-managed deployment of capital resulted in growth of 13% year-over-year and 6% quarter-over-quarter in AUM. This reflected CAD 3.8 billion of originations, up CAD 1.5 billion from suppressed levels in Q3 last year. As Andrew said, we purposely skewed growth in favor of wider merge in conventional loans, all while remaining within our prudent risk appetite framework. Growth in those assets, combined with wider spreads arising from lower funding costs, provided NII and NIM expansion in Q3, and a favorable tailwind for earnings in the coming quarters. The work we've done to broaden and improve funding sources is paying off. Total deposits of CAD 98.8 billion were up 21% year-over-year, including

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digital bank deposit growth of 60%. Quarterly revenue increased to an all-time high of CAD 162.1 million, plus 9% year-over-year and plus 2% sequentially. The outcome was our best quarterly earnings performance of 2021 so far with Q3 diluted EPS of CAD 4.14 a share. Just as a reminder, the numbers we present today are on a pre-split basis as the 2 for one common share split occurred into Q4 as of trading on October 26. Reporting on a new share count basis will be at the Q4 results.

Compared to last year, Q3 EPS was lower by CAD 0.16, half due to an increase in diluted shares outstanding, 1/3 resulting from planned investments into new capacity, digitization and process improvements. And the remainder of the results of temporarily elevated gains in securitization last year due to COVID-related funding market disruptions. EPS through the first 9 months of 2021 was the best ever and up 38% from 2020. On ROE, our bank delivered again at 16% in Q3 and 16.6% year-to-date, compared to our target of 15% to 17%. We chose to deploy more of our excess capital in Q3 to generate higher future earnings. Notwithstanding, CET1 remained well in our target range of 13% to 14%. If CET1 was at our target floor of 13%, ROE would have actually been about 17.2% in Q3. We think expressing excess capital versus the target for, rather than the mid-range of CET1 as we've done in the past, provides a more meaningful reflection of our excess capital. As in Q2, we did have a PCL reversal in Q3, reflecting improving economic variables. Aside from the impact of PCLs, pre-provision pre-tax income was higher than in Q2 and in Q1, and book value per share shot ahead to CAD 105.8 a share after breaking the CAD 100 barrier for the first time last quarter.

Moving to funding. Our markets continue to provide everything we need to grow with our recent success in adding more digital deposits, expanding our institutional deposit note program with a highly successful first issuance of our European covered bond program. We've improved our cost of funds sequentially. We issued EUR315 million of covered bonds in September, or more than CAD 500 billion. This is at a spread of just 15 basis points over euro mid swaps, which translates to this becoming the lowest cost of wholesale funding under stack, more than 55 basis points cheaper than GICs. We were very pleased to earn participation by more than 40 net new international institutional investors across 15 countries, resulting in a 3 times oversubscribed first issuance. These bonds have been trading well since the issuance and are now marked at a spread of 11 basis points over Euro mid swaps or about 4 basis points tighter than issue, making it successful transaction from both the issuer and investor perspective. We have CMHC's approval to make this a CAD 2 billion program, and you can rest assured, we will take full advantage. We expect to be back in the market later in Q2 or into Q3 next year. I've mentioned this in past calls, but I will reiterate that our program maturity with this early success, we could expect to see annual cost of fund savings of more than CAD 11 million, higher than previous guidance. We are well positioned with liquidity of CAD 3.2 billion at the end of Q3, and a liquidity ratio of 9.3% versus 9.1% a year ago. The combination of higher asset growth and lower cost of funds translated into Q3 NII growth of 18% year-over-year to CAD 150.9 million and NIM of 1.83%. NIM expanded both sequentially and year-over-year. In both cases, this is the result of the shift to conventional loans, particularly alternative single-family. Compared to 2020, NIM growth in Q3 was also due to higher levels of prepayment income within the personal bank loan portfolio. Sequentially, this was a headwind. The highest yielding business line contributes -- continues to be leasing at 9.8% in Q3, which is a little lower than a year ago, reflecting Bennington's success in growing its prime business, which has increased approximately 73% year-over-year.

NIM for the remainder of 2021 is expected to be relatively consistent with Q3 as we continue to shift our mix of business to uninsured assets, while prepayment income declines from the seasonally high summer months. Prepayment income is variable as are other factors such as seasonal variations in our liquidity holdings that may shift them in a given quarter. Currently, the Bank's noninterest income growth is heavily influenced by derecognition volumes and gains on sale, both of which were abnormally high last year due to funding market disruption caused by the pandemic, and lower in Q3 this year as markets stabilized. This revenue from gains on sale has returned to normalized pre COVID levels. In Q3, fees and other income grew 12% year-over-year. This is an early reflection of our plan to increase the flow of non-interest income from new products like the EQ Bank US Dollar Account. It will take time to make this flow more meaningful, but we are challenging ourselves to work towards double-digit growth in non-interest income annually, outside of gains on sale, which are driven by other market factors. This will include flow from some of the payment innovations that Andrew mentioned. Our new aggregator business, FX, continued gains from strategic investments in fintechs, wealth solutions and much more to come.

On our last call, I said to expect expense growth to return to low single-digit quarter-over-quarter levels in both Q3 and Q4 after a big uptick in the first half of 2021. And that's exactly what transpired. Total non-interest expenses were up 3.8% sequentially. This means we continue to operate within our 2021 full year efficiency target of 39% to 41%. After 3 quarters, we're at 40.3%. We expect to end 2021 within our target range. We've been making incrementally smart -- more smart investments for the future while generating our North Star ROE and keeping a lens to our best-in-class efficiency. We look at costs in 3 buckets, of people, process and platform. For people, we increased compensation costs 19% year-to-date and 3% quarter-over-quarter. The sequential increase reflected growth in FTE, the year-to-date increase reflected talent additions, but also more competitive

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compensation. We have world-class talent we need to compensate accordingly. For processes, including corporate and marketing categories, expenses were down slightly quarter-over-quarter, even as we launched a campaign in June to support our reverse mortgage business, which contributed to a sizable market share gain. Growth in process improvements over the first 9 months reflected marketing support for reverse mortgages in EQ Bank with good results. In platform, Q3 product costs were up 4% quarter-over-quarter and 27% year-over-year. These are good costs. We refer to them as investments as they will pay off next year and beyond. I think it's worth noting that amortization and increasing technological programs can have an impact in this category. 5 percentage points of the 20% increase in non-interest expenses over the first 9 months was due to overall higher depreciation and amortization. Within our 2021 guidance, we said to expect a continued positive trend in credit metrics and the reopening of the economy. In Q3, we had a CAD 3.5 million reversal of Stage 1 and Stage 2, as previously expected, credit losses did not materialize, and I'm pleased to say macroeconomic forecast improved across 2-key variables since Q2, unemployment and HPI. These positive macro-variable changes resulted in a decline in expected loss rates on both Stage 1 and Stage 2 loans. While reversals occurred across all portfolios, our single-family and leasing portfolios benefited to a greater extent from this positive trending than our commercial real estate book. Of note, we did not make any changes to our 5-scenario weights. And if our base case translates, we will be in a position to release potentially CAD 4.2 million. Our overall ACL now sits at CAD 52.1 million, 8% lower compared to Q2, and 25% lower year-over-year, but still up from what we would view as a potentially normalized level of approximately CAD 49. To put this into context, we currently hold 17 basis points in ACL, appropriately elevated from 14 basis points prior to the emergence of COVID, but gradually reducing to near-normal levels as the economy continues to improve. As a forward-looking comment, we expect credit loss provisions on our loan book to remain low or reverse further next quarter and into 2022, assuming the path that Canada's economic recovery reflects our base case and losses remain low. Arrears in our personal bank and commercial bank are also expected to remain low, with midterm annualized loss rates of 1 to 2 basis points for our mortgage portfolio and 150 to 200 basis points for equipment leasing. Gross impaired loans were down 40% sequentially and down 21% year-over-year. The improvement since Q2 was due to the resolution of 2 commercial loans amounting to CAD 40.1 million, plus a CAD 9.4 million net reduction in single-family mortgages and equipment leases. While we have a great track record of managing risk, we also know how to resolve problem loans when they occur.

Moving to capital. The story of the quarter is about increased deployment to build an even stronger earnings platform for 2022. RWA increased 8% sequentially to CAD 12.4 billion in Q3. As a result, the CET1 ratio of 13.7% was down 7 basis points from Q2. But as I mentioned earlier, this remains within our range of 13% to 14%. Compared to our 13% target floor, we now have excess capital of about CAD 88 million or CAD 5.17 a share. From our perspective, this is the best way we can deploy excess capital toward organic growth that will provide consistent and predictable NII growth in coming quarters. We were also pleased to gain strong shareholder support for our first ever stock split on a 2 for one basis, with 82% of eligible votes cast and 99.9% support. As I noted, shares began trading on a split basis on October 26. This is part of our broader program towards closing what we firmly believe remains a material discount in our share price at fair valuation. In closing, we're moving from strength to strength. Q3 has set us up perfectly to deliver on our annual growth targets, and we expect to start 2022 in great shape, ready to take on the challenge associated with our new, next level ambitions, as Andrew outlined this morning.

With that, I'll ask the operator to open the line up to your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Meny Grauman with Scotiabank.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

Chadwick, you highlighted risk-weighted asset growth, 8% sequentially. Clearly, strong loan growth is a big part of that story, but it doesn't seem to be explaining everything. So I'm just wondering if there's anything else driving that. I don't know if it's simply as business mix. Anything you can add to highlighting what's driving that RWA growth that's so strong on a sequential basis.

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Chadwick Westlake - *Equitable Group Inc. - Senior VP & CFO*

Yes. It is the conventional loan portfolio, though, Meny. So as you've seen, a lot of our growth -- the focus of our growth has been the alternative portfolio in key commercial categories, including the great growth, say, for example in specialized leasing right across the commercial book. So those have higher risk weights, of course, which are driving up the RWA at a faster pace, but they're going to translate with better margins. And that's part of why we had the conviction in improving NII growths from here. That's really the art of it. Because, of course, again, when you look at the pipeline or when the loans were booked, it was -- sometimes that can land a little bit later in the quarter, right? So you see the RWA go up, but the earnings are not yet reflected, hence the set one dropped a little bit.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Meny, just to reiterate what Chadwick said. To finish that, I think it's important to reinforce that you're not really seeing the earnings growth from that risk-weighted asset growth. Flow-through in this -- entirely this quarter. But obviously, we start at the beginning of October in great shape because we've got those assets on our books. But I would say that September was where we started to see a lot of the asset growth. The other thing is, just similarly, on the covered bond side, the covered bond was issued quite a bit towards the end of the quarter, so we didn't really see much benefit from that in the current quarter, but in the quarter we're just reporting, but in this current quarter, we should start to see that flow-through.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

And then just in terms of the outlook for RWA growth based on your guidance for 2022, it seemed like you're expecting RWA growth to moderate in 2022. Just wanted to check your thoughts on that.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Just a little bit. I mean clearly, we've seen some dramatic growth in the alternative single-family business. We continue to believe that the market is in great shape, and we're really well-positioned to continue to gain market share within it. But nonetheless, I think our guidance, as we commented in the script, is based on a slightly more normal cadence for the sales in the housing market.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

And then in terms of the outlook for 2022, I'm not sure if you mentioned it, but what's baked in terms of your rate expectations for 2022, underpinning some of the guidance that you provided us?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. We don't really build in any rate expectations. So we don't see that as -- we haven't certainly built in any kind of increase in NIM based on rates going up. I did allude to that in my comments around a belief that as Prime rates increase, for example, that we wouldn't follow lockstep in the EQ Bank side of things. So maybe some reasonable NIM to be captured if you do see Prime go up, but that hasn't been factored into any of our projections at this point.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

And then just one more for me on that front. You highlight portfolio growth expectations for 2022 over a number of categories, but I'm wondering if you sum it all up, how does loan growth look relative to the 8% to 12% range that you gave for 2021. What would you expect for 2022?

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Chadwick Westlake - *Equitable Group Inc. - Senior VP & CFO*

Yes. So the average for this year was more in that 8% to 12% range. The next year, we'll look more in the 12% to 15% range.

Operator

Your next question comes from Jaeme Gloyn with National Bank.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

First question is on the payments card launch. If you could maybe just give us a little bit more color as to what you're expecting from customer acquisition, client retention and potential revenue coming off of that in our change fees, or is there anything else that we should be thinking about on the payments card launch?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. So thanks for that question. So the -- we know from our customer research, we do have some really interesting conversations with our customers, and that really drives our thinking about where to go next with product, that there are -- a significant number of our current customers and particularly some customers that choose not to sign up with us because they believe they can't make payments or direct cash. So the principal part of the play, at least at this point for us is to eliminate that objection and allow them -- allow people to use the EQ Bank product as a much more fundamental source of -- much more fundamental relationship. It will be -- we almost have to get there and deliver the card to see how that will play out. Now in order to -- there is obviously a cost around building a card solution. And so in order to defray our cost because we can spread them across a broader range of services, but also provide useful services to our -- many of our partners already in the fintech community. We'll be launching that bin sponsorship approach so that's for non-regulated FIs that want fintechs -- that want to offer a prepaid card solution, we would be the card new would be the bank underlying those solutions. So that gives us 2 elements -- 2 sides to the story. The interchange revenue, we'll give you better guidance when we get to, say, the Investor Day and the early part of next year. We're not building a lot of interchange revenue associated with this from our own operations, but we do already see significant revenues coming from third-party services. We currently have 1/3 party fintech under contract with us to deliver the service. And we've got 3 inactive state of negotiations. So we're seeing some pretty good interest in the solution.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. So both interchange and third-party fee is going to be the revenue component from a payment card. This is -- I would assume this is like step 1, do you have also step 2, 3, 4 to add other payment options like credit, or with the e-commerce platform, anything with respect to the "buy now pay later" where you've made some investments in the past?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

I mean, certainly, we have been looking -- poking around "buy now pay later" don't -- haven't really pushed hard there. Clearly, as we start to get into payment cards, there may be a need for some of our customers may see some benefit in providing lines of credit that support temporary cash demands. So certainly that's where it leads to next. To date, we see that payment card as a functionally more like a debit card - a way to make a payment from money that's already in the account.

Chadwick Westlake - *Equitable Group Inc. - Senior VP & CFO*

Of course, with the payment solution. That's the direct question is yes, but as you can appreciate, this is programming at the entire digital bank. This is one of the top requested solutions by our customers today. And we believe this will help further increase customer acquisition, improve

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that ratio of customer lifetime value the customer -- cost to customer acquisition and then further engagement, which we publish as well, more products to bring them in. So here we're looking at the whole economics as it starts to come into play. I'm really excited about that momentum we're going to establish.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Excellent. Second theme was just on the all pay single-family book. Obviously, really, really strong growth in originations. I think it was that all pay originations were CAD 2 billion in the quarter, which is obviously a really strong result. Can you talk about what you're hearing from the boots on the ground in terms of market share competitive dynamics? How is that market -- how do that market play out in Q3, and then what are some of the adjustments you're looking at today in the Alta space as we're seeing 5 interest rates back up a little bit.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. So I mean, the adjustments you make are effectively as we change pricing, things like GDS, TDS automatically, people have to have more income. So that's an automatic credit adjustment, if you like. Certainly, we are hearing that our team are doing a great job on customer service. We're engaged with the brokers, we've delivered some pretty good technological solutions in the first half of the year -- or the first 3 quarters of the year that are making us easier to deal with. And we expect to have some more advancements -- a pretty significant advancement launch before the end of this year to continue that journey to really excel our customer service, which has really always been our calling card. So I'm pretty excited about how this business will be positioned in coming into next year. And that's in contrast with how we started last year. And as I've mentioned on this call in the past, it's on me, but we were overly cautious last year in the middle of the year, because of fraying of the broker relationships with as it turns around in retrospect overly sensitive of how the credit might play out in the face of pandemic. And so it's -- the team has done a great job, frankly, rebuilding those relationships and with it delivering digitally enabled innovation, is going to take us up to the next level here.

Jaeme Gloyn - *National Bank Financial, Inc., Research Division - Analyst*

Okay. And do you deal from your conversations that you've grabbed some market share here, or is this more a case of the industry doing really, really well as a whole?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

We certainly are understanding from boots on the ground, feedback from our sales team, business development managers. And from the data that we get, we do have some proprietary data around market share. It's not entirely clear. It's not entirely crisp, and it is a bit more focused in Ontario rather than -- it's more available in Ontario than other provinces. But certainly, our understanding, will obviously see us the other people participating in the space report. But certainly, our belief is that we've gained share.

Operator

Your next question comes from Graham Ryding with TD Securities.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Just on the interest rate mortgage rate side, as we start to see interest rates rise here, what are you seeing in terms of mortgage spreads, both on your Alta and your commercial book?

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Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Essentially, those spreads remain the same. As we've mentioned many times, we use our ROE calculator to calculate the spreads and returns we're driving. When rates move very fast, things can get a little bit out of whack for a short period of time, but we're pretty quick to adjust. So certainly seeing spreads being well maintained. Probably in this period of -- what looks like some pretty significant volatility in upcoming and interest rates, we'll need to be on our toes to keep adjusting rates. But again, we compete in the old space with other people that fund through similar mechanics than us, used most of the funding coming out of the broker GIC market. We obviously have some really good funding sources and covered bonds now, which are cheaper than GICs and our proprietary channel is EQ Bank, which may give us a slight funding advantage vis-à-vis our major competitors. But broadly speaking, we have the same kind of cost structure there, and similarly on commercial. So commercial is much easier because it's priced on a loan-by-loan basis, and people understand that we're -- how we're thinking about that. We do have to be a bit more rapid to change in the single-family business, which is more of a rate card type of business, but those rate cards do change fairly frequently as we see underlying rates change in the market. So I do think compared to many other types of special services, we have, we're a pretty good position to push rates through as well as our underlying funding costs rise.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Okay. I appreciate that. On the funding side. So my math tells me that deposit notes and your covered bonds represent about 8% of your deposit mix today. Where would you be targeting to see that by the end of '22, perhaps?

Chadwick Westlake - *Equitable Group Inc. - Senior VP & CFO*

Yes. Higher for sure, Graham. So we -- you're right. So the deposit note program, where Andrew was mentioning our competitive position with funding in the markets where as our program has matured. In some cases, we're seeing spreads in entirety GICs as well and in deposit notes and then cover bonds we see higher. So the answer to your question, we would see cover bonds being at least double from where it is now. So if you call it 2%, go to 4% in deposit notes, probably -- if it's a CAD 1 billion program in now, you may see that another 50% increase by next year. So you do the math on that and assume this level of growth rates, too, that we've projected for EQ Bank, you can build that funding stack up. Also when we're saying another 20% to 30% growth and you keep that deposits and that updated perspective. And then brokerage GICs would come down a little bit more on the funding stack, so had some tailwind.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. Just a follow-up on that. The one number that's important in terms of dropping at the bottom line is how much we do in deposit in covered bonds and when we do those. Broadly speaking, the deposit note cost is roughly speaking, the same cost as depends on any day, any market -- the day in the market. But roughly speaking, the same prices or same cost to us, net as broker deposits. So in terms of your models, I don't think we're particularly sensitive to the growth in the deposit mode program, although it's great from a safety and diversification of funding basis. But clearly, saving that 50 basis points or so on covered bonds becomes really important.

Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Okay. Understood. I thought deposit notes were a cheaper funding source as well, but it's just so recovered bonds. That's where you're going to get the funding cost benefit?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. I mean deposit notes sometimes it could be ten times cheaper for that thing. Not as though they're not. It's not those completely inconsequential. But I think when you're building out aggregate model of the bank, it's probably not going to be a big driver, but the covered bonds certainly just because the Delta is that much bigger with more sensitivity to the earnings there.

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Graham Ryding - *TD Securities Equity Research - Research Analyst of Financial Services*

Okay. And my last one, if I could. Just with the rollout of payments, you said second half of '22, any material expense associated with just the infrastructure or the marketing behind that, or should we expect that to just be embedded within a reasonable expense growth rate that we've seen this year?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Yes. I mean of course, as you're building these new programs, generally you're capitalizing a lot of that cost, so that, that then starts to kick in, in the second half of next year. But none of that, obviously, when Chadwick is projecting our kind of efficiency ratio, the ROEs he's projecting. That is how the team is doing that buildup. So nothing that you should be overly concerned about.

Operator

(Operator Instructions) Your next question comes from Geoffrey Kwan with RBC.

Geoffrey Kwan - *RBC Capital Markets, Research Division - Analyst*

I just have one question. As you look to get your transition to AIRB at the start, I think it's 2023. Are you able to talk about in terms of where the areas of your loan book that you would get the most risk-weighted asset relief. In particular, just curious if that changes your appetite on where you want to grow the business versus what you're doing right now?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Ron can maybe add some more color to what I'm saying. Certainly, we expect -- in our current business, we would expect pretty significant capital relief in a single-family mortgage business and in much of our commercial business. It does, they become a bit more nuanced in our commercial business, some parts business where capital relief would be more significant. And I do think it will allow us to compete in better quality commercial assets where the risk weights will reflect the fact that we're lending on lower risk assets. So things like cash flow apartment buildings will become an area where we can be more competitive post AIRB than we are today. So it will change the mix of our business, and I think generally, move it to a less risky asset business. Ron, you're deep in the weeds on AIRB. Can you align with what your thinking?

Ronald Tratch - *Equitable Group Inc. - Senior VP & Chief Risk Officer*

It absolutely aligns. Geoffrey, the only comment that I would make in addition to what Andrew has said is recognize that typically when a bank is less with the AIRB approval from the regulator, the capital savings are typically staged in over a period of time, could be 3, 4, 5 years. And so it gives management a lot of time. It's not a cliff-like effect where we would immediately change the composition of the book. It would be a very gradual change. Your question was directed at specific business lines, but we are -- when you become here, you do have to hold a certain percentage of capital at the top of the house. So management will have some very interesting decisions to make in terms of how we deploy capital to the various businesses. But if you think of it being staged over time, limited at the top of the house, you could -- it helps you to understand it will be a gradual shift into some of these areas that Andrew has referenced.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

And Geoff, just to reinforce, I mean, which is the way we think about this is there's 2 things that really exciting about AIRB. One, is to be able to support our clients over a longer life span. So today I find it really frustration that we help a customer build an apartment building, for example, the but then with tenants get to a lower risk type of assets and then we can't compete with AIRB banks because that asset is now safer, and therefore,

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they're able to use lower risk weights. So in our new world, we would envision holding high-risk weights on that assets. We first put on the books, lower the risk weight as the risk weight drops and be able to support a customer over a longer period of time. And it should be relatively cheap for us to service that customer because we obviously have the history of that for that client relationship. The other thing is that the bank is becoming more sophisticated, and we'll show this to you in spades in our investor meeting in the spring. But as we become more sophisticated, we need to have better ways to measure credit risk across the various books and be entirely objective about how we're allocating capital. So AIRB allows us to do that, and we're well aware that under standardized approach some sort of approximations to risk being used and we think about that a lot. But AIRB allows us to align our capital allocation with the true underlying risks.

Geoffrey Kwan - *RBC Capital Markets, Research Division - Analyst*

And maybe if I could just a quick follow-up on that, is your comments around the single-family residential book in your Alta book. Do you foresee that -- I mean, does that allow you or do you plan to use that to your advantage in terms of improving further your competitive position in that space?

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Well, certainly, I think I believe it opens up that opportunity. And today, as you know, we have -- you have Prime mortgages and you have old mortgages. And we -- all of those mortgages are risk-weighted 35% under standard approach. The big banks are risk-weighting their mortgage books in somewhere in the 10% to 20% range, so, much, much lower. And clearly, there are buckets of risk within that mortgage business that within the old and prime mortgage businesses that do should quite correctly demand different risk weights. And so we will be able to be more finely tuned as a bank in terms of which parts of the space we choose to compete in based on the pricing that we can demand in the marketplace for that component and the risk weights that should be applied.

Operator

There are no further questions at this time. Please proceed, Mr. Moor.

Andrew R. G. Moor - *Equitable Group Inc. - President, CEO & Director*

Well, thanks, Pam. If you would like to engage on any of the topics we discuss today. Our door is always open. Thank you for your time and attention, and have a great day.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a great day.

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