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EDITED TRANSCRIPT

EQB.TO - Q4 2016 Equitable Group Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 17, 2017 / 3:00PM GMT

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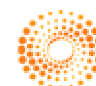

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PRESENTATION

Operator

Good morning, ladies and gentlemen. I'd like to welcome shareholders and analysts to the Equitable's fourth-quarter 2016 conference call.

(Operator Instructions)

We would like to remind you that certain forward-looking statements may be made on this call including statements regarding possible future business and growth prospects. you are cautioned that such forward-looking statements involve risks and uncertainties detailed in the Company's periodic filings with Canadian regulatory authorities. Many factors could cause actual results or performance to be different from those expressed by such forward-looking statements.

Equitable does not undertake to update any forward-looking statements made by itself or on its behalf except in accordance with applicable securities laws. This call is being recorded for replay purposes. It's now my pleasure to turn the call over to Andrew Moor, President and CEO of Equitable Bank. Please go ahead, Mr. Moor.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Thank you, Ashley, and good morning, everyone, and welcome to our call. I'm joined by Tim Wilson, Chief Financial Officer of the Bank. During today's call, we will provide our thoughts on 2017 and the way forward. We will begin with a recap of Equitable's record annual results and strong fourth-quarter finish to the year.

As a reminder, our slide deck at eqbank.ca that accompanies our remarks is a valuable reference tool that I encourage you to review as part of our analysis. the MD&A being the definitive source of information. 2016 was a transformative year for Equitable; four highlights stand out. First, we continue to differentiate the Bank on superior service delivery in our lending businesses. So while maintaining our rigorous underwriting and risk management standards, we built our reputation with mortgage brokers across the country and gained market share.

Mortgages under management were up 26% to CAD21 billion on record single-family originations, and the best showing in our commercial business in the five years. Second, we introduced our EQ Bank digital platform positioning Equitable to innovatively answer the needs of a cashless society. Some of our customers tell us that they already consider EQ Canada's leading digital bank based on value, features, and functionality.

That means a lot to us as does the fact in just over 11 months, EQ has become an important funding channel. The EQ Bank Savings Plus account attracted CAD1.1 billion of deposits adding 27,000 new customers to Equitable. Having just launched the new digital bank features, we look to build on our initial success as we'll discuss later in the call.

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Third, we retained our entrepreneurial culture even as we became a big organization with more expertise. This is illustrated a number of ways but perhaps the best is our October deal to secure an interest of CAD3 billion of outstanding NHA-MBS pools originated by Maple Bank. This transaction demonstrated the Bank's ability to quickly draw on our finance, capital markets, legal, compliance, mortgage underwriting, and risk assessment resources to thoroughly evaluate bid, execute, and close a complicated transaction that added CAD0.07 to EPS in 2016 and will continue to be accretive through 2020.

Fourth, we remain a performance leader amongst Canada's banks on all key value creation metrics even though we invested significantly to develop our digital platform and our prime business at a cost of CAD0.82 per share. We grew net income 10% to a record CAD138 million, delivered ROE of 16.9%, and funded two more common share dividend increases. These results test the competitiveness of Equitable's business model, attention to every detail that makes for a successful customer experience and the consistency of our value creation process.

By consistency, we're proud to note that Equitable's average ROE of 17.8% over the past five years has far outpaced the average of Canada's big banks of 15.6% over the same period. The Bank's ROE has been between 16.5% and 18.7% over the last 10 years. Equitable's EPS has grown every year for the past decade and by 17% compounded annually over the past five years. Equitable's book value has grown every year for the past decade and by 17% compounded annually over the past five years.

Equitable's common share dividend has risen 11 times in seven years including twice in 2016 and once already in 2017, as you will note from last night's press release. While delivering these financial results, we've been bearing the heavy expense of new initiatives and brand building activities that surely build the value of the bank's franchise for the longer term. Inclusive of common share dividend payments, our five-year total shareholder return was 160% compared to the TSX capped financial index return of 101%.

You heard all about change coming in the banking industry, and I think these very positive outcomes demonstrated Equitable, as a pure branchless and increasingly digital bank, is clearly well-positioned to grow as change comes to the industry, and Equitable's focus on service delivery without bricks and mortar branches becomes a clearer advantage. We're using technology to rethink how Canadians want to bank, and with our Savings Plus account redefining the role of the everyday bank account, eliminating the artificial distinction between checking and savings accounts that give Canadians a single all-digital solution to pay bills, transfer money, and grow their savings faster.

As those of you attended our recent investor day know, our digital vision is just starting to unfold, and over the next few years by building on our competence in digital banking, continue to broaden our services in the mortgage broker community, and investing with the fintech committee, we intend on cementing our leadership position as Canada's challenger bank.

The Equitable team has done a remarkable job this past year in bringing the Bank another step closer to realizing our vision of leadership while generating consistently great results for shareholders, savers, borrowers, and our partners. My sincere thanks to all Equitable employees for their dedication, outstanding productivity, and enthusiasm in embracing change, and doing the hard work required to execute on an ambitious plan and excellence in day-to-day service.

Now let's look at the financial performance. In the fourth quarter, Equitable finished strongly with net income of CAD41.7 million, up 33% from the fourth quarter of 2015, and diluted EPS of CAD2.56. Both of these metrics were property records and led to ROE of 19.3%, well above our Bank's typical expectations.

The Bank's core performance was driven by growth in our mortgage book. Record mortgage originations of CAD2.2 billion in the fourth quarter seem to us to be a sure sign that our strategies and plans are working as intended. This is the third consecutive quarter that originations surpassed CAD2 billion. Origination growth at 25% year over the year reflected positive results in every one of our lending businesses.

The most important contributor to our earnings was single-family alternative lending. Fourth quarter originations were CAD930 million, also 29% above last year. This reflected market share gains in the broker channel that we earned over the past 12 months as a result of our outstanding service quality. Share gains were supplemented by growth in the overall alternative market.

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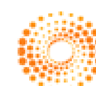

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[Thinking back], single-family alternative mortgage principal ended the quarter at CAD7.9 billion, up 22% from a year ago with positive implications earnings in 2017. Let's take a moment to stress that we achieved to this growth without sacrificing quality. We have maintained our rigorous approach to underwriting. We will not overreach for growth. Credit management is paramount to the Bank and is critical to the achievement of our longer-term goals.

For the third consecutive quarter since refining its approach to the market, commercial lending operations posted strong performance. Commercial fourth-quarter originations grew by 46% to CAD378 million, its most productive period in five years. We have a very experienced team in commercial driving these results and through our focus on service, they continue to increase the size and quality of their deal flow pipeline.

As a result of recent growth, commercial lending mortgage principal stood at CAD2.8 billion, 27% ahead of last year and up about CAD170 million from Q3. Commercial balance growth has been helped by retention, which has been high in recent quarters and the surprise is on the upside. We do expect attrition to climb a bit as we progress through 2017.

Moving on to prime single-family, fourth-quarter originations of CAD652 million, up 33% from a year ago, bring total prime originations for the year to CAD2.1 billion and prime mortgages under management to CAD3.9 billion. Internally generated prime originations were CAD125 million in the fourth quarter or 16% above last year, so we've made good progress.

Keeping with our goal of developing a track record as a consistent dividend grower, our Board increased our common share dividend again yesterday, this time by 4.5%. Meaning that the dividend to be paid on April 6 will be 15% ahead of the dividend declared by our Board in February last year. While paying an increased dividend of 14%, we believe that we have a strong CET 1 ratio that provides a solid foundation for the Bank's future growth.

Our capital position was assisted by a CAD50 million equity investment made in December by OMERS, the first call we've had since completing the equity raise and we thought a bit of color on our thinking might be helpful. Toward the end of last year as part of our annual strategic planning process, we assessed the richness of opportunities and we concluded there was a compelling business case to be made for additional equity.

Following this assessment, we took a decision to complete a private placement with a highly regarded pension manager, a move that allows us to pursue more growth and value creation without sacrificing our always strong capital ratios. We are always keenly aware that new equity is diluted to existing shareholders, so we would not have completed this offering without being confident in the Bank's potential for ongoing growth.

Maintaining appropriate capital levels for banks is always a judgment and might change over time, but our own view is that running with a CET 1 ratio of about 13.5%, plus or minus 1% or so, is the right place for Equitable to be. Moving on to credit risk, you will note the net impaired mortgage assets of CAD36.8 million were up by almost CAD5 million from last quarter. This increase was entirely a result of impaired formations in Alberta and Saskatchewan, But those levels, they are still only 0.21% of our total mortgage book, down 1 basis point from a year ago.

Our allowance for credit losses, which is the amount reserved on our balance sheet for total credit losses, represented 19 basis points of our total loan assets. This is much higher than that Bank's average loss rate experience of 4 basis points over the past 10 years. All things considered, we remain well reserved. The provision for credit losses that you see on our income statement, which represents the net additions to the allowance in the current period, with CAD900,000 in the fourth quarter, or 2 basis points to average mortgage principal.

This was down from a year ago and from Q3 and in line with the Bank's long-term loans and well below the industry average. Looking at the west for a moment, our Alberta and Saskatchewan portfolios have performed better than we had expected to date in the face of energy price declines. That said, impaired loans did trend higher in the fourth quarter in these markets to CAD14.6 million from CAD11.6 million in the September quarter.

How the total delinquencies in the fourth quarter, which includes the earlier raise, remains small in the context of our overall business and are down from Q1. Although oil prices and economic conditions appear to be stabilizing, we expect to raise rates on impaired loans in these provinces to rise in 2017. But continue to expect that losses, if any, would be manageable and certainly less than we might have expected two years ago as only prices dropped dramatically.

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Overall for the Bank as a whole, we expect our arrears rates and credit loss provisions to be low in 2017, assuming the Canadian economic conditions stay within the broad range of market expectations. I'll return with thoughts on 2017 in a few minutes, but first, Tim will provide his report.

Tim Wilson - *Equitable Group Inc. - CFO*

Thank you, Andrew, and good morning, everyone. As you've now received an update on the Bank's annual results and long-term track record, I'll focus on a few specific aspects of our Q4 financials. As Andrew said, the fundamentals of our business continue to be strong. our performance was really a story about the sustained growth of our mortgage assets. That growth exceeded expectations, the markets, and our own by several hundred million dollars.

Also contributing to Q4 performance was the Maple deal that we closed in the quarter. It had a CAD0.07 per share positive impact on earnings. We had expected accretion of between CAD0.06 and CAD0.08 per share so it came in at the midpoint of that range. We also recorded CAD1.3 million in gains related to some defaulted insured mortgages that we acquired from the liquidators after the Maple deal closed and referenced it as an item of note in the MD&A.

Continuing on Maple, now that we have better data about how these mortgage pools actually perform, we believe that income for 2017 will be closer to the top end of our original range, which was CAD0.25 to CAD0.30. We also expect a few hundred thousand dollars of gains on some more defaulted mortgages that we have acquired and which are insured by CMHC.

The fourth quarter got an assist from two other factors, unusually strong prepayment income and derivative gains, which together contributed CAD.010 to our EPS. These items don't necessarily repeat each quarter and are therefore not ones we count on to drive results, but we'll take them nonetheless. Even after removing these items, fourth-quarter performance was strong, and net interest income, it was an all-time quarterly record of CAD78 million, up 23% from a year ago on growth and average asset balances and stable margins.

We had indicated that margins would be around 1.64% in the quarter, consistent with Q3, and they came in 6 basis points higher, a real positive for earnings. This increase was a function of a few different factors, including prepayment income in our securitization financing business, growth of the high margin commercial portfolio, favorable pricing in the GIC market, and the benefits of interest rate reductions on our EQ Bank and brokered high interest savings accounts.

Looking to 2017, our outlook for net interest income is for more growth at year-over-year rates in the mid to high teens on continued similar growth rates in our assets. I'd now like to move to our margin outlook and we use Q4, our most recent performance, as my reference point. The various drivers of that margin outlook are itemized in our MD&A along with our key assumptions but I will touch on a few of them now.

Looking at our expectations for the various portfolios, we anticipate that 2017 core lending margins could be up to 5 basis points lower than in Q4 2016 even though margins within single-family and commercial should be relatively consistent with Q4. This decrease is the effect of a portfolio mix shift towards lower spread but higher ROE single-family assets.

On securitization financing NIM, we anticipate that it will also decrease slightly, mainly due to the unusually high level of prepayment income that we recorded in Q4. Prepayment income aside, margins should be relatively stable. Margins in prime will be highly dependent on the market's reaction to regulatory changes, however, so we may need to revise our thinking there as we gain perspective in the coming months.

Moving on, current growth in the business as well as investments in support of our key business strategies led to an increase in Q4 non-interest expense as compared with last year. This increase was planned, and it was designed to create long-term value for our shareholders. Fourth-quarter non-interest expenses, excluding the impact of strategic investments, increased by 17% or CAD3.7 million year over year.

FTE was again the primary driver as our headcount increased by 15% in order to support high levels of service and risk management. Similarly, FTE and costs grew in line with one another quarter over quarter with both up 3%. Non-interest expenses to support strategic initiatives amounted to CAD4 million, 69% above last year's level. These are important investments that will help to drive future shareholder value and brought total investment in our future to CAD17 million for 2016 as a whole.

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Due to these investments, our efficiency ratio was higher in 2016 than in past years, 37.8%. Although as expected, it did decline throughout the year. It dropped to 33.9% in the fourth quarter, but that was a function of the denominator as much as it was good cost management. As noted earlier, we had some revenue tailwinds in Q4 that served to reduce our efficiency ratio below expected levels.

Looking forward, we expect total non-interest expenses to continue increasing at year-over-year rates consistent with the growth rate of the Bank's assets. We expect our efficiency ratio will remain just above the mid-30% level in 2017, a rate that would once again qualify Equitable as Canada's most efficient Schedule 1 bank, a title we have held for many years without interruption.

Finally, and as Andrew said, the recent equity investment by OMERS increased our capital base and will allow us to pursue the best opportunities available in our lending business. On a related note, and you will likely already have this baked into your forecast, please remember that the equity issued, 809,000 shares and CAD50 million in dollar terms, will really only begin to affect our EPS and our ROEs starting in Q1.

The weighted average impact of the issuance on Q4 was negligible given that the transaction closed on December 23. With that, now back to Andrew.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Thanks, Tim. We look to make 2017 another year of great performance for our shareholders through the execution of our strategies and value creation model. There's no question that recent regulatory moves, which we discussed in previous forums in detail, including our third quarter call, will have an impact on the single-family mortgage market.

The degree of that impact is still an open question. While there are early signs of softening activity levels, I think we need to wait for the spring market to unfold before we have a really good sense of that effect. At this point, we are not in the position to constantly say how much change will happen with consumer and comparative behaviors. What we do know is the prime insured single-family represents less than 2% of our overall earnings so any decline in this market will not have a noticeable impact on our 2017 earnings.

Also on the regulatory front, you are likely aware that the government has circulated a proposal for lender risk sharing on insured mortgages. While the details are still being worked out, we do not believe that any [impressions] proposals need in the Canadian market and could have significant unintended consequences on competition and access to housing.

We are actively engaged with industry groups and regulators to get across this perspective and know that it is shared by many. We will have more to share on this development as we move through the year. In this environment, consistently delivering shareholder value means realizing our vision of being Canada's leading branchless bank. That involves additional investments and further development of our digital capabilities and solutions.

And that [I am flight], I am pleased to report that we've just launched some new EQ Bank features to add more value and convenience for our customers, and in so doing, attract more deposits. EQ to EQ transfers new functionality that allows money to be moved instantly between EQ Bank Savings Plus accounts. So if you and your daughter both have accounts with us, and you want her to have funds to buy some textbooks, say, you simply log on and do an EQ to EQ transfer.

Unlike other forms of money transfer, ours is almost instant, free. It does not use email so it is more secure without burdening the receiver with password requirements each time it's used and there is no hold on the deposit. It is straightforward and almost frictionless. We believe this functionality will encourage more Canadians to open EQ Bank Savings Plus accounts because let's face it, for most of us, the transfer of funds between friends and family is an almost weekly occurrence, and why should Canadians pay extra for that convenience.

In addition, because we respect the fact that many Canadians work with more than one bank and hold several different accounts, we make it possible for customers to easily link our EQ Bank to up to 10 different accounts versus just three for the other well-known digital bank in Canada. We've also enabled electronic preauthorized deposits and payments reasoning that for most of us, there is no better way to save them to have your paycheck deposited directly to your EQ bank account, start collecting interest, and then move your money from there.

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Being able to set up automatic bill payments to add to the bill payment functionality that already existed adds additional convenience for our customers and value. At other banks, this capability is typically only offered for a non-interest-bearing checking account while with EQ Bank, our customers earn interest every moment until the money is withdrawn. Because our core banking platform was purposely built for a digital world, these new features were relatively easy to add from a technology perspective.

Our team invested time and effort to ensure that we had the best customer experience and the most elegant view as possible. These additions are part of our strategy on diversifying our sources of deposits while offering different choices to the large and growing segment of Canadians who know intuitively there are better ways to bank and that trusting Equitable to deliver that to them.

Over time, and in fact again later this year, we expect to add more convenience and additional value to our EQ Bank offerings, and in the process, continue to further our standing as Canada's challenger bank. This year, our goal is more qualitative than quantitative. We want to create the services that allow EQ Bank customers to choose Equitable for the vast majority of their day-to-day transactions.

Engaged customers that think of EQ as a key provider of financial services will of course help build the Bank's franchise value. We also determined to grow our lending businesses by using service to create stronger and deeper relationships with both our distribution partners and borrowers.

At times like these when regulations are changing the home buying calculus for many Canadians, the support and advice that Equitable provides is more important than ever. We always expect competition in our businesses, and I'm sure 2017 will be no different, so maintaining our customer service edge and making sure our products are competitive and properly priced will be important again this year.

To summarize, this was a transformative year, our quest to cement our position as Canada's challenger bank. The successful launch of our digital platform positions Equitable well for the evolution of banking in a cashless society and creates an important new funding channel for the Bank that we continue to develop.

Our lending business has performed at record levels and we believe there are plenty of potential to grow assets with higher rates through to the end of 2017 and beyond. We sustained our multi-year track record as one of the Canadian banking industry's best creators of shareholder value even while reinvesting heavily in our business. That said, our job is not to celebrate past records; it's to create long-term value.

In that regard, we look forward to channeling our advantages including our efficient business model, ability to innovate and change, proven capital allocation process, and the enthusiasm of our team into more performance for our shareholders and 2017 and the years beyond. That concludes our prepared remarks, and now we'd like to invite your questions. Ashley, can you please open the lines to our analysts that have questions?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Jaeme Gloyn, National Bank.

Jaeme Gloyn - *National Bank Financial - Analyst*

Yes. Good morning

Andrew Moor - *Equitable Group Inc. - President & CEO*

Good morning.

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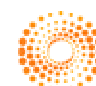

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Jaeme Gloyn - *National Bank Financial - Analyst*

First question is related to deposit funding. Just looking at the strong performance obviously from EQ Bank and good year-over-year growth from brokered HISAs, but just looking at brokered HISAs on a quarter-by-quarter basis, there's some fluctuations there.

I was just wondering if you could speak to how you managed the brokered HISA accounts and building those relationships with investment advisors and wealth managers.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, we have a broad network of wealth advisors across the country. Interesting to think about the brokered HISA, that typically is not something that's listed by the higher up affiliates of the big six [desibs], so this is typically coming from independent investment dealers.

We have seen some changes on one or two boards where one of our competitors is paying a higher commission and as a result, they were discouraging advisors from using us. But other than that, it's a fairly stable environment and we continue to be in good dialogue with all of the significant distributors of that product.

Jaeme Gloyn - *National Bank Financial - Analyst*

Okay. So it's primarily coming from wealth managers. The big six don't participate in the brokered HISA arena.

Andrew Moor - *Equitable Group Inc. - President & CEO*

That's right. The big six see that is comparative to their sort of core business of providing interest savings accounts.

Jaeme Gloyn - *National Bank Financial - Analyst*

Great. Okay. In terms of the breakdown of deposits, how do you see that progressing over the course of 2017 to fund uninsured mortgage origination growth?

Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, I think it's not going to change dramatically over the upcoming year. We're not --as we related to you, our focus on the digital bank has continued to build capabilities and provide more services to the same customers. We do -- we actually are seeing good deposit growth in that channel right now. But that's not really the goal for the year.

The goal is really to get people in a more engaged relationship with us so that we can be more confident that those relationships are going to withstand ups and downs in the market. And frankly, we're seeing plenty of opportunity in the brokerage GIC market to fund all of our needs.

In fact, I would say that if you look at the pricing of GICs, that if the GICs were able to raise vis-a-vis say government rates, which is the way we think about that as a benchmark, those spreads have actually being tighter in the last little while and so we've been able to get plenty of liquidity at attractive funding sources.

That gives you a good look at the liquidity position we ended here at that was partly reflective of that. We saw a good opportunity to raise money relatively cheap to benchmarks at year end.

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Jaeme Gloyn - *National Bank Financial - Analyst*

Okay, and how do you look at the risk in the deposit funding channel? Do you see any areas where you may be concerned? Maybe you could elaborate on that?

Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, I think, one is always concerned about control. We live in a banking industry that's fairly concentrated, so to the extent that some of our large distributors decided for whatever reason not to deal with us, that's a risk. And that obviously is the -- maybe they are doing that to keep the funding for their own book. For example, it could be one of the motivations.

So certainly, the EQ Bank play is very much about being able to go directly to the consumer and control our distribution channel. And I think what we showed in the first few months of the year in particular when we were relatively aggressively trying to build that book and our ability to go direct to Canadians and raise funding is much stronger.

I sleep much better at night now knowing that we have always can turn that tap on more aggressively if we needed to fund the Bank. And I think that really positions us well. It's a really strong solid funding source.

Don't forget these are CDIC insured deposits, so what we saw in 2017, 2018 when I was running the Bank then was that people liked to deal with small institutions and have the comfort of the CDIC limit even though there are bigger institutions with higher credit ratings but they of course not all the deposits sits within that CDIC limit, so they like to spread it around amongst the smaller banks.

Jaeme Gloyn - *National Bank Financial - Analyst*

Right, and just one last question drilling into the brokered HISA. What is the concentration I guess within the wealth management community? Is it well diversified? Are you exposed to a handful of advisors or shops? How does that breakdown look?

Andrew Moor - *Equitable Group Inc. - President & CEO*

It's fairly well diversified. I mean, there was one broker that had about CAD30 million or so of deposits with us. But you know there has been some chatter on the boards about it. It did reduce the position we had with them.

We're in very active dialogue with the senior executive team there, and I'm pretty comfortable to be back on that board before the end of the year. And a lot again, a lot of that goes to I think that the underlying decisions there are really more related to compensation issues then they are particularly to some other sort of views.

But it is fairly well diversified so we do call on a lot of small independent Op managers and distributors, and that book is pretty well diversified. I think there is one or two that might be close to 100 million --.

Tim Wilson - *Equitable Group Inc. - CFO*

A little in excess of that. That's right. But I think it is a very well diversified book, and on top of that, the brokered HISA period adds to our overall funding diversification. As you know, we've moved from about two funding sources to seven over the course of the past couple of years so are actually feeling very good about our ability to manage those related risks.

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Andrew Moor - *Equitable Group Inc. - President & CEO*

I meant to tell you we are paying 0.9% on that HISA and the book is growing I think slightly. We're not looking actively for money in the HISA. We're more tended to focus on the -- not on the brokered HISA. We're looking for more to the branded EQ Bank interest savings account or savings class account depending on preference.

Jaeme Gloyn - *National Bank Financial - Analyst*

Great. That's excellent color. I appreciate that. Just shifting gears quickly to the core lending in your guidance of single-family originations of 18% to 20% asset growth for the 2017.

Some of what's driving that is the improved renewal rates is a bullet in the rationale and assumptions. I was wondering if you could just elaborate on what you're seeing there, how you're driving improved renewal rates, and how does that compare to industry standards.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Actually, I'm not entirely sure -- we are expecting good retention this year. Renewal rates have been relatively stable over the last couple of years, and we think we've done a good job, maybe an opportunity to sneak it up. One of the things that is interesting this year though is the significantly lower portion of our book is actually up for renewal this year, so a lower percentage of the overall book actually needs to be renewed this year.

So clearly, that is encouraging for retention. I think that delta alone -- I was just doing some math on the back of an envelope, but I think that delta alone was what actually helps potentially the portfolio growth by about 3%.

Jaeme Gloyn - *National Bank Financial - Analyst*

Okay, so it's not really anything that you are doing with fee changes or actively pursuing I guess mortgages that are up for renewal at some point. There is no real change in the strategy, it's just the mix of mortgages renewing is different this year.

Andrew Moor - *Equitable Group Inc. - President & CEO*

I would say we've stepped up our game with our people. I mean our people have always been fantastic. [Jessica off] and our team are some of the most dedicated employees we have, and they have simplified some of the documentation [or rather that] and they really do try to spend a lot of time on the phone with our customers making sure the customers understand what their options are and where they can go, and we find that that's the biggest determinant of renewal performances is that engagement with our customers, helping people make their decisions, these obviously important decisions, and taking it forward from there.

So I think there's always -- I think even though I think the team is doing a fantastic job, I think they would be the first to acknowledge there's always room for improvement.

Tim Wilson - *Equitable Group Inc. - CFO*

And I think, Jaeme, just to add a bit of additional color on that, I think part of our expectation and again, we may not be right on the mark with this given the uncertainty is that the regulatory changes that were introduced last fall could cause us to increase our renewal rates. It might -- those changes might make it a little bit more difficult for borrowers to move from one lender to another and make it totally -- slightly easier for us to retain the customers that have maturing mortgages.

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Jaeme Gloyn - *National Bank Financial - Analyst*

Okay. Great. Thanks, all. I'll let somebody else jump in.

Operator

Geoff Kwan, RBC Capital Markets.

Geoff Kwan - *RBC Capital Markets - Analyst*

Hi. Good morning. I just have one question, and just I guess maybe getting a little bit of an update on the move to AIRB just in terms of the timing. Is it still in line with what you guys were originally expecting?

And then two, if you're just able to talk even if it's a little bit higher level is with the benefits you get on the capital perspective, how you think about how that plays out in terms of you getting your business and your various mortgage segments whether or not on the residential side or on the commercial.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Yes, thanks, Geoff. The AIRB is actually sort of moves hand in glove with IFRS 9 change, and I don't know who's really up to speed with IFRS 9, but IFRS 9 is a huge project for banks. It moves to an expected credit loss model.

It involves many of the same aspects that are involved in AIRB, so our team -- the AIRB team have been pretty focused on the transition to IFRS 9 in recent months, but we've put in a software made by a company called Wolters Kluwer to model all of this, and we are progressing along well. The big picture is we still are on track for AIRB overall timing although the focus has been slightly less AIRB and more IFRS 9 related but those two things are quite closely linked.

We don't -- I know there's other banks out there suggesting that there's a lot of capital relief from AIRB. That's not really what we're after with respect to AIRB. It's more about being able to be more precisely defined about how we're allocating and making sure that our capital aligns with our risks in the business and being more quantitative about that as our business grows.

So for example, today on the standardized approach, a construction loan is 100% risk weighted. A fully cash flowing apartment building at 30% loan to value is also 100% risk weighted. It's very clear that the risks inherent in those two buildings, two properties, are different and as a result, we find it very difficult to complete on that lower risk project.

So we would hope that on a commercial business in particular would benefit from being able to price certain loans that reflect a lower risk weight and thereby be able to continue to grow faster because they would be chasing a broader spectrum of opportunity. [Tim, do you want to say anything on the progress?]

Tim Wilson - *Equitable Group Inc. - CFO*

Are you able to get any sort of benefits on the residential side of your business because certain -- not all players out there that are on the regulated side would be on the AIRB, they'd still be on the standard approach?

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Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, I think the big issue for us --I was sort of getting into that a little bit on the risk sharing arrangement, is that the big banks put very little capital up against the residential mortgage books even though for example, generally speaking, the mortgage is not that different than ours frankly. It's 35% risk weights.

I think many of the big banks are operating in a 8% to 15% risk weights, so it would make it very difficult on the short mortgage book if we end up having risk sharing because we would be putting up 35% risk weights or something on the inherent risk left where they'd be putting up say a third of the amount or less. So again, being on a level playing field when we've got assets of similar quality will be helpful to us.

So it's always tough to compete with people that might be working under a different regulatory regime, and I think that's really where AIRB leaves you. In other institutions that are using a standardized approach in the Canadian Western Banks or [interest] banks as well that are also compared of course do use a standardized like us today so that's a much fairer level playing field.

Geoff Kwan - *RBC Capital Markets - Analyst*

Yes. Sort of what I was getting is if you are under the AIRB on the prime side, can you better compete with a lot of the other big players out there, but on the non-prime side, I would have thought you might get sort of bit of a benefit rather than having to put the 35% risk weight. Is that a fair assessment?

Andrew Moor - *Equitable Group Inc. - President & CEO*

But I think that's a fair assessment. Of course, how the regulator allows you to actually use that is a tricky thing to figure out. But certainly our view would be that under AIRB, our risk weights would be more appropriately in the kind of 20% to 25% level on the single-family book.

Geoff Kwan - *RBC Capital Markets - Analyst*

Okay. Great. Thank you.

Operator

(Operator Instructions)

Graham Ryding, TD Securities.

Graham Ryding - *TD Securities - Analyst*

Hi. Good morning.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Good morning, Graham.

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Graham Ryding - *TD Securities - Analyst*

I think you showed on your supplemental, you mentioned on the call your employment count is up 15% year over year which is in line with the growth of the book. But I'm just wondering how you actually managed that when you're looking at your underwriting teams and trying to manage the risk properly around a business that's growing at such a high rate.

What's your approach to making sure that you don't compromise or sacrifice at all on the underwriting side?

Andrew Moor - *Equitable Group Inc. - President & CEO*

I think that's actually what constrains our growth to some extent. We feel comfortable at the levels we're at. I think we would be less comfortable growing faster frankly, so and it's not as scientific now but adding 15% is not such a hard number to onboard, to train.

We have people with some experience in the industry but we do have a dedicated training team within the single-family business that can teach new underwriters and particularly mortgage officers the Equitable way. And often we find that people migrate through the organization so they might start in certain areas of the Company, administration or fulfillment and then move into underwriting over time.

And so it's relatively easier to onboard people into some of those jobs and then as they gain experience, move them up the ladder. Ad it's certainly a big focus that we have is identifying talent in certain areas of the Company and then deploying them into those areas where they can be really useful to us in making those critical risk judgments, and so on.

It's probably worth saying that we are an A1 platinum employer in terms of employee engagement, so we actually have a really engaged workforce that are really committed to helping us grow, and we are very picky about who we bring on.

In fact, every single person that comes into this organization is a -- we apply intelligence tests, too, and other kinds of tests around character to make sure that we've got the right people joining our team and that's really important to our culture and having the people with skills to actually be able to execute in what's a pretty challenging business.

Graham Ryding - *TD Securities - Analyst*

Okay. That's helpful. The Toronto housing market is getting a lot of attention from media but also some economists. How are you feeling about I guess underwriting mortgages into the market right now with the price growth above 20%?

Andrew Moor - *Equitable Group Inc. - President & CEO*

It certainly is something that we keep looking at, studying. I think it is something that we need to be -- we're constantly monitoring it and certainly looking for product pockets that might be particularly overheated, and we take a very granular approach to that. So there are some condo buildings, for example. We won't lend on them.

We just view them as inherently over valued and likely to cause difficulties. So I note it's certainly a time to be more cautious rather than more aggressive in the Toronto market.

Graham Ryding - *TD Securities - Analyst*

And how do you deploy that, a more cautious approach?

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Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, a lot of that comes through in sort of in the debt service ratios so they don't forget. People that we are lending to have to have the employment income to support the debt service on higher loan amounts, which were a function of higher property prices. So a lot of people do get -- and by not being able to borrow at full amount so they would like to borrow because they just haven't got the debt service ratios to do that.

So that's kind of an automatic feature of the lending criteria we've put forward, so that in particular is an area that has a lot of focus. Is the income there, is it real, can it service the debt.

Graham Ryding - *TD Securities - Analyst*

Got it. And then what would you have to see in this market for you to decide that you want to slow down the growth of your portfolio?

Andrew Moor - *Equitable Group Inc. - President & CEO*

Well, I think it could be a number of things. It's in particular the concern is always something that would change the immigration pattern into the city. So one of the things that's causing a -- the increase in housing prices is clearly strong immigration into the city based on a strong economy and a relative lack of supply of housing.

So if, for example, we suddenly decided we're going to build houses all over the greenbelt, that obviously could dramatically increase supply so we'd look at the supply side of that. And also, if there was anything that actually limited immigration to the city, or maybe that's attractive, that would also be something we'd be looking for. It's those fundamentals.

In fact, when we think about it in a Canadian context, so obviously Toronto is getting a lot of attention right now and others might get attention at different times. If oil prices spike again, you could see the same thing happening in Alberta, and we look to lend in those cities where you are seeing growing populations, so we look at the census data over the last five years.

We like to lend into those communities that have got growth. And frankly, while there may be risk in Toronto today, the highest risks historically in Canada have been lending in small towns where actually the populations are dropping and it's just a natural function that real estate prices tend to be declining in an environment with less demand.

Graham Ryding - *TD Securities - Analyst*

Great, and maybe I could sneak one more in just within the broker channel, with respect to mortgage rates and also broker commissions, are you seeing any pressure or any change with those factors?

Andrew Moor - *Equitable Group Inc. - President & CEO*

Certainly on the prime side, mortgage rates are very tight, as we mentioned in the script. And certainly one of our competitors come out with what they view as a sort of middle range product between prime and alt, so we don't really understand why it's priced the way it is, so that's a little bit of pressure for us.

It's not something that means something we can respond to, at least in the short term. Commissions is always -- adds a bit of concentration on the broker side. We need to support those larger brokerage houses and have a little bit more leverage with us frankly. But we work with brokers right across the country and there's always a satisfactory arrangement that can be made.

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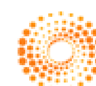

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Graham Ryding - *TD Securities - Analyst*

Okay. Thank you.

Operator

Jaeme Gloyn, National Bank.

Jaeme Gloyn - *National Bank Financial - Analyst*

Yes. I just wanted to follow along the conversation of single-family, core single-family lending growth by geographical areas. Looking at British Columbia, quarter-over-quarter growth is about 12%. It led the pace of quarter-over-quarter growth as well as on an annual basis, up almost nearly double from Q4 2015.

I'm just -- I just want to get your comments on what you're seeing in the BC market and the rapid pace there, granted that it is only a small piece of the overall pie. But some commentary would be nice.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Yes. It's a small piece of the overall pie, and actually it goes back to almost some of the questions that were asked earlier actually around kind of how do we think about that. In 2011, we were very concerned about overheated prices in Vancouver and chose to back away from the market there which is why we have a historically smaller book there.

And just to give you some sense of it, we're not really a lender in downtown Vancouver. I mean, we will lend there occasionally but more generally, if you think about this book, it's lending on houses that are worth CAD700,000 to CAD1 million in the Langleys and the White Rocks and the kind of areas in the lower mainland, close to Vancouver but not actually in Vancouver itself and to kind of a middle-class households.

And we have -- first of all, we've really cranked up our sales effort there. We have a really excellent sales team in Vancouver supporting our growth, which wasn't the case a couple of years ago, and that's seeing us with higher penetration.

Probably now we put an office there only two years ago, so we have been making further inroads into that market, and we continue to be relatively optimistic about that market although there is obviously a lot of low noise around Vancouver itself in the high-end homes and the question about sort of foreign capital flows and capital taxes, but really that's not the market we're participating in.

Jaeme Gloyn - *National Bank Financial - Analyst*

And does the -- I mean, the condo market has all that pretty wealth in Vancouver and those homes that are priced in the range that you are lending into, but does that not concern you that single detached homes are down 20%, and that's sort of flowing, trickling down to the market that you are lending into at a more aggressive pace right now?

Andrew Moor - *Equitable Group Inc. - President & CEO*

I think that's again another area we've absolutely got our eyes on closely, and the market is doing what real estate markets tend to do when they go through adjustment which is slow down dramatically first before you have really good price discovery, so it's definitely an area for concern that we need to be looking at closely.

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Jaeme Gloyn - *National Bank Financial - Analyst*

Okay. Thank you.

Operator

I would like to turn the call back over to Mt. Moor for any closing remarks.

Andrew Moor - *Equitable Group Inc. - President & CEO*

Thanks, Ashley, and thanks, everybody, for your participation. We look forward to delivering our next quarterly report in May and to seeing you at the annual shareholders meeting here at our office on May 17 at the Equitable Bank Tower in Toronto. Thank you, everyone, for listening, and we look forward to talking with you next quarter.

Operator

That concludes today's conference. Thank you for your participation. You may now disconnect.

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